D.C. Tax Revision Commission

MEETING MINUTES

Subject:	D.C. Tax Revision Commission Meeting
Date:	Oct. 30, 2013
Time:	3:00 p.m. to 6:00 p.m.
Location:	Room W250 1101 4th Street, S.W. Washington, D.C. 20024

Members Present:

Anthony Williams	Mark Ein
Teresa Hinze	Kim Rueben
Fitzroy Lee	Ed Lazere
Catherine Collins	Stefan Tucker
Pauline Schneider	

Staff:

Gerry Widdicombe	Steven M. Rosenthal
Ashley Lee	Richard C. Auxier
Elisha Gaston	

I. Call to Order (Anthony Williams)

Mr. Anthony Williams, the chair of the D.C. Tax Revision Commission (the "Commission"), called the meeting to order at 3:23 p.m., and began by thanking the Office of the Chief Financial Officer (OCFO), the Office of Revenue Analysis (ORA), and the Office of Tax and Revenue (OTR) for their exceptional contributions to the Commission's work. He announced that electronic copies of the materials for the meeting were available on the Commission's website, and invited members to consult Ms. Ashley Lee for hard copies. Mr. Williams notified those present that the Commission's next meeting would be held on Nov. 4, 2013, from 3 p.m. to 6 p.m., in the same room (Room W250 1101 4th Street, S.W., D.C.), and that the Nov. 4 meeting would focus on tax administration.

II. Distribution of Minutes

Mr. Williams asked if there was a motion for approval of the meeting minutes from Sept. 30 and Oct. 7. Mr. Ed Lazere made a motion to approve and Ms. Kim Reuben seconded his motion. Mr. Williams announced that the minutes were approved without objection. Mr. Williams noted that members would have an opportunity to review the minutes from the Commission's Oct. 21, 2013 at a later date.

III. Discussion of Commission Schedule and Deliberation Process

Mr. Williams briefly explained that the Commission's deliberations would focus on real property taxes. He then turned the floor over to Mr. Gerry Widdicombe to brief the room on the Commission's upcoming schedule. Mr. Widdicombe announced that the tax policy options being considered would be presented by two members of the Commission's staff: Mr. Steven Rosenthal and Mr. Richard Auxier. He explained that the Commission would not be voting during the meeting, and that the Commission would revisit some issues at a catch-all deliberation meeting on November 18, 2013. He then asked Mr. Rosenthal to begin the deliberations.

IV. Deliberations: Property Taxes

Mr. Rosenthal began by pointing out that D.C. relies heavily on business taxes for revenue, and that commercial real property tax revenue is far larger than the revenue generated from business franchise taxes. He explained that D.C. taxes the first $3 million of commercial property value at $1.65 per $100 of assessed value and every additional dollar of value at $1.85 per $100. He noted that D.C.'s commercial property tax rate is high relative to its neighbors. In contrast, D.C.'s residential property tax rates ($1.65 per $100 of assessed value) are relatively low. Mr. Rosenthal commented briefly that vacant and blighted properties re taxed at a much higher rate in order to encourage use for better purposes, although the actual tax collection rate from abandoning owners was very low. Mr. Rosenthal announced that, as in previous meetings, proposals would be presented in groups of related policy options.

Options No. 38, No. 39 and No. 40: Adjust Property Tax Rates

Mr. Rosenthal explained that option No. 38 reduces the tax rate on commercial and increases it on residential property, option No. 39 lowers the rate on commercial property (with no corresponding change to residential property), and option No. 40 taxes all commercial property at the same rate ($1.85 per $100) and creates a tax credit for small business.

Mr. Rosenthal noted that the multiple options for rate changes in No. 38 were all revenue neutral—the revenue increase in the residential tax hike offsets the decrease in the commercial rate cut. He said such changes would bring D.C.'s tax rates more in line with surrounding jurisdictions. But he also mentioned that D.C.'s high commercial tax rates reflect the reality that D.C. has very valuable commercial property.

Ms. Reuben asked what the rental payment is per square foot in D.C., and how it is affected by the proposed rate changes. Mr. Widdicombe answered that the rate in D.C. is about $50 per square foot, compared to $40 to $45 in neighboring jurisdictions, and added that a lot of the rate differential is due to varying tax rates. He pointed out that higher tax rates on commercial property help reduce the tax burden on residents by shifting it business and non-residents.

Mr. Stefan Tucker noted that commercial property tax rate in Tysons (a locality in Virginia) is not very different from the rate in D.C. He said that high property values in D.C. are responsible for the difference in total tax burdens on commercial properties. As such, he did not see a reason to lower rates.

Ms. Reuben commented that D.C.'s property taxes are high to compensate for D.C.'s inability to tax income at the source. She suggested that perhaps instituting a local services tax on employers (as discussed in the Oct. 21 meeting) may balance any cuts to the commercial rate.

Mr. Tucker responded that the large amount of exempt property in D.C. is what drives the higher commercial property tax rates and not D.C.'s inability to tax non-resident income.

Ms. Catherine Collins noted that residents pay the property tax and the income tax, and that she was uncomfortable with considering the option to raise the residential property tax rate.

Ms. Reuben responded that the Commission might consider raising the property tax in order to pay for cuts to the income tax.

Mr. Fitzroy Lee noted that D.C.'s nominal property tax rates are not the same as effective tax rates. Properties in D.C. are eligible for numerous relief options that decrease tax burdens.

Mr. Ed Lazere added that D.C. has a law that triggers reductions in the property tax rates if total revenues grow at excessive levels. He advocated removing these triggers.

Mr. Anthony Williams stated that he had no desire to raise taxes on residential property because this would remove a competitive advantage for the city.

Ms. Pauline Schneider noted that while the cost of taxes on business property can be spread over several years, residents must pay the tax with annual income. She added that D.C. is currently doing pretty well in attracting business and saw little need to lower commercial tax rates.

Mr. Lazere added that D.C.'s commercial vacancy rate is consistently lower than in the surrounding jurisdictions in Maryland and Virginia.

Mr. Rosenthal explained that option No. 40 would apply one tax rate ($1.85 per $100) to all commercial property, and assist small businesses with a tax credit. He added that this would target tax relief to small businesses rather than the current policy of providing relief to all property owners via the lower rate on the first $3 million of property.

Mr. Lazere commented that current two-tiered rate is not well targeted; providing benefits to all property owners instead of small businesses. He argued that providing a tax credit based on gross receipts would be more administratively complex but better policy. He also noted that a targeted credit could also benefit businesses that rented instead of owning property. Mr. Lazere said a related proposal is in current D.C. Council legislation proposed by Councilmember Tommy Wells.

Ms. Schneider asked whether the Commission should weigh in on pending legislation.

Ms. Reuben agreed that helping small businesses that rent was a worthy idea.

Options No.41: Eliminate the "vacant" and "blighted" property classifications or combine them.

Mr. Rosenthal said option No. 41 would eliminate the "vacant" and "blighted" property classifications—along with the higher tax rates that apply to such properties—or combine them and apply one rate ($5, $7.50, or $10 per $100 of assessed value). He explained that these proposed changes would eliminate some of the administrative complexity involved in identifying and taxing such properties.

Ms. Schneider said that she understood why the Commission might want to do impose higher rates on vacant and blighted properties, but questioned whether it is worth the trouble given that it raises very little revenue. She asked whether vacant or blighted properties typically get sold if the tax liability is never satisfied.

Mr. Auxier said that many properties are not purchased because the owners are in financial trouble, and the cost of the accumulating tax bill makes the cost prohibitive for new buyers.

Mr. Williams said the higher rates were created when blighted and abandoned property were acute problems for the city. Since their implementation, however, D.C. has seen substantial economic growth and this sort of tax-based motivation may no longer be necessary.

Mr. Tucker said he still saw value in the special tax rates. He also asked how liens are administered, and more specifically, inquired about how a vacant building is defined.

Mr. Jed Ross, an employee of the D.C. Department of Consumer and Regulatory Affairs (DCRA) introduced himself and explained that he was previously in charge of overseeing all vacant and blighted properties in D.C. He explained that taxpayers are required to register properties as vacant if they are vacant for over 30 days. He added that people do not typically follow this rule, but an enforcement mechanism is in place. Mr. Ross also explained that taxpayers typically appeal to DCRA for an opportunity to use the money to get the classification overturned rather than pay tax.

Ms. Reuben asked whether taxpayer request are usually granted.

Mr. Ross explained that requests are typically granted because owners have time to fix their properties.

Mr. Widdicombe asked for an explanation of what a blighted property is.

Mr. Ross answered that a boarded-up building is prima facie evidence that a property is blighted. He noted that there are no exemptions for blighted properties, while some exist for vacant properties.

Option No. 42: Provide "Circuit Breaker" Relief via the Property Tax Instead of the Individual Income Tax

Mr. Rosenthal explained that option No. 42 would change how D.C. provides property tax relief to low-income residents. Currently, such tax relief (known as a "circuit breaker" program) is delivered through the individual income tax: qualified low-income residents with high property tax payments get an income tax credit, known as Schedule H. Under the proposal, qualified residents would instead receive a reduction in their property tax payment. Mr. Rosenthal noted this change would provide more direct tax relief but also would not be available to renters (who benefit from the current program). He then stated that the Commission's subcommittee, created to examine all low-income tax relief programs in a more holistic manner, was studying the issue and asked Ms. Reuben to comment on the program.

Ms. Reuben said the subcommittee is considering providing relief through a combined approach that included a property tax credit for property owners and an income tax credit for renters

Ms. Collins added that it might make more sense for the Commission t described the credit to renters as a "renter's credit" rather than a property tax credit. She noted that this would be a way of giving people some relief who can't afford to live in the city.

Ms. Hinze asked if anyone could weigh in on whether providing relief via the property tax would simplify administration or not. Mr. Rosenthal suggested that the Commission could get Mr. Steve Cordi to address administration during the Commission's next meeting.

Mr. Lazere noted that a circuit breaker program is a way to connect property taxes to income (and therefore ability to pay). He voiced concern that it is not clear how to implement this measure, and said that there is no easy answer.

Mr. Rosenthal expressed hope that the subcommittee would be able to address administrative concerns at a future meeting, and said that the Commission would ask Mr. Steve Cordi to address this as well.

Option No. 43: Eliminate the Senior Tax Credit and Option No. 44 Eliminate or Reduce the Homestead Deduction.

Mr. Rosenthal noted that D.C. offers a generous senior property tax credit to residents ages 65 and older who have an adjusted gross income below $125,000. He explained that D.C. also offers a very generous homestead deduction, and that he coupled options No. 43 and 44 together because they both shrink the property tax base.

Mr. Rosenthal pointed out that Virginia and Maryland also provide property tax relief to seniors but are not as generous as D.C. He also reported that neither state provides a homestead deduction.

Ms. Reuben commented that since D.C. recently increased the income threshold on the senior tax credit that it would be difficult to convince the Council to now eliminate it. She added that the homestead deduction benefits only residents who are paying income taxes. Therefore, eliminating the deduction to pay for a lower tax rate (that would benefit all property owners) might shift the tax burden to residents.

Mr. Widdicome stated that of approximately 145,000 homes in D.C., 87,000 receive the homestead deduction while 58,000 do not.

Mr. Tucker asked whether D.C. has a way of verifying residency claims for those claiming the homestead deduction.

Mr. Steve Cordi, the Deputy CFO, introduced himself and explained that D.C. sends out inquiries to residents, and that those who fail to respond are not eligible for the homestead deduction.

Mr. Tucker said that New York assumes that those who purchase homes are New York are residents and forces them to prove that they are not. He said D.C. should consider using such an assumption in an effort to collect more income taxes.

Ms. Hinze asked for a description of the legislation proposed by Councilmember Anita Bonds that also attempts to provide property tax relief to seniors. Mr. Lazere explained that the new legislation would eliminate all property tax payments for residents ages 75 and older, who have lived in the city for 25 years and earn less than $60,000 in income.

Option No. 45: Introduce "Equal Yield Budgeting" for Commercial Property

Mr. Rosenthal explained that D.C.'s current commercial property tax revenues are not allowed to grow by more than 10% annually. If the 10% threshold is surpassed then the tax rate on the first $3 million of property (currently $1.65 per $100) is lowered until the revenue threshold is reached. He explained that option No. 45 extends that concept so that in years when collections are projected to grow by more than 3%, tax rates would be lowered to meet a new 3% threshold. Additionally, in years when collections are projected to decline by more than 3%, tax rates would be increased to limit the commercial tax revenue decline to established threshold.

Mr. Widdicombe said that although D.C. is currently doing well, establishing such benchmarks is something that other cities do to protect from big drops in revenue when commercial property assessments substantially decrease.

Mr. Lazere stated that, from a policy perspective, D.C. should not cap budget growth at 3% a year because service costs are rising at a rate of much higher than 3% a year. He further argued that capping revenue was outside of the Commission's agenda. Mr. Lazere said elected officials can decide to lower rates when necessary and that there is no reason to put a cap on such a strong base of tax revenue.

Ms. Reuben said that 3% is way too low of a target. She suggested 7%, which is the current growth threshold for D.C.'s residential property.

Mr. Williams stated that it is the Commission's job to recommend the overall level of revenue that D.C. should aim to collect, and to determine the structure of that tax system. He disagreed with the idea that expenditures require exponential growth and said that legislatures need to be reined in to curb future spending. He added that revenue constraints force government to function more efficiently, and that without constraint the government can overburden their communities.

Ms. Collins suggested that D.C. could take a middle road by providing taxpayers with a proof of tax notifications, showing what their rates would be in order to generate the same amount of revenue as last year, and then in order to increase the rate beyond that limit, D.C. would have to take some sort of proactive measures.

Mr. Lazere said that he appreciates Mr. Williams' suggestions, but that the Commission's goal is to provide revenue-neutral recommendations and not comment on the appropriate size of government. He also asked why commercial property should be singled out for a cap. Why not cap individual income tax revenue?

Ms. Reuben disagreed with Mr. Lazere and said that a way of keeping assessment from automatically translating into revenues is not necessarily a bad thing.

Mr. Lazere pointed out that virtually every tax rate in city had been reduced recently, with the only increase being in hotel taxes for the convention center, and that D.C.'s total taxes are lower than they were 15 years ago.

Mr. Williams commented that Mr. Lazere's point is well articulated, but that he saw merit in tax revenue restrains.

Option No. 46: Tax Land and Buildings at Different Rates

Mr. Rosenthal explained that the next option would collect the same amount of tax revenue as current policy but tax land at a higher rate than buildings. He said taxing buildings at a lower rate would incent owners to enhance their property value through development.

Ms. Scheider asked whether it isn't implicit now that land gets valued at one level and property at another level, and whether D.C. wasn't essentially doing this already. Mr. Widdicombe responded that while both land and buildings are assessed that the total is the only thing people currently care about. Splitting the rate could affect behavior.

Mr. Tucker said that the current system is simple and straight forward and warned against creating new administrative problems.

Option No. 47-49: Residential Property Assessment Limitations

Mr. Rosenthal explained that these options pertain to D.C.'s assessment limitation. Currently, if a taxpayer qualifies for a homestead deduction then her annual assessment cannot rise by more than 10%. Option No. 47 would eliminate the limitation. In contrast, option No. 48 would further restrict assessment growth to 5% annually. Option No. 49 would increase the minimum assessment from 40% to 50% (or higher) of market value.

Mr. Lazere commented that he was not originally a fan of assessment limitations, but noted that limitations provide protection for taxpayers when property values are rising but incomes are not. He added that he was not sure whether D.C. should decrease the assessment limitation to 5%, because the average home in D.C. is already assessed at approximately three-fourths of market value. He stated that he would he would be okay with raising the floor of taxable assessment to at least 60% of market value.

Ms. Reuben suggested that if the Commission decides to raise the assessment limit, it should consider doing so over a span of time to prevent a substantial one-year increase in property taxes.

Option No. 50: Eliminate Miscellaneous Property Tax Exemptions

Mr. Rosenthal explained that D.C. has numerous properties that are exempt from taxes. Option No. 50 would eliminate these exemptions for property labeled as "miscellaneous" by ORA that are also office buildings valued at more than $3 million. There are currently 21 of these buildings.

Mr. Williams noted that many organizations receiving property tax exemptions get such a subsidy because D.C. believes they provide value to the city. He said removing individual exemptions would be problematic.

Mr. Tucker said that when these exempt properties expand they take away commercial, and therefore taxable, property from the city.

Ms. Hinze asked why only property valued at more than $3 million should be considered.

Ms. Collins asked how accurate assessments are on tax-exempt property. There was general agreement that these estimates are not precise.

Option No. 51: Create a PILOT Program for Tax Exempt Properties

Mr. Rosenthal explained that option No. 51 establishes a payment in lieu of taxes (PILOT) program for certain organizations that do not currently pay property taxes. The payment would be voluntary and negotiated between property owners and the D.C. government. The payment is made to offset the burden these properties put on city services.

Ms. Collins commented that this creates transparency problems.

Ms. Schneider said that the problem is that the payment would not be uniform.

Ms. Reuben said a PILOT would be a hard sell in D.C. given that tax revenues are currently doing well. She said only organizations looking to expand would need to make deals with D.C.

Mr. Tucker said that he prefers that these universities pay taxes, but in the absence of the ability to impose a tax that these entities should bare some burden. He said a PILOT is probably the best option for D.C. to recoup some of this tax revenue.

Mr. Lazere agreed that this idea makes sense because many major institutions with valuable property currently pay nothing in property taxes. He added that a PILOT would extract some fraction of what they would be paying if eligible for property taxes. However, he noted that another option was creating a per-employee tax, as discussed at a previous meeting.

Option No. 52: Establish Criteria for Property Tax Exemptions, Option No. 53: Regularly Review and Sunset Legislated Tax Expenditures, Option No. 54: Improve Criteria to Grant Tax Abatements

Mr. Rosenthal explained that these three proposals are process options: ways to establish criteria for tax property expenditures. He asked how much the commissioners wanted to weigh in on process.

Ms. Schneider said that regular review of tax exemptions is a good idea worth pursuing.

Ms. Reuben agreed.

Ms. Collins said testing expenditures before implementation and reviewing results after are both good ideas. She said organizations should be forced to justify their expenditures.

Mr. Lazere said that D.C. lags behind almost every other state in its review process, and that the Commission should review all of D.C.'s tax expenditures and not just property tax expenditures.

Mr. Auxier said that, while the options before the Commission were specific to the property tax, that a larger policy option to review all expenditures—provided by the Pew Charitable Trusts—would be included in a future meeting.

Mr. Williams commended Pew for their report, but added that some of D.C. recent economic growth is the result of aggressive public policies such as tax expenditures. He said there is a cost in excessive review that should not be ignored.

While there was some agreement that creating criteria for expenditures was a good idea, that D.C.'s current "but for" test on property tax abatements (option No. 54) is doing a good job and does not need to be changed at this time.

Option No. 55: Increase the Deed Tax Rate for Commercial Property from 2.9% to 4%, Option No. 56: Eliminate Deed Taxes or Reduce the Combined Rate to 0.433%, Option No. 57: Eliminate Notch in Deed Tax Rate by Using Marginal Rates, Option No. 58: Create More Brackets With Marginal Rates.

Mr. Rosenthal noted that these options were complied with the great and much appreciated assistance of Jason Juffras, a fiscal analysis with ORA. Mr. Rosenthal said that D.C. has both a deed recordation and a deed transfer tax that it imposes when taxable properties are sold or transferred, and that the deed transfer tax must also be paid on the increased value when commercial property is refinanced.

Mr. Rosenthal noted that the rate for residential properties under $400,000 is 2.2% of market value, but that the rate increases to 2.9% if value exceeds $400,000, creating a "notch" or "cliff" effect. All commercial property is taxed at 2.9%.

Ms. Schneider said that some of the revenue generated from these taxes goes to debt service, and therefore the Commission should be very careful with any possible change.

Mr. Ein said that these taxes are rolled into a property's value. Therefore, these taxes do not affect decisions to buy or sell.

Mr. Tucker said that he has never seen a transfer tax or recordation fee affect a transaction. He added that it just affects the price, and suggested that the Commission not recommend changes to these taxes.

Ms. Reuben noted that the "notch" is a problem worth addressing.

Option No. 59: Raise the Exemption from 120% of HUD Low-Income Standard to 200% and Option No. 60: Waive Deed Taxes for First Time Homebuyers

Mr. Rosenthal explained that these options would increase an exemption from these taxes for low income households and waive them for first-time homebuyers.

Mr. Ein said that these options may not be in line with the goals of the Commission.

Ms. Reuben said the she would be happy if the Commission were to leave these taxes aside for now.

V. Commission Business

Mr. Williams thanked all present for their participation.

Mr. Widdicome announced that the subcommittee on low-income tax relief met prior to the public meeting. He also announced that the Commission would be hearing from tax administration experts at its next meeting. He added that the Commission would hold a public hearing on Nov. 12.

VI. Adjournment

Mr. Williams announced that the meeting was adjourned at 5:45 p.m.