COUNCIL OF THE CITY OF PHILADELPHIA

COMMITTEE ON FINANCE

Room 400, City Hall
Philadelphia, Pennsylvania
Thursday, May 23, 2013
2:25 p.m.

PRESENT:
COUNCILMAN BILL GREEN, CHAIR
COUNCILWOMAN JANNIE BLACKWELL
COUNCILMAN W. WILSON GOODE, JR.
COUNCILMAN WILLIAM K. GREENLEE
COUNCILMAN DENNIS O'BRIEN
COUNCILWOMAN BLONDELL REYNOLDS BROWN
COUNCILMAN MARK SQUILLA

BILL 130009 - An ordinance amending Chapter 19-2600 of The Philadelphia Code, entitled "Business Income and Receipts Tax," as it relates to nonprofit activity...

BILL 130123 - An ordinance amending Section 2-305 of The Philadelphia Code, entitled "Office of Property Assessment; Chief Assessment Officer; Powers and Duties," by providing for standards for tax exemptions and for documentation requirements...

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COUNCILMAN GREEN: Good afternoon. The Finance Committee is called to order for a hearing on Bills 130009 and 130123.

I note the presence of a quorum in the persons of Councilmembers O'Brien, Goode, Greenlee, and Reynolds Brown.

I would ask the Clerk to read the title of the bills.

THE CLERK: 130009, an ordinance amending Chapter 19-2600 of The Philadelphia Code, entitled "Business Income and Receipts Tax," as it relates to nonprofit activity, under certain terms and conditions; and

Bill No. 130123, an ordinance amending Section 2-305 of The Philadelphia Code, entitled "Office of Property Assessment; Chief Assessment Officer; Powers and Duties," by providing for standards for tax exemptions and for documentation requirements, all under certain terms and conditions.

COUNCILMAN GREEN: Thank you.

I'd like to ask the Director of Policy, Planning, and Outreach from the Nutter Administration to come testify. We'll take your testimony on both bills to begin with.

(Witness approached witness table.)

COUNCILMAN GREEN: Please state your name for the record and proceed with your testimony.

MR. AFESSA: Tilahun Afessa.

Good afternoon, Chairman Green and members of the Committee on Finance. My name is Tilahun Afessa and I am the Director of Policy, Planning, and Outreach for the Department of Revenue. I am here today to testify in support of Bill No. 130009 and Bill No. 130123.

Bill No. 130009 amends Chapter 19-2600 of The Philadelphia Code, entitled "Business Income and Receipts Tax," as it relates to non-profit activities that excludes any business conducted by a non-profit corporation or association organized for religious, charitable or education purposes from the definition of Business. Over the years, the term "any business" has created considerable confusion. Some non-profit entities have interpreted the term to include profit-making activities not directly related to the entities' non-profit purpose to the extent the profit is used to further such purpose. Bill No. 130009 makes the intent of the legislation clear by adding a clarifying provision which specifically states that this exclusion does not apply to commercial activity that does not directly serve and is not directly connected with the corporation or association's religious, charitable or education purposes. We believe Bill No. 130009 shall help the Department of Revenue's compliance, enforcement, and outreach efforts and shall lead to a gradual increase in the business income and receipts tax revenue generated from for-profit activities of non-profit entities.

Bill No. 130123 is a companion bill to Bill No. 130009 and relates to real estate tax exemption provided by law to non-profit entities. Bill No. 130123 amends Section 2-305 of The Philadelphia Code, entitled "Office of Property Assessment; Chief Assessment Officer; Powers and Duties," by providing standards for real estate tax exemptions and for documentation requirements. Currently, Section 2-305 provides with no specificity that the Chief Assessment Officer shall establish standards for recommending tax exemption for properties and shall consider and determine applications for tax abatement and tax exemption. Bill No. 130123 specifically provides that the Chief Assessment Officer shall only grant an exemption when the property is occupied, and actually and regularly used, by the exempt entity only for the purpose of purely public charity. The bill further provides that for the property to remain exempt, the exempt entity shall derive no income of the real estate other than from the recipients of its bounty.

The other important provision of this bill is the requirement that the exempt entity shall annually file with the Office of Property Assessment a sworn testimony certifying its continued status as a purely public charity and the continued use of the exempt property or the portion of it for such purpose. The bill requires additional application for the exempt entity to claim additional property or additional portion of property for exemption. We believe these requirements shall induce exempt entities to voluntarily declare to OPA currently exempt properties or a portion of it not used for the purpose of purely public charity. By increasing the real estate tax base, we believe Bill No. 130123 will lead to an eventual increase in real estate tax collection from properties owned by non-profit entities.

Thank you for giving me the opportunity to testify today. I am ready to answer questions you may have regarding these bills.

COUNCILMAN GREEN: Thank you very much.

Are there any questions from any members of the Committee?

(No response.)

COUNCILMAN GREEN: I thank you very much for your testimony.

MR. AFESSA: Thank you.

COUNCILMAN GREEN: Next we will hear on Bill No. 130009 from the Philadelphia Association of CDCs, Beth McConnell, and Art Sanctuary/Greater Philadelphia Cultural Alliance, Valerie Gay, if you would come up together.

(Witnesses approached witness table.)

COUNCILMAN GREEN: Please I guess, Ms. McConnell, if you want to begin. State your name for the record and proceed with your testimony.

MS. McCONNELL: Sure. My name is Beth McConnell, Policy Director for the Philadelphia Association of Community Development Corporations, PACDC.

Would you like me to offer testimony on both those bills or were you just focusing on one today?

COUNCILMAN GREEN: If you have testimony on both, please provide it.

MS. McCONNELL: Great. Thank you.

PACDC is a citywide association of 100 organizations, including the nearly 50 CDCs that have extensive experience working to revitalize Philadelphia's neighborhoods.

PACDC is very concerned about the impact that Bills 130009 and 130123 will have on non-profit organizations that work to revitalize Philadelphia's neighborhoods and provide affordable housing. If the Finance Committee chooses to move the bills forward, we ask that the Committee members and Chairman Green consider some amendments to those.

Bill No. 130009 could subject some non-profit revenue to the business income and receipts tax if the revenue is earned from activity that does not directly serve its charitable purpose. Non-profits, including CDCs, are constantly challenged to fulfill their missions in face of massive budget cuts. In fact, the City's overall annual budget for housing and community development has been cut by more than $39 million since FY09. That includes the projected effects of the FY14 sequester. And this is largely due to cuts in the Community Development Block Grant, CDBG, funds and the HOME funds, and that directly affects the programmatic work of CDCs in our communities. The City's General Fund contribution to community development and affordable housing have also been significantly shaved over the years.

We've also struggled to respond to decreases in philanthropic giving as a result of the economic downturn and changing funding priorities of foundations, and plenty of other non-profits have fared similarly.

So as a result of this, non-profits have been forced to be more creative in raising revenue. Some rent out their facilities for functions and meeting space, others offer consulting services to other organizations or sell products or services to the general public, all of which is designed to raise critical revenue to fund their core work. In fact, a whole new field is emerging called social entrepreneurship in which businesslike strategies are employed to address social problems and needs, sometimes under a non-profit corporate structure but not always. And that kind of revenue generation by non-profits is a necessity in our changing economic and political environments.

Now, most CDCs could make the case that their revenue-generation strategies further their charitable mission and would not be subject to BIRT under the language proposed in Bill No. 130009. But we are concerned that the language in the proposed ordinance is so broad that it would give the Department of Revenue too little guidance in determining what revenue-generation strategies are consistent with the organization's mission and which are not. CDCs, large and small, will have to take on the additional burden of time and expert help from tax attorneys to make the case to the Revenue Department, without really having clarity in advance how the Department will make that determination.

At best, exposing non-profits to potential BIRT taxation will eat into the already razor-thin margins of small to mid-sized organizations or cause them to spend more time and money on accountants or tax attorneys to determine their liability. At worst, it would defer non-profits from being innovative in their approach to revenue generation and force them to be even more reliant on government and private foundation grants that are shrinking every year.

I also just want to note very quickly that not all of the businesslike approaches used by non-profits realize an actual profit each year. I'm aware of at least one CDC project that's currently operating at a loss, but as I understand the project and the way that it operates, it could be subject to the receipts portion of the BIRT under this proposed measure. So, of course, that would further drain resources from the critical community development work of this organization.

What we might suggest is amending the bill to make it clear that activity non-profits engage in that generates revenue that is reinvested back into their charitable mission is not subject to BIRT. An additional strategy would be to exempt a certain amount of non-profit revenue, excluding traditional grant funds, from the BIRT and to not subject non-profits to the receipts portion of the BIRT.

Bill No. 130123 would require that non-profits that receive a property tax exemption file a sworn statement annually, along with supporting documentation required by the Office of Property Assessment, that the use of the property is still consistent with the charitable mission. PACDC believes that this is a reasonable goal and does not object to some regular review of the non-profit property tax exemption, but one CDC reports that applying for the initial exemption for just one of their facilities cost over $6,000 to hire an outside firm to do the complex work that was required by OPA. Now, this organization did not have to reapply in the second year, nor spend another $6,000 because OPA did in fact visit and inspect the facility in the second year and required that the organization in fact certify the structure was still being used for the exempt purpose. So in this case, the current rules worked and were not burdensome. The language in Bill No. 130123 seems to suggest that OPA engage in a similar process as it did in this instance.

Now, we were unable to survey all of our members to determine how regular OPA's inspection and recertification practice is now. We understand that OPA may be inconsistent in their application of this process, thus the need to codify that in legislative language. But what we wouldn't like to see, the situation in which OPA began requiring an entirely new complete application process each year. I don't think the legislation specifically spells that out, but we think if there were some minor changes directing OPA to that effect, it would give us some assurance that the renewal process wouldn't get out of hand. And for our members who own multiple properties, it would also make it easier on the organization to be able to certify more than one property in a single application each year.

I want to thank you for the opportunity to testify. I'm happy to answer any questions.

COUNCILMAN GREEN: Thank you.

Ms. Gay, please state your name for the record and proceed with your testimony.

MS. GAY: Certainly. My name is Valerie Gay, and I actually will be testifying only on BIRT.

Thank you. I am the Executive Director of Art Sanctuary and Vice Chair of the Board of Directors of the Greater Philadelphia Cultural Alliance. Thank you for inviting me to testify today regarding Councilman Green's proposal to tax Philadelphia's charities and non-profits.

I know the bill only seeks to tax non-mission related commercial activities, but I fear that inadvertently it could end up being a burden and a tax on our ability to fulfill our missions and to do our work. Cultural non-profits aren't in the business of making ourselves rich. Our activities aren't commercial. They are educational, inspirational, and transformative for the City.

At Art Sanctuary, we've collaborated with Opera Philadelphia on Hip H'Opera, a program that empowers school students to express themselves. By working with professional musicians from the Opera, students have made a form of music typically foreign to them speak to their lives and experiences. We also organize the annual Celebration of Black Writing, which, in its 29th year, has grown from a one-day gathering to right now a month-long series of events that expose thousands of students and residents to the best in African American literature and art.

The unfortunate truth for Art Sanctuary and for a vast majority of Philadelphia's cultural non-profits is that we've had to do that work with fewer resources at hand. The recession's impact on arts and culture in the City has been profound. Larger organizations saw their endowments dwindle. All of us faced cuts to government, foundation, and corporate support that pushed many of the City's non-profits to the edge of financial collapse.

According to the Cultural Alliance's 2011 Portfolio report, when the recession began, operating margins were thin, but positive at plus 2 percent. Two years later, almost half of the organizations in the report were in the red, with an average operating deficit of negative 9 percent. While things aren't quite as bad now as they were in 2009, they aren't much better either. To survive, we've had to do more with less. We've had to cut staff and overhead. Maintenance and repairs have had to be put off. At Art Sanctuary, we recently had to cut our full-time staff from seven to two people.

Despite these tough times, arts and culture in Philadelphia has continued to be both excellent and accessible. Philadelphia's cultural community has worked to put on first-rate events, productions, and exhibitions, and that work has paid off. In 2011, readers of Travel and Leisure Magazine named Philadelphia the top cultural destination in America. This year we were celebrated as an art capital and named one of the top five U.S. destinations by Lonely Planet travel guides.

We have also helped to keep the arts accessible for people in

Philadelphia so that we can all enjoy the fruits of our labor. Of the 17 million visits to cultural organizations, more than half are free, and those that are paid are heavily subsidized. The median cost of production is $48, while the median cost of a ticket is just $15.

This is fantastic. It's a source of pride for all Philadelphians, and it couldn't have been accomplished without the hard work of City Council. So thank you for your ongoing support of the Cultural Fund; the Office of Arts, Culture, and the Creative Economy; and everything you do to support our community.

What we fear, however, is that this proposal will have unintended but serious economic consequences. City Council could inadvertently damage a sector that is already making massive financial contributions to the City. We may be struggling, but we are popular. Arts and culture supports the hospitality industry, our retail corridors, and burgeoning culinary scene. In total, the non-profit culture sector had a $2.8 billion economic impact on the City. We support 30,000 jobs, and we generate $59 million for the City's tax coffers. Over and above these economic impacts, arts and culture also generates enormous educational and social benefits as a significant contributor to the City's quality of life.

When it comes to cultural non-profits, we think that applying the BIRT tax to our virtually non-existent commercial activities will provide little, if any, additional tax dollars for the City of Philadelphia. Instead, what it will accomplish is the creation of an entirely new layer of red tape, forcing an already strained workforce to prepare another annual filing on top of the ones we are already required to do with Harrisburg and the IRS, pay more fees, apply for licenses on commercial activities, and spend even more of our scarce resources on lawyers and accountants.

Our economic recovery is still precarious, but our sector is crucial to the vitality of Philadelphia. It would be a shame to let a short-term search for revenue undermine what we've already built together.

Thank you for your consideration.

COUNCILMAN GREEN: Thank you very much for your testimony.

Just to clarify the record, everything that will be required as a consequence of this, other than the annual certification, which is a certification, not an application, it requires the -- so the certification requires someone at the charity to say under oath that you're using it for a purely public purpose. That is the only purpose of that certification. It is to essentially assist the City in focusing on not-for-profits that fail to file the certification. It also creates a penalty for a change in use that is not certified for the individuals running the organization. So it makes the law much easier and less expensive to enforce. It does not in any way change the existing law with respect to whether or not your property is tax exempt. It is or it isn't, and the test for that is defined by the State Constitution, which we can't change, called the HUP test.

With respect to filing annual taxes for any kind of commercial activity or getting a license for any kind of commercial activity that is not part of your charitable mission, that is already the law. It is already required to be done every single year. And so if you are not complying with that, then you have a problem already.

So to the extent you're doing things that are earning you income that don't promote your charitable purpose, that's commercial activity that's taxed under the law today. This law doesn't change that. This law clarifies that portion of the law to make very clear that those receipts, if they're not related to your charitable mission, are required to be reported and tax is required to be paid on them.

Fortunately for you, the tax is a -- the profit that you make -- there's a 6.45 percent net income tax and there's a 4 mills gross receipts tax. That's what it will cost you to comply with the law, and hopefully that's what you'll do going forward.

I just want to ask the person here from the Department of Revenue if I have misstated anything with respect to these laws, I'd like you to come up and correct me, or if you have any comments to these, I'd like to give you the opportunity to come up. You don't need to, but...

(Witness approached witness

table.)

MR. AFESSA: I believe what you have said, almost everything what you've said is correct. This law is a clarification, and all along Revenue Department's position is that non-profit entities engaged in other than non-profit activities are subject to tax on that activity, but the ordinance as is is not very clear as to the responsibility. It says any business -- when it comes to the exemption exclusion, it says any business of a non-profit is excluded. And I've been in the Audit Unit. I worked in the Audit Unit for 15 years, and personally I know by directly auditing and reviewing books that when they have activities -- let me give you an example. Parking activities, some non-profits have a parking garage outside, adjunct to their building, and they're rented out for parking for outsiders. There is a collection. There is a parking tax. Sure enough the parking tax is paid, but the activity is also subject to business income and receipt tax, but they never reported it because of that provision which says any business of a non-profit is not subject to the business tax.

So this one clarifies it to say "any business" does not include commercial activities. So to that extent, it is a clarification. It helps the Audit Unit write their regulation specifically saying this is what the intent of --

COUNCILMAN GREEN: And you intend to write regulations to make very clear to the not-for-profit community what is business activity and what is not?

MR. AFESSA: Exactly.

COUNCILMAN GREEN: Thank you.

Are there any questions from members of the Committee?

(No response.)

COUNCILMAN GREEN: Seeing none, thank you all for your testimony.

MS. GAY: Thank you.

COUNCILMAN GREEN: Philadelphia Jobs with Justice, Gwen Snyder. And there is written testimony before you and available on the Finance Committee website, as is all the testimony for anybody who would like to see it. In particular, there's written testimony from the Committee of Seventy, who asked that it be submitted for the record and can't attend.

(Witness approached witness table.)

COUNCILMAN GREEN: Please state your name for the record and proceed with your testimony.

MS. SNYDER: My name is Gwen Snyder and I'm the Executive Director of Philadelphia Jobs with Justice. We're a non-profit coalition of over 50 organizations of faith, student, labor, and community types.

I'm here today to express my support for both bills, but in particular

Bill No. 130123, and to thank Councilmembers Green, Goode, and Reynolds Brown for their introduction of the bill.

Bill No. 130123 would allow the City to require non-profits to report annually on their land use in order to renew their property tax exemptions. This bill would simply institute a more responsible system for tracking these exemptions. These kinds of accountability measures aren't onerous. In fact, they're already the norm in the non-profit sector. Private foundations almost universally require that non-profits demonstrate how grant money was used in order to use it to further charitable work. Property taxes don't need to be any different.

The data that this bill would generate would also allow the City to easily analyze how and when these exemptions are improperly used.

Last month we joined with eight other organizations, including AFSCME DC

47, Women's Community Revitalization Project, and Philadelphia Unemployment Project, in formally launching Good Neighbors Philadelphia. This campaign calls on Mayor Nutter to require mega non-profits to pay taxes on land used for non-charitable purposes, like vacant land and profit-generating ventures such as hotels or rental space. This policy could generate tens of millions of dollars for our city. Bill 130123 would allow the City to estimate more exactly the potential for revenue generation under the Good Neighbors policy.

The organizations that Jobs with Justice represents organize, fight for, and consist of working Philadelphians, the folks who were hit the hardest by austerity budgeting. The churches and community groups serve in neighborhoods hit by firehouse brownouts and school closings. Poverty rates among City workers, including firefighters, librarians, sanitation employees and more, have doubled under the Nutter Administration.

Meanwhile, mega non-profits like Jefferson and Penn have seen record growth and profit. Yet, they skate by, contributing barely a pittance towards funding the schools that educate their workers and the public services they rely on to fight their fires and keep their sewers from overflowing.

Every year, the City grants 528 million in subsidies in the form of property tax exemptions, many of these granted based on decades-old applications. How many of these exemptions are granted to properties used for genuinely charitable purposes and how many are the results of a cynical exploitation of our current exemption system? Bill No. 130123 will give us answers.

In addition, I just would like to respond to some of my colleagues' testimony about the burden of paying taxes on commercial enterprise as a non-profit. Our feeling and the feeling of many of our members, including many non-profits, is absolutely there's nothing wrong with social entrepreneurship. We absolutely support those efforts, but it is an engagement with business, and like any other kind of business, a cost of doing business is paying for your streets, your sewers, your firefighters. Any kind of tax on these commercial properties, whether property or receipts, it's not about stifling social entrepreneurship. It's simply making sure, like any other business in Philadelphia, they're paying their fair share.

Thank you so much, especially to Councilman Green's office for inviting me to speak, and thank you for your time.

COUNCILMAN GREEN: Thank you.

Any questions for this witness?

(No response.)

COUNCILMAN GREEN: Seeing none,

anybody else here to testify on this bill?

(No response.)

COUNCILMAN GREEN: Seeing none, we will recess the public hearing and go into the public meeting.

I'd ask Councilmember Greenlee to move 130009.

COUNCILMAN GREENLEE: Thank you, Mr. Chairman. I move that Bill No. 130009 be reported out of this Committee with a favorable recommendation and a rules suspension to allow for first reading at our next session of Council.

(Duly seconded.)

COUNCILMAN GREEN: It's been properly moved and seconded that Bill No. 130009 be reported from this Committee with a favorable recommendation, that the rules be suspended to allow first reading at the next session of Council.

All in favor?

(Aye.)

COUNCILMAN GREEN: Any opposed?

(No response.)

COUNCILMAN GREEN: The ayes have it.

Councilmember Greenlee, 130123.

COUNCILMAN GREENLEE: Thank you, Mr. Chairman. I move that Bill No. 130123 be reported out of this Committee with a favorable recommendation and that the rules of Council be suspended to allow for first reading at our next session of Council.

(Duly seconded.)

COUNCILMAN GREEN: It's been properly moved and seconded that Bill No. 130123 be reported from this Committee with a favorable recommendation and a rules suspension.

All in favor?

(Aye.)

COUNCILMAN GREEN: Any opposed?

(No response.)

COUNCILMAN GREEN: The ayes have it.

This concludes the public

meeting on the bills just reported from this Committee.

Thank you for everybody's attendance.

(Committee on Finance concluded at 2:55 p.m.)

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CERTIFICATE

I HEREBY CERTIFY that the proceedings, evidence and objections are contained fully and accurately in the stenographic notes taken by me upon the foregoing matter, and that this is a true and correct transcript of same.

MICHELE L. MURPHY

RPR-Notary Public

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