Submission to Tax Revision Commission: A plan to make DC's tax structure progressive and more capable of sustainable funding of essential needs in DC's budget

Introduction

As a result of a significant revenue surplus, funding of low-income programs was partially restored after a five year period with cumulative cuts of more than $200 million (http://afsc.org/resource/report-state-human-rights-dc). Nevertheless, several programs remain severely underfunded, such as TANF with its benefit level below poverty. Increasing TANF benefit to above the poverty level, combined with complementary programs such as literacy, substance abuse and workforce development, would significantly reduce our shockingly high child poverty rate in DC (http://www.childrensdefense.org/newsroom/cdf-in-the-news/press-releases/2012/child-poverty-remains-high.html). DC has one of the highest income gaps between rich and poor in the nation (http://www.dcfpi.org/a-big-gap-income-inequality-in-the-district-remains-one-of-the-highest-in-the-nation). There is very strong evidence for income inequality as a prime driver of bad health and a lower quality of life for the whole community (e.g., Richard Wilkinson and Kate Pickett, "The Spirit Level: Why Equality is Better for Everyone" Penguin Books, 2010). A progressive tax structure would be an important step towards reducing income inequality in the District by providing tax relief for our majority, now suffering from income insecurity, as well as generating badly needed revenue with a modest increase in the tax rate of our wealthiest residents.

Restructuring DC Taxes: Principal Objectives

1) Make the District's tax structure for individuals and families fair, that is *progressive,* with tax rates increasing with income level for a given family size, so that the tax burden falls on those most able to bear it.

A fairer tax structure will require giving needed tax relief to the low to middle income 80% of DC individuals and families while getting the best-off District residents paying their fair share of city taxes. Once the tax structure is made progressive, tax rates for all residents can be lowered with the expansion of the tax base resulting from a decrease in income inequality and increase in mean income. Reducing income inequality and the improvement of quality of life particularly for our now economically-stressed majority would empower the struggle for DC Statehood. Achieving DC Statehood would generate a very significant increase in revenue from reciprocal taxation agreements with surrounding jurisdictions, with 70% of our non-resident workforce subject to income taxation.

2) Make the city's tax system *sustainable,* that is insuring it can generate badly needed revenue targeted to funding essential programs, such as affordable housing and childcare, in the District budget.

3) Make the tax system and budget more *transparent and accountable,* by engaging in a detailed review of tax exemptions and abatements for commercial and non-profit properties. Taxpayers and elected officials must be able to evaluate the community benefits (if any) from these tax giveaways to big developers and other corporate interests.

DC's Tax Structure is Regressive above $50.2K Average Family Income

An updated 2013 Who Pays? for DC (ITEP), which includes the funding of expansion of Schedule H as well as the change of sales tax rate to 5.75% shows that the top 1% bracket pays a lower rate of DC taxes, 6.2% of family income (taking into account the federal deduction offset) than all even the poorest residents, averaging $12.6 K (6.3%), with regressivity above a $50.2K average family income (having the highest tax rate, 10.8%) (see attached, Graph A, 1st sheet labeled "Final 2_post2013"). Even without the federal deduction offset, regressivity again sets in above $50.2K average income. In 2011, the most recent data available, DC returns with adjusted gross incomes of $1 million and above had a taxable income of $3.3 billion (those returns with adjusted gross incomes of $100K per year and above had a taxable income of $12.4 billion, 67% of the DC total, while making up 22% of all returns (IRS data, http://www.irs.gov/uac/SOI-Tax-Stats---Historic-Table-2).

Our Steadily Progressive Alternative

1) *Tax reform for DC's families*

A key feature of Our Steadily Progressive Alternative (SPA) is the consistent increase of overall DC tax rate with family income before the federal deduction offset. SPA includes the following provisions:

a) The DC income tax structure is based on a flat percentage of the federal income tax payment using the present federal tax structure, thereby simplifying the payment process and increasing fairness. The DC Earned Income Tax Credit is retained.

b) The Schedule H low-income property tax credit in the DC income tax schedule is expanded to generate greater benefit for middle-income families and individuals.

c) A built-in deduction for sales/excise taxes, the most regressive part of the tax burden, is included in the DC income tax schedule, insuring an overall progressive structure for DC residents. Sales tax revenue from non-residents such as commuters and tourists would not be reduced, since they do not pay DC income tax.

The SPA simulation for the October 2009 DC Tax Structure includes these provisions (see attached, Graph B).

Details of this simulation:

1) 45% of the federal income tax payment is used.

2) Schedule H:

- The income limit for eligibility is raised to $70,000,

- The maximum credit is raised to $3,000.

3) This package is estimated to increase D.C. tax revenues by at least $116 million annually.

Once implemented, the proposed DC Tax Structure would reduce income tax payments for most DC families and individuals.

Rather than going into the General Fund, revenue enhancements shall be targeted to underfunded essential programs in the DC Budget. Specific funding should be determined each budget cycle in consultation with Fair Budget Coalition, DC Jobs with Justice, Empower DC, and other groups that truly serve the interests of the majority of our residents.

Recognizing potential changes in the federal income tax structure in future years, the legislation implementing a steadily progressive DC structure should include provision for readjusting the percentage of federal income tax payment. Other adjustments to insure progressivity and capacity to fund essential needs could be made by legislative amendment as needed.

Update: Since the first SPA simulation discussed above, additional modeling is shown in Graph A, 2nd sheet, labeled "Final 2_pfed_post2013, a simulation based on the present tax structure (shown in 1st sheet) which generates $250 million more revenue per year using 42% of the federal income tax payment, though without consistent progressivity. An updated SPA simulation is in preparation. We expect a very similar structure and revenue generation level as shown in Graph B.

Will a modestly higher tax rate for the wealthy erode our tax base?

According to Councilmember Jack Evans " the [Tax Revision] Commission will take a hard look at a number of tax proposals and hopefully come up with a rational set of integrated proposals that balance the need to fund our operations in the short term with longer term goals of fostering business development and retention of District residents and families that too often choose to move to Maryland or Virginia **(partly so they can avoid our high taxes!) [bold added] ((**Jack's Newsletter, September 14, 2012)
However, "There is no evidence supporting the idea that a new tax bracket would lead to "rich flight" from the District. Critics often respond that top earners would simply move to a place with lower income taxes. Yet they offer no data to support their claim, and a Princeton University researcher has found that this effect is minimal" (http://www.dcfpi.org/raising-revenue-by-creating-a-new-tax-bracket-for-top-earners-a-progressive-approach-to-addressing-dcs-budget-shortfall**). An excellent letter to the Current newspaper by David Power in June made the same case (Appendix).**

Of course, we will hear the oft-repeated objection by protectors of our regressive tax structure and growing income inequality, that even modest tax hikes on our wealthy residents would drive them out of the District, thereby reducing our tax base. However this argument ignores the fact that the wealthy have been steadily moving into the District in the last two decades, despite the lower tax rates of suburban Virginia. In the last twenty years, federal income tax returns in the greater than one hundred thousand dollar bracket (adjusted gross income) increased in number from twelve thousand to fifty-nine thousand (in 2011).

It is highly misleading to argue that wealthy DC residents will leave the District if they are required to pay slightly higher rates, given the advantages of living here, namely lower commuting costs and especially time, cultural opportunities, etc. A study by the Center for Neighborhood Technology found that transportation costs for an average Washington household average twelve thousand dollars per year (*Washington Post,* March 24, 2010, B4). Further, the thirty-one hours of congested traffic per week on the Capital Beltway alone would discourage most wealthy District residents from considering moving to the suburbs (*Washington Post,* January 21, 2010, B1). Who will buy their high-priced homes if they move? And as a further step to help prevent a small fraction from moving as well as to fully capture the income tax owed by cheaters who pretend not to be DC residents, the council should seriously consider hiking the property tax for homes of so-called non-residents. Reducing the income gap and "misery index" in the District would benefit the wealthy as well as everyone else by reducing crime, stimulating our local economy, and reducing class/racial polarization.

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All tax simulations were done by Matt Gardner, Executive Director, ITEP.

Appendix

On The Current's "Junk Economics" The Current Wednesday, June 6, 2012 page 11
Letters to the Editor by David F. Power Forest Hills

Current's analyses use 'junk economics'

"The Current often publishes groundless suggestions that D.C. should not raise more income tax revenue or that raising tax rates on the wealthy would reduce revenues. Recently, The Current claimed that retirees have an "incentive" to change their legal residence to avoid taxation, based solely on an anecdote from an anonymous retiree ["Top officials talk retiree taxes, possible incentives for Georgetown store," May 30].

The Current argues that raising income taxes on the wealthy or taxing retirement income would either harm D.C.'s economy or cause residents to migrate away from D.C. Both are myths. The Institute on Taxation and Economic Policy rightly calls the myths fomented by The Current, D.C.'s business community and members of the D.C. Council (such as Jack Evans) "junk economics." The institute concluded, "There is no reason for states to expect that reducing or repealing their income taxes will improve the performance of their economies." It showed that from 2001 to 2010, six of nine "high rate" states had growth in real per capita gross state product that far exceeded the average of all states. Maryland was a leading example, with real per capita gross state product growth of 12.6 percent. Your readers probably do not know that D.C.'s rate of real per capita gross domestic product growth over a very similar period (2000 to 2010) was more than 25 percent, double the growth rate of Maryland, and fourth highest in the nation over that period. The Political Economy Research Institute at the University of Massachusetts recently published an extensive survey of economic literature concluding, based on years of empirical research published in peer-reviewed journals, that if taxes are raised, "The rich will not go on strike. They will not cease working, stop investing, or even move … ." The Center on Budget and Policy Priorities reported that experts have found that raising taxes on high-income households does not harm economic growth.

Thus, the D.C. Council and the mayor have no excuses for pretending to "fund" chronic safety net needs by eliminating vacancies, or selling city-owned buildings, or vastly expanding speed-enforcement cameras, or extending bar hours, or undertaking any other short-term, unsustainable gimmicks. There is no excuse for cutting investment in affordable housing, or cutting employment training for needy families, or cutting homeless shelters, or cutting services for homeless families.

D.C. must raise more revenues from the wealthy so it can increase its employment rolls, inject more money into the local economy, fund economic security programs, fund long-term growth of affordable housing, and put residents to work immediately to rebuild D.C.'s infrastructure. Please stop using junkeconomics in your newspapers."