Testimony of

District of Columbia Association of REALTORS® (DCAR)

before the

District of Columbia Tax Revision Commission

Anthony Williams, Chairman

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Presented by:

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Introduction

Good evening Chairman Williams, Commissioners, and staff. My name is Ed Krauze and I am the Chief Executive Officer of the District of Columbia Association of REALTORS® (DCAR). DCAR serves as the state-level association representing nearly 2,400 residential and commercial REALTORS®, property managers, title attorneys and other real estate professionals licensed in the District of Columbia.

DCAR would like to first thank you, Chairman Williams, for leading the Commission and commending all of the Commissioners for your diligence in taking on the daunting task of making the District's tax code fairer and simpler. As highly esteemed experts in your fields, you have been entrusted to make objective recommendations that can drastically enrich our residents' lives. This unique position allows you to truly examine which of the District's tax policies are just and which are out of line with our city's current and future needs.

In respect for your time, we will attempt to align this testimony of the recordation and transfer taxes with the Tax Revision Commission's stated goals. *You will see it is arguably impossible to reconcile recordation and transfer taxes and the Commission's stated goals for the District.*

DCAR's General Principles on Real Property Tax Reform

DCAR acknowledges there is a nexus between certain ongoing real property taxes and public benefits for residents, such as schools, safety, and infrastructure. As have been reinforced by the reports presented to the Commission, the District should nevertheless avoid unnecessarily raising taxes on the real estate industry in a quest to fund an ever-increasing Budget[1], currently at a record high of approximately $12.1 billion[2] for 630,000 residents[3]. We see that you have begun a healthy discourse on property taxes, in particular the very high Class 2 Commercial Property tax rate, and are confident we can work together to keep these taxes as low as possible.

Unfortunately, the District's haphazard real property deed recordation and transfer taxes are so egregious we feel it necessary to urge the Commission to recommend their abolishment and vehemently oppose any potential increase.

DC's recordation and transfer taxes are:

- ***Highly discriminatory;***
- ***Inefficient; and***
- ***In direct conflict with the Tax Revision Commission's overarching goals of fairer, broader based taxes that encourage job growth and make the District more regionally competitive.***

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[1] From Fiscal Year 2001 – Fiscal Year 2011, DC expenditures have increased an overall 58.9%. *Source*: Spaulding, Jim. Office of Budget and Planning: D.C. Operating and Capital Budget (Presented to the Commission on Oct. 1, 2012).

[2] *Sources*: B20-198, "*Fiscal Year 2014 Budget Request Act of 2013*" and B20-199, "*Fiscal Year 2014 Budget Support Act of 2013.*"

[3] The US Census Bureau estimated the District's population for 2012 at 632,323 residents. Retrieved June 24, 2013 at http://quickfacts.census.gov/qfd/states/11000.html.

Background

The taxation of property transfers in the US dates back to the War Revenue Stamp Act, where they started as a simple service charge to cover the cost of filing documents.[4] Unfortunately, while the Federal Government and 14 States have already done away with recordation and transfer taxes altogether, with four of them going so far as to pass **Constitutional amendments**[5] against their creation, the District's recordation and transfer taxes have exponentially grown[6] to become a major impediment on the efficient transfer of real property.

BOTH the combined recordation and transfer tax rates of 2.9% and 2.2% are in **EXTREME** excess of any administrative fees associated with the administration of property-ownership records.[7]

In fact, according to Professor Green, there is already a $290 Recorder of Deeds fee that brings in $5 - $9 million dollars a year[8]. We respectfully submit that should more than cover the 18 employees in the Recorder of Deeds office and additional overhead. Those costs are a far cry

[4] *Source:* Sexton, Terri. *Taxing Property Transactions versus Taxing Property Ownership* (Lincoln Institute of Land Policy, Georgia State University, Andrew Young School, April 2008).

[5] Professor Green in his June 3, 2013 oral presentation before the DC Tax Revision Commission questioned the applicability of the trend toward abolishing recordation and transfer taxes with the justification that the states that had done it were "red" states. The four states that passed Constitutional amendments are actually not all "red" states. Oregon elected President Obama by overwhelming majorities in both 2008 and 2012, with six Democrats and only one Republican in their entire Congressional Delegation; Missouri and Montana, while lending marginal victories to Romney in the 2012 Presidential election, elected Claire McKaskill (D) and Jon Tester (D) in their 2012 Senate races, respectively. Oregon, Montana, and Missouri also each have Democratic Governors, leaving only Louisiana as a true "red" state amongst the four. *Sources*: www.house.gov, www.senate.gov, and www.usa.gov.

[6] "Since 1962, there have been several changes to the legislation affecting both the recordation and transfer taxes. In 1976 the tax rate was increased from 0.5% to 1.0% of consideration. In 1989 the tax rate was increased from 1% to 1.1% of consideration….Also, as a result of a shortfall in revenues in the city, the tax rates were temporarily increased that year from 1.1% to 1.5%. This higher rate did not apply to residential properties sold for under $250,000. The Fiscal Year 2005 Budget Support Act of 2004 decreased the DRT and PPT rates from 1.5% back to 1.1% effective October 2004. In 2006 DRT and PPT rates were increased to 1.45% for all commercial properties and for those residential properties sold for $400,000 or more. Residential properties valued at less than $400,000 were still taxed at 1.1%." *Source*: Green, Rodney and Mulusa, Judy. *The Deed Recordation and Real Property Transfer Taxes in the District of Columbia: A Comparative Analysis of Their Rates, Rational, Structure, and Implementation With Policy Options.* (Howard University Department of Economics, May 31, 2013), Page 7.

[7] Residential properties sold for less than $400,000 pay 1.1% rate for both recordation and transfer taxes, while residential properties sold for $400,000 or more and all commercial properties pay a 1.45% rate for both.

[8] "In addition to the DRT and the PTT, the District of Columbia charges a recording fee of $290 for recording deeds, deeds of trust, and other instruments of record." *Source*: Green, R and Mulusa, J. *The Deed Recordation and Real Property Transfer Taxes in the District of Columbia* (May 31, 2013), Page 7.

from the approximately $285 million the District collected in recordation and transfer taxes in 2012[9].

Tax Revision Commission Goal #1: Provide for fairness in apportionment of taxes - NO RECORDATION AND TRANSFER TAXES DO NOT PROVIDE FAIRNESS

To begin, the District's recordation and transfer taxes are characteristically discriminatory because they single out one particular type of asset and activity – the purchase of real estate. How is it fair to punitively tax real estate transactions out of the millions of other transactions that take place in the District every year? Recordation and transfer taxes blatantly discriminate against buying a home versus buying some other type of asset such as stocks, bonds, or other ownership interest purchases. Why are we choosing to discriminate those who want to invest in their family and the District of Columbia?[10]

In fact, these taxes are in direct conflict, to Mayor Williams Housing Task Force Report of 2006 and Mayor Gray's Housing Task Force of Report of 2013 that aim to increase the District's homeownership from its minority status of 41%.[11]

A household that moves frequently, for whatever reason, neither derives additional millions of dollars' worth of benefits nor places additional burdens on public services (except for minimal administrative costs that arguably are already covered by the Recorder of Deeds fee) as

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[9] *Source:* Green, R. and Mulusa, J. *The Deed Recordation and Real Property Transfer Taxes in the District of Columbia* (May 31, 2013).

[10] It should be noted that when properties are sold, the revenue contributions of new property owners are invaluable to the District's economy. Residential buyers invest millions of dollars in retail as they make improvements and decorate their new homes (e.g., sales tax revenue and increase in property value assessment revenue). New families with children are particularly vital with their commitment to schools and public safety. On the flip side, commercial buyers bring in revenue through jobs and stimulating economic development.

[11] *Source:* District Comprehensive Housing Strategy Task Force. *Bridges to Opportunity—A New Housing Strategy for DC.* (2013). Retrieved June 24, 2013 at http://www.taskforce2012.org/Portals/1/docs/Bridges_to_Opportunity-A_New_Housing_Strategy_for_DC-Official_Report.pdf.

compared to someone who does not move at all.[12] Unfairly taxing mobility violates the principle of horizontal equity, which holds that people who are equal should pay similar taxes. [13]

More importantly, from the real estate market perspective, if people cannot move up from starter homes, it actually has negative effects on overall affordable housing perspectives because there will be less affordable housing stock available. Those who have the ability to move from their older properties may also be hesitating because of all the costs associated—stifling the improvement of these properties[14].

Further on a side note of Professor Green's June 3rd testimony before the Commission, the justification that a portion of recordation and transfer taxes are allocated towards the Housing Production Trust Fund (HPTF)[15] is a red herring that should be irrelevant to your economic conversation. The Council can allocate for affordable housing or other priorities in any number of different ways.[16] There is ***no specific reason*** why funding for the Housing Production Fund has to come from this particular revenue stream or tax.

In fact, as Professor Green mentions, DCAR along with other leaders of the affordable housing community, such as the Coalition for Nonprofit and Economic Development, DC Fiscal Policy Institute and others, advocated for eliminating the percentage funding from the Recordation and

[12] Again, movers give the District MORE revenue with the various costs associated, such as moving trucks, inspections, and home improvements.

[13] The National Association of REALTORS® has also done an extensive study on the negative effects of recordation and transfer taxes throughout the nation. available for your review. *Source:* National Association of REALTORS®, *Potential Impacts of Increase in Real Estate Transfer Taxes* (August 2003.) Retrieved June 24, 2013 at http://archive.realtor.org/sites/default/files/retransfertaxes.pdf.

[14] DCAR has heard from members about the detrimental effects of recordation and transfer taxes on sellers because in many instances they would be required put up these additional funds in cash because recordation and transfer taxes in practice are not "full incidence on the buyer" as Professor Green noted in his June 3, 2013 PowerPoint presentation before the Commission. It is generally SPLIT between the buyer and the seller and we are glad to provide you with examples of this. In fact, we have heard from members that it is often the SELLER who has more trouble coming up with these individual funds, causing the manipulation of prices to lower their costs.

[15] As correctly pointed out by the District of Columbia Fiscal Policy Institute, "[s]ignificant portions of Housing Production Trust Fund…[have in previous years] been redirected to other
Purposes," and "[the] HPTF's source of funding is volatile, because the volume of property sales in the city can fluctuate greatly in real estate booms and busts. In bad economic times, taxes dedicated to the HPTF can drop significantly. This makes it difficult for the District to maintain funding for ongoing production of affordable housing." Retrieved June 24, 2013 at http://www.dcfpi.org/wp-content/uploads/2009/03/8-20-12-HPTF-brief.pdf.

[16] It should also be reiterated that only **15%** of recordation and transfer taxes are "earmarked" for the HPTF. Even if this money continues to be earmarked through recordation and transfer taxes, at approximately $43 million for FY 2012, this effectively could be done by "***severely***" decreasing them to a lower rate.

Transfer taxes and advocated for a set significant sum to stabilize the HPTF and not leave it to the volatility of the number transactions from year to year. This would allow affordable housing developers much more predictability.

And although this only happens from time to time, I particularly enjoyed working with Commissioner Lazere and his DC Fiscal Policy Institute colleagues on this issue.

Tax Revision Commission Goal #2: Broaden the tax base—NO
RECORDATION AND TRANSFER TAXES DO NOT BROADEN THE TAX BASE

Next, the Commission's goal of optimal tax policy calls for broad low tax rates to minimize excess burden on specific populations. One of the disadvantages of the property transfer tax is that it is a very narrowly based tax on a single item – the value of property when ownership is transferred from one party to another. Such narrowly based taxes are a fundamental problem because the burden of paying the tax falls on only a small percentage of residents of a jurisdiction, which can dramatically change from year to year. [17]

Each year this tax is paid by randomly self-selected people, who may or may not pay this tax again for the rest of their natural lives. How can we effectively broaden the base if the individuals paying from year to year are for the most part completely different people?

Tax Revision Commission Goal #3: Make the District's tax policy more competitive with surrounding jurisdictions—NO
RECORDATION AND TRANSFER TAXES ARE IN NO WAY COMPETITIVE

With regards to regional competitiveness, DC maintains elevated recordation and transfer tax rates relative to most surrounding communities. Fairfax and Prince William counties, which have

[17] For a more comprehensive overview of how recordation and transfer taxes are narrowly based taxes resulting in "deadweight loss of taxation", please refer to National Association of REALTORS'® report, *Potential Impacts of Increase in Real Estate Transfer Taxes* at http://archive.realtor.org/sites/default/files/retransfertaxes.pdf.

recordation and transfer taxes at a *FRACTION* of the District's, are very affluent overall. It is no coincidence these jurisdictions have not imposed substantial costs upon mobility.

And any relative comparison to Maryland, one must first take into account Maryland first-time homebuyer tax reduction and Montgomery County's exemption of the first $50,000 for recordation taxes. Even then, only Prince George's County rate for properties under $400,000 is higher than the District. And quite frankly, ladies and gentleman, we are not sure from an economic competiveness perspective that DC wants to encourage a race to the highest rate with Prince George's County.

Relative to other major US cities, ***only one city in the entire country***, New York City, with its abundance of global financiers, is associated with higher recordation and transfer tax rates. Again, DCAR surely hopes that being the second highest jurisdiction in the entire country is not what the Commission aspires to.

We understand there are many factors that determine the jurisdictions to which residents will move, but you have heard innumerable times that taxes play a significant part in that decision. **ANY** increase in recordation and transfer tax rates from this point forward would prove counterproductive by limiting homeownership gains, reducing mobility, thereby hindering Mayor Gray's Comprehensive Housing Strategy Task Force goal of increasing homeownership by 3%.[18]

Additionally, any action that would cause an increase in the commercial recordation and transfer tax would be unconscionable. [19] *It is unjust public policy to continuously use the commercial real estate market as a limitless ATM for politically savvy pet projects*. Moreover, the justification

[18] *Source:* District Comprehensive Housing Strategy Task Force. *Bridges to Opportunity—A New Housing Strategy for DC (*2013).

[19] "[I]t is unlikely that a **[NEARLY 70%] tax increase** (*emphasis added***)** on [commercial rates for high-end properties] would damage the local economy in any significant way." *Source:* Green, R. and Mulusa, J. *The Deed Recordation and Real Property Transfer Taxes in the District of Columbia* (May 31, 2013), Page 4. This would be a ***70% tax increase*** and at some point, as correctly pointed out by Commissioner Ein at the June 3, 2013 Tax Revision Commission meeting, investors ***need to see a return*** on their investments or they will retreat to the many other rapidly growing cities in our country—there are only so many law firms that can locate to the District.

that these taxes are exported is in opposition to the District's goal bringing in global businesses.[20] Further, it completely disregards the long arc of the District's history when attracting business in general to the District was much more challenging than it is in this moment in time.

Overall, raising the cost of purchasing commercial property directly translates into higher rents, which leads to offices searching in Crystal City and beyond. Inducing even a few commercial users to locate their business elsewhere has a direct negative effect on employment.

Tax Revision Commission Goal #4: Modernize, simplify, and increase transparency in the District's code—NO
RECORDATION AND TRANSFER TAXES ARE INHERENTLY NOT MODERN, SIMPLE, OR TRANSPARENT – THEY ARE VOLATILE

We have discussed the history of recordation and transfer taxes and Dianah Shaw[21] has described how not simple the tax is to individual buyers. But just to further clarify any confusion, transfer or recordation taxes differ from ordinary property taxes in that the transfer or recordation tax is a one-time payment ***made at the transfer of the land***. It is a misconception that these taxes are amortized into the mortgage or capitalized into to the price of the property.[22]

This difference significantly affects the stability of tax revenue—transactions ***actually need to transpire*** for a jurisdiction to collect transfer or recordation taxes. Excessive dependence on these as a significant share of government revenue is risky given the ups and downs of real estate markets and transactions. Conventional property tax revenue, however, tends to be more stable

[20] *See* all of the economic goals in the *Letter from Mayor Vincent Gray* on inaugural D.C. Tax Revision Commission meeting (Aug. 3, 2012). Retrieved June 24, 2013 at http://media.wix.com/ugd/ddda66_f5ece23abc9ae12d4f44e34bc9952b61.pdf.

[21] Dianah Shaw presented individual testimony before the Commission as a real estate professional.

[22] Professors Green and Mulusa state that "[I]n housing markets generally, the taxes are generally capitalized in the price of the property, which means that the net price received by the seller will generally be reduced by the full amount of the tax." *Source*: Green, R. and Mulusa, J. *The Deed Recordation and Real Property Transfer Taxes in the District of Columbia* (May 31, 2013), Page 3. DCAR argues that this assertion is incorrect. After speaking to numerous brokers, agents, and lenders, we have overwhelmingly heard that the recordation and transfer taxes are not simply capitalized in the mortgage because they cannot simply be calculated into the principal loan—at the very least they interfere with the proper calculation of down payment percentages. DCAR is glad to provide additional information from practitioners on this issue to the Commission.

over time since property continues to be owned (by some party) even during periods of downturn.

Professor Green's and Mulusa's study even recognizes the volatility of recordation and transfer tax collections. Between 2004 and 2009, the percentage of District of Columbia tax collections comprised by recordation and transfer revenues fell by more than half (8.6% to 3.6%)—bouncing from:

$105 million in 2000 to

$379 million at its height in 2007 to

$285 million in 2012 doesn't seem to be in the best interest of the District.[23].

At the very least decreases recordation and transfer tax could decrease this volatility and make tax revenues more stable.

Tax Revision Commission Goal #5: Encourage business growth and job creation—NO RECORDATION AND TRANSFER TAXES DO NOT HELP DC BUSINESS GROWTH

Finally, recordation and transfer taxes negatively impacts transactional volume by much more than what Professor Green's and Mulusa's report purports[24]. They do not take into consideration the resulting losses of less income to **title companies, brokers, appraisers, inspectors and others who participate in the transactional supply chain**.

Moreover, to the extent that new owners would have invested additional monies into their properties, the District of Columbia also forfeits higher future property tax collections since assessments will not increase as rapidly as they otherwise would. There would also be a

[23] Professors Green and Mulusa acknowledge numerous times in their study that DC's recordation and transfer tax revenues are volatile both absolutely and as a share of the District's tax revenue (from 3.5% to 8.6% over the past 13 years). *Source:* Green, R. and Mulusa, J. *The Deed Recordation and Real Property Transfer Taxes in the District of Columbia* (May 31, 2013) Pages 8-9. DCAR will be glad to provide additional examples throughout the country from the states that actually still employ the use of these taxes.

[24] "In the final analysis, recordation and transfer taxes are modest one-time levies. Adjustments in them will only have modest impacts on the economic development of the city." *Source:* Green, R. and Mulusa, J. *The Deed Recordation and Real Property Transfer Taxes in the District of Columbia* (May 31, 2013) Page 33.

corresponding loss in income tax collections due to the loss of business volume among **surveyors, engineers, architects, construction workers, interior designers among others.**

Simply put, every dollar spent on recordation and transfer taxes is potentially one less dollar of improvement to the home; one less dollar spent at Frager's, one less dollar at the design stores on 14^{th} Street.

Conclusion

At the June 3, 2013 Tax Revision Commission meeting, Commissioner Ein in the first question to Professor Green asked, "What is the purpose of this tax?" Professor Green answered, "TO RAISE REVENUE".

Commissioners, DCAR respectfully proffers to you that is not a fair or just answer for this Commission to accept.

The efficient transfer of real property is at the heart of District real estate. Excessive recordation and transfer taxes that negatively impact housing purchases and economic development have no place in the District's revenue stream. All these excessive taxes seem to do is reinforce a perception and precedent of the District haphazardly taxing anything that can generate revenue.

We recognize the political reality of taxing someone when they are arguably at one of their happiest time of their life. Families often choose to ignore or swallow the tax because they can't wait to get into their property and are vulnerable to be nickel and dimed at settlement. And once they are in their property they may forget the taxes they paid at closing because they are busy rearranging furniture, meeting the neighbors, and getting ready for their next chapter of life. Maybe that's what Professor Green meant by "*modest*" and "*minimal*"? You swallow this tax medicine, move on and generally don't complain because you are happy to be in your new home.

But, just because it's a convenient, easy tax for the District to impose, DOES NOT make right or equitable.

The fact is you, DC Tax Revision Commissioners, can make a difference here and do the right thing.

In your recommendations, DCAR encourages you to take a stand, and recommend abolishing or significantly rolling back real property deed recordation and transfer taxes. ***Taking into account all of the above arguments, this could/should be one of the easiest recommendations you can make.***

Thank you for taking the time and allowing us this opportunity to present testimony. We will be glad to provide any supplementary information on any of the issues we have discussed.