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City Council Testimony on The Economics of the Historic Residential
Preservation Through the Property Tax Exemption
Presented by John H. Robinson of 2727 Manoa Road, Honolulu, HI
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Good morning, and thank you for the opportunity to speak before the Council again. This week my purpose is to clear up what I believe are some misconceptions regarding the economics of historic home preservation and to provide the Council with incentive based solutions that I hope will benefit all constituencies.

First, in terms of quantifying the issue from a budget perspective, according to state officials, there are currently 255 homes on the state historic homes registry. I have heard estimates of lost revenue from the real property tax exemption ranging from \$12 million to as high as \$100 million. In truth, the cost of the exemption is probably much, much smaller. Assuming an average property tax bill of \$10,000 for these homes – which I submit is a high estimate – the total cost of the exemption, assuming zero economic benefit realized by the community from the exemption – would be just \$2.5 million – an infinitesimal sum in relation to a municipal budget of over \$1 billion.

From an economics perspective, one of the trickier aspects of the current ordinance is that while the cost is relatively easily quantifiable, the economic benefit the community receives in return is abstract and difficult to quantify. On this score, the value of historic preservation is no different than music and the arts. While it is difficult to quantify the value the community receives from its financial support of, for example, the state art museum, I think we all agree that the arts are an important aspect of our culture that warrants our financial support. The same applies to preserving our architectural heritage. Unfortunately, one of the best ways to indirectly measure the value of historic preservation is to look back on what has been lost. I am sure Historic Hawaii can show you many photos of wonderful old neighborhoods and gorgeous old houses that have been lost to development. As a single simple example, I offer this photo of the Spreckles Mansion that stood on Isenberg Street in Moiliili. Looking at the 1960s low rises that stand there now, I ask you whether our community suffered a loss when this building and scores of others like it were demolished for development?

This leads into another misconception I would like to dispel, which is that the purpose of the property tax exemption is to assist the owners of historic homes in offsetting the higher costs of maintaining their homes. Contrary to this view, the real property tax exemption has absolutely nothing to do with providing property maintenance incentives, but rather to create a disincentive for property buyers and owners to demolish old homes in favor of modern development. Used in this manner, there is a abundant empirical research to support its effectiveness. Ironically, from a behavioral economics perspective, it can be argued that the proposal being considered to replace the property tax exemption with a maintenance reimbursement tax credit would actually create an incentive to develop rather than preserve.

In my opinion, the single, blunt-edge solutions for improving the current historic preservation ordinance that have been proposed to date represent flawed public policy, and that more effective policy solutions that appease all constituencies can be found by taking a mulit-faced approach. I have attached an outline of potential solutions with this testimony.

In closing, to borrow a line from the best selling book **Freakonomics**, *“Incentives are the cornerstone of modern life. And understanding them – or, often, ferreting them out – is the key to solving just about any riddle, from violent crime to sports cheating to online dating.”* I would argue that they are the key to implementing a productive policy for preserving our architectural heritage as well.



THE SPRECKELS MANSION.

A CHINESE pagoda accommodated to Hawaiian conditions would not be an inapt description of this house. It was planned to catch and sift through the rooms the breeze from whatever quarter it might come, and intolerant of shade-trees like its owner was of industrial rivals, its cupola overlooks a goodly expanse of territory. The "sugar king" might have built a more august dwelling, but it is scarcely probable that it would have seemed as grandiose as this modernized three-story pagoda with its cool verandas, tall windows, and beautiful grounds, in which no large trees near detract from its architectural

**PUBLIC TESTIMONY RELATING TO THE REAL PROPERTY TAX
EXEMPTION FOR HISTORIC RESIDENTIAL REAL PROPERTY**

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Introduction:

This submission to the Honolulu City Council proposes an alternative solution to the well-publicized issues surrounding the current property tax credit granted to owners of residential properties listed on the Hawaii Register of Historic Places. Although this new proposal incorporates some elements presented in 2010 Bill #s 55 and 57 and 2011 Bill #s 2, 3, and 4, its distinguishing feature is that it rejects blunt-edge single solutions in favor of a multi-faceted approach that better serves the interests of all constituencies. Specifically, the solution proposed herein (1) addresses the current budget crisis and the City and County's need for increased property tax revenue, (2) acknowledges the failings of Section 8-10.22 in its current form by proposing more stringent qualification criteria, stricter enforcement, and greater punitive measures for lack of compliance, and (3) creates and improves economic incentives to preserve Oahu's cultural and architectural heritage.

Summary

- Section 8-10.22, Revised Ordinances of Honolulu 1990 provides an exemption from real property taxes to residential property owners whose homes are listed on the Hawaii Register of Historic Places ("Chapter 6E"). This register was established by the State legislature in 1976 in recognition of the value of conserving and preserving the states historic cultural and architectural heritage for future generations.
- Recent media exposes have highlighted a lack of enforcement of the Ordinance's requirements that allow property owners to receive the property tax exemption and have also suggested that the Ordinance, in its current form, offers little public benefit while unfairly exempting often affluent homeowners from paying their fair share for municipal services.
- The City's current fiscal budget crisis combined with the public outcry over perceived unfairness of the Ordinance understandably makes the property tax exemption under Section 8-10.22 a target for repeal or revision.
- Since abuses of Section 8-10.22 were highlighted in the media in mid-2010, five City Council "Bills for an Ordinance" have been introduced proposing to repeal and/or replace the current Ordinance. These bills, all of which are still active, are 2010 Bill #s 55 and 57 and 2011 Bills 2, 3, and 4.
- From the 1880s through the 1930s, Oahu had a rich and diverse period of development that included classic examples of Victorian, Arts & Crafts, Colonial Revival and Tudor style residential architecture. Today, the legacy of this development is preserved largely in photographs, because startlingly few examples of these homes have survived to the modern era.
- The amount of property tax revenue lost to the elimination of the property tax exemption for historic homes is easily quantifiable, and is a tempting target for cash-strapped city government. However, careful consideration should also be

made of the less tangible, but very real, economic cost of permanently losing Hawaii's historic homes to development. It should also be recognized that certain aspects of the State's cultural and architectural history are priceless and irreplaceable, and thus need to be protected.

Proposed Amendments to the Tax Incentive for Historic Residential Real Property Tax Exemption Provided Under Section 8-10.22, Revised Ordinances of Honolulu 1990.

- (1) Repeal the existing historic residential property tax exemption for one year with the option to extend the repeal annually, at the City Council's discretion, for up to an absolute maximum of 5 years.**

Discussion: The budget shortfall outlined by Mayor Carlisle is dire and the need for increased property tax revenue undeniable. Although the elimination of tax incentives for programs intended to preserve the State's cultural heritage may be viewed by many as ill-conceived, short sighted public policy, it can also be argued that desperate times call for desperate measures. While it is acknowledged that this measure effectively eliminates any immediate incentive for homeowners to forgo altering or destroying historic structures, the temporary nature of the repeal should ameliorate some of this concern.

- (2) Upon the reinstatement of the property tax exemption, the tax exemption shall equal 50% of the property owner's real property tax bill if the property were not on the historic homes registry.**

Discussion: This measure would likely go a long way toward appeasing citizens who claim that a near 100% exemption unfairly allows property owners to avoid paying their share for municipal services. At the same time, while it reduces the current tax exemption, the measure would continue to offer owners of historic homes a significant economic incentive to preserve their homes.

- (3) Provide a \$1:\$2 property tax credit to owners of historic homes for qualifying maintenance costs and improvement expenditures during the period in which the property tax exemption is repealed. The tax credit would be allowed for up to 50% of the historic homeowner's property tax bill. Upon the reinstatement of the property tax, owners of historic homes would have the option each year of claiming the standard 50% property tax exemption or, alternatively, of claiming up to a 75% credit for \$1:\$2 improvements.**

Discussion: This measure contains real economic incentives to preserve and improve historic homes and, because it requires the property owners to invest their own money in order to receive additional tax benefits, it should appease many critics of the current ordinance.

- (4) Provide more stringent registration qualifications and improved enforcement over what is currently provided in Ordinance 8-10.22. Specifically, the regulation may wish to (1) expand the current definition of visual access to a “reasonable man” standard, (2) contain provisions that the require the historic home owners to maintain the property, (3) require the property owner to seek special approval for any renovations or additions to the home that might, by a reasonable man standard, be deemed to diminish the architectural heritage or integrity of the property**

Discussion: These suggestions are an acknowledgement that the current qualifications for registration are extremely liberal and require little responsibility of the homeowner. In exchange for the homeowner receiving the economic benefit of the tax exemption, this proposal is aimed at increasing the responsibilities of the home owner. The three ideas introduced above are merely intended as starting points.

- (5) Provide for more severe punitive measures for those homeowners who abuse the spirit and/or letter of the Ordinance. Measures may include revocation of historic home property tax exemption, repayment of past taxes, and separate fines and penalties. Because the City does not have funds available to hire an enforcement officer, it makes sense to have the public fill this role. To this end, the City may wish to require each homeowner to display a clear sign noting his property’s status as an historic home and providing a phone number for the public to call if there is reason to believe that the property does not meet the criteria outlined in the ordinance. Failure to display the sign in clear public view would result in additional fines.**

Discussion: This proposal addresses the current problem of lax enforcement by turning the task of monitoring over to the public.

