D.C. Tax Revision Commission Policy Options

Policy Option #38: Reduce the Tax Rate Gap Between Commercial and Residential Property

MEMORANDUM

Proposal: Lower the property tax rates on commercial property and raise the rate on residential
Tax Type: Property
Origin: Nicola Whiteman/ Daphne Kenyon/Public
Commission Goal: Competition and business growth

Current Law

Real property in D.C. is separated into four classes for taxation:

1) Residential property
2) Commercial property
3) Vacant buildings
4) Blighted buildings

Residential property is taxed at $0.85 per $100 of assessed value. If total property tax collections from residential properties are projected to grow by more than 7% in the upcoming budget year then the rate is lowered so that total revenue remains below the threshold.

The tax rate for commercial property is graduated: the first $3 million of assessed value is taxed at $1.65 per $100 of value and any additional amount is taxed at $1.85 per $100. If commercial property tax collections are projected to grow by more than 10% in the upcoming budget year then the rate on assessed value below $3 million is lowered so that total revenue remains below the 10% growth rate threshold.

Proposed Change

Decrease the tax rates on commercial property and increase the rate on residential property. Please see “Possible Rates and Revenue Estimates” below for a detailed description of proposed changes to the rate structure.

Reason for Change

D.C. has the highest commercial property tax rate ($1.65/$1.85 per $100) in the Washington region. Rates vary among localities—property taxes are generally local and not state taxes—but neighboring Maryland jurisdictions tax commercial property at roughly $1.22 to $1.42 per $100 of assessed value while jurisdiction in Virginia tax property at just over $1 per $100 of value. This possibly gives companies looking to locate in the region an incentive to purchase property outside of D.C.

Meanwhile, D.C. has the lowest residential property tax rate ($0.85 per $100) in the Washington region.

The tax rate for local jurisdictions in the Maryland suburbs range from $1.068 to $2.921 per $100 of assessed value while in Virginia the rates range from $0.958 to $1.213 per $100.
D.C. could lower its commercial property tax rate, which might attract more businesses, and offset some of the lost revenue by raising the residential tax rate. Notably, the residential rate can be raised and still be comparable to other local jurisdictions.

Pros

- Could make D.C. more competitive in attracting businesses to the city, possibly spurring business growth and job creation.
- Shifting the two rates closer to each other could mitigate any revenue loss from lowering the rate on commercial property.
- D.C. could raise residential property tax rates and still remain lower or equal with neighboring jurisdictions. This limits any tax incentive for residents to leave D.C. or new residents to choose a neighboring jurisdiction over D.C.

Cons

- Would increase residents' property tax payments.
- The high tax rate on commercial property helps "export" D.C.'s tax burden. The high rate was established in part to offset the tax revenue D.C. is not legally allowed to collect from the income of non-residents who work in D.C. Lowering the commercial property tax rate and increasing the residential property tax rate would shift the tax burden back to the city's residents.
- There are other ways to finance a reduction in the commercial property tax rate without increasing the tax burden on residents. Specifically, a lower commercial rate could be funded through broadening the tax base: removing or limiting property tax expenditures (such as exemptions and abatements).

Possible Rates and Revenue Estimates

The Office of Revenue Analysis (ORA) estimates that in the first year of implementation the following property tax rates would be revenue neutral (i.e., raise as much tax revenue as the current tax rates).

Residential (per $100)	Commercial (per $100)
$0.95	$1.82
$1.05	$1.77
$1.10	$1.74
$1.51	$1.51

Please note: For simplicity, these estimates do not include homestead property or and Class 2 properties with assessed value less than $3 million. These properties account for 25% of all property tax revenue.