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Home building fees in Cross fire

n Homebuilder: Local residents account for most new home sales

By John Callow
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When it comes to representing the position of home builders in Rutherford County, Paul Cross readily admits he has a built-in bias, but that doesn't mean he doesn't understand other points of view.

"I understand the perspective of those who have lived on a tract of land for many, many years and have looked out their windows and seen nothing but cedar trees and deer, and the level of disappointment they have when their neighbor goes to the nursing home, the property is sold and it's being developed," said Paul Cross. "I clearly understand that. But that's a quality of life issue, and I don't think it has anything to do with the current debate over who pays for what costs."

Cross, an independent administrative consultant, has become a voice for the local homebuilders. Study and statistical analysis have led to some interesting discoveries, he said.

"The adequate facilities tax bill as drafted says people moving here need to pay their fair share, so it does not put an unfair burden on the existing residents of the county," Cross said. "There is a perception in the community that growth is caused by people moving here from other places. That is not the case. It's absolutely not the case. I spent hours going over census data and doing the counting, so I could be satisfied.

"Seventy percent of the growth in Rutherford County is internal and a great majority of the new homes and new residential units are not being filled by people who are moving in here," he said. "They're being filled by people wanting to stay here. That's a very important factor in all these considerations. I think Rutherford County needs to recognize that."

- **The people involved in building houses in Rutherford County have put on a full-court press against any kind of fee or tax solely on new-home construction in the county. Is that a fair representation?**

They're opposed to any new taxes that are only on new-home construction. That's an absolute fact. No question about it.

- **Why the full-court press?**

There are a couple of reasons. The first is the up-to-$2-a-square-foot tax the county wants. If it were just a $2-a-square foot tax and that were it, you could deal with it. What they're talking about is $2 per square foot on top of what's already in the neighborhood of $6 to $9 a square foot in other fees. And it's not just the development tax. The development tax is $1,500, but it's only a small part. Then you've got sewer tap fees, basin fees, impact fees in Smyrna and La Vergne. Consolidated Utility has a growth fee and a development fee. That's an additional $500. All of these things are added to the price of a house, and they add nothing of appraisable value.

Right now, for a typical house, you're talking about $14,300 in the price of that house being government-related fees and taxes that do not buy one pipe, one inch of asphalt, no water, streets or curbs. It pays for nothing (related to that house). It goes to the government. So you have to overcome those fees in the value of the house. You've got to build the house efficiently enough to overcome that $14,000 in added costs and still have the commodity appraised so people can meet the loan-to-value ratios that are required.

If the county adds $2 a square foot on that average house, a 1,700- to 1,800-square-foot house, that's $3,400 more added to the cost of that house with nothing of value added to the house. It's got to stop. We can't add any more fees.

- **Why?**

Because we're generating appraisal problems. You have some people buying new homes because they want a new home, and you have others who buy new homes because that's the best deal for their economic situation. If you're buying an existing home, you have to deal with the appraised value; you have to deal with the seller's financial situation, you have to deal with the lending institution's closing requirements; and often, especially with a first-time buyer, they can't overcome the cash difference between the appraised value of an existing home and the price of that existing home. They've got to make up that difference.

With a new home, builders build new homes today, so they know they will appraise at or slightly above the selling price. So a person who doesn't have $5,000, $10,000 or $15,000 in wiggle room because they have cash in the bank can't go buy an existing house, but they can get in a new house. If you continue to add fees to the price of the house without doing anything to increase its appraisable value, you set up a set of circumstances people can't overcome, they can't make up that difference and they can't buy a home.

The people who can raise fees need to understand that every time they do, it has a direct impact on people's ability to buy a house. We're putting so much on, the traffic won't be able to bear it. That's the concern. That's why the full-court press.

The interesting thing is the public perception that builders are opposed to this — doing the full-court press — because it's just another $2 a square foot that's going to come out of their pocket. These taxes do not touch the builders at all. They simply front the money, and they recover it at the time of closing. It's not a tax on builders. It's a tax on homebuyers. And they wind up having to pay a real estate commission on top of it; plus they have to roll it into a mortgage. They finance that tax over the life of the mortgage and they don't get to write it off their income tax, either.

We recommended some taxes that would have been directly on builders. The excise tax is a perfect example. We've also said if the county would do a one-time assessment on all existing residential property, we'll drop our opposition to the development tax and the adequate facility tax. The reason for that is then all property is classed the same, new-home buyers are not penalized and then the market is a level playing field.

- **Is that approach legal?**

You'd have to pass enabling authority. But why would it be illegal to put a tax on a new home and not put the same tax on an existing home? The people who buy existing homes benefit from the infrastructure just like the people who buy new ones.

The flip-side of that argument is how would it go over if only the people who paid the development tax were allowed to go into the new facilities built with the tax? You live across the street from the new house, but you didn't put any money into the new elementary school, so you can't go. That's the flip side of the argument you have to pay because you just got here.

A one-time assessment would level the playing field, and we would drop our opposition because from an economic point of view, things would be in balance.

- **Which brings us to the $550 million question. We're being told that's what the county school system will need for building projects in the next decade. Where does it come from?**

Most of it is going to come from property taxes and sales taxes. It's going to be financed. The development tax was implemented in 1996. From 1996 to 1999, the development tax generated $14.6 million. It generated $7.2 million last year. It's generated $4.6 million to date this year. I can't recall off the top of my head what was collected from 2000 to 2003, but add all that together — all they've collected since 1996 — and it's not even 10 percent of $550 million. It's obvious you're not going to be able to generate that $550 million from a development tax. If you tried to tax new development to that level would shut it down.

So it's going to have to come from the same sources it's always come from. (The Rutherford County Commission is) trying to find ways to pick up additional tax dollars and spread it out with a variety of other taxes. Up until 1963, government was essentially paid for by the property tax. They began the sales tax in the mid-1960s and the sales tax is now considered to be a burden on taxpayers.

At that same time, most municipal utilities would run lines out to areas to encourage development. The city paid for that with the idea they would lower the cost of services by adding to the customer base. Now developers are paying for every inch of water line, every inch of sewer line — and then pay a fee for the right to tap onto that. For that part of the infrastructure, development is paying its way.

The schools are another matter, and I'm not sure where we look for options. Beginning in '63 we did sales tax. About 1970 we started a wheel tax and they've reached the same level as sales taxes in that any talk of increasing it brings about a painful cry. Then they came up with this category of fees and taxes I call growth taxes. They were fostered in communities that thought they were suffering from growing pains. Now, in virtually every community in which they were enacted beginning in the late 1980s, they reached the point of substantial resistance. I think that's indicative of why we came up with the alternative revenue task force in Rutherford County last year. Is there some other means of financing this? I still think it will generally have to come from the property tax and the sales tax, trying to pick up some portions of it from growth taxes where they can — or the possibility of something like a real estate excise tax. I think that has tremendous possibilities. But you have to stick with the broadest base tax you've got so you don't reach the point you meet the kind of resistance you're meeting with wheel taxes and now with growth taxes.

- **As you've mentioned, the county's options for raising revenue are limited by state statute to the property tax, the wheel tax and the development fee. Last year the Legislature declined to let Rutherford County increase our development fee. Do any of your suggestions have the legs to make it through the General Assembly?**

My personal opinion is the real estate excise tax has a relentless logic about it. It would be very broad-based in that it would tax all real estate. The development community — and I'm talking statewide; let's look at the bigger picture — will likely not resist the excise tax. They see it as a replacement for development and growth taxes. At some point we're going to see a down cycle in new homes. It could go on for three, four or five years. The revenue from growth taxes would fall off.

Real estate sales might fall off, but in a dynamic environment such as Tennessee, not to the same degree. Our geographic location is responsible for the fact we do have a lot of high-growth counties. We are at a nexus in the United States for transportation. That's feeding a lot of the activity. In a college town, where people come for four or five years and some decide to stay, real estate is going to continue to change hands. Whether people build new houses or not, the market for existing houses is going to generate sales and every time a piece of property is sold, government would get a small part of that. It would be a tremendous recurring revenue stream not as subject to economic change as new home building.

The education needs and the financial needs of the state of Tennessee are such that something new is going to have to be used. From the state's budgetary point of view, when state government begins to look at the revenue potential of a real estate excise tax, you'll see them get very interested in doing that. The leadership in the Senate is looking at it right now because we forced that issue, but they like what they see. In the Washington model, the state of Washington gets 1.28 percent from a real estate excise tax. The counties and municipalities are enabled to claim up to 75 basis points (3/4 of 1 percent) dependent on their participation in a growth management plan.

As the state looks at it for a source of revenue and the counties look at it as a source of revenue, this offers a tremendous potential. Let's face it: There's not much real estate being sold at a loss. People who don't sell, people who are retired who are going to stay in their homes are never going to pay it. If they do sell their property, it's likely they're going to see a rather significant appreciation and there would be no other tax on that appreciation up to $500,000. It's not a "back-breaker" tax in that respect. A real estate excise tax has tremendous potential; it's not going to solve the needs of every local government, but it could be a part of the mix that funds growth in the schools.

I have suggested the real estate excise tax be earmarked for education. I can see it being earmarked for facilities and start-up costs so there would be a time when some of it could be allocated for what we traditionally consider operational costs. There are 95 counties, and in most counties, education claims the biggest part of the budget. I think you could put together a pretty strong coalition in favor of that tax. There are going to be some opponents, just like there are to most taxes.

- **The real estate community?**

What the real estate community has said is they're opposed to any additional taxes on new construction or real estate until such time as the government goes and looks at another potential base. One example of that would be manufacturing. Go tax car makers. Put a privilege tax on manufacturing radiators. Put it on the people who make the parts.

- **In other words, put it on someone else?**

The problem gets back to the fact that right now, through the development tax and the amount of sales tax we pay on a new home, we're making a pretty hefty contribution already. We pay sales tax on every rock, on every nail, everything that goes into that commodity. On that average house, the sales tax on materials above the ground amounts to about $5,300 in sales tax. Half of what comes to the county in that sales tax goes to education. The reality is we don't attract growth. We respond to it. The growth is coming from jobs and a wonderful educational institution. People come here and they need a place to live. We're taxing something we have to have. I think what real estate is saying, "We're in the manufacturing business, but there are a lot of other people in the manufacturing business that export their products out of the county and you don't get any sales tax when their product is sold. You get tax from us on everything we do, so how about going to the others and picking up a little here and a little there." You have to believe that if counties were enabled to put privilege taxes on manufacturing, sooner or later that's going to have to happen. It would follow logically as each sector of the economy reaches the point of the full-court press, they'll have to go look somewhere else.

- **Depending on whom you talk to, the home building industry in Rutherford County is either No. 1 or No. 2 in the county and the automotive industry is the other. Is there any way to quantify the impact of home building?**

The home building industry is not seen by the public as a single entity like you would look at Nissan or Tridon or Southern Container or any of the other large companies because we all show up at different places to punch the clock. But if you put under a single roof all the enterprises in Rutherford County that are directly involved in providing goods and services for the home building industry in this county, it would make Nissan look like a duck blind. But we're individual business people. With just a few exceptions, these are home-grown businesses. If the public could see how many people show up to punch the clock, I don't think you'd see what I think is a casual effort to tax this industry. I think the industry would have more respect.

A few of the state's largest builders reside in and operate out of Rutherford County, and there's a perception that's the building industry. But that's not true. The building industry is a lot of individual contractors, subcontractors and small businessmen who have two and three employees. It's a huge industry and it's making an incredible contribution in terms of the amount of money spent. And most of those dollars go right back into the local economy. The majority of these people are not spending that money somewhere else. It's being spent here.

- **What happens if there's a slow-down?**

If it closed down, it would be catastrophic. There will be some slow-downs. The economy is cyclical, and there will be things that cause that to happen. Rutherford County is so dynamic because of its geography; we're much less susceptible to that. If the homebuilding industry sees a 20 percent drop nationwide, you'd probably be looking at 3 to 5 percent in Rutherford County. But you can tax it to death. You could put enough tax on it that it would shrink dramatically, and that wouldn't be good. If it starts to shrink, then sales tax dollars start to fall. If you had a 20 percent drop in housing starts, you'd create a problem with a drop in the collection of the $1,500 development tax. The county would notice it immediately; but for the last several years, it's been running significantly ahead of what they thought it would do. Some of that may be because you pay it at two points, when you plat the lot and when you get a building permit. There may be a lot of platted lots out there that have paid half that tax. If there is a slowdown, the amount of drop could be even greater.

- **Rutherford County already has a development fee on new residential building.**

It started at $750 in 1996, and they doubled it in 2000.

- **That means it's been in effect almost nine years. Has that fee had any negative effect on the industry to date?**

No. It hasn't slowed down the numbers in terms of housing starts. What it does is affect buyers. As those fees go up, there are more would-be home buyers it gets out of reach for them for the reasons I said before. We're not seeing so much a drop in the number of homes we sell; we see a change in the nature of the buyer. People who would have qualified for more house are buying less house. I wouldn't say the development tax has hurt, but for the first time since the development tax was initiated, we have seen situations in the last two months where appraisals have fallen below the selling price. That's never happened, and I attribute that directly to the fees that are already there.

- **Not just the development fee?**

No, the development tax is just one piece. The development tax hasn't increased since 2000, but other fees and other regulatory requirements have been placed on the building industry. A great example is the national effort to deal with water quality through stormwater controls. An ordinance came into effect Jan. 1, and it seems like a minor thing. The requirements we have now that based on the costing we did, it's added $1,000 to the cost per lot to the cost of the house. We have to silt fence each individual lot. We also have to provide siltation barriers to keep the stormwater system clean. We have to keep the streets clean. We're doing the right thing, but that is going to increase the cost, and you're not going to add to the value of the house. For a thousand bucks you could add a fireplace or upgrade to a Jacuzzi tub. There are a lot of things you could do with that $1,000 that would enhance the appraisal of the house. But as it is, we're going to spend that $1,000 and we're not going to give people anything but a clean street.

- **What I hear you saying is you don't want to penalize one class of potential taxpayer, but doesn't that just mean the burden is spread thicker on all of us?**

That raises a couple of questions. The first is who owns the infrastructure when it gets built? Just the taxpayers who are paying for it or all the taxpayers? If the man who bought a house that's been sitting there for 20 years moves into a house in town or across town zoned for a specific school and there's a new development across the street and another moves into that new home, they're both longtime residents of Rutherford County, the man who buys the new home is going to pay his pro rata share of the cost of the new development to get his home there. If there's a new school financed through a growth tax, the children in both homes are going to benefit from that new school. Is that right?

- **What about the home owner who has no children in the school system?**

That's never been fair. But the way the government is established, we all own the government's assets in common. Generally speaking, I think people all ought to share in the cost of what they benefit from. Now I would make the argument that everybody in a community benefits from good education, whether you've got children or not. I think we have good education. I think the Rutherford County school system has done an incredible job. Based on this year's report cards, if you stack Rutherford County against counties that spent more per pupil, you're going to find out Rutherford County did better in the key factors than a lot of the counties that spent more money. That tells me something about the quality of what's going on in those classrooms.

One of the things that bothers me on a personal level is when two people with three children are living at their income level, and we've all heard how many people are living one paycheck away from disaster. Part of the reason that happens is people haven't saved and when something comes up they feel they have to have, they've gone and gotten it on credit. The majority of the people who have gotten in trouble with credit are not the ones who have bought boats and motorcycles. They were people who would use the credit card for a birthday party or a vacation ,and they would begin to roll all those day-to-day expenses into their debt and they kept doing that until they couldn't make the minimum payments. I see the same thing happening in government, especially local government. We've seeing a shift away from increasing sales taxes and wheel taxes and onto growth taxes. Now the growth taxes are altogether different because they can be in the form of a tap fee or a development tax. What's happening in those expenses and the objects that money represents are being purchased just like the birthday party or the vacation and its being rolled into the debt of the government entity which is the debt of the taxpayers. There's going to be a saturation point.

Government can borrow money more cheaply. If the development tax were paid at the end of the transaction, the taxpayer would save on the 6 percent of the real estate commission. Instead they're rolling all that and the fees into the mortgage and they're paying interest on it for 30 years. So we're putting the financing of government on the backs of the most important people in the economy, the people who are buying homes and living the American dream. That has got to be addressed. People have got to understand we can only afford so much government and we have to figure out where to draw that line instead of hiding it like we hide expenses on a credit card bill.

- **Would metropolitan government provide answers to any of the county's revenue questions?**

The quick answer to that is "yes," but I'm not sure that's the right answer. A very long and detailed analysis needs to be done and that would involve each governmental entity in the county studying the efficiency of their own operations. You would assume that if both the education systems were consolidated, there would be some duplication of services. But traditionally we don't see that much consolidation and elimination. We typically see consolidation, but no elimination. Davidson County is spending more than $2,000 per pupil more than Rutherford County. They have a slightly higher percentage of disadvantaged students than Rutherford County, but not by much. They're expending $2,000 more per student, they're not graduating as many seniors, they don't have as many highly qualified teachers in their ranks and the overall performance is not where it is in Rutherford County. That's a consolidated school system and a consolidated government.

Consolidation may be the way to go, but I'm not comfortable yet. It definitely needs to be studied as an alternative. And if nothing else, maybe it will motivate all these existing entities to become more efficient so they can avoid it.

- **What's the most important thing happening in Rutherford County?**

What I consider is a concerted effort to address underemployment in the county. Any program, any idea that addresses that issue is of extreme importance in Rutherford County. We're attracting jobs, but we haven't been seeing the kind of increase in median household and median personal income Rutherford County deserves to see. We need to make a concerted effort to achieve that. There's no county in the state with more to offer than Rutherford County. I don't think there's a county with better geography. There's no county with more history and tradition. We've got a wonderful university. But if we're not careful, because of our location, we could wind up with commercial enterprises that revolve around warehousing and distribution and not around the kinds of jobs that will enable the county to achieve what it can achieve. That would address many of the housing concerns people have about small houses. Small houses are not built to see how many you can squeeze off an acre of land. Small houses are built because that's where the market is. Anything that enables this community to advance personal income and median household incomes to a higher level is good. We need more individual efforts internally. We need to look inward and make the most of our assets and sell ourselves. That's the issue that concerns me most.
