

# Economic Impact Statement

Montgomery County, Maryland

## Bill 5-25                      Demolition Tax for Affordable Housing Production

### SUMMARY

The Office of Legislative Oversight (OLO) anticipates that Bill 5-25 would have a short-term negative impact on economic conditions in the County in terms of the Council's priority economic indicators. By imposing a \$20,000 excise tax on certain demolitions and renovations of single-family homes, the Bill would primarily affect developers that specialize in building individual homes and buyers, particularly in the areas of Bethesda, Potomac, and Chevy Chase where this has been most common in the County. Developers would be required to pay the excise tax to receive a permit for demolition from the County. As a result, the tax would increase capital expenditures for affected developers, which, holding all else equal, would decrease business income. However, developers would likely pass through some or all the additional costs to buyer, who would pay higher home prices.

In the long term, the Bill could provide economic benefits by using excise tax revenues to support the construction of mixed-income, mixed-use developments. These investments could increase the supply of affordable housing in the County. While the magnitude of the Bill's effect on affordable housing is uncertain, these long-term benefits may offset the Bill's short-term economic costs.

### BACKGROUND AND PURPOSE OF BILL 5-25

In 2021, the Council established the Housing Production Fund (HPF), which allows the Housing Opportunity Commission (HOC) to finance construction of mixed-income and mixed-use developments in the County. Thirty percent of the units in these developments must be income-restricted, with 20% of the units affordable at or below 50% of the Area Median Income (AMI) and 10% affordable at 65% to 70% of AMI.<sup>1</sup>

Bill 5-25 would establish a \$20,000 excise tax on certain demolitions and renovations of single-family homes. This would include partial demolitions of attached or detached single-family homes that result in the destruction or removal of at least 50% of an existing home.<sup>2</sup> Revenues from the new excise tax would be used exclusively for the HPF for financing the construction of mixed-income, mixed-use developments.<sup>3</sup>

The Bill also outlines the following proposed exemptions from the excise tax:

- The existing home is deemed unsafe or condemned under County Code;
- The replacement single-family home would be a moderately priced dwelling unit;
- The replacement single-family home would be the owner's principal residence for a minimum of 5 years;
- The gross floor area of the replacement single-family home would be less than or equal to the original home's gross floor area;

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<sup>1</sup> [Housing Production Fund](#), Housing Opportunity Commission, Accessed 2/19/2025.

<sup>2</sup> [Introduction Staff Report for Bill 5-25](#), Montgomery County Government, Introduced 2/11/2025.

<sup>3</sup> Ibid.

- The replacement single-family home is necessary due to a medical condition or disability of an individual that will reside in the home; or
- The demolition is necessary due to unforeseeable circumstances beyond the owner's control and reasonable ability to remedy.<sup>4</sup>

The Council introduced Bill 5-25, Demolition Tax for Affordable Housing Production, on February 11, 2025.

## INFORMATION SOURCES, METHODOLOGIES, AND ASSUMPTIONS

As required by 2-81B of the Montgomery County Code, this Economic Impact Statement evaluates the impacts of Bill 5-25 on residents and private organizations in relation to Council's priority economic indicators. In doing so, it examines whether the Bill would have a net positive or negative impact on overall economic conditions in the County.<sup>5</sup>

While some local jurisdictions have implemented demolition taxes to help finance affordable housing development, OLO found no existing impact evaluations assessing their economic effects.<sup>6</sup> To analyze the potential effects of the Bill, OLO relied on:

- Broader research on the relationship between housing regulation on home prices; and
- Montgomery Planning's analysis of prior legislation before the Council that proposed an excise tax on certain demolitions and renovations of single-family homes.<sup>7</sup>

OLO uses these sources of information to base its conclusions on the Bill's economic impacts to private organizations and residents, namely certain developers and home buyers.

## VARIABLES

The primary variables that would affect the economic impacts of enacting Bill 5-25 are the following:

- Cost pass-through ratio; and
- Total number of affordable housing units.

## IMPACTS

**WORKFORCE ■ TAXATION POLICY ■ PROPERTY VALUES ■ INCOMES ■ OPERATING COSTS ■ PRIVATE SECTOR CAPITAL INVESTMENT ■ ECONOMIC DEVELOPMENT ■ COMPETITIVENESS**

<sup>4</sup> [Introduction Staff Report for Bill 5-25](#), Montgomery County Government, Introduced 2/11/2025.

<sup>5</sup> ["Sec. 2-81B, Economic Impact Statements,"](#) Montgomery County Code.

<sup>6</sup> Impact evaluations are a core tool of evidence-based policymaking that seek to answer cause-and-effect questions regarding the impact of a policy intervention on a specific outcome(s). Using a randomized control trial or quasi-experimental design, they aim to account for what would have occurred in the absence of a policy intervention by comparing treatment groups (i.e., cases where the policy has been implemented) and control groups (i.e., cases where the policy has not been implemented). Paul J. Gertler et al., [Impact Evaluation in Practice, Second Edition](#) (Washington, DC: Inter-American Development Bank and World Bank, 2016); Kirsten Collins, ["What Is Impact Evaluation?"](#), Text, American University Online, April 2, 2015.

<sup>7</sup> Jason Sartori and Lisa Govoni, ["Montgomery Planning Analysis of Bill 34-19, Taxation – Development Impact Taxes – Affordable Housing – Housing Impact Fairness Act"](#) (Montgomery County Planning Department, December 5, 2019).

## Businesses, Non-Profits, Other Private Organizations

OLO anticipates that Bill 5-25 would have negative impacts on certain private organizations in the County in terms of the Council's priority economic indicators.

By imposing a \$20,000 excise tax on certain demolitions and renovations of single-family homes, the Bill would primarily affect developers that specialize in building individual homes.<sup>8</sup> Developers would be required to pay the excise tax to receive a permit for demolition from the County. As a result, the tax would increase capital expenditures (i.e., costs incurred in acquiring or improving a property) for affected developers, which, holding all else equal, would decrease business income. However, developers would likely pass through some or all the additional costs to buyers, as has been demonstrated empirically in the literature on housing regulation and home prices.<sup>9,10</sup>

Analysis from Montgomery Planning suggests that the potential impacts of the excise tax on developers would likely be minor. In its 2019 report on similar legislation before the Council, Montgomery Planning analysts wrote,

Over the last ten years, there has been an average of 219 single family detached home demolition permits issued per year by the Department of Permitting Services. Approximately 87 percent of the demolition permits occurred in Council District 1, which includes the areas of Bethesda, Potomac, and Chevy Chase.<sup>11</sup>

The analysts found "734 records where transactions occurred both pre and post demolition permit between the years of 2014 and 2017." **Table 1** presents the average price increases following construction of the replacement homes. Throughout the County, the average sales price increased by over \$1 million. A \$20,000 excise tax would constitute approximately 2 percent of the price increase.

**Table 1. Price Increases Following Single-Family Home Demolitions in Montgomery County (2014-2017)**

Town/City	Average 1st Sale	Average 2nd Sale	% Increase	Price Increase	\$20K Tax as % of Price Increase
Potomac	\$854,583	\$1,901,000	122%	\$1,046,417	1.9
Bethesda	\$742,830	\$1,736,534	134%	\$993,704	2.0
Chevy Chase	\$924,328	\$2,272,003	146%	\$1,347,675	1.5
Cabin John	\$567,500	\$1,417,500	150%	\$850,000	2.4
Kensington	\$514,746	\$1,337,897	160%	\$823,151	2.4
Silver Spring	\$297,866	\$782,725	163%	\$484,860	4.1
Rockville	\$781,042	\$2,059,242	164%	\$1,278,200	1.6
<b>Montgomery County</b>	<b>\$735,083</b>	<b>\$1,748,385</b>	<b>138%</b>	<b>\$1,013,301</b>	<b>2.0</b>

<sup>8</sup> Ibid.

<sup>9</sup> Raven Molloy, "[The Effect of Housing Supply Regulation on Housing Affordability: A Review](#)," *Regional Science and Urban Economics* 80 (January 2020); Joseph Gyourko and Raven Molloy, "Regulation and Housing Supply"; Keith R. Ihlanfeldt, "[The Effect of Land Use Regulation on Housing and Land Prices](#)," *Journal of Urban Economics* 61, no. 3 (May 1, 2007): 420–35; Vicki Been, "Impact Fees and Housing Affordability," *Cityscape* 8, no. 1 (2005): 139–85.

<sup>10</sup> For more on the theory of cost pass-through, see RBB Economics, "[Cost Pass-Through: Theory, Measurement, and Potential Policy Implications](#)" (Report prepared for the Office of Fair Trading, United Kingdom, June 17, 2014).

<sup>11</sup> Sartori and Govoni, "Montgomery Planning Analysis of Bill 34-19."

While OLO does not have data on the profit margins developers specializing in building individual homes, the Bill is unlikely to deter substantial private sector capital investment in this sub-sector. First, as previously discussed, developers would likely pass through a portion of the costs to buyers. Second, the excise tax represents a marginal portion of the substantial increases in average sale prices following renovation. As a result, developers may be able to offset the cost increase without a major impact on investment decisions.

Beyond these potential impacts, OLO does not expect the Bill to affect private organizations in terms of the Council's other priority indicators.

## **Residents**

OLO anticipates that Bill 5-25 would have mixed impacts on certain residents in the County in terms of the Council's priority economic indicators.

The Bill would primarily affect buyers of replacement homes, particularly in the areas of Bethesda, Potomac, and Chevy Chase where "boutique" home building has been most common in the County.<sup>12</sup> Buyers would likely pay higher home prices accounting for the excise tax.

Additionally, by using revenues from the new excise tax to finance the construction of mixed-income, mixed-use developments, the Bill would likely benefit certain residents in the long-term by increasing the supply of affordable housing in the County. However, due to information constraints, OLO is unable to estimate the magnitude of the Bill's effect on affordable housing.

Beyond this potential impact, OLO does not expect the Bill to affect residents in terms of the Council's other priority indicators.

## **Net Impact**

OLO anticipates that Bill 5-25 would have a short-term negative impact on economic conditions in the County in terms of the Council's priority economic indicators. The \$20,000 excise tax on certain demolitions and renovations of single-family homes would primarily affect developers that specialize in building individual homes and buyers, primarily in Bethesda, Potomac, and Chevy Chase. The excise tax would increase capital expenditures for affected developers, which, holding all else equal, would decrease business income. However, developers would likely pass through some or all the additional costs to buyers, who in turn would pay higher home prices.

In the long term, using excise tax revenues to support the construction of mixed-income, mixed-use developments could provide economic benefits by increasing the supply of affordable housing in the County. While the magnitude of the Bill's effect on affordable housing is uncertain, these long-term benefits could help offset the Bill's short-term economic costs.

## **DISCUSSION ITEMS**

Not applicable

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<sup>12</sup> Ibid.

## CAVEATS

Two caveats to the economic analysis performed here should be noted. First, predicting the economic impacts of legislation is a challenging analytical endeavor due to data limitations, the multitude of causes of economic outcomes, economic shocks, uncertainty, and other factors. Second, the analysis performed here is intended to *inform* the legislative process, not determine whether the Council should enact legislation. Thus, any conclusion made in this statement does not represent OLO's endorsement of, or objection to, the Bill under consideration.

## AUTHOR

Stephen Roblin (OLO) prepared this report.