The homestead exemption is a constitutional provision that shields the first $75,000 of fair market value of owner-occupied homes from state, parish and special ad valorem taxes. The exemption does not apply to municipal taxes for general government services, except in New Orleans. There, it applies to all taxes except the fire and police taxes that are the subject of the 2014 constitutional amendment. These two taxes generate about $3.7 million per mill. Because these taxes apply to a broader base, that is about $475,000 more per mill than the amount generated by City taxes for which the homestead exemption applies.

The constitution specifies that the revenue from the proposed tax increase must be used for fire services that directly contribute to residents’ safety. The City takes the position that this restriction poses no difficulty for the planned use of the tax revenue on pension and back-pay because such payments are part of firefighter compensation and therefore a direct cost of providing fire protection. The constitution also prohibits the new revenue from being used to reduce or replace City funding for fire services as established in the baseline year of 2013. This is not an issue because the City plans to spend $21.6 million more on fire services in 2017 than it spent in 2013.

If voters approve the proposition, the owner of a $350,000 home would pay an additional $87.50 in taxes each year. For each additional $100,000 of value, the tax would be $25 per year. Commercial property owners would pay $35 per $100,000 of value.

Analysis

The City indicated it will use the revenue from the proposed tax increase to help pay for an existing agreement that settles tens of millions of dollars in legal judgments.
the City owes to firefighters and their beleaguered pension system. This settlement is not contingent upon passage of the tax. If voters reject the tax, the City must still cover the settlement costs.\(^8\)

The settlement takes the form of a cooperative endeavor agreement signed in March 2016 by the City, the firefighters’ union and the New Orleans Firefighters Pension and Relief Fund. The City committed to pay $75 million to cover back-pay for firefighters who did not receive raises that the state mandated decades ago. The City also agreed to shore up the firefighters’ pension fund by increasing its annual contributions by about $12 million. In exchange, firefighters gave up their claim to $68.5 million in interest from the back-pay judgment. Firefighters also agreed to support certain legislative changes to reform pension fund governance and reduce the City’s costs for their pensions and other benefits. The Legislature enacted a host of changes this year to the firefighters’ pension as outlined in the settlement. The changes included raising the retirement age for new hires and reducing the rate at which their benefits accrue.

The settlement also requires the pension fund to implement reforms concerning investment decisions and the administration of benefits. An advisory committee of citizens with investment experience will provide advice on pension fund investments.

The agreement resolves many of the challenges surrounding the firefighters’ pension fund. The agreement also includes safeguards designed to prevent the fund from falling back into financial distress.

While the rejection of the proposed tax would not derail the settlement, it would affect the timing of the City’s $75 million in back-pay distributions to firefighters. In January 2016, the City made an initial $15 million payment, consistent with the settlement terms.\(^9\)

If the tax passes, the remaining $60 million would be paid in annual installments of $5 million over the 12-year duration of the tax. Passage of the tax would also trigger a $4 million reduction in the City’s 2017 allocation to the firefighters’ “old” pension fund. If the tax does not pass, the settlement calls for the City to try to find another revenue source for the remaining back-pay. If the City is unable to do so, it must use existing revenue sources to make the payments on a more relaxed schedule. At a minimum, the City would have to pay $1 million annually for seven years starting in 2019, $2 million annually for the following six years, and $17 million for each year thereafter until the $60 million was fully paid.\(^10\)

The other terms of the settlement would be the same whether voters approve or reject the tax. After voters rejected the joint fire and police tax proposition in April, the settlement required the City to place a second fire tax proposition on the ballot prior to 2019. The current proposition satisfies that requirement.

While the settlement does not hinge upon approval of the tax, City officials say they need the tax revenue to cover the City’s costs under the settlement. Without the tax, they would have to cover those costs using existing City revenues, probably by cutting other areas of the budget.

If the millage passes, the City’s additional annual costs under the settlement include about $12 million for higher pension contributions and $5 million for back-pay. Some of these $17 million in new costs will be offset by savings from changes to the firefighters’ pension and other benefits. These savings are difficult to estimate with precision, in part because some rely on matters that the parties have agreed to submit to a judge to resolve.\(^11\) In addition, the City’s contributions to the firefighters’ “old” pension fund are projected to decline by about $700,000 each year. This will free up a growing pool of funds that could be applied to the settlement costs. For example, the reduced costs for the old pension would be about $700,000 in the first year, $1.3 million in the second year and $2 million in the third year.\(^12\)

Given all of the variables at play, it is not possible to precisely assess how well the size of the tax proposal squares with the settlement costs. The bottom line is this: The $8.9 million that the tax is expected to yield
The fire tax will provide a temporary funding source to help resolve large, long-standing City obligations to firefighters. Without the tax, the City would have to cut other areas of the budget in order to meet these obligations.”

will not be sufficient to fully cover the settlement costs for at least the first several years, but it may well be more than enough in the later years.

City officials emphasize that the settlement costs are in addition to huge increases for the firefighters’ pension that are already built into the City’s annual budget. City spending on the firefighters’ pension has increased 60% from $27 million in 2009 to a budgeted $43.2 million this year. The officials say that if the tax does eventually generate more money than the minimum needed to meet the new settlement costs, that additional revenue could help relieve the pressure the firefighters’ pension is placing on other areas of the City’s budget. They also emphasize that the tax is temporary, lasting 12 years.

The cooperative endeavor agreement includes a provision that dedicates all revenue from the proposed tax, beyond the back-pay distributions, to pension contributions. This appears to make back-pay distributions the first priority for the tax revenue. However, the City says it does not believe the provision requires use of tax revenue for back-pay. The City commits to using other revenues for the back-pay distributions and applying the full $8.9 million from the proposed tax toward the $12 million in additional pension contributions under the settlement.

Still, passage of the tax would expedite the back-pay distribution schedule under the agreement. Some tax proponents say this is important because some firefighters have been waiting decades for payments and others have died before receiving the money they were owed. If voters approve the tax, firefighters would receive their remaining back-pay in steady $5 million annual payments starting in 2017. If voters reject the tax, the City would not have to make any payments, beyond the initial $15 million payment, until 2019, when it would start making small annual payments for 13 years. The City would not make the

BGR Position

FOR. The fire tax will provide a temporary funding source to help resolve large, longstanding City obligations to firefighters. Without the tax, the City would have to cut other areas of the budget in order to meet these obligations.

SEWERAGE & WATER BOARD DRAINAGE TAX RENEWAL

What It Would Do

Voters in Orleans Parish will decide whether to renew a property tax to support the Sewerage & Water Board’s drainage system. The tax, currently levied at 4.66 mills, would be renewed at 4.46 mills. The renewal would take effect in 2017 and remain in place for 30 years, expiring in 2046.

Background

The Sewerage & Water Board (S&WB) is responsible for the City’s major drainage system, including drainage pipes 36 inches or larger in diameter as well as the City’s drainage canals and pumping stations. The drainage system is funded by three, 50-year property taxes, which total 16.43 mills.

The oldest property tax, currently levied at 4.66 mills, has been in place since 1967 and will expire in 2016 unless voters approve the current proposition. The proposition would continue the millage for 30 years, beginning with the 2017 tax bills.

For 2016, the S&WB projects its drainage revenue will total $51.1 million. Property taxes account for $49.9
The S&WB revenue from the drainage system’s current dedicated taxes is consumed by operational costs, cash-funded capital improvements and debt service. The S&WB does not have adequate funding for its capital plan. In 2016, it deferred $49.9 million of planned work. The amount of deferred costs in the capital plan could exceed $270 million by 2020 if the S&WB does not find a new funding source.

Additionally, the S&WB must soon begin to meet significant new financial obligations. Operating costs for the three lakefront outfall canals and pumping complexes will become the responsibility of the S&WB once the U.S. Army Corps of Engineers completes its work, projected to occur in 2017. Beginning in 2019, the S&WB will also be responsible for a share of the costs for the Corps’ multiple drainage improvement projects under the Southeast Louisiana Urban Flood Control Project.

The S&WB has made multiple attempts during the past three decades to increase funding for the drainage system. These efforts have encountered resistance or inaction. In 1985, the S&WB proposed a city-wide stormwater fee, but voters rejected the proposition. In 1991, voters twice rejected a 4-mill property tax renewal which, at the time, made up 31% of the drainage system’s capital budget. And in 1998, the S&WB proposed another city-wide stormwater fee and claimed that the City Council could impose the fee without a public vote. The Council took no action on the proposal.

The S&WB is once again examining stormwater fees as one of the options for meeting new drainage system obligations.

Voters should be aware that during the past year the Office of Inspector General has raised concerns about the effectiveness and efficiency of the S&WB. These concerns were not specific to the drainage department. They include problems collecting City sanitation fees, weaknesses in the management of take-home vehicles, and a lack of documentation for reimbursements. Furthermore, the Inspector General recently wrote to the City Council that the S&WB lacks appropriate controls on overtime pay, noting that S&WB employees earned three times the amount of overtime as employees in Jefferson Parish’s water department and stating that the S&WB is at a “very high risk of payroll fraud.”

The S&WB is putting in place a new billing system that will address the collection of sanitation fees and officials say that the issues with vehicles and reimbursements were immediately corrected. The S&WB says the excessive overtime has been a result of operational necessity, but it is currently reviewing its work processes and exploring ways to build up its work force to reduce overtime. Furthermore, the S&WB over the past several years has been in the process of reforming its governance. In line with BGR recommendations, the S&WB has changed its board structure, reduced the board’s involvement in contracting and disadvantaged business enterprise processes, and increased collaboration with the City’s Department of Public Works. However, addressing the S&WB’s operational challenges will require continued focus and diligence.

Analysis

The existing property tax, currently levied at 4.66 mills, is projected to generate $16.1 million in 2016. Voter approval of the proposition would continue the property tax, but at the slightly lower rate of 4.46 mills. The S&WB projects that the proposed millage rate will generate $15.4 million annually. The difference between the current and proposed millage rates – 0.2 mills – could result in a decrease in drainage system revenue of about $690,000 a year.

If voters approve the proposition, the overall tax rate for the S&WB’s drainage system would decline from 16.43 mills to 16.23 mills. A homeowner with a homestead exempt property valued at $350,000 would pay $6 less per year and see his S&WB tax bill decrease from $452 to $446. Commercial properties would pay $62, instead of $65, per $100,000.
If voters reject the proposition, the overall tax rate for the S&WB’s drainage system would decline even further from 16.43 mills to 11.77 mills. A homeowner with a homestead-exempt property valued at $350,000 would pay $128 less per year. The taxes on a commercial property valued at $750,000 would be $489 less per year, decreasing from $1,725 to $1,236.

Renewing the property tax would essentially maintain the status quo. The drainage system’s dedicated revenue would continue uninterrupted, allowing the S&WB to maintain its current level of drainage operations. S&WB officials say that renewal of the property tax is critical because dedicated tax revenue for the drainage system is fully absorbed by current expenses and required operating reserves.

Without the property tax renewal, the drainage system will lose 28% of its annual revenue starting in 2017. A system that the S&WB says is already underfunded would be in a worse position. The drainage system would begin consuming cash on hand to meet operating costs and debt service, but it would run out of money in 2020.

In the short-term, the drainage system might meet the shortfall on an emergency basis by borrowing funds from the water or sewer systems. This could give officials additional time to determine the next course of action. But this is only a temporary solution, and it carries significant risk.

If voters reject the renewal, the S&WB could place a new tax on the ballot. It could also try to meet the shortfall as part of a citywide stormwater fee.

As noted above, the S&WB has attempted to impose stormwater fees in the past; it is giving the funding mechanism serious consideration once again as a means of meeting its new obligations. If properly structured, a stormwater fee could have several advantages over a property tax, including: a broader payer base, because a stormwater fee can apply to properties exempt from ad valorem taxation; more accuracy and fairness because stormwater fees are more objectively calculated than property assessments; a stronger nexus between who pays the fee and the demands a property places on the drainage system; and built-in incentives to reduce those demands. BGR will explore stormwater fees more fully in a forthcoming report.

However, implementation of a stormwater fee remains a future prospect and is uncertain. The S&WB cannot implement a fee at will; it would require City Council and, possibly, voter approval. The duration of this process adds an additional element of uncertainty.

Keeping the drainage property tax in place has advantages. The tax is already well-established, and voters understand the property tax process well. The information needed to calculate the tax is readily available. A collection method is already in place. The property tax, as a funding mechanism, provides continuity and certainty in the short and long-term. Some also argue that, because property value is an index to part of the owner’s wealth, an owner’s ability to pay property taxes is roughly keyed to the burden of the taxes.

Moreover, a property tax and stormwater fee can coexist; they are not mutually exclusive. Even with a property tax renewal, the S&WB can pursue a stormwater fee down the road for infrastructure maintenance expenses and new drainage obligations that are beyond the scope of the current budget.

BGR Position

FOR. The drainage system is among the most critical components of New Orleans’ infrastructure, and the property tax is vital to the maintenance of that system.
ENDNOTES


3 See La. Const. Art. IV, Sec. 26(E). The tax exceeds the previous 5-mill cap because it was rolled forward due to a drop in assessed property values.


5 BGR has consistently opposed the homestead exemption on fairness as well as fiscal grounds. In addition to limiting the city’s revenue-generating capacity, the exemption unfairly shifts the tax burden to other property owners. (BGR, Who’s Behind the Tree? The Homestead Exemption and Taxpayers in the New Orleans Area, March 2009.) BGR supported the constitutional amendment to double the cap on the police and fire taxes that are not subject to the homestead exemption. (BGR, On the Ballot: November 4, 2014, September 25, 2014, p. 7)


7 BGR assumed that land value accounts for 20% of total value.

8 Cooperative Endeavor Agreement between the City of New Orleans, the New Orleans Firefighters’ Pension and Relief Fund and New Orleans Firefighters Local 632, signed March 3, 2016, Sec. (I)(B)(9).

9 The cooperative endeavor agreement requires the City to pay employment taxes on the back-pay distributions. For the $15 million distribution, this amounted to an additional $16,000 to cover the City’s Medicare contributions for some firefighters.

10 Cooperative Endeavor Agreement, Sec. (I)(B)(11).

11 On October, 26, 2016, a state judge ruled in the City’s favor on the proper interpretation of pension benefits calculations set forth under state law. The judge ruled in firefighters’ favor in determining that pension benefits for retired firefighters who retired before January 1, 2016, cannot be offset by the amount of supplemental earnings benefits they are receiving under the state workers compensation program. Both rulings can be appealed. New Orleans Fire Fighters Pension and Relief Fund, et al v. the City of New Orleans, et al, No. 12-7061 (Civ. Dist. Ct., Orleans Parish 2012).

12 Estimates provided by the Business Council for New Orleans and the River Region, which helped facilitate the settlement.

13 The 2017 budget, as proposed by the mayor, includes a significant increase, to $50.4 million, for the firefighters’ pension.

14 Cooperative Endeavor Agreement, Sec. (I)(B)(8). The provision states “If the voters approve the 2016 Millage Proposition, dedicate to the extent allowed by law any and all revenue collected from the Proposition, beyond the Longevity Class payments, to the City’s funding obligations to the Old and New Funds.”

15 The back-pay issue is significant because, as previously noted, the Louisiana Constitution requires use of revenue from the proposed tax for services that directly contribute to residents’ safety. There are questions about whether back-pay owed from prior years meets this requirement. The City told BGR that back-pay does meet that requirement. The City reasoned that back-pay, regardless of how long ago it should have been paid, is part of firefighters’ compensation and, therefore, is a fundamental cost of providing fire protection. It is not certain that this interpretation would survive a legal challenge. However, if the provision that appears to prioritize back-pay were found to be illegal, it likely could be eliminated under the severability clause in the cooperative endeavor agreement. See Sec. VIII(E) of the agreement. Additionally, the City’s commitment to using the tax revenue for pension contributions, and not back-pay, seems to overcome the concern of a constitutional violation.


17 Agreement between the City of New Orleans, Department of Streets, and the Sewerage and Water Board of New Orleans, July 1, 1992. The remainder of the drainage system, or the minor drainage system, is the responsibility of the Department of Public Works. The minor drainage system consists of the catch basins and smaller drainage pipes beneath the City’s streets and public rights-of-way.

18 City of New Orleans, 2016 Adopted Operating Budget, p. 65.

19 La. R.S. Sec. 33:4124. The millage was originally levied at 3 mills. A second property tax, currently levied at 4.71 mills, will expire in 2027. See La. R.S. Sec. 33:4137. A third property tax, currently levied at 7.06 mills, will expire in 2031. See La. R.S. Sec. 33:4147.


21 Ibid., p. 85.

22 Ibid. The S&WB’s capital program for 2016 to 2025 totals $919.1 million. It had planned to undertake $114.9 million in 2016, but could afford to budget only $65 million. Most of the budgeted money comes from FEMA and other sources outside the S&WB. See S&WB, 2016 Adopted Capital Budget, pp. 17-21.

23 U.S. Army Corps of Engineers, Permanent Canal Closures &
ON THE BALLOT: DECEMBER 10, 2016

Pumps, July 2016.

24 Black & Veatch, Report on Operations for 2015, p. 72. The S&WB is responsible for 35% of project costs. The remaining 65% of project costs is the responsibility of the U.S. Army Corps of Engineers. The projects are primarily concentrated in the Uptown area.


27 Home Rule Charter of the City of New Orleans, Sec. 3-101(2).


32 BGR calculations based on S&WB’s assumed 97% collection rate.

33 New Orleans City Council Res. No. R-16-422, adopted September 8, 2016. The official ballot language states: “Shall the City of New Orleans (the “City”) continue to levy an ad valorem tax in the amount of 4.46 mills on all property subject to taxation within the City for a period of thirty (30) years, beginning in the year 2017 and ending with the year 2046 (an estimated $15,400,000 reasonably expected to be collected at this time for an entire year from the 4.46 mills levy), to be used solely and exclusively for the purpose of operating and maintaining the City’s drainage system and for the construction and extension of said drainage system?”


35 BGR calculations. BGR assumes that land value accounts for 20% of total value.


37 Ibid., p. 75.

38 The water and sewer systems are more financially stable than the drainage system. The water and sewer systems are funded primarily through user fees. In 2012, the City Council approved incremental annual increases in water and sewer rates leading to a doubling of rates by 2020. See New Orleans City Council Ord. Cal. No. 29,296, adopted December 6, 2012.

39 See La. R.S. Sec. 38:90.17(A)(1)(a) and La. R.S. Sec. 38:90.17(A)(3). See also, Home Rule Charter of the City of New Orleans, Sec. 3-101(2).

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