

**UNDERSTANDING TAXES THAT CAN RAISE REVENUES TO HELP OFFSET GROWING
WEALTH INEQUALITY IN THE DISTRICT OF COLUMBIA**

**Statement of
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**before the
Committee on Business and Economic Development**

Council of the District of Columbia

**B24-0236 - THE “CHILD WEALTH BUILDING ACT OF 2021” AND TAX
POLICY PROPOSALS TO BUILD WEALTH EQUITY IN THE DISTRICT’S
POST COVID-19 ECONOMIC RECOVERY**

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* The views expressed are my own and should not be attributed to the Urban Institute, its trustees, or its funders.

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Councilmember McDuffie and other committee members, thank you for inviting me to discuss the District of Columbia’s revenue system and policy options for building wealth equity for all District residents. These conversations are especially timely given the disproportionate impacts of the COVID-19 pandemic and the opportunity we now have for an inclusive rebuilding and recovery for all Washingtonians.

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We have heard from others about specific plans to help increase the wealth of DC residents with low incomes, who are disproportionately Black people and other people of color. This panel is charged with addressing ways of paying for these policy changes and examining if current policies might add to the disproportionate ways that wealth is generated and accumulated across generations.

My remarks today will cover three major points, and I am happy to answer questions. Much of the information is based on data available on the Urban Institute’s website (www.urban.org).¹

- 1. The District of Columbia is a relatively rich jurisdiction, but it also has a high level of income inequality, especially across racial and ethnic groups and neighborhoods.**
- 2. The District’s revenue system is fairly progressive overall, which helps reduce racial and ethnic income inequalities. But there is room to further offset income and wealth inequalities.**
- 3. Taxes on wealth at the local level are extremely tricky, and policymakers must think hard about regional economic mobility and interactions with federal policies when designing them.**

The District of Columbia Is Home to Stark Inequalities

The District has both relatively high per capita income and a high poverty rate. The District’s per capita income was \$87,064 in 2020, well above the national average of \$59,729. However, the District’s poverty rate was 16.2 percent in 2019, also above the national rate of 13.4 percent.²

Moreover, neighborhoods reflect significantly disparate outcomes. For example, Ward 8’s median household income was \$35,245, and its poverty rate was 32.9 percent averaged over the five years from 2015-2019; Ward 3’s median household income was \$128,670, and its poverty rate was 7.6 percent over the same period. And although the District’s average unemployment rate in 2020 was 4.1 percent for white residents, it was 14.7 percent for Black residents and 8.9 percent for Latinx residents.

As noted by other panelists, wealth disparities within the District, which build up over generations, can be even more stark than disparities in one-year incomes—we simply have more data available about the latter than about the former. And these disparities were exacerbated by the COVID-19 pandemic’s

¹ “How the COVID-19 Pandemic Is Transforming State Budgets,” Urban Institute, last updated May 14, 2021, <https://www.urban.org/policy-centers/cross-center-initiatives/state-and-local-finance-initiative/projects/state-fiscal-pages-covid-edition>.

² “State and Local Backgrounders.” Urban Institute, State and Local Finance Initiative, accessed May 20, 2021, <https://www.urban.org/policy-centers/cross-center-initiatives/state-and-local-finance-initiative/state-and-local-backgrounders>.

disparate effects on specific communities, industries, and city regions.³ Understanding how we can recover and expand opportunity for all residents through public policy, specifically tax policy, is important.

The District Has a Progressive Revenue System, But It Could Do More to Address Income and Wealth Inequalities

The District government has already created one of the most (if not the most) progressive tax systems in the country. In fact, when I testify in front of or consult with government officials in other states about progressive tax policy changes, I often cite policies in the District of Columbia as examples worth emulating.

Most state and local government revenue systems are regressive. That is, lower-income residents pay more taxes as a share of income than higher-income residents. This is mostly because state and local governments rely heavily on regressive taxes such as sales taxes, user fees, and charges.

But the District levies a progressive individual income tax that shifts more of the tax burden onto higher-income residents. Further, it has a relatively high corporate income tax and a commercial property tax that collect taxes from the large businesses that operate here.⁴

More importantly, the District offers several tax programs that directly assist low-income working families. The District's earned income tax credit, or EITC, is the highest state EITC for workers who do not claim children on their tax return. This program was also enacted, albeit temporarily, at the federal level by the American Rescue Plan Act. The District also provides a generous property tax credit to both homeowners and renters, and this credit is independent of income tax liability, meaning filers can claim the full credit even if it is more than they owe in DC taxes.

None of this is to say the District's work is finished. But part of being a leader on progressive tax policies means that the simple solutions and changes that a less-progressive jurisdiction could quickly adopt are not available to the District. Instead, leaders must think through more challenging and tricky tax policy changes if they want to further improve the equity of its revenue system.

³ State and Local Finance Initiative, "How the COVID-19 Pandemic is Transforming State Budgets," Urban Institute, last updated May 14, 2021,

<https://www.urban.org/policy-centers/cross-center-initiatives/state-and-local-finance-initiative/projects/state-fiscal-pages-covid-edition>.

⁴ Government of the District of Columbia Office of the Chief Financial Officer Office of Revenue Analysis, *DC Tax Facts* (Washington, DC: Government of the District of Columbia, 2020).

<https://cfo.dc.gov/sites/default/files/dc/sites/ocfo/publication/attachments/Tax%20Facts%202020.pdf>.

Local Wealth Taxes Are Complicated and Their Effects Can Depend on Regional Economic Mobility and Federal Policies

Because white families hold most financial and nonfinancial assets at significantly higher rates than Black and Latinx families, wealth taxes could also help close gaps across racial and ethnic groups.⁵

Here are some things to keep in mind when exploring new tax policies for the District.

1. The District is relatively small, and its economic activity crosses into Maryland and Virginia.

People and investments have some flexibility in moving across borders. Although there is not strong evidence that higher income tax rates have led to people leaving specific states or jurisdictions (taxes do not tend to be the primary consideration when people move), introducing new taxes on wealth or the stock of goods could have larger migratory effects.⁶ This is especially important to keep in mind following the pandemic, when relocations and remote work have become more common, as well as when examining any taxes on assets or people that are not necessarily tied to a specific place.

2. Enforcement and reporting are challenging. It is often easier for state and local jurisdictions to rely on information and enforcement from the federal government.

Like most other states, the District currently taxes capital gains at the same rate as wage income, not allowing a tax preference that mainly benefits high-income households.⁷ If the District were to introduce new taxes on wealth, it would need a way to measure the value of wealth within the District that would be subject to local taxes.

This would be easier to do if the measures or rules were based on information required and collected by the federal government. Depending on the outcomes of discussions about estate, inheritance, and capital gains taxes at the federal level, such wealth taxes could be easier to implement for some types of wealth than for others (e.g., traded stocks versus paintings or art) and at specific points in time (e.g., a “stepped-up basis at death”).

3. Taxes on homes or physical property or other real estate are more straightforward. But new taxes can have direct and indirect effects.

The District already has a homestead exemption that reduces the assessed value of owner-occupied properties and a 10 percent cap on property tax increases. It also offers programs to help alleviate ownership costs for new homeowners.

⁵ Aravind Boddupalli and Kim Rueben, “State and Local Government Revenues and Racial Disparities” (Washington, DC: Urban-Brookings Tax Policy Center, 2021).

<https://www.taxpolicycenter.org/publications/state-and-local-government-revenues-and-racial-disparities>.

⁶ Cristobal Young, *The Myth of Millionaire Tax Flight* (Palo Alto, CA: Stanford University Press, 2017).

<https://www.sup.org/books/title/?id=27987>.

⁷ Elizabeth McNichol, “State Taxes on Capital Gains” (Washington, DC: Center on Budget and Policy Priorities, 2018). <https://www.cbpp.org/research/state-budget-and-tax/state-taxes-on-capital-gains>.

The District could introduce higher property tax rates or new taxes on the transfer of property. It could also introduce different property tax rates depending on value or use of property, such as new rates of property taxation for properties owned by people out of state.

However, any changes to property taxes could also be passed along to renters. The incidence (or who actually bears the burden of the tax, as opposed to who pays it) is unclear. There can also be different rates for property above a certain value.

The District already has different rates or costs when property is sold because it has variable rates and both a recordation fee and deed transfer tax. These are charged on buyers and sellers respectively and are higher for properties valued above \$400,000. The District also recently increased these rates to equal 5 percent combined for high-value commercial or mixed-use property valued at more than \$2 million. District leaders could think about a similar rate for the transfer of high-value residential properties as well. This would be similar to the “mansion taxes” in states such as Connecticut, New York, and New Jersey.⁸

Further, recent research has found that property tax assessment and appeals process outcomes tend to be regressive and disproportionately burden Black and Latinx households with higher property tax bills.⁹ If the District were to increase its reliance on property taxes for revenue, it may benefit from conducting an equity review of its property tax assessments.

The District is an attractive location for tourism and foreign residents. The District’s revenue system is one of the most progressive in the country. Although more can be done to try and mitigate income and wealth inequality, we also need to recognize the complications that arise because the District of Columbia is a relatively compact area that shares economic activities and interests with neighboring states.

⁸ Michael Leachman and Samantha Waxman, “State “Mansion Taxes” on Very Expensive Homes” (Washington, DC: Center on Budget and Policy Priorities, 2019).
<https://www.cbpp.org/research/state-budget-and-tax/state-mansion-taxes-on-very-expensive-homes>.

⁹ Carlos Avenancio-León and Troup Howard. 2020. “The Assessment Gap: Racial Inequalities in Property Taxation.” Working paper (Washington, DC: Washington Center for Equitable Growth, 2020).
<https://equitablegrowth.org/working-papers/the-assessment-gap-racial-inequalities-in-property-taxation/>;
Christopher Berry “Reassessing the Property Tax.” Working paper (Chicago: University of Chicago, 2019).
<https://cpb-us-w2.wpmucdn.com/voices.uchicago.edu/dist/6/2330/files/2019/04/Berry-Reassessing-the-Property-Tax-3121.pdf>.