



<b>Subject:</b> Refinement of Home Demolition Tax Ordinance Proposal	
<b>Meeting Date:</b> September 17, 2019	<b>Staff Member:</b> Scot Siegel, Planning and Building Services Director  <b>Department:</b> Planning and Building Services
<b>Action Required</b> <input type="checkbox"/> Motion <input type="checkbox"/> Public Hearing <input type="checkbox"/> Ordinance <input type="checkbox"/> Resolution  <input type="checkbox"/> Information Only <input checked="" type="checkbox"/> Council Direction <input type="checkbox"/> Consent Agenda	<b>Advisory Board/Commission Recommendation</b> <input type="checkbox"/> Approval <input type="checkbox"/> Denial <input type="checkbox"/> None Forwarded <input checked="" type="checkbox"/> Sustainability Advisory Board and Historic Resources Advisory Board  <b>Comments:</b> None
<b>Staff Recommendation:</b> Provide direction for drafting a Home Demolition Tax ordinance.	
<b>Recommended Language for Motion:</b> NA	
<b>Project / Issue Relates To:</b>	
<input checked="" type="checkbox"/> Council Goals/Priorities <input type="checkbox"/> Adopted Master Plan(s) <input type="checkbox"/> Not Applicable	

### ISSUE BEFORE COUNCIL

Should the City adopt a home demolition tax to discourage demolition of single-family homes and raise funding for parks maintenance?

### EXECUTIVE SUMMARY

Staff is requesting direction on whether to proceed in drafting a demolition tax ordinance for possible City Council adoption this year. Members of the City Council and advisory boards have expressed interest in creating an incentive for preserving older, less expensive homes as opposed to demolition and replacement with larger, more expensive homes. If set high enough,

a demolition tax might discourage tear-downs in favor of remodels and additions to existing homes. The Council has also considered the tax as a means of raising revenue for parks maintenance.

## **BACKGROUND**

The City has recently adopted measures that encourage the retention of existing housing by reducing the time and cost for developing accessory dwelling units. These include streamlining the permitting process for Accessory Dwelling Units (ADUs) (Ordinance 2784), and exempting ADUs from paying system development charges (Ordinance 2810).

On April 16, 2019, the City Council discussed the concept of a Home Demolition Tax as a means of encouraging retention of existing housing stock and to raise revenue for parks maintenance. The key issues at that time related to the demolition tax rate, exceptions to the tax where home remodels are impractical, and preferred use of tax revenues (parks maintenance).

At a study session on March 6, 2018, the Council considered the concept of a Construction Excise Tax (CET)<sup>1</sup> and other strategies to encourage the production of affordable housing. That led to code changes supporting development of accessory dwelling units and the adoption of financial incentives, including waiver of SDCs and development review fees, for affordable housing. The Council was not interested in pursuing a CET at that time.

## **DISCUSSION**

The Comprehensive Plan contains the following Recommended Action Measure:

“Encourage the remodeling, restoration, and reuse of existing housing as an alternative to tearing down functional buildings.” (Complete Neighborhoods & Housing, RAM ‘B’)

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<sup>1</sup> ORS 320.192 and 320.195 place limitations on city-imposed construction taxes. Construction taxes for residential property are limited to new residential structures or additional square footage for existing structures, including remodeling that adds living space. The tax rate for residential construction cannot exceed one percent of the permit valuation.

Construction taxes can be imposed on improvements to commercial and industrial property (including commercial and industrial portions of mixed-use property) that result in a new structure or additional square footage in an existing structure. There doesn’t appear to be a rate limitation for the non-residential taxes.

ORS 320.195 limits the use of construction tax revenues. For residential construction tax revenues, after deducting up to four percent or administrative expenses, 50% must be used for “developer incentives” under ORS 197.309 (5)(c) and (d) and (7) [statute on affordable housing requirements and incentives]; Fifteen percent must go to the Housing and Community Services Department for down payment assistance programs; and thirty-five percent must be used for city programs and incentives related to affordable housing.

For commercial and industrial construction tax revenues, after the administrative expenses, 50% must go to fund city programs “related to housing.”

Currently, when new homes replace existing (demolished) homes, the City does not impose systems development charges (SDCs) because it is assumed the replacement home does not put a new, additional, burden on infrastructure. State law requires that SDCs be used only for land or capital improvements that increase system capacity. However, the City has the authority to impose a tax on demolitions or new construction, which could be used for infrastructure maintenance and other projects that cannot be funded with SDCs.

The Council has discussed establishing a demolition tax of up to \$25,000 per home. By comparison, total SDCs for a new single family home are approximately \$37,500; the parks and transportation portions of the SDCs are approximately \$26,217. Based on a conservative estimate of 30 demolitions per year, a tax of \$25,000 per demolition would generate \$750,000 annually. The Council could set a higher or lower amount. A lower amount would have less influence in preserving existing housing stock. The Council may also want to index the tax rate so that it increases annually, as occurs with some SDCs.<sup>2</sup>

Potential impacts of the tax include increased construction costs, which would likely be passed on to sellers of land and/or buyers of new homes. If the cost is borne by sellers, it could disproportionately impact older residents whose retirement savings is in the value of their property. In addition, the tax would target neighborhoods that are redeveloping rather than the city as a whole, which could be viewed as unfair if the tax is used solely for parks maintenance. Further, unless the tax is tied to lot size, floor area, or some other objective measure, it would be regressive because the same tax would apply to all demolitions regardless new home's value. The City of Portland recently considered but abandoned a similar tax proposal in 2018.

## ALTERNATIVES

Staff requests the Council's feedback and direction on the following:

1. **Tax Rate.** The City Council previously expressed interest in setting the demolition tax rate high enough to discourage demolitions, but not any higher. The Council discussed a general range of \$10,000 and \$25,000. Alternatively, the rate could be set closer to the full cost of SDCs on a new single-family home, which is \$37,458.

The downside to this approach, other than cost, is that the demolition tax, like SDCs, is regressive. It is the same for all demolitions regardless of the cost of the new home to be constructed. At \$25,000, the tax would add 5% to the cost of constructing a \$500,000 house (excluding land and utilities), as compared to 2.5% on a \$1 million house.

2. **Demolition versus Remodel.** One option is to use the current definition of "demolition."<sup>3</sup> Another option is to tax demolitions and major remodels where floor

<sup>2</sup> Transportation system development charges are indexed annually by the Engineering News Record Construction Cost Index for 20-City Average, per Resolution 18-08.

<sup>3</sup> "Demolition" or "demolish" means: i. Removal of all exterior walls; ii. Removal of the superstructure (the part of the building or construction above the lowest subflooring; "lowest subfloor" is the bottommost structural floor

area is expanded by a certain percentage. This is not recommended however due to the difficulty of enforcement and the possible unintended effect of encouraging demolitions where a house may otherwise be remodeled. In any event, where the owner's objective is to build a substantially larger home it is often preferable to demolish the house than to leave one wall standing or to build onto an existing floor and foundation. There are also marketing advantages with "new construction" as compared to remodels. Where a structure is almost entirely removed, with only a portion retained (one wall left standing), it is typically for code-based reasons – to maintain an existing nonconformity, such as a substandard setback or lot coverage.

3. **Exceptions.** The Council previously discussed providing exceptions. This could include:
  - a. Where a house is condemned or declared unsafe by the Building Official, or where the owner can document structural deficiencies that make remodeling impractical. This may serve as a safety valve where saving an older home is not feasible or is cost-prohibitive. The burden of proof would be on the applicant.
  - b. An exception where the site is going to be redeveloped with multifamily housing or affordable housing (e.g., dwellings that are affordable to households earning 80% or less of Area Median Income). This might require the recording of a covenant on the property.
4. **Timing.** Depending on when the tax goes into effect it could unfairly impact homebuilders with current projects who purchased property before the tax was enacted. Phasing in the tax and/or delaying the effective date of the ordinance could give the market time to adjust though it could encourage a rush on demolitions.
5. **Use of Revenue.** The Council has discussed using demolition tax revenue for parks maintenance. While it is not necessary for the ordinance to specify how the tax dollars will be used, it would be good policy for Council to at least state its general intent. In addition to parks maintenance, are there other uses that Council is considering?
  - a. The Sustainability Advisory Board and Historic Resources Advisory Board have recommended a reduced tax or credit when the method of demolition is "deconstruction" and materials are salvaged for reuse or recycled. (See Attachment 1)
  - b. Given the policy objective is to discourage or mitigate the loss of smaller, more economical homes, one option is to allocate a portion of the tax revenue to a

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laid as a base for a finished floor), such that none of the existing superstructure is maintained; or iii. Alteration, abandonment or removal of all of the existing perimeter foundation. [LOC 45.12.100]

home improvement program for low income households. Grants or low-interest loans for weatherization and other energy efficiency home improvements could help to advance three Council objectives: affordable housing, sustainability, and protection of neighborhood character. Such a program could be modeled after the City's existing historic preservation/restoration grant program.

The downside to these options is that they would require additional staff resources to administer and would reduce the amount of revenue available to Parks. If the Council is interested in these concepts but first wants to ensure that the goal for Parks maintenance is met, the demolition tax could be adopted on a trial basis and other uses of the revenue could be phased in later subject to Council's review of the tax after the first year.

#### **FISCAL IMPACT**

A home demolition tax would have a positive impact on revenue. A tax rate of \$25,000 per demolished home, would generate up to \$750,000 annually, based on 30 demolitions per year. The cost of administering the program would be minimal if the ordinance relies on existing codes and permitting procedures for demolitions.

#### **RECOMMENDATION**

Provide direction to staff on whether to prepare a Home Demolition Tax ordinance based on Council input and considering the attached feedback from the Historic Resources Advisory Board and Sustainability Advisory Board (Attachment 2). Schedule a public hearing, as applicable.

#### **ATTACHMENTS**

1. Memo from Sustainability Advisory Board and Historic Resources Advisory Board

July 12, 2019

To: Lake Oswego City Council  
From: L.O. Sustainability Advisory Board (SAB) and the Lake Oswego Historic Resources Advisory Board (HRAB)  
Re: Deconstruction as an alternative to demolition for Lake Oswego home remodels or rebuilds.

SAB and HRAB are hereby requesting direction from the City Council in regard to an investigation of deconstruction as an alternative to demolition.

Currently in Lake Oswego, most homes that are remodeled or replaced are demolished rather than deconstructed. Currently the city receives an application to completely demolish a house on average every 10 days.

Deconstruction is the process of systematically dismantling a structure in an environmentally, economically, and socially responsible manner, aiming to maximize the recovery of materials for reuse and recycling. Environmentally, deconstruction reduces landfill waste, reduces air pollution, reduces carbon dioxide emissions, preserves resources, and saves energy by decreasing the extraction and processing of raw materials. For older buildings that contain lead and asbestos, deconstruction is a much safer way to clear a property. Property owners can obtain a tax deduction by donating materials for resale. Deconstruction can also provide business and local employment opportunities.

Several years ago, the L.O. Sustainability Advisory Board (SAB) investigated deconstruction as an alternative to demolition, but the discussion was put on hold, in part, because there seemed to be no clear mechanism to provide an effective incentive. However, the Climate Actions document appendix developed by the SAB, and approved by the Council, recommended further study of the benefits and costs of deconstruction.

The City Council is currently in the process of considering a fee for demolition of residential properties that are being replaced with new construction; see City Council Study Session of April 15, 2019. The total fee remains to be determined, but the Council discussion mentioned amounts ranging between about \$14,000 and \$45,000.

If the City Council approves a demolition fee, it opens the opportunity to incentivize deconstruction by offering a reduction in the demolition fee. Preliminary calculations suggest that a reduction of \$5,000 to \$10,000 would put deconstruction roughly on par with demolition, although further investigation is needed to determine the comparative costs.

The City of Portland has mandated deconstruction of homes built before 1916 (over 100 years old at the time the ordinance was passed). This has resulted in about 1/3 of the house removals since 2016 carried out by deconstruction (about 230 total). The number of contractors licensed to carry out deconstruction has increased, as well as the number of businesses that sell salvaged construction material. Portland is considering amending their mandate for deconstruction to

include newer homes that could increase the proportion of deconstructions to about 2/3. (Personal Communication, Shawn Wood, 6/3/2019, Portland, Bureau of Planning and Sustainability).

SAB and HRAB are requesting direction from the City Council in regard to further investigation of deconstruction, in particular in the context of a proposed demolition fee. If so directed, the SAB and HRAB would jointly undertake a more complete study of the costs and benefits of deconstruction and prepare a report for the Council.



Recent demolition