PUBLIC HEARING ON

"Children's Hospital Research and Innovation Campus Equitable Tax Relief Act of 2019"

Before the
Committee on Business and Economic Development
Council of the District of Columbia

The Honorable Kenyan McDuffie, Chairman

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Good morning, Chairman McDuffie and members of the Committee on Business and Economic Development. My name is Nancy Fox and I am the Senior Policy Analyst in the Office of Finance and Treasury in the Office of the Chief Financial Officer (OCFO). I am pleased to testify for the OCFO on Bill 23-577, the "Children's Hospital Research and Innovation Campus Equitable Tax Relief Act of 2019"

The proposed legislation would exempt a portion of Lots 824 and 826 in Square 2950 from real property tax, deed transfer tax, and deed recordation tax. These exemptions would preserve the administrative exemptions of these properties that were valid prior to the time they were leased to business entities created to obtain federal tax benefits under the federal New Market Tax Credits and Historic Tax Credits.

Lots 824 and 826 are owned by Children's National at Walter Reed (CNWR), a wholly-owned subsidiary of Children's National Medical Center (Children's). Children's and CNWR are non-profit entities whose property is generally entitled to exemption from real property taxes in the District of Columbia. CNWR received a conveyance of 11.85 acres, located on the former Walter Reed medical campus, from the U.S. Department of the Army in 2016. Children's plans to develop this conveyance, which includes Lots 824 and 826, over time as the Children's National Research and Innovation Campus (CNRIC). CNRIC will be the site of Children's cutting-edge work in the realm of pediatric genomic and precision medicine, and will include partnerships with JLABS and Virginia Tech.

Lots 824 and 826 are part of CNRIC's first phase, which is currently under construction. Phase I includes the renovation of three historic buildings. On Lot 824, Building 52 will become an outpatient, primary care, and genetic services clinic. Building 53 will become an auditorium to be used for medical conferences and community meetings. On Lot 826, Building 54 will become a biomedical research building focused on pediatric research and innovation. Phase I will also include a parking garage and other infrastructure.

CNWR requested and received a partial administrative exemption from the Office of Tax and Revenue (OTR) for all of the property that will be developed as CNRIC. OTR determined that Lot 824 is approximately 98.7 percent exempt and Lot 826 is approximately 92.6 percent exempt based on the proposed building uses.

For the construction of Phase I, Children's took advantage of the opportunity to use federal New Market Tax Credits and Historic Tax Credits to reduce the funding that Children's would need to commit from its own resources or from its donors. Conforming to federal tax credit requirements, in 2019 CNWR conveyed a leasehold interest in Lots 824 and 826 to two newly-formed entities (the Tax Credit Entities). Children's maintains majority ownership and control over the Tax Credit Entities, but the Tax Credit Entities' property interest disqualifies Lots 824 and 826 from receiving the administratively granted tax exemption. As a result, Lots 824 and 826 will have an added real property tax liability of approximately $1.2 million in the current tax year, increasing to an estimate of nearly $3.5 million in Tax Year 2022, the first full year that Phase I is in operation, in addition to transfer and recordation tax liabilities associated with ground leases and a Deed of Trust recorded against these properties.

Financial Analysis

The OCFO examined the impact on CNRIC and Children's if the legislatively proposed exemptions are not granted, using information provided by Children's. The facilities comprising Phase I of CNRIC are expected to operate at a loss with or without the tax exemption. Children's is funding the construction of Phase I, budgeted at over $200 million, using its own resources as well as philanthropic gifts, proceeds from the sale of a portion of the parking garage, and the proceeds provided from the tax credit investments. The project does not include debt financing to be repaid with revenues from the building.

Based on a review of the financial information provided to the OCFO, Children's is a large, financially healthy institution with sufficient resources to bear the additional cost of the estimated tax liability for Lots 824 and 826 without the tax exemption. Based on the OCFO's analysis of the information provided, Children's does not require a tax exemption to fund or to operate the new CNRIC facility, and therefore the exemption is not fiscally necessary. However, the OCFO's analysis finds that the financial benefits of the tax credit structure to Children's will be substantially diminished, or completely offset, by the added property tax liability resulting from the ownership structure that includes the Tax Credit Entities required to receive the tax-advantaged investments. According to

Children's, the effective loss of this financial benefit decreases the resources available to the patient care and research activities integral to Children's mission.

Fiscal Impact

A fiscal impact statement will be prepared separately for this legislation. My office calculates the estimated value of the tax exemptions over the time period that the Tax Credit Entities are expected to have a leasehold interest in the properties at over $27 million.

Thank you for the opportunity to testify. This concludes my testimony and I am happy to answer any questions you have at this time.