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Tax Abatement in Saint Louis: Reforms Could Foster Equitable Development

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Background

Across the United States, municipal governments use tax abatement in various ways¹ to incentivize development and revitalize urban areas. In Saint Louis, historical housing trends related to deindustrialization, redlining, and “white flight” led to the City’s depopulation, creating the current need to incentivize development. However, in certain neighborhoods, development now occurs without tax abatement, and some homeowners and developers receive tax abatement despite being able to afford paying taxes. This points to a need to understand where and when tax abatement is necessary, and whether it is being used effectively.

In this brief, we ask the following questions: (1) Does Saint Louis use this policy differently than other cities, and (2) What is the most effective use of tax abatement when considering equitable development of blighted areas? We begin by exploring the history of tax abatement and some of the debate surrounding it as an effective policy tool for housing and economic development. We then compare tax abatement policies in Saint Louis to those of other cities to better understand the variation of possible uses. Based on the comparison, we offer four policy recommendations to improve the use of tax abatement in Saint Louis.

1. The City of Saint Louis needs a plan for the use of tax incentives, which includes applying the “but for” test to tax abatement.
2. Tax abatement should be increased outside of the Central Corridor.
3. When used within the Central Corridor, tax abatement should prevent displacement of existing residents and should include inclusionary zoning requirements.
4. State-level policy should clarify the definition of “blight.”

Tax Abatement and Its Current and Historical Uses

Tax abatement is the exemption or relief of tax liability, usually on the increased value of a property after improvements.² Referring to the taxes frozen to preimprovement assessed values, tax abatement is one subsidy used to close the gap between a developer’s equity and debt. According to Missouri law, tax abatement may only be used in areas deemed “blighted,” but the legal definition of “blight” remains vague; in practice, the determination of “blight” is left largely to the discretion of the City’s Alderpeople. Tax abatement is one the largest development incentives used in the City of Saint Louis, amounting to \$307.5 million from 2000 to 2014.³

Tax abatement was first used in Connecticut in 1640.⁴ In the period after the Civil War, southern states used the policy to recruit industry from the Midwest and Northeast to industrialize a predominantly agriculture-based economy.⁵ In later years, the rise of tax abatement policies is largely attributed to the manufacturing boom following the second World War.⁶ Since World War II, states have allowed more local economic development programs greater freedom, with local governments growing in number, size, and strength.⁷ Overall, there has been an increase in the use of tax incentives including tax abatement, tax increment financing (TIF), and Enterprise Zones.⁸

The Debate around Tax Abatement

There is significant debate regarding the effectiveness of tax abatement.⁹ Proponents of tax abatement often justify it by stating that it redirects business investment with the ultimate goal of urban revitalization. They argue that tax abatement may help developers or homeowners “take the leap” when deciding whether to invest in redevelopment. Alex Ihnen of *nextSTL* has argued that it would not make financial sense for many developers in Saint Louis to

invest in a project that is not tax abated.¹⁰

In theory, tax abatement could be targeted to support efficient, sustainable development. Because areas with declining populations tend to have underutilized infrastructure, redevelopment of these areas is less likely to require costly new infrastructure. Tax abatement could be used to encourage economically, socially, and environmentally sustainable development, but in Saint Louis it has yet to be used in concert with any comprehensive development plan.¹¹

Tax abatement is effective only at certain times and under specific conditions.¹² The success of tools for urban revitalization depends on their greater application in truly blighted areas than in wealthier communities. If both types of areas use tax abatement aggressively, total economic activity may not change, thus negating the incentive.¹³ In practice, though, development incentives do not appear to be more common in low-income areas; the term “blight” has come to be applied quite widely.¹⁴

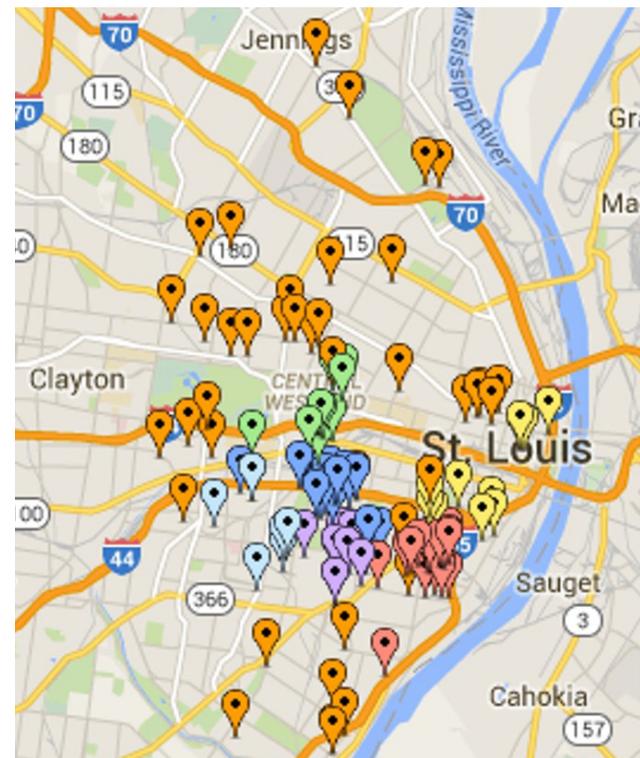
Additionally, the current use of tax abatement raises concerns about the unequal distribution of tax burdens. Tax breaks for new businesses may mean that long-standing local businesses and residents see increased tax burdens. Moreover, the process of granting discretionary tax incentives is complex and often not transparent. Particularly in the case of “spot blighting,” decisions are made in ad hoc ways without links to a broader city plan. This process can be unduly influenced by political considerations, with incentives granted to well connected firms or campaign contributors. In an analysis of local governments across the United States, jurisdictions in states with more corrupt political cultures were more likely to offer tax abatements.¹⁵

A related concern is that politicians may grant incentives regardless of the economic rationale. Public policy researchers from Indiana University conclude that tax abatement programs are often too generous, and recommend that tax abatement is effective only partially, temporarily, and conditionally. Local governments should limit the granting of tax abatement, allowing for the achievement of positive net benefits.¹⁶

Tax Abatement in the City of Saint Louis

To understand why the discussion of tax abatement is critical in the City of Saint Louis, we must begin with a brief history. Saint Louis—a city scarred by depopulation, underdevelopment, and economic turmoil in the past decades—faces a massive economic and population decline. Saint Louis City, at its peak in the 1950s with almost 860,000 residents, today reports just over 300,000 residents.¹⁷ Indeed, Saint Louis City had lost more than half a million people by 2000—not unlike the infamous depopulation of Detroit.¹⁸ Population is often hailed as a critical indicator of a city’s health; by this metric, Saint Louis is quite unhealthy. Tax abatement is seen as one means of stemming this population loss

Figure 1. 2015-2016 Tax Abatement Bills in the City of Saint Louis



Dark Blue - 6th Ward
Yellow - 7th Ward
Red - 9th Ward
Light Blue - 10th Ward
Green - 17th Ward
Orange - All Other Wards

Map created by Andrew Arkills

Box 1. The Use of Tax Abatement across Selected Cities

City of Des Moines, Iowa

Property tax abatement percentages vary depending on the type of improvement and property location. New additions and renovations of less than \$40,000 anywhere in the city are eligible for a 115% abatement for 10 years. New construction and rehabilitation projects of more than \$40,000 are eligible for 100% abatement for five years anywhere in the city; properties in specified locations are eligible for a 10-year abatement.

City of Portland, Oregon

Single-family, owner occupied homes in selected neighborhoods designated as Homebuyer Opportunity Areas are eligible for a 10-year property tax abatement on the value of improvements from rehabilitation or new construction. The property's sale price must be \$275,000 or less, and the total annual income of all property occupants must not exceed \$73,000. This amount is adjusted annually.

City of Cleveland, Ohio

Newly constructed single-family homes receive a tax abatement of 100% of the increase in real estate property tax for 15 years. In other words, owners only pay a property tax on what the land was worth before it was improved with the new construction. Residential projects must meet Cleveland Green Building Standards.

City of Cincinnati, Ohio

Tax abatement is detailed by the Residential Property Tax Abatement program aimed to stimulate community revitalization, retain city residents, attract homeowners, and reduce development costs for homeownership and rental projects. The tax abatement program allows for owners to pay property taxes just on the pre-improvement value of the property for 10-15 years. Properties with current abatements will have their tax abatement revoked if inspectors find violations and the developer does not resolve the violations.

California (statewide)

The Mills Act provides tax incentives for the restoration and preservation of qualified historic residences. Local governments negotiate these property tax abatements on a case-by-case basis with owners of qualified historic properties. Owners can achieve property tax savings of 40% to 60% per year. The Mills Act program is considerably more complex than other tax abatement programs discussed.

The Saint Louis tax abatement policy is described as a tool designed to assist developers, businesses, and individuals with renovations and new construction projects.¹⁹ Tax abatement in Saint Louis freezes the tax assessment on improvements to the property at the predevelopment level. To be eligible for tax abatement, a developer must make significant investment in the property, generally either new construction on vacant land or gut rehabilitation of an existing building. Applicants who wish to apply for tax abatement must do so before construction begins, and the usual term for tax abatement is five to 10 years.²⁰ The City of St. Louis website also details that it is imperative for a company or an individual seeking tax abatement to obtain the support of the Alderperson of the Ward in which the development is proposed.²¹

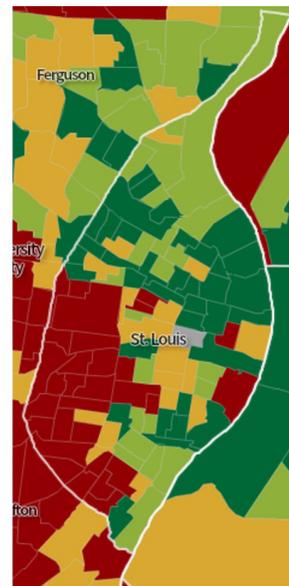
In 2015, the St. Louis Development Corporation commissioned an analysis of the City's use of tax abatement and other incentives. That report suggests that tax abatement is focused strongly in and around the Central Corridor of the city.²² Yet unlike other cities, there is no city-wide plan guiding the use of this tool.

As is evident from Box 1, many cities use tax abatement as a tool for redevelopment of "blighted" areas but go about this policy in very different ways. Compared with other cities, Saint Louis has yet to develop its tax abatement policy in connection with a more intentional plan.²³ Indeed in Saint Louis, tax abatement is often perceived as automatic or "assumed" by the developer when it comes to applying for the incentive.²⁴

Figure 2. Proposed Guidelines for Tax Abatement of Single-Family Homes

Poverty Rate in Census Tract	Time Limit for Single-Family Homes*
<10%	0 (None allowed)
10-19.9%	5 years
20-39.9%	10 years
≥40%	15 years

***With exceptions possible for existing, low-income residents**



Data Source for Poverty Rates: American Community Survey 5-Year Estimates, 2014

Policy Recommendations

The City of Saint Louis needs a plan for the use of tax incentives, which includes applying the “but for” test to tax abatement. For the City of Saint Louis to truly revitalize “blighted” areas and encourage redevelopment, it must begin by evaluating evidence of tax abatement success. This will require more nuanced data analysis of when and where tax abatement is being used and its resulting economic growth. Though a “but for” test is not currently legally required for tax abatement in St. Louis, this is the question policymakers should, in fact, be asking: What would happen on the proposed abatement site “but for” the abatement?

Tax abatement should be increased outside of the Central Corridor. Tax abatement should be focused in areas with fewer economic resources—places that meet a conventional definition of the term “blighted.” As the evidence suggests, tax abatements are most effective when they are used in these areas. As suggested by the Lincoln Institute of Land Policy,²⁵ Saint Louis officials must determine their goals for tax incentives, and evaluate whether current policies are meeting these goals. Some have suggested tying incentives to Saint Louis’s Market Value Analysis (MVA). We appreciate this suggestion,

but only if the MVA is used to attract investment outside of the Central Corridor and to encourage affordable housing within the Central Corridor. One challenge of the MVA is that it is difficult for a layperson to understand. Using a simpler criterion for investment, such as the poverty rate in a Census tract, could be a way to add clarity and encourage greater public participation in the discussion on tax abatement. For instance, with regard to single family homes, guidelines could recommend limited use of abatement in areas with <10% poverty, five-year maximums in areas with 10-19.5% poverty, 10-year maximums in areas with 20-39.9% poverty, and 15-year maximums in areas with >40% poverty (Figure 2).

When used in the Central Corridor, tax abatement should prevent displacement of existing residents and include inclusionary zoning requirements. Where tax abatement is used for multiunit properties, it makes sense to include inclusionary zoning requirements for affordable housing, particularly within the gentrifying Central Corridor. The displacement of the Black population, and specifically lower-income African American households, is widespread throughout the Central Corridor.²⁶ The regional “OneSTL” initiative and the Lincoln Institute of Land Policy recommend the use of inclusionary zoning, and provide examples and recommendations of best practices.²⁷

State-level policy should clarify the definition of “blight.” There are also state-level policy changes that could improve the use of tax abatement and other development incentives. The State of Missouri should better specify the definition of “blight.” Having standard criteria²⁸ and having a metric with which to measure and prove “blight” will help city officials determine whether or not a property is appropriate for tax abatement.

Conclusion

In addition to the four policy recommendations above, city officials should make the tax abatement policies and the process more transparent and instill greater oversight. Though we offer some broad suggestions for policy reform in this brief, we believe that this issue should be taken up more fully by the public. We hope to see it become a central issue in the upcoming mayoral election in the City of St. Louis.

Endnotes

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