

# House Committee on Taxation

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## **House Bill 2135**

In 1995 federal legislation was enacted authorizing the Department of Defense to enter into legal arrangements with private sector partners as the best solution to improve and modernize on-post military family housing. Limited liability companies (LLCs) and limited partnerships, jointly owned by the service branch (the Army at Ft. Riley) and the private partner, are the most commonly used structures. This structure enables the military/private sector LLC or partnership to raise private equity and debt to fund much needed improvements to the military housing inventory and also allowed developer experts to operate and manage the housing under the terms of fifty-year ground leases. This program has been hugely successful and has resulted in dramatic improvements in the overall quality of life for military families.

While the land remains wholly owned by the United States Government (as lessor), the improvements are owned and managed by the LLC (as Lessee). The homes are required to be leased by the LLC to military families at rents equal to the soldier's Basic Allowance for Housing (BAH). Any surplus cash during the development period must go to developing the homes, and most cash flow over the life of the ground lease is expected to be used at the Army's direction to renovate and replace those homes, as needed. At the end of the fifty-year lease term, exclusive control of the improvements reverts back to the United States Government. This structure has many benefits to the Army including the level of control and participation that the Army retains through this unique private/public partnership arrangement.

The Army's housing at Fort Riley, Kansas was transferred to Riley Communities, LLC on July 1, 2006. Riley Communities, LLC (owned by the Army and Riley-Picerne Partners, LLC) entered into a fifty-year ground lease with the Army, took possession of the existing homes and raised \$283 million in private debt. That initial debt, plus net cash flow generated by the military tenants' BAH, less the expenses to operate and maintain the homes, is expected to fund a development program during the project's initial development period, of \$536 million. This \$536 million re-development and construction program will result in the construction of over 2,100 new homes, the demolition of approximately 1,400 substandard homes and over 1,300 renovations. The financial plan allows not only the construction of new and renovated homes but also addresses quality of life issues through the development of parks and other ancillary facilities. One key assumption that private lenders used in order to determine the amount of debt that the project could support was the fact that the homes had always been exempt from real property taxation and that they would remain so under privatization. The resulting lower expense level left a higher amount of net income to support the financing.

At the closing of the loan in 2006, both the lender and the Army relied on tax comfort letters provided by the Geary and Riley County Attorneys. Both attorneys cited a recent Attorney General's opinion letter (Opinion 2005-19) that had been issued on behalf of Fort Leavenworth's privatization partnership. However, in 2009, a new Attorney General issued a contradictory opinion (Opinion 2009-1) citing differences in the language of the ceding statutes of Forts Leavenworth and Riley. These statutes date back to the 1880's. Lawmakers at

that time could not have anticipated the unique nature and ownership structure of military housing projects today. Nevertheless, the conclusion was that the Fort Riley project, unlike the Fort Leavenworth project, is subject to Real Property Taxation.

HB 2135 will eliminate the uncertainty that the Army currently has with respect to the status and financial health of its housing partnership at Fort Riley, and would result in no added financial burden to the local taxing jurisdictions. Neither Riley nor Geary County has ever levied a tax on military housing on Fort Riley, and the counties perform no services for Riley Communities, LLC. However, based on the current estimate of value, taxation would result in a combined payment to both counties of approximately \$2.4 million per year. Any form of tax payment (not assumed in the original financial plan) will have a detrimental impact on both the number of homes that the project can afford to build or renovate and the quality and sustainability of the homes (and services) that Riley Communities, LLC can provide for the benefit of Fort Riley soldiers and their families in the future, and as a result, jobs that would be otherwise generated by this work will be lost.

Any form of Real Property Taxation also ignores many of the positive benefits to both the counties and the State as a result of Fort Riley's housing project. Positive economic impacts of the Fort Riley housing partnership include:

- Significant creation of high-paying jobs relative to median income and associated Payroll Tax Revenues of approximately \$2.5 million since the Project inception.
- \$536 million of construction spending amounting to an approximate \$2.5 billion impact to the local economy over a 10-year period (2006 – 2016).
- The Project supports local and small business in addition to veteran and women owned, HUB Zone and disadvantaged businesses. To date, the Project has spent \$241 million with businesses of such classifications.
- Significant Sales Tax collections from Construction and Property Management spending (estimated \$8.5 million since the project's inception in 2006).
- Mortgage recording fees paid to the counties in excess of \$700,000.
- Over 20 companies have relocated to the area which create economic stimulus in the form of increased demand for local goods, services, off-post housing and tax revenue.

Loss of the project's tax exempt status could significantly reduce the amount of impact aid for schools that the State of Kansas and Geary County receive from the Federal Government. Total payments for FY 2010 were approximately \$11.2 million based on the tax exempt status of the Fort Riley housing. This amount would have been reduced to approximately \$2.3 million if the housing was subject to property taxation.

In conclusion, both the number of homes and the quality of the homes on Fort Riley plays an important role in helping the First Infantry Division to carry out its very important mission for the Army. Insuring the financial health of housing projects on military installations throughout the State of Kansas will demonstrate to military soldiers, their families and to the Department of Defense that the State of Kansas is equally committed to its role of supporting these critical missions and for maintaining the military's continued role as an important economic engine for the State of Kansas now and in the future.

I ask for your favorable consideration of HB 2135.