Mills Act 101

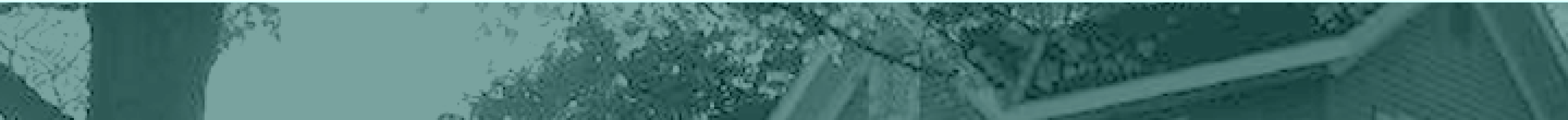
Preservation Through Tax Incentives

Presented by the City of San Luis Obispo and Office of Historic Preservation

June 1, 2007

What is the Mills Act?

- A local property tax incentive to encourage restoration, rehabilitation and preservation of privately owned historic resources.
- A historic preservation tool to revitalize historic residential neighborhoods and commercial districts.
- Program designed and administered by the city with help from the assessor. No state government oversight.

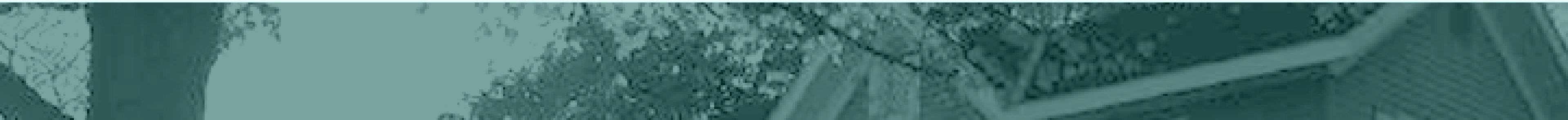


State's role in Mills Act

- No state oversight. Authority rests with cities and counties. Disputes handled by courts.
- Office of Historic Preservation advises and consults with property owners and local governments; serves as clearinghouse of information.
- Board of Equalization advises and interprets for County Assessors.

Benefits to Property Owner

- Incentive to keep historic property rather than develop or sell.
- Only financial incentive available to historic homeowners in California.
- For commercial owners, can be packaged with other incentives.
- Tax benefit runs with title – a selling point.
- Accepting tax benefit is voluntary.
- Tax benefit is indefinite.



Benefits to Local Government

- Helps retain and maintain historic properties.
- Can foster preservation of historic neighborhoods.
- Incentive can help revitalize downtown commercial districts.
- Can preserve historic fabric of community, boost cultural tourism and increase civic pride.

More Benefits to Local Government

- Program is flexible. Can be designed to target specific resources.
- City controls number of contracts, property values that can be included. This allows cities to cap revenue loses.

Addressing cost- lost revenue

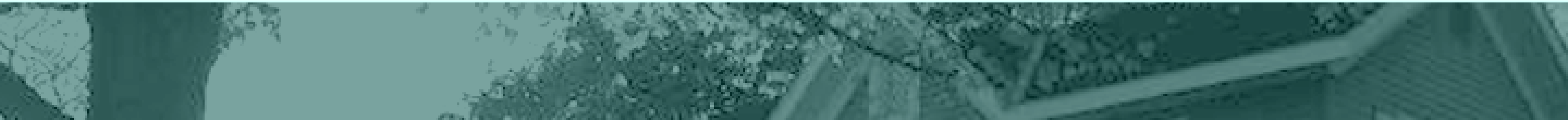
- Lost revenue is property tax, often a small portion of city revenue stream.
- Fees can offset administrative costs.
- Mills Act investment can generate positive economics increasing property values and promoting businesses growth.

How Does Mills Act Work?

- Cities may enter into a contract with property owner. In exchange for tax relief owners agree to restore or maintain historic property in accordance with federal, state and local standards.

Mills Act Framework

- Properties must be on a local, state, or national register of historic places or contribute to a national historic district. Cites can narrow that definition.
- Properties must be privately owned and subject to property tax.
- Contracts are 10 years minimum. Contracts extend one year annually unless either party chooses not to renew.



Mills Act Framework, Cont'd.

- Local government administers program. Local government controls application process and does annual inspections.
- Contract specifies what maintenance or rehabilitation is to be done.
- Property must be restored and maintained in manner compatible with its architecture and uses and original fabric retained where feasible. Federal and local standards apply.

Mills Act Framework, Cont'd.

- Local government can enforce a contract by judicial means. If that fails a contract can be cancelled for breech and after a hearing. There is a penalty of 12 ½ percent of value of property for owners whose contract is cancelled, paid to State.
- Assessor calculates Mills Act tax assessment annually.

Mills Act History

- 1972 – Sen. John Mills authors “Mills Act” in response to plight of Coronado Hotel in San Diego.
- 1973 – Law determined unconstitutional.
- 1976 – Voters approve constitutional amendment.

Mills Act History, Continued

- 1985 - Mills Act amended to reduce minimum contract period, eliminate visibility to public and public access and reduce penalty for cancellation.

- 1993 – Act amended to define restoration and rehabilitation as meeting the standards of the OHP, State Historic Building Code and Secretary of Interior's Standards

Mills Act Participation

- 85 Mills Act cities in California.
- More than 2,375 contracts.
- Three cities added program in 2006.
- At least four cities considering now.
- Interest growing rapidly as property values soar and resources are lost.

Mills Act Mathematics

- “Income” or capitalization formula used.
- Can result in tax savings of 50 percent or more.
- Formula complex.
- Only assessor can calculate actual savings.
- Assessor determines key elements.

Basic Formula:

Single-family Owner-Occupied Home

Gross income (fair rent)	
$1,500 per month x 12 months	$18,000
Less anticipated vacancy and collection loss	
$18,000 x 5 percent	-900
Effective gross income	$17,100

Basic Formula:

Single-family Owner-Occupied Home

Maintenance costs

Operating expenses	$600	
Grounds maintenance	$400	
Fire Insurance	$360	
Management fee	$360	
Water and Garbage	$240	
Building maintenance	$500	$2,100

Net Operating Income

$17,100- $2,100 = $15,000

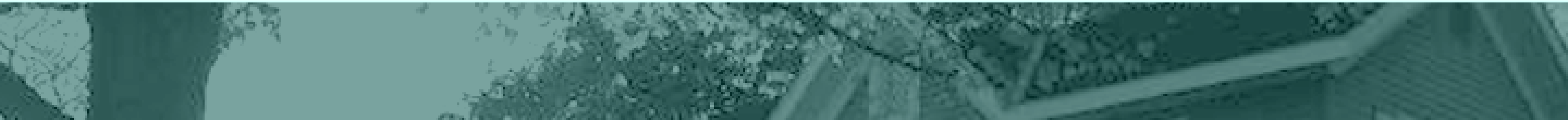
Basic Formula:

Single-family Owner-Occupied Home

Restricted Capitalization rate

Rate Components

Interest Rate	.080	
Risk	.040	
Property tax (basic tax plus any special taxes for district)	.015	
Amortization rate* (50-year remaining life; improvements 70 % of total property value .02 x .70	.014	.149
Restricted value $15,000 / .149		= $100,671



Basic Formula:

Single-family Owner-Occupied Home

Tax Value - Three way comparison

Restricted value

$100,671 x .015 = **$1,510**

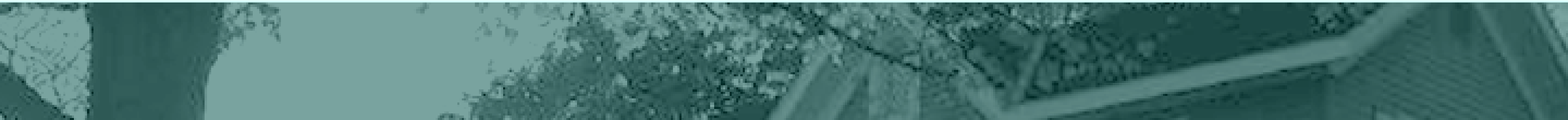
Factored base year value (prior change in ownership)

$357,000 x .015 = $5,355

Current market value (based on comparable sales)

$450,000 x .015 = $6,750

Potential Tax Savings $5,240



Basic Formula:

Commercial Property

Gross income (fair rent)

140,000 sq. feet @ $1.75/sf – 245,000

X 12 months = $2,940,000

Less anticipated vacancy

and collection loss

$2,940,000 x 5 percent -147,000

Effective gross income $2,793,000

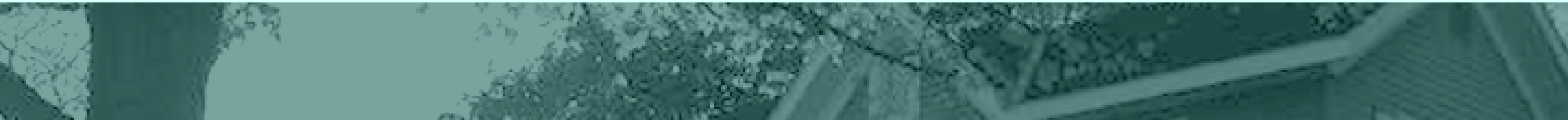
Basic Formula:

Commercial Property

Maintenance costs

Operating expenses	$140,000	
Insurance	$75,000	
Management fee	$290,000	
Utilities	$360,000	
Building maintenance	$95,000	-960,000

- *Net Operating Income*
  $2,793,000 - *$960,00* = *$1,833,00*



Basic Formula:

Commercial Property

Restricted Capitalization rate

Rate Components

Interest Rate	.080	
Risk	.020	
Property tax (basic tax plus any special taxes for district)	.011	
Amortization rate (50-year remaining life; improvements 75 % of total property value .02 x .75	.015	.126

Restricted value

$1,833,000 / .126 = $14,547,619

Basic Formula:

Commercial Property

Tax Value - Three way comparison

Restricted value

$14,547,619 x .011 = $**160,024**

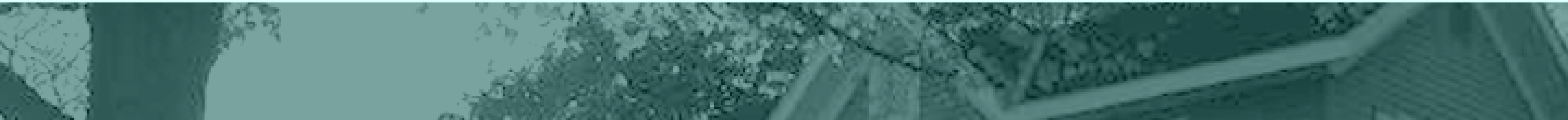
Factored base year value (prior change in ownership)

$18,181,077 x .011 = $199,992

Current market value (based on comparable sales)

$21,000,000 x .011 = $231,000

Potential Tax Savings $71,000



Where Mills Act Formula components come from

Gross income (fair rent) - *Determined by assessor.*

Maintenance costs - *Determined by assessor, based on information provided by property owner.*

Interest Rate - *Determined annually by Board of Equalization as of the preceding December.*

Risk – *Set by Mills Act statute (4% residential, 2% commercial)*

Amortization rate – *Determined by assessor.*

Non-renewal

- Once either party notifies the other of a non-renewal the tax benefit reduces by about 1/10 annually. By year 10, the property owner should be paying the same tax they would have paid before the Mills Act.

Implementing a Mills Act Program: Choices are city's

- Can be formal ordinance or less formal resolution.
- Can target certain properties by limiting what qualifies.
- Can choose level of enforcement.

Ordinance approach

- Spells out Mills Act in Historic Preservation Ordinance.
- More structured approach, less flexible.

Resolution Approach

- Council approves program. Delegates to staff administer.
- Council approves final contracts.
- Approved Council resolution forwarded to County to initiate program.

Work in Advance With Assessor

- Mills Act may be new to assessor.
- Assessor needs lead time to prepare tax assessment.
- Assessor must keep information up to date.
- Get political buyoff.

Sell Community on Mills Act

- Hold Informational meetings.
- Be ready for tax reduction opponents.
- Address perceptions.
- Work with other government agencies that share property tax revenue. Schools redevelopment agencies especially sensitive.

Mills Act Quirks

- Longtime owners (pre-1985) may not benefit.
- Law does not address multiple owners.
- Surprise increases if assessors don’t keep up on data.
- Government owner/developer lease deals addressed by law.
- Tax benefits may take effect in year following approval of Mills Act contract.

Summary of Mills Act Pros

- Only incentive available to historic home owners.
- Can be used with other commercial property preservation incentives.
- Tax incentive especially helpful to recent buyers.

Summary of Pros Pros

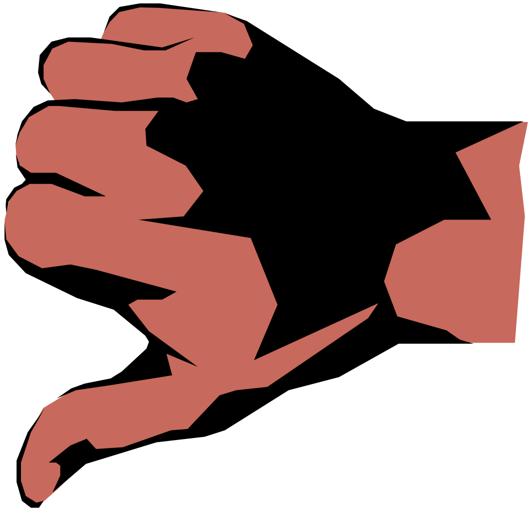
- Mills Act contract goes with title - a selling point.
- Program permissive, city can craft to its needs.
- Contracts don’t have to be renewed if city/owner needs change.
- Fees can offset program costs.
- Can encourage owners to seek historic designation.

Yet more Pros

- Can help revitalize, maintain historic civic cores.
- Helps keep up historic neighborhoods.
- Boosts civic pride.
- Helps retain civic history, character.

Mills Act Cons

- Lost tax revenue.
- Program costs.
- Lost revenue to other agencies.
- Not much benefit to longtime owners.
- Perception issues.



Note:
There are More Pros than Cons

Questions/Contact Information

- Jeff Hook, Senior Planner AICP (805) 781-7176 or www.jhook@slocity.org

- Lucinda Woodward, OHP Mills Act contact, (916)653-9116 or lwoodward@parks.ca.gov

- Lisa Gofourth, SLO County Assessor’s Office, (805) 781-5643

Handouts

- Mills Act Statute (Government Code and Tax and Revenue Code)
- Example of council resolutions
- Examples of Mills Act contract
- Secretary of the Interior's Standards

PowerPoint created by Dennis Weber, OHP and Jeff Hook, City of San Luis Obispo

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