

FISCAL AUDIT

**DEPARTMENT OF FINANCE, REAL ESTATE DIVISION**

**Tax Abatements Programs-Act 42 and Local Economic Stimulus Tax Assistance (LERTA)**

Office of City Controller

**MICHAEL E. LAMB  
CITY CONTROLLER**

Douglas W. Anderson, Deputy Controller

November 1, 2017

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November 1, 2017

To the Honorables: Mayor William Peduto and  
Members of Pittsburgh City Council:

As authorized by the recent City Council legislation, The Office of the City Controller is pleased to present this review of the *City's Tax Abatement Programs* conducted pursuant to the Controller's powers under Section 404(b) of the Pittsburgh Home Rule Charter.

### EXECUTIVE SUMMARY

Under Pennsylvania Act 42 originally enacted in 1971 (and amended 1977), the City provides various Tax Abatements programs in which it forgoes tax revenues (or provide tax credits) due to increase in property assessments as a result of property development or renovations for a specified period of time in exchange for specific actions that contribute to the economic and community development in distressed neighborhoods. The City also offers 3 types of abatements under the *Local Economic Revitalization Tax (LERTA) act* enacted in 1977(amended, 1988) which authorizes taxing authorities to provide for tax exemptions for property improvements and commercial constructions in certain deteriorating areas in economically distressed communities. LERTA provides tax credits to qualifying development programs within 4 defined areas (except for Commercial LERTA) in the City.

We performed certain procedures to assess the process by which the City's tax abatement programs are administered as well as to determine the total projected incoming revenue from the expiration of these programs. The tables included in this report represent compiled projection of incoming revenue from the expiring tax abatement programs. A projected incoming annual revenue from all the expiring programs totaled **\$2,833,940** (Table II) for the years 2019 through 2026. A projected incoming cumulative revenue from the expiring programs totaled **\$9,514, 935** for the same period is also shown on the table.

Our report also includes recommendations for improving the abatement program to ensure adequate availability of adequate records, reliable estimates, and overall management improvements. These are further discussed in the report.

Sincerely,

  
Michael E. Lamb  
City Controller

## INTRODUCTION

This audit of *the City's Tax Abatement Programs* was conducted pursuant to the Controller's powers under Section 404(b) of the Pittsburgh Home Rule Charter.

## SCOPE AND METHODOLOGY

This audit was conducted pursuant to Article IV, Section 404 (b) of the City of Pittsburgh Home Rule Charter. Our procedures included a review of the data provided for the period 2007 to 2026.

The objective of our audit was to gain an understanding of the various abatement programs offered by the City as well as to provide a projection of incoming revenues resulting from their expiration.

We compiled data provided to us by the City's Finance Department, under the 2 programs starting from 2007 through 2018. We also compiled potential revenue (for 2019 through 2026) that the City will be receiving due expiring tax abatements. We also performed limited testing to vouch for the reliability of the data and evaluate internal controls related to the data.

Our procedures consisted primarily of inquiries and the examination of documents supporting data that was provided to us. These procedures were neither designed nor intended to be a detailed audit of the Department of Finance, Real Estate Division. Accordingly, the information presented in this report only pertains to the data that was made available to us and the related records examined. Specifically we:

- Interviewed City personnel involved with the abatement programs to gain an understanding of the programs and any related internal controls.
- Examined and analyzed data made available to us showing the potential income to be received from the expiration of these programs.
- Reviewed general procedures related to the administration of the abatement program
- Performed analytical reviews of the abatement records.

## Background

### **Introduction**

The City of Pittsburgh offers several tax abatements as incentives to promote economic and community development and growth. These special tax provisions are made available in accordance with the various state legislature and City ordinances and are for a limited time to encourage improvements and developments in deteriorating properties or areas around the City. These programs are administered by the Department of Finance, Real Estate Division (Finance) in conjunction with the Urban Redevelopment Authority (URA). In addition, the applications for two of the programs are reviewed by Allegheny County. The URA reviews and approves applications for the Residential and Enhanced LERTA. The County is also involved by reviewing applications for the Commercial LERTA and the Visibility Residential program.

Under Act 42 originally enacted in 1971 (and amended 1977), the City provides various tax abatement programs in which it forgoes tax revenues (or provide credit) due to increase property assessments as a result of property development or renovations for a specified period of time in exchange for specific actions that contribute to the economic and community development in distressed neighborhoods. Under this act, the City abates taxes due to increase in property assessments as a result of property development or renovations and is awarded as set dollar amounts that are received as tax credits or reduction of the assessed property value. Applications under this act are reviewed by the Finance Department's Real Estate Division and processed on the Real Estate's system. Approved applications are marked pending on the system until there is an increase in assessment value after construction is completed and the property is assessed by the County. An updated file with the new assessments is sent to the City's Department of Innovation and Performance to be uploaded into the system. Abatement amounts are calculated on the increased assessment value multiplied by the current millage rate.

**Types - Two types:**

- ***Act 42 Residential*** - Available for 3 years as an assessment reduction (based on millage rate) for renovations or new constructions on residential or vacant land to be used for residential, for sale or rental. Applications were previously reviewed by the County but are now reviewed by the City. The total amounts reduced are limited to \$86,750 on new constructions and \$36,009 for renovations. The application must be filed within 180 days of the issuance of the building permit.
- ***Act 42 Enhanced Residential*** – Same as above program except for the assessment reduction is available for 10 years and up to \$250,000 and is available for property located in 28 specified areas.

The City also offers 3 types of abatements under the ***Local Economic Revitalization Tax (LERTA) act*** enacted in 1977(amended, 1988) which authorizes taxing authorities to provide for tax exemptions for property improvements and commercial constructions in certain deteriorating

areas that are in economically distressed communities. LERTA provides tax credits to qualifying development programs within 4 defined areas (except for Commercial LERTA) in the City and, applications are reviewed by the URA.

Three types:

- **Residential LERTA** – Available for a period of 10 years with the credit limited to \$150,000 for new construction or renovations. Typically, the current use of property is commercial or industrial and the future use of property is for residential rental or hotels.
- **Residential Enhanced LERTA** – Similar to above except for the annual limit of \$2,700 for new construction or renovations. Typically, the current use of property is commercial or industrial and the future use of property is for residential, separately assessed units.
- **Commercial LERTA** – Available for 5 years with annual (tax) abatement limits at \$50,000 for new construction or renovations. This is available for property city-wide.

In addition, the City offers other programs:

- **The Local Economic Stimulus** - A tax credit available for 10 years that is applied to the incremental increase in taxes as a result of construction or improvements costs in excess of one million dollars. The annual (tax) abatement is limited to \$250,000 for new construction or renovations. Typically, the current use of property is commercial, industrial or vacant land and the future use of property is for residential, commercial or industrial. This credit is offered for property city wide and applications are reviewed by the City.
- **Visibility Residential** - Tax credit available for 5 years which can be used concurrently with other residential tax abatement programs. The annual (tax) abatement limited to \$2,500 for new construction or Renovations. Typically, the current use of property is residential, vacant land, commercial or industrial and the future use of property is for residential, single family, duplex, triplex, adaptive reuse. This is offered for property city wide and applications are reviewed by Allegheny County. Data provided indicated only \$500 fund available from expiration of the credit under this category.

**Result**

Below is the result of our procedures:

***Historical Analysis:***

A total of \$14,296,640 in revenue was collected from expired tax abatement programs from 2007 through 2018:

<b><i>Table I - Estimated Available Funds Due to Expired<sup>1</sup> (Act 42 and LERTA) Programs For January 1, 2007, to December 31, 2018<sup>2</sup></i></b>			
<b><u>Year</u></b>	<b><u>Amount</u></b>	<b><u>Year</u></b>	<b><u>Amount</u></b>
2007	\$ 248,643	2013	\$ 1,424,160
2008	555,090	2014	1,689,527
2009	964,625	2015	2,345,681
2010	1,267,291	2016	2,649,600
2011	1,374,683	2017	111,451
2012	1,478,693	2018	187,196
<b><i>Subtotal</i></b>	<b><i>\$ 5,889,025</i></b>	<b><i>Subtotal</i></b>	<b><i>\$ 8,407,615</i></b>
<b><i>Grand Total \$ 14,296,640</i></b>			

***Estimated Incoming Revenue from Expired Abatement Program:***

Data provided showed potential revenue from expired abatement programs for the period 2019 to 2026 totaled \$2,833,940 as detailed below:

<b><i>Table II – Estimated Available Funds Due to Expiring Programs For the period January 1, 2019 to December 31, 2026</i></b>									
<b><u>Program</u></b>	<b><u>2019</u></b>	<b><u>2020</u></b>	<b><u>2021</u></b>	<b><u>2022</u></b>	<b><u>2023</u></b>	<b><u>2024</u></b>	<b><u>2025</u></b>	<b><u>2026</u></b>	<b><u>Total</u></b>
<i>Act 42</i>	\$108,313	\$45,065	\$ 27,385	\$ 78,142	\$ 74,400	\$52,324	\$69,423	\$38,270	\$ 493,322
<i>LERTA</i>	157,745	153,251	122,329	206,037	144,550	79,013	175,086	658,213	1,696,224
<i>Visibility</i>	-	500	-	-	-	-	-	-	500
<i>Local Economic Stimulus</i>	-	-	-	-	25,667	229,140	41,089	347,998	643,894
<b><i>Total</i></b>	<b><i>\$266,058</i></b>	<b><i>\$198,816</i></b>	<b><i>\$149,714</i></b>	<b><i>\$284,179</i></b>	<b><i>\$244,617</i></b>	<b><i>\$360,477</i></b>	<b><i>\$285,598</i></b>	<b><i>\$1,044,481</i></b>	<b><i>\$2,833,940</i></b>

<sup>1</sup> Per data provided by the Department of Finance, Real Estate Division

<sup>2</sup> Expired abatements for this year assumed to be reflected in the 2018 Budget

Table III shows a breakdown for the totals included for Act 42 and the LERTA programs listed in Table II:

<i>Table III - Detailed Estimate of Available Funds Due to Expiration of Act 42 &amp; LERTA</i>									
<i>For the period January 1, 2019 to December 31, 2026</i>									
<b>Program</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>	<b>2022</b>	<b>2023</b>	<b>2024</b>	<b>2025</b>	<b>2026</b>	<b>Total</b>
<b>Act 42:</b>									
Enhanced Residential	\$ 80,679	\$ 45,065	\$ 27,385	\$ 78,142	\$ 74,400	\$ 52,324	\$ 69,423	\$ 38,270	\$ 465,688
Residential	27,634	-	-	-	-	-	-	-	27,634
<b>Subtotal</b>	<b>\$108,313</b>	<b>\$ 45,065</b>	<b>\$ 27,385</b>	<b>\$ 78,142</b>	<b>\$ 74,400</b>	<b>\$ 52,324</b>	<b>\$ 69,423</b>	<b>\$ 38,270</b>	<b>\$ 493,322</b>
<b>LERTA:</b>									
Commercial	\$ 93,165	\$ 53,952	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 147,117
Residential	3,450	75,572	1,032	167,223	98,965	68,618	160,151	587,514	\$1,162,525
Residential Enhanced	61,130	23,727	121,297	38,814	45,585	10,395	14,935	70,699	386,582
<b>Subtotal</b>	<b>\$157,745</b>	<b>\$153,251</b>	<b>\$122,329</b>	<b>\$206,037</b>	<b>\$144,550</b>	<b>\$ 79,013</b>	<b>\$175,086</b>	<b>\$658,213</b>	<b>\$1,696,224</b>
<b>Grand Total</b>	<b><u>\$266,058</u></b>	<b><u>\$198,316</u></b>	<b><u>\$149,714</u></b>	<b><u>\$284,179</u></b>	<b><u>\$218,950</u></b>	<b><u>\$131,337</u></b>	<b><u>\$244,509</u></b>	<b><u>\$696,483</u></b>	<b><u>\$2,189,546</u></b>
<b>Cumulative Effect</b>	<b><u>\$266,058</u></b>	<b><u>\$464,874</u></b>	<b><u>\$614,588</u></b>	<b><u>\$898,767</u></b>	<b><u>\$1,143,384</u></b>	<b><u>\$1,503,862</u></b>	<b><u>\$1,789,460</u></b>	<b><u>\$2,833,940</u></b>	<b><u>\$9,514,935</u></b>

### Observations

#### **#1: Historical Data**

Data provided for the period 2007 to 2016 for the Tax Abatement programs were not separated into those that were currently active and those that expired. These amounts were also not separated under the 7 programs that the City offers. Therefore we were unable to determine how much from those totals were actually from expired abatements or how much was for each program. Per our discussions with the Real Estate Division personnel, the data breakdown is unavailable. The current real estate system utilized for these programs does not allow for the retention of such historical information on the system. The department is currently working on a new real estate system.

## **#2: Reliability of Estimates and Projected Revenue from expired programs**

Due to the lack of access to the appropriate data, we were unable to perform audit testing necessary to enable us to vouch for the data provided to us or perform other necessary audit testing required in an audit. We attempted to test the abatement process and the validity of the abated amounts by selecting a sample of parcels from the data that was provided. Providing us with the supporting records for these parcels proved difficult. Records such as applications, abatement schedules as well as the calculations of the abatement amount were not readily available to allow for a timely completion of our audit. In order to vouch for the reliability of this type of data, Finance needs to maintain the appropriate records that will enable recalculation as well as vouching.

## **#3: Improved Role in managing the Programs**

The abatement amounts for all applications are calculated by the Real Estate Division including those that are approved by the URA (Residential LERTA, Residential Enhanced LERTA) and the County (Commercial LERTA, Visibility Residential). Applications from these entities are forwarded to the City once approved. The Real Estate division is responsible for the calculations and updating of the tax bill to reflect the reduced tax due on the real estate system. An abatement schedule<sup>3</sup> is included in the application packet which details the calculation of the abatements amounts. As previously indicated, these applications (including the necessary abatement schedule) were not readily available. Also, the calculation process itself is not well documented for each abated amounts. It is our understanding that the current real estate system does not automatically calculate the abatement amount throughout the term of the abatement period. The Real Estate Division (with limited personnel) is responsible for the yearly calculations for each property which involves physically pulling abatement schedules from each file in order to complete the abatement amount for that year. This information is then entered into the real estate system to reflect the year's taxes due.

## **#4: Tracking and Updating expired Programs**

There is no formal procedure for when abatements are approved or expire. Approved applications (before the abatement start) are shown as pending until Finance is alerted that there is an increase in the assessment value. The application for an occupancy permit by the owner will trigger an assessment by the County Assessors who then enters the new value into the County real estate system that gets uploaded into the City's real estate system. A report is generated by the Real Estate division personnel that show properties with an increase in assessment. This report serves as an alert that abatement period should start in the following year. The abatement or assessment reduction amount is then calculated and entered into the system to update the real estate tax due. No information is sent to the owner to communicate approval and/or amount of the abatement. This process creates the risk that abatement may expire but not reflected as a result of which the City may not be collecting the tax due.

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<sup>3</sup> This schedule does not include pre- and post-construction assessments to allow for recalculations of the increase in assessment values

## Recommendations

**#1: Historical Data** - We recommend that the Finance Department include in its consideration of the new system that data captured by the system are readily available and that necessary steps are in place to ensure data on these programs is retained to provide adequate paper/audit trail as well as allow for audit testing to validate the amounts reported. This is especially important not only for the newly implemented/pronounced Council legislation requiring audits performed but also to provide adequate support for numbers reported on the City's annual financial report (CAFR) as a result of the requirements from the newly implemented GASB 77.

**#2: Reliability of Estimates and Projected Revenue from expired programs**- Adequate support for the abatement programs should be maintained. Records such as applications, abatement schedules as well as the calculations of the abatement amount should be retained and be readily available to allow for a proper audit of the programs.

**#3: Improved Role in managing the Programs** – Finance should consider implementing procedures to enhance the abatement process. Specifically, Finance should consider:

- Improving process to ensure availability of the Abatement Schedule
- Consider electronic application process (or scanning the current ones) to ensure permanent records are easily available
- Explore the possibility of automating the process for the calculation of the abatement amounts and uploading into the system
- Retention of the assessment increases to support calculation of abatement amounts

**#4: Tracking and Updating expired Programs** - Consider a formal notification of the approval, start and end dates as well as the abatement amount to the applicants. It will be helpful to also have the have an option on the real estate system that shows an end date for the abatement program.

