The District's Dime
Going Beyond the Budget Book

The DC Fiscal Policy Institute blog
www.dcfpi.org

August 28, 2014

Tech and Taxes: Why Tax Incentives Are A Bad Strategy to Boost Investment

By Wes Rivers

Strengthening DC's emerging technology community has become an issue on the DC campaign trail, which is important because high-tech companies could be a major vehicle for future economic growth. Unfortunately, the discussion has turned to the idea of tax cuts for wealthy tech investors, which are unlikely to do much to promote the tech sector. Instead, tech tax breaks would worsen income inequality in DC and divert tax resources from things that can strengthen DC's business climate and help local start-ups succeed.

It is unclear why this idea is being raised, given that it has been roundly rejected in the District. In 2013, the DC Tax Revision Commission considered and rejected a proposal to cut income taxes by two-thirds for income from tech investments. Before that, the DC Council voted against the same measure. Here's why:

A tech capital gains tax cut would cost a lot but do little to affect tech investments. There is no evidence that lowering capital gains taxes leads to higher economic growth. That's likely because investors make decisions based on a start-up's potential for success, including its access to an educated workforce and other resources. A tax break will not turn a risky investment into a good one.

Yet tax cuts on tech investments could be very costly. A capital gains tax cut would benefit investors after companies take off and become successful, when the investment gains would be large. This would divert significant resources and make it harder to support things that make DC an attractive city – such as schools, parks and libraries – or that directly help business, such as public grants for workforce development and business incubators.

Table 1: Existing Incentives for High Tech Companies
Tax Exemptions:
- Corporate income tax for first 5 years
- Sales tax on hardware and software
- Sales tax charged for retail sales and services
- Personal property taxes for first 10 years
Other Incentives:
- 6 percent corporate income tax for life of company (after 5 years)
- $10,000 wage reimbursements per new hire
- Workforce training tax credits
- Relocation reimbursements

Source: Deputy Mayor of Planning and Economic Development, dmped.dc.gov

Tax breaks for tech investments would benefit wealthy investors and an industry that already gets substantial tax support. Any capital gains tax cut would likely mean that investment income would be taxed at rates lower than those faced by working DC residents. That would widen income inequality in DC, which already is fourth highest level any large city.

Tax breaks for investment income would go to tech executives whose companies already benefit from large incentives for operating in the District (see **Table 1**). No other industry gets such large subsidies for companies and their owners.

If the District wants to promote tech investment, it can do so by providing entrepreneurs with the upfront supports and resources they need to attract investors – highly skilled employees, affordable workspace, and access to experienced business expertise. Focusing incentive programs on income taxes benefits very few and does nothing to help DC's start-up community grow.