LEAGUE of MINNESOTA CITIES

March 2, 2023

Re: SF 1957– 4d property class rates modification and appropriation

Dear Chair Rest and members of the Senate Tax Committee:

The League of Minnesota Cities appreciates the opportunity to provide comments on SF 1957. While we respect the intent of the bill author, we have concerns that a reduction of the class-rate of 4d(1) properties in Section 5 will have unintended consequences for cities and their residents.

Cities support the current Low-Income Rental Classification Program commonly referred to as 4d as a tool to provide affordable housing opportunities. Under current law, the class-rate for 4d property is 0.75 percent on the first-tier value and 0.25 percent of the value exceeding the first-tier amount for each qualifying unit. Section 1 of the bill eliminates the 0.75 first-tier class rate and sets the 4d class-rate for all existing and future qualifying properties to 0.25 percent.

When the two rates were first put into place, the first tier had a class rate of 0.75% on the first $100,000 of value. The second tier rate was 0.25% above that level. The lower rate was intended to reflect that even though 4d property is income producing property, low income housing does not monetize its full value. The $100,000 class rate break was indexed for inflation, so that the 0.75% class rate would cover more value each year to correspond with values rising across the state.

By 2021 the class break had risen from $100,000 to $174,000. In 2021 the legislature reset the class break back to $100,000 starting with taxes payable in 2023. 4d properties have yet to benefit from that tax benefit and will for the first time with their taxes payable this May. Under current law the class break will remain at $100,000 for taxes payable in 2024 and resume indexing again after that. The 2021 law change also addressed concerns raised at the time that inflation had eroded the tax benefit of the 0.25% rate.

The 2021 omnibus tax bill also included a requirement that the Department of Revenue complete a report on 4d property. That report found that the number of units receiving the classification increased by 34% from 2012 to 2021. The report also found that about 18% of class 4d value in the first tier would qualify for the second tier after the 2021 law change. The report examined impacts to local tax bases as well. It found that there are 75 cities where 4d property represents at least 1% of their tax base, and 17 cities where it represents at least 2%. So while the shifts across the state may appear small, they can be concentrated in certain jurisdictions.

We appreciate the local approval requirement included in section 3 of the bill. However, this provision appears to not apply to existing property owners that may only have a portion of their units designated as 4d units in their building that may want to transition more of their existing non-4d units to 4d units given the more favorable property tax break with the class-rate change. We also appreciate the transition aid in section eight of the bill. But it is important to note that the aid

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only partially offsets the impact to the local property tax base, is provided only for two-years and is static without regard to any new 4d units in existing or new buildings that come online.

Thank you for your consideration.

Sincerely,

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