

THE CIVIC FEDERATION

Graduated Real Estate Transfer Tax and Bring Chicago Home Proposal:

Position Statement

MARCH 13, 2024

Homelessness and a lack of housing affordability pose critical challenges for a growing number of people living in Chicago and at the same time contribute to a larger destabilization of the City's ability to attract residents and businesses. These issues combined constitute the local dimensions of a national social and policy crisis that the City of Chicago and other governments must address with holistic attention to both their immediate humanitarian imperatives and impact on the larger community. Bring Chicago Home (BCH) advances not so much a solution as a response to certain aspects of a crisis that has arisen from a dynamic, evolving and complex set of policy and economic failures. However, there are a number of questions left open by the proposal in its current form. The referendum presents both an opportunity and a risk for Chicago. It is an opportunity to generate a new dedicated revenue stream for the homelessness crisis in Chicago that at the same time presents the risk of negatively impacting the real estate market, especially for a commercial sector already in distress.

The Civic Federation has serious concerns about both the tax as proposed and the program it is intended to serve as currently articulated. The referendum would establish a new graduated, marginal real estate transfer tax structure to fund homelessness programs. If the constitutionality of the referendum is upheld by the courts and it is approved by the voters, an implementation ordinance would then need to be passed by City Council. Our concerns focus on a lack of crucial information and analysis about the proposal, its implementation and its potential negative impact on the local economy.

The City's work on this policy proposal is incomplete. Given the stakes, it is critical that City leaders move quickly to meet the moment with additional public-facing details about implementation and analysis of possible consequences, both positive and negative. The homelessness policy space into which the BCH proposal falls is wide-ranging and involves all levels of government locally and nationally and a potential international component should Chicago fail to care for the tens of thousands of migrants bused here from Texas and other border states. The City's long-term homelessness challenge preceded the current migrant crisis. However, and as noted by proponents of BCH, Chicago may be at the precipice of their convergence, consolidation and exponential expansion.

The City of Chicago has existing low-income housing programs and services dedicated to unhoused people, as well as other proposals for generating additional funds for housing, such as the economic development and housing bond proposal. However, how BCH fits into this wider policy picture has not been sufficiently explained, nor does the proposal outline specific strategies it would implement separate and apart from the BCH proposal and how they are tied to broader housing and social services goals. Without well-articulated goals and metrics and a full accounting of alternative or related measures that would mitigate Chicago's existing housing challenges, it will be impossible for the residents of Chicago to hold the City accountable for whether funds generated by the new tax have actually helped to improve the lives of people who are experiencing or at risk of homelessness.

The graduated real estate transfer tax has some advantages, but it is a volatile, economically sensitive revenue source. The chosen tax structure would shift much of the burden of the tax from residential to commercial property transactions, narrowing its impact to a portion of one sector of the economy. There has been insufficient attention by the City to the condition of the real estate market onto which the new tax would fall. Commercial real estate sales in the Chicago area were down 44% in 2023 from the prior year. The downtown Chicago office market saw vanishingly few sales and the buildings that did sell were at significant declines in sale price of as much as 63% from a decade ago.[1] With so much uncertainty in the downtown real estate market, assessing the potential consequences of a new tax on a key economic sector should have been part of the policy evaluation process by the City, not only for its possible effect on the larger economy but on its potential adverse impact on achieving the broad stated objectives of the BCH proposal itself. As it is, the Civic Federation has stepped in with data and analysis that in significant part provides some estimates of potential impact.[2]

The Civic Federation's critiques and concerns include:

- Plans for use of the funds have not been publicly articulated beyond a presentation from the City of broad strategies to address homelessness and affordable housing;
- The reasons for the marginal rate structure of the tax have not been sufficiently explained, separate and apart from the still open legal question of its legality as a referendum question on which the Civic Federation takes no position;
- The proposal lacks sufficient oversight and accountability measures to ensure that funds will be effectively and efficiently utilized for the intended purpose;
- Because the proposed tax structure would significantly shift the transfer tax burden to a single sector—from residential to commercial property transactions—it has the potential to have precipitously negative impacts on an already struggling commercial real estate market that includes already depressed downtown properties as well as multi-family housing across a broad portion of the city;
- The volatility of the tax, which arises from both the potential diminution of property values and avoidance strategies seen in other cities, means that it could fall short of the Bring Chicago Home funding goals, which would prevent the City from achieving the stated goals; and
- The measure does not address or reduce significant existing barriers to creating affordable housing through both alternative and companion measures available without tax consequences, such as reforming aldermanic prerogative or changing the zoning code.

The following sections present the Civic Federation's critiques, concerns and accompanying recommendations to address those concerns, organized by the following topic areas:

- Planning and articulation of goals of the Bring Chicago Home proposal;
- Financial stewardship, capacity and accountability;
- Barriers to affordable housing;
- Potential impact of the tax on the real estate market and the economy; and
- Acceptability of the tax structure.

The Civic Federation developed this position based on empirical research; communications with representatives from the City of Chicago about the financial, operational and implementation

[1] Rachel Herzog, "Chicago-area commercial property sales down 44% in 2023," *Crain's Chicago Business,* January 25, 2024.

[2] See the Civic Federation, "Graduated Real Estate Transfer Tax and Bring Chicago Home Proposal: Data and Policy Analysis," March 13, 2024.

questions surrounding the proposal; and an extensive analysis of property transfer data provided by the Illinois Department of Revenue. The findings of our research and data analysis can be found in an accompanying **white paper**.

The Federation recognizes that the referendum question on the March 19 primary ballot is in flux due to ongoing litigation. If the referendum question is approved by voters and upheld by the courts, the City Council will need to pass an ordinance to implement the measure. If the referendum question is struck down, the City could put forward a revised version of the measure on the November 2024 general election ballot. Regardless of the court outcome, there is time to improve the measure and the level of transparency from the City surrounding plans for Bring Chicago Home. We offer these recommendations to improve the efficacy and transparency of the measure.

Planning and Articulation of Goals

Background:

The Bring Chicago Home draft implementing ordinance outlines broad goals of addressing homelessness and creating affordable housing, but no specific written plan has been made publicly available. The framework as defined in the draft ordinance for use of the tax funds will be guided by eligible uses and populations. City of Chicago staff have noted the importance of retaining flexibility with regard to the use of the funds rather than earmarking certain amounts of funding for specific purposes. This would allow them to direct annual spending plans toward the highest priorities once sufficient resources have been collected from the tax, which could be several years from now. If the City follows its stated intention to wait to spend funds until a sufficient amount has been collected in the dedicated fund, the earliest BCH funds would effectively become available for use is in 2026.

According to City of Chicago staff, there are several broad goals of the proposal, including increasing permanent supportive housing and transitional housing for vulnerable populations, reducing barriers to access and reducing the number of people experiencing homelessness. However, the goals have not been sufficiently articulated or defined by the City for the public and the ordinance implementing the graduated RETT could be subject to change.

Civic Federation Concerns:

- There is not enough public information at this time about how the City of Chicago will spend proceeds of the proposed graduated RETT for voters to make an informed decision.
- The goals of the program have not been clearly identified so that City policymakers and leaders can be held accountable and an evaluation of progress can be made.

Civic Federation Recommendations:

- The City of Chicago should release more detailed spending plans that would allow voters to understand specifically how the proposed tax increase would help people experiencing homelessness and at risk of homelessness.

- The City of Chicago should publicly release clearly articulated goals and metrics by which any progress toward those goals can be evaluated. Examples of more detailed descriptions of goals, programs, budget, impact and selection criteria can be found in the City's recently released materials on its proposal to issue bonds for housing and economic development.

Financial Stewardship, Capacity and Accountability

Background:

Financial Stewardship: The City of Chicago has a mixed record of effective and transparent stewardship. In some cases, such as ending the practice of scoop-and-toss debt financing, the City has been transparent and adhered to best practices. In other areas, transparency has been insufficient for residents and taxpayers to assess whether tax dollars are being used most efficiently and based on long-term financial planning. One example is Police Department expenditures and deployment of policing resources. Fiscal accountability is further hampered by the absence of any meaningful legislative oversight from the City Council historically, which has been a product of structure, authority and culture.

The City of Chicago also lacks a strong track record of effectively spending funds it already has. The City has been slow to spend millions of dollars in American Rescue Plan Act funding allocated to addressing homelessness. The Illinois Answers Project found that only 15% of the ARPA funds dedicated to homeless programs had been spent as of August 2023, and a more recent analysis released on February 12, 2024, by WTTW News pegged the percentage at 32.4%.

There is also the issue of ensuring that the additional revenue raised through the marginal, graduated RETT structure would be additive to existing programs and capacity, rather than used as a replacement of other existing sources of funds. The City should avoid the issue that occurred with the Illinois Lottery whereby Lottery funds replaced other State funds used for education, rather than increasing overall funding to education.

Capacity: Effectively addressing homelessness will require the cooperation of other levels of government with Chicago, but recent lack of coordination on the migrant crisis between the City, County and State of Illinois does not give confidence that such cooperation will be forthcoming on this critical issue.

Mayor Johnson created a Chief Homelessness Officer position via executive order in October 2023, but it is unclear how that position will interact with Bring Chicago Home or improve capacity within the Departments of Family and Support Services and Housing to address homelessness.

Representatives from the City of Chicago's Department of Housing told Civic Federation staff that the department has been enhancing administrative capacity in several ways. They noted it is building capacity by requiring affordable housing developers who work with DOH to set aside 5% of affordable housing being constructed for supportive housing, which previously was a voluntary requirement. They believe this will increase the pool of developers with supportive housing experience. Additionally, the City has been working with the White House's ALL INside initiative, which is providing technical support to the City as part of a national initiative to reduce homelessness by 25% by 2025.

Accountability: Oversight of Bring Chicago Home spending would be through a 23-member Advisory Board established under the draft Bring Chicago Home implementation ordinance, to be appointed by the Mayor, with approval of the City Council. The Advisory Board would include 15 voting members composed of community members, service providers and citizens directly impacted by homelessness. The Board would also include three non-voting ex officio members and five designated non-voting members. The Advisory Board's powers and duties would include holding public meetings, conducting community outreach, making spending recommendations, establishing goals and metrics and tracking participant and program outcomes. However, the draft ordinance does not require representation from members with financial or budgetary expertise, policy implementation experience, taxpayer representatives or representatives from non-homelessness advocacy groups such as the developer, real estate or business communities.

Existing City ordinance includes a requirement for the Chicago Department of Housing and Department of Family and Support Services to produce an annual report on homelessness and housing. The draft Bring Chicago Home ordinance would allow the Advisory Board to request information about outcomes associated with the Bring Chicago Home initiative to be included in the report. The draft ordinance does not, however, provide sufficient authority for the Advisory Board to obtain all relevant materials that it would need in order to report on program outcomes.

Approval of annual appropriations would be handled through the City's annual budgeting process and thus would be subject to change.

Without specific goals and metrics by which to measure progress, it would not be possible to evaluate the effectiveness of the tax itself or any spending that would come from the revenue it generates. Therefore, the accountability of City leaders in fulfilling their promises to the voters and to the homeless and those at risk of homelessness, who are supposed to be served by BCH, would be significantly hampered.

Civic Federation Concerns:

- The Civic Federation has a number of concerns about the City's capacity to spend BCH funds efficiently and effectively. Some of the concerns derive from existing issues within city government and others from an ongoing lack of information about performance measurement, including:
    - The capacity of the City to spend a potentially large influx of revenue to address homelessness effectively, given the experience with ARPA funds; and
    - How well a large advisory board whose only membership requirements are representatives of the social service provider community and housing developers and providers will be able to independently make and evaluate proposals for spending BCH funds from City staff.

- Details on the membership of an Advisory Board composed of advocates and social service providers could be expanded upon in the draft ordinance, as could information on how funds would be allocated by the board and the City's required reporting to the board.

- As currently laid out in the referendum and draft ordinance, there will not be enough accountability on the part of City leaders for whether homelessness will be affected by the tax and how it is spent.

Civic Federation Recommendations:

- If the referendum passes, the enabling ordinance should clearly specify that the additional funds would add to existing resources rather than replace other sources of funding currently used for existing service programs.

- The Civic Federation recommends a number of improvements to the draft ordinance that would strengthen the proposed advisory board:
    1. Incorporate additional skills and areas of expertise (such as financial or budgetary expertise, policy implementation experience, taxpayer representatives or representatives from non-homelessness advocacy groups such as the developer, real estate or business communities) into the composition of the Advisory Board in the draft implementing ordinance in order to represent a wider variety of perspectives.
    2. Since some Advisory Board members representing direct service providers could conceivably be called upon to vote on programs that would be delivered by their organizations, it is imperative that the implementing ordinance include stringent provisions on conflict of interest disclosure and ethics requirements.
    3. A provision should be added such that service on the advisory board is not and will not be compensated.
    4. Provide the BCH advisory board with sufficient authority to obtain all relevant materials that it would need to evaluate and report on program outcomes.
    5. Require that the City Council hold a subject matter hearing on the annual report from the Department of Family and Support Services and Department of Housing regarding progress made to address homelessness and housing.
    6. In addition to an annual report, the Civic Federation recommends the additional reporting requirements be added to the draft implementing ordinance through the submission of quarterly progress reports and/or a public dashboard to supplement the Annual Report so that the public and policymakers will have more detailed and transparent information on progress and barriers that Bring Chicago Home will encounter. Stakeholders would be able to better understand how funds are being spent and how much progress is being made toward meeting programmatic goals. Also, more frequent reporting will enable faster responses to issues that may emerge.

Barriers to Affordable Housing and Potential Impact of Spending

Background:

Nationally, groups such as the Bipartisan Policy Center, Urban Institute and the U.S. Department of Housing and Urban Development (HUD) have found that barriers to affordable housing include a lack of financing and regulatory barriers. From the financial perspective, tightening credit conditions, unfavorable tax policies and the perception of affordable housing as a high-risk investment result in a lack of affordable units. Regulatory barriers include exclusionary zoning restrictions and land use regulations, lengthy permitting and environmental review processes, building codes, fees and charges and other local policies.

Locally, research from organizations such as the Metropolitan Planning Council (MPC) and the Institute for Housing Studies at DePaul University finds that barriers specific to the Chicago area include:

- Loss of affordable rental supply, driven by an increased proportion of high-income units, a decrease of low-cost rental units in favor of single-family housing and local/political opposition;
- Rising costs for new and existing homeowners, including high mortgage rates and property tax increases; and
- The Chicago practice of Aldermanic Prerogative, which the United States Department of Housing and Urban Development recently found to be discriminatory and a mechanism to block affordable housing in wards through unfettered aldermanic veto power.

The funding provided through BCH could address some of the barriers governments face in finding funding for the population of unhoused and at-risk Chicagoans who are not eligible for federal resources, such as those temporarily staying with others. The major areas for spending outlined in the draft implementing ordinance include permanent affordable housing and services necessary to obtain affordable housing. Communications with the City's Department of Finance and Department of Housing indicate that the eligible uses for BCH encompass permanent supportive housing, preservation and rehabilitation of housing, homeless shelters, and wrap-around services. The Civic Federation is not able to evaluate these potential areas of spending compared to others.

Civic Federation Concerns:

- In order for additional spending to address homelessness to be maximally effective, it must be paired with efforts to address barriers to affordable and supportive housing in Chicago. Specifically, if exclusionary zoning and the practice of aldermanic prerogative are not addressed, it will be impossible to increase the amount of affordable or supportive housing in many areas of Chicago.

- From an economic perspective, the large population of people who are experiencing homelessness or at risk of homelessness in Chicago and a lack of housing affordability are destabilizing to the City's ability to attract and retain residents and businesses. Human suffering on such a scale—which is a growing problem nationwide—should be addressed by all levels of government following best practices and in a measurable way.

Civic Federation Recommendations:

- Review the many studies over the years of the reasons for the lack of affordable housing in Chicago and re-commit to reducing those barriers as part of the Bring Chicago Home initiative.[3]

- Reform aldermanic prerogative such that alderpersons cannot block affordable housing in their wards without regard to the demonstrated need for such units.

- Review exclusionary zoning structures currently in place in Chicago and enact comprehensive zoning reform to increase the supply of affordable housing, improve access to affordable housing and increase racial equity in housing outcomes.

Potential Impact of the Graduated Real Estate Transfer Tax on the Real Estate Market and Economy

Background:

The **neutrality principle** posits that tax systems should aim to be neutral so that economic decisions are made on their own merits, not just for tax related reasons. In other words, taxes should not unnecessarily distort economic choices made by individuals or businesses and incentivize tax avoidance activities. The RETT proposal is likely to incentivize tax avoidance and change economic choices, thereby increasing the likelihood of a disruptive impact on the Chicago economy and tax base. The new marginal tax structure, if upheld by the court and approved by voters, would shift more of the transfer tax burden to commercial property transactions and reduce the burden on residential property transfers. Therefore, it could also have a negative impact on business locational decisions, reducing the economic attractiveness of Chicago to business and thereby lead to a potential loss in tax revenue and economic activity.

Because the incidence of the City portion of the real estate transfer tax is on the buyer rather than the seller, increasing Chicago RETT taxes above those imposed by other nearby jurisdictions could create an incentive for businesses to locate outside of Chicago. Early results from the increased real estate transfer tax in Los Angeles implemented in April 2023 showed an immediate negative impact on high end property sales in Los Angeles and much less in revenue compared to projections.

[3] Mayor Brandon Johnson issued an Executive Order on December 11, 2023 that gave 14 departments within the City of Chicago a 90-day timeline to identify ways to streamline the regulatory process for real estate developments.

Civic Federation Position:

- There has not been a sufficient study of how the tax could affect the real estate market in Chicago, particularly the downtown commercial market, which is experiencing an ongoing downturn.

- The Civic Federation's research and estimates provide a more expansive view of who would pay the tax, but they do not take the place of Bring Chicago Home's proponents providing an explanation of the tax structure they chose given its potential impact on the still sluggish commercial real estate market in downtown Chicago.

Civic Federation Recommendation:

- The City of Chicago and supporters of BCH should revisit their proposal and make evidence-based changes to its structure that will not overburden a struggling sector of the economy.

Acceptability of the Tax

Background:

When considering whether the graduated real estate transfer tax is an acceptable way to fund homelessness services, there are arguments to be made both for and against this particular tax source. Homelessness programs could be funded from municipal general funds, property taxes or other taxes, although voters in some other jurisdictions including Los Angeles and Santa Fe have approved using real estate transfer taxes to fund homelessness programs specifically.

On its face, the proposed RETT structure aligns well with the **ability-to-pay principle** as it is a graduated, marginal rate tax that has the greatest impact on high value properties. However, there has been insufficient explanation for how and why the proposed structure with marginal cutoffs of properties valued under $1 million, between $1-1.5 million, and over $1.5 million was chosen. The vast majority of funds from the new RETT tax structure will come from the top bracket of properties valued over $1.5 million. The number of properties that fall within the middle bracket, properties valued between $1 million and $1.5 million, is a very small portion of total property transactions historically. Alternative structures could include a broader base, taxing property sales at a higher rate with a lower dollar threshold, or higher thresholds with lower rates.

It is less clear that the RETT structure proposal aligns with the **benefits principle**, which is that there should be a clear link between a tax and the benefits it funds, such as a gasoline tax funding road construction and repair. While in theory there is a link between the real estate transfer tax and benefits provided through housing and related services, it can be argued that all Chicagoans benefit from reducing homelessness because homelessness is destabilizing to the City's ability to attract residents and businesses. Such a clear connection has not been established by proponents of the graduated tax structure and they have not convincingly argued why the commercial real estate market should bear the brunt of paying for services to address homelessness rather than a tax that would apply more equally across economic sectors.

The real estate transfer tax is also economically sensitive. Proceeds fluctuate depending on market conditions. When property sales are robust, revenues increase. The reverse is true when property sales and/or values decline due to negative economic conditions such as the COVID-19 pandemic in 2020, when commercial transactions dropped and proceeds deposited into the City's general operating fund fell to $130.3 million from 2019's proceeds of $152.4 million. Likewise, the portion of the real estate transfer tax that provided increased funding for the Chicago Transit Authority beginning in 2008 fell well short of expectations for several years after its implementation due to the real estate market crash and slow recovery. It has since exceeded budget expectations in some recent years, but the amount of revenue generated over time has varied. For example, 2023 proceeds of $55.7 million were far below budget projections of $93 million for that year.

Civic Federation Position:

- The Civic Federation has concerns about the volatility of the proposed graduated real estate transfer tax. While City staff have explained that they will wait until a sufficient amount of revenue has been collected before disbursing the proceeds of the tax to any programs or services, in reality there will be intense pressure to spend whatever is generated. Additionally, while there are provisions in the draft ordinance that would hold the Corporate Fund harmless, those provisions could be overset by alderpersons during the budgeting process, which could create a shortfall in the City budget.

- There has not been enough information provided by the City or supporters as to why they chose the proposed tax structure and its marginal cutoffs. This resulted in a lawsuit being filed by business and real estate organizations, which led to uncertainty about the legal standing of the referendum.

Civic Federation Recommendations:

- The City of Chicago and supporters of Bring Chicago Home should explain their choice of this funding source over any other tax and why they chose the structure outlined in the referendum over other potential structures. Additionally, potential shortfalls of any proposed tax should be overtly addressed in plans for budgeting the proceeds of the tax, not as an afterthought.

- Any future changes to the proposed rates and marginal cutoffs, possibly for the election in the fall, must be accompanied by an explanation of why they are legal, why they were chosen and why they would be effective.