
Fiscal Architecture of the District of Columbia

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Overview

- Summary of economic and demographic trends
- Impact on D.C.'s revenues
- Potential options
- “What-if”-sensitivity of trends and impacts

D.C.'s Fiscal Architecture

- Revenue and expenditures are driven by many factors including economic and demographic characteristics
 - For example: Population size, age distribution, concentration of specific economic activity
- These factors change over time and may affect the natural growth of revenues and the basket of expenditure needs
 - Growth in service sector (loss of tax handles?), growth in very young (increased demand for education?)
- Institutional context may affect ability to respond to these changes

Does D.C.'s current revenue structure capture growth in the economy?

Concept

- Simple premise:

$$\text{Revenue collection (receipts)} = \text{tax rate} * \text{tax base} * \text{administrative/compliance efficiency}$$

- Similar case for expenditures (though not as much a focus in this report):

$$\text{Expenditure need} = \text{client population} * \text{per unit cost of production}$$

Driver's of Fiscal Architecture

- Factors affecting these relationships or any component affect revenues and expenditures in the short and long-term
- Factors studied include:

Demographic	Economic
Age Distribution	Employment and output
Household Composition	Personal income
Race/ethnic diversity	Globalization
Population Size	Real Estate

Highlights in Trends

- Population:
 - Growth in relatively young population (labor and school aged)
 - Growth in elderly (less than the U.S. average)
- Household size/composition:
 - Smaller than average households
 - Non-family households (roommates and singles)
- Ethnic/racial diversity
 - Large black population
 - Diversity of immigrant population
- Income:
 - High median income
 - Growing income gap

Trends, con't.

- Employment and output
 - Growth in service sector
 - Growth in education/health services
 - Decline in federal employment
- Globalization and technology
 - Continued competition for capital and labor
 - Growth in business activity via internet
- Real estate
 - Growth in residential component
 - Impact of federal policies
 - Densification

What to Expect, Options, and What-Ifs

- Population growth and employment mix
 - Projected job growth is in lower paid sectors of health and education, reducing natural growth in income tax revenue
 - Stability of commercial property tax base is uncertain (federal government decisions, densification)
 - OPTIONS TO ADDRESS:
 - Continue to make D.C. an attractive place to live and age in place (from young to old)
 - Target expansion of affordable housing
 - Use of property tax to incentivize development and commercial occupancy
 - What if?
 - Growth and age transitory

What to expect, con't.

- Service sector growth in employment and output
 - Reduces tax handles, service-based industries are more difficult to identify and possibly to value
 - Employment in sector is less defined by location than by skill (outsourcing), reducing growth in income tax
 - Services less heavily taxed under traditional sales tax systems
 - OPTIONS TO ADDRESS:
 - Broadening the base of the sales tax
 - Substituting a simplified business tax for the corporate income tax
 - What if?
 - Federal sequestration and permanent reduction in growth



- Increase in share of elderly
 - Greater portion of their income is tax-exempt (Social security, pensions)
 - Greater share of consumption is tax-exempt (health care, food at home)
 - Property tax exemption that is not means tested
 - OPTIONS TO ADDRESS:
 - Means test the exemptions
 - If D.C. seeks to have its population age in place there will be increased demand for services including transportation and healthcare
 - What if?
 - Elderly migrate?

What to expect, con't.

- Globalization and Technology increase competition and decrease labor's share of output
 - Competition forces focus on differences in tax rates (income and sales)
 - Capital's share of output and tax base increases, but capital provides a difficult "tax handle"
 - Internet sales will continue to pick away at the sales tax base
 - OPTIONS TO ADDRESS:
 - Leadership role in rationalization of the taxation of internet sales (Streamlined Sales Tax, "Amazon Laws")
 - Reduced reliance on corporate income/profits based tax to a simplified minimum tax
 - Reassess areas to substitute fees and charges for income taxes

What to expect, con't.

- Disparities among the population
 - Health of children is poor (obesity)
 - Income is increasing disparate
 - Pressure on services (health care, low income support)
 - Pressure on long-term income tax growth (lower health status and migration of tax to the high income earners)
 - Increases consumption of health services
 - OPTIONS TO ADDRESS:
 - Increased efficiency in public services—those valuing distribution through the tax system will increase if their own needs are met
 - Reduce tax exemptions (broaden income tax base)
 - What if?
 - Affordable housing not available

Wrap-Up

- Summary:
 - Pressures on:
 - Current Individual Income Tax and Corporate Income Tax
 - Expectations/need for public services
 - Opportunities:
 - Sales tax base expansion
 - Simplified business taxes
 - Fees/charges commensurate with public service expectations
 - Institutions
 - Taxation at source?
 - Engineering the demographics