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Before the Committee on Business and Economic Development
Council of the District of Columbia

Budget Oversight Hearing Regarding Chief Financial Officer

April 22, 2024

Legal Aid DC[1] submits this testimony to urge the Chief Financial Officer and this Committee to grow the District's budget through meaningful taxation on DC's wealthiest residents and businesses. Unlike the current proposed FY25 budget, the District should equitably invest dollars from fair taxation into programs that benefit low-income residents and, in turn, all of DC. Targeted tax increases on DC's wealthiest would barely affect those with the majority of wealth in the city. However, it would be life changing if the revenue generated from increased taxes is invested in programs that support and uplift low-income DC residents.

The mayor's proposed budget vastly reduces or eliminates funding for vital programs for low-income DC residents, further sacrificing their quality of life. These cuts paired with DC's high cost of living mean, low-income residents and workers, like our clients, will continue to barely make ends meet. In order to address the budget cuts, the District should implement policies and revenue raisers that will not further harm low-income residents, and that will increase their ability to achieve financial stability.

[1] Legal Aid DC is the oldest and largest general civil legal services program in the District of Columbia. The largest part of our work is comprised of individual representation in housing, domestic violence/family, public benefits, and consumer law. We also work on immigration law matters and help individuals with the collateral consequences of their involvement with the criminal legal system. From the experiences of our clients, we identify opportunities for court and law reform, public policy advocacy, and systemic litigation. For more information, visit www.LegalAidDC.org.

Low-income Residents Need and Deserve an Equitable Budget and Fair Taxation

Legal Aid participates in coalitions that provide a well detailed roadmap for meaningful investments and revenue raisers for DC's low-income residents. We have also testified before the Tax Revision Commission in support of equitable tax policies for low-income residents with our advocacy partners.[2] As such, we ask that the Committee consider the proposals in the Fair Budget Coalition's FY25 Platform, which seeks to create the actual financial security District residents need and deserve.[3] Also, as a Just Recovery DC coalition member, we recommend that this Committee consider the entire Platform for incorporation into the FY2025 budget with specific attention to raising income tax, taxing capital gains, property tax increases, and a business activity tax as described below.

The District Should Raise Income Taxes to Generate at least $70 million in Revenue

Currently, the top 5% of earners in DC ($400K+) pay less proportionally in taxes than middle income earners ($56k-$399K).[4] DC can add further progressivity to the local marginal income tax rates on high-income earners by increasing the rate on incomes over $500,000.

[2] Testimony of Jen Jenkins, Policy Counsel, Before the Tax Revision Commission, (April 18, 2023), https://www.legalaiddc.org/media/3924/download?inline; Joint Testimony of Tzedek DC and Legal Aid DC with support of the Washington Lawyer's Committee on Civil Rights and Urban Affairs, (Nov. 6, 2023), https://www.legalaiddc.org/media/3916/download?inline; Joint Testimony of Legal Aid DC and Tzedek DC, Reforming Delinquent Debt, https://www.legalaiddc.org/media/3917/download?inline; Legal Counsel for the Elderly and Legal Aid DC, Joint Statement of Legal Counsel for the Elderly and Legal Aid DC P-11, P-12, P-13, P-14, P-15, P-16, P-17, (Nov. 6, 2023), https://www.legalaiddc.org/media/3922/download?inline.

[3] Fair Budget Coalition, Safety is Investing in Community, https://fairbudget.org/wp-content/uploads/2024/03/Desktop-View.pdf.

[4] *See* Institution on Taxation and Economic Policy, Who Pays? 7th Edition, https://itep.org/whopays-7th-edition/; DC Fiscal Policy Institute, Top 5 Percent of DC Earners Pay Lower Effective Tax Rate Than Bottom 95 Percent, https://www.dcfpi.org/press-releases/top-5-percent-of-dc-earners-pay-lower-effective-tax-rate-than-bottom-95-percent/.

For example:

- $500k - $1m: 10% (.25% increase)
- $1m - $5m: 11% (.25% increase)
- $5m+: 12% (1.25% increase)
- $1m - $3m: 11.5% (.75% increase)
- $3m+: 12.75% (2% increase)

Alternatively, the Council could also consider a millionaire surtax similar to Massachusetts' recently enacted surtax. In Massachusetts, personal income taxpayers began paying an additional 4% surtax on taxable income over $1,000,000, increased annually for inflation beginning in 2023.[5] Either proposal would make a significant difference for District residents currently viewed as disposable in the proposed budget.

The District Should Tax Capital Gains to Generate $163 million in Revenue

Capital gains, the profit that an investor makes from the sale of an investment such as stock shares, should be taxed at higher rates for top earners. Currently, individuals with assets may pass their property on to their heirs without taxation on the value or gains accrued while holding the assets. In order to capture this passive form of generation wealth, DC should tax the gains realized at the time of transfer or implement a carryover basis tax, which would allow heirs to defer payment on the gains accrued prior to an heir's ownership of the assets until they sell them.

As proposed in Just Recovery's All in for DC Platform,[6] we recommend raising the tax on capital gains to 13%, an increase from 10.75% for top earners, and creating a credit for taxpayers with incomes in the bottom 80% of earners so they do not face a tax increase. This capital gains tax should be paired with a credit to offset any tax increase for families in the bottom 80% of incomes, so approximately 77% of the tax increase would be paid by those with incomes above $428,000 (top 5% of DC earners) and approximately 57% from those with incomes above $1.2 million (top 1%). This highly targeted proposal would increase taxes on passive income sources like selling stocks, property, or other assets and would impact only those with more than $159,000 taxable income.

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[5] Massachusetts Dep't of Revenue, https://www.mass.gov/info-details/4-surtax-on-taxable-income-over-1000000.

[6] The People's Tax Plan, All in for DC's Tax Policy Platform, https://justrecoverydc.org/our-platform.

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The District Should Raise Property Taxes to Generate $35-$50 million in Revenue

Another opportunity for the District to increase revenue is the adoption of higher marginal property tax rates on single family homes. The All in for DC recommendation is to increase tax rates on homes valued over $1.5 million and target current caps for homestead deduction to low and moderate income households. Notably, this recommendation would primarily impact homes in Wards 2 and 3.[7]

DC's current property tax rate is a flat $.85 per $100 of assessed value and is the lowest property tax rate in the region.[8] The District should create 2-3 additional property tax brackets for very high-value properties. For example:

- $1 per $100 on homes valued over $1.5M (+15 cents)
- $1.50 per $100 on homes valued $2-$5M (+65 cents)
- $2 per $100 of assessed value for homes valued over $5M (+$1.15)

With increased property taxes on the highest value homes in DC, those with the most wealth will be investing in a safer[9] and more equitable DC.

[7] See Eliana Golding, DC Can Advance Racial Equity and Black Homeownership through the Property Tax, Table 3, Eighty Five Percent of DC's High Value Homes are Located in Wards 2 and 3, https://www.dcfpi.org/all/dc-can-advance-racial-equity-and-black-homeownership-through-the-property-tax/.

[8] See Office of Tax Revenue, Real Property Tax Rates, https://otr.cfo.dc.gov/page/real-property-tax-rates (last visited April 15, 2024).

[9] *See* Thea Sebastian, Hanna Love, Sam Washington et al., Brookings (Sept. 21, 2022), A New Community Safety Blueprint: How the Federal Government Can Address Violence and Harm Through A Public Health Approach, https://www.brookings.edu/articles/a-new-community-safety-blueprint-how-the-federal-government-can-address-violence-and-harm-through-a-public-health-approach/#:~:text=For%20instance%2C%20increasing%20access%20to,total%20crime%20reduction%20of%2025%25.

The District Should Enact a Business Activity Tax For $300 million in Revenue

We also strongly support the implementation of a Business Activity Tax. A business activity tax, or BAT, is a tax on economic activity of a business rather than profits of its owners, and having such a tax in DC would help ensure all businesses in the District pay their fair share. Currently, many businesses are organized to pass their profits through to owners as personal income and are therefore exempted from corporate and unincorporated business taxes. If their owners (partners) live outside the District, federal law prohibits DC from taxing those owners.[10] As a result, a lot of business activity in the District goes untaxed and locally owned businesses and residents shoulder the responsibility of paying for public services that untaxed businesses profit from. Because the BAT is based on business activity rather than profits, it also ensures that corporations with good accountants cannot use tricks that downplay profits to avoid taxes. A BAT is calculated by taking all the money a business brings in and subtracting purchases from other firms.

According to the Tax Revision Commission ("TRC"), the BAT would not be enacted or implemented overnight, and more detailed fiscal analysis would be required.[11] The TRC also suggested that a transition might be warranted in which tax filers do not immediately pay the BAT but instead submit information on a form showing how much they would owe in order to help the Office of Tax Revenue ("OTR") calibrate fiscal estimates.[12] While we agree with this information gathering approach, we also direct your attention to New

[10] *See* 602(a)5 of the Home Rule Act; see also Bishop v. District of Columbia (1979) ("The distinction between a tax on gross receipts and one on net income is important. When a jurisdiction taxes net income, it does so, in effect, because its object is to raise revenue by taxing the consumable wealth of its taxpayers. Moreover, it seeks to serve auxiliary purposes such as redistribution of wealth, equalization of consumption, and taxation of the ability to pay.... [A} gross receipts tax is levied for the purpose of either taxing a privilege, such as the right to do business, or simply raising revenue...").

[11] DC Tax Revision Commission Staff, Letter to DC Tax Revision Commissioners, Regarding Business Activity Tax, https://drive.google.com/file/d/1FZuSERsRaJcqTdfMCgcFs9uj8M0kqBEJ/view.

[12] DC Tax Revision Commission Staff, Letter to DC Tax Revision Commissioners, Regarding Business Activity Tax, https://drive.google.com/file/d/1FZuSERsRaJcqTdfMCgcFs9uj8M0kqBEJ/view.

Hampshire who, in 1993, put the law into effect without any model forms to great success.[13]

These four tax increases are well researched and targeted and, combined, would raise approximately over $800 million dollars in revenue. The future of the District is at stake, and we urge this Committee to invest in low-income DC residents, so that the workers and families who make DC what it is can remain and thrive.

The Child Tax Credit and Earned Income Tax Credit Are Investments in DC Residents

Legal Aid has testified before this Committee in support of the child tax credit, and we remain adamant that the Child Tax Credit ("CTC") is a strong investment in District families.[14] We also call on this Committee to ensure the District's lowest income workers are more financially secure by restoring the Earned Income Tax Credit ("EITC") funding and expanding its reach.[15] In the absence of an expanded Earned Income Tax Credit ("EITC"), low-income District residents will suffer, while the wealthiest DC residents and businesses still do not pay their fair share of taxes. The CTC and EITC could be in place with targeted and meaningful revenue raisers.

Conclusion

In the face of an austere proposed budget from the mayor, this Committee and the Council should make the sound decision to increase the District's budget through targeted taxes on the District's wealthiest residents and businesses in order to fund programs and initiatives that support DC's vulnerable and low-income residents.

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[13] *See* New Hampshire, Business Tax Data, Dep't of Revenue, https://www.revenue.nh.gov/transparency/business-tax.htm#:~:text=The%20Business%20Enterprise%20Tax%20(%22BET,or%20after%20December%2031%2C%202019.

[14] *See* Testimony of Jen Jenkins, Policy Counsel, Systemic Advocacy and Law Reform Legal Aid DC, (Jan 24, 2024), https://www.legalaiddc.org/media/3835/download?inline.

[15] *See* B25-0784 Fiscal Year 2025 Budget Support Act of 2024 as introduced, Title VII Finance and Revenue, Subtitle D Earned Income Tax Credit Match Level. (The subtitle would freeze the match percentage at 70 percentage in tax year 2025 and all subsequent years.).