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What Revenue Changes Are In The Final FY 2017 Budget?

SUMMARY OF REVENUE CHANGES IN THE FINAL FY 2017 BUDGET

- DC's projected revenues are \$7.45 billion in FY 2017. Revenues have grown very modestly in the last few years, partly due to continuing tax cuts.
- The fee and tax on hospitals that was implemented last year was extended this year. It will provide \$17 million to help reimburse hospitals for Medicaid services delivered, but again will expire after one year without another legislative change.
- The budget includes a very small expected revenue increase (\$9 million) from new compliance measures and technical changes.
- The budget "sweeps" several funds that could have been used for better purposes.
- The limited increase in revenues partly reflects the impact of tax cuts that have been implemented since the FY 2016 budget. \$45 million in tax cuts have been implemented in the past year. The FY 2017 budget leaves these reductions in place and offers no offsetting revenue increases.
- Barring a legislative change, additional tax cuts will be triggered any time that the District's revenues grown faster than projected. This is problematic, because the Council should have the ability to deliberate and decide how to spend its revenue on a case by case basis, depending on the city's needs.

DC's Revenues Will Grow Only Modestly in 2017

Projected revenues in FY 2017 total \$7.45 billion, an increase of just 0.8 percent over last year, after adjusting for inflation.¹ Revenue growth has slowed dramatically in the last couple of years, in part due to implementation of tax cuts. In fact, revenue collections in 2017 will be roughly the same as in 2015. Slow revenue growth limits the ability to keep up with the rising costs of services or to make new investments to meet important needs of DC residents.

DC's tax and fee collections have fluctuated greatly over the past decade, as a result of the Great Recession and subsequent recovery. Revenues dropped sharply in FY 2009 and FY 2010 – falling by nearly \$500 million – which led to substantial cuts in a range of programs and services. The collections started to rise in FY 2011, in part due to a variety of tax and fee increases. Between 2010 and 2015, revenue collections grew a healthy 4 percent faster than inflation each year.

¹ This includes taxes that are used for specific purposes, such as sales taxes used to pay off the Convention Center debt, but it does not "special purpose revenues," special fees tied to certain uses.

However, revenue growth has slowed to a crawl since then, as shown in **Figure 1**. The projected \$7.45 billion in revenues in 2017 represents growth of just 0.2 percent annually since 2015, adjusting for inflation. As discussed below, the slow revenue growth partly reflects the impact of recently implemented tax cuts.

Revenue Changes in the FY 2017 Budget

The FY 2017 budget extends two taxes on hospitals adopted in 2016 and includes several modest policy changes to increase revenue in FY 2017. See **Table 1**.

Hospital Fees to Pay for Medicaid Services Extended for an Additional Year: The FY 2017 budget continues two taxes on hospitals, based on hospital revenues for in-patient and out-patient services, that were adopted in 2016 on a one-year basis. The taxes will be used to maintain Medicaid’s 2016 hospital reimbursement rates for services for the District’s “fee-for-service” beneficiaries, those not in the city’s managed care program, who largely are elderly residents and residents with disabilities or chronic conditions. The District currently reimburses hospitals for 98 percent of the costs for in-patient services, far above the national average of 87 percent. Without a continuation of this tax, reimbursement rates would likely have been cut.

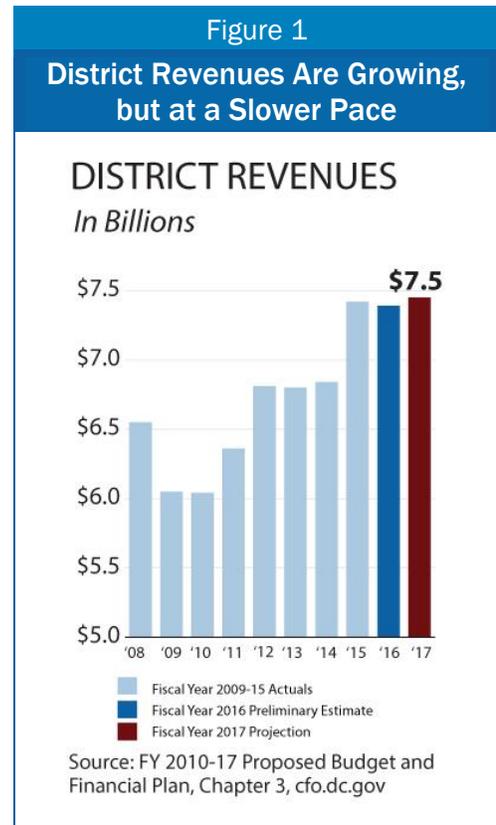
Together, the hospital taxes and outpatient fee will raise \$17.1 million in dedicated local funding, and this will generate \$40 million in federal Medicaid funds.

However, similar to last year, these sources of revenue from hospitals will again be in place for only one year. This means that the issue of Medicaid reimbursements to hospitals will once again have to be revisited in the FY 2018 budget.

Delay of Certain Business Income Deductions: The budget delays by five years the effective date for which business tax filers can claim certain deductions. This is expected to increase revenues by \$7.4 million in FY 2017.

Office of Tax and Revenue “Clean Hands” Initiative: This initiative will allow the District to check for missing sales and income tax withholding when businesses seek various permits or services, such as contract approvals and license renewals. For FY 2017, the sales tax portion is expected to raise \$500,000, and the income tax portion will raise \$1.5 million.

Supermarket Tax Credit Expanded: The budget allows one new grocery store in Ward 4 to qualify for the real and personal property tax exemptions for supermarkets in under-served areas. This is expected to cost \$237,000 in FY 2017.



Expanded Eligibility for High-Tech and Media Company Tax Credits in 2021: Beginning in 2021, companies located in the Ballpark TIF area would be eligible for the Qualified High Technology Company (QHTC) designation, and a new designation of “Qualified Digital Media Company” would be created for some media companies. These designations allow companies qualify for certain tax breaks. The QHTC expansion is expected to cost \$7.25 million in 2021.

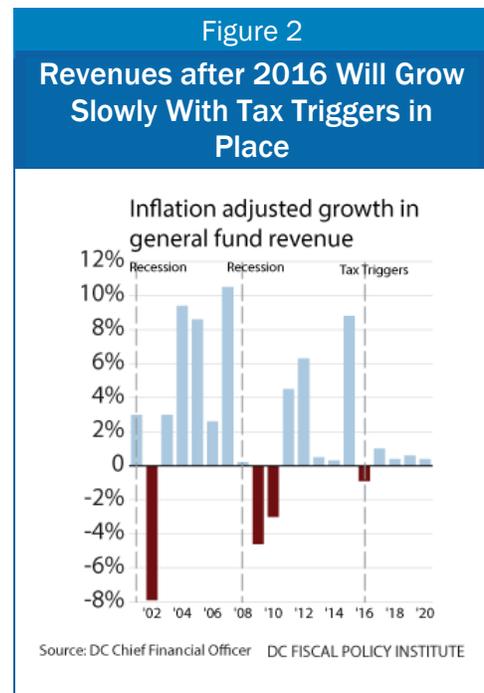
Table 1	
Summary of Select Policies Impacting General Fund Revenues for FY 2017	
Revenue Source	Fiscal Impact (In thousands)
Hospital Fund – Medicaid Hospital Inpatient Fee*	\$10,400
Delay certain deductions by 5 years	\$7,443
Hospital Provider Fee Fund – Medicaid Hospital Outpatient Fee*	\$6,709
Compliance Initiatives at OTR (income taxes)	\$1,500
Compliance Initiatives at OTR (sales/use taxes)	\$500
Supermarket Tax Credit	(\$237)

Source: Mayor’s Proposed Budget for FY 2017, Chapter 3, Revenue.
* These are dedicated taxes that cannot be used in the local fund.

The Budget Sweeps Some Funds that Could Have Been Used for Better Purposes

The FY 2017 budget removes funding from:

- Healthy DC:** The FY 2017 budget removes \$6 million in accumulated resources from Healthy DC Fund to support other parts of the city’s budget. This follows a similar sweep of Healthy DC Fund resources in 2016. The reduction leaves less money available for health services, including the locally funded Healthcare Alliance program and the local portion of DC’s Medicaid program.
- Income Assistance to Residents with Disabilities:** The budget removes \$1 million from the Supplemental Security Income (SSI) Payback Fund, a dedicated fund for the Interim Disability Assistance (IDA) program, which supports low-income residents with disabilities. IDA provides temporary cash benefits to individuals who have applied for federal SSI disability benefits and are awaiting an eligibility determination. When an individual is approved for SSI, the federal government reimburses the District for the IDA benefit the individual received. These reimbursement dollars are put into the SSI Payback Fund so the District can provide benefits for future IDA applicants. The \$1 million reduction translates to roughly 300 residents with disabilities who will be unable to get IDA assistance in 2017.



Recent Tax Cut “Triggers” Have Limited the Ability to Fund New Investments, and Will Make It Hard to Adequately Fund Services in Future Years, Too

As a result of Council efforts to prioritize implementation of a tax cut package based on recommendations from the DC Tax Revision Commission, some \$45 million in tax cuts has been implemented in the past year. These tax cuts contribute to the slow growth of revenues in FY 2017 and limit the ability to fund new initiatives.

Legislation adopted by the Council triggers automatic implementation of a series of tax cuts recommended by the Tax Revision Commission. The tax cuts are triggered when projected revenue collections increase after the given year’s budget has been adopted. The tax triggers automatically devote 100 percent of these revenue increases to tax cuts, which means that none of the growing revenues is available to invest in new services.

The full list of tax changes yet to be made represent over \$139 million in revenue reductions, a large enough figure that it is likely that no revenue growth will be available for other purposes. (See **Table 2** for the tax cuts and the order in which they would be implemented.)

Using additional revenue *solely* for tax cuts is problematic for several reasons:

- **Tax triggers are contributing to historically low rates of revenue growth:** With tax triggers in place, revenues will grow no more than 1 percent per year, adjusting for inflation, between 2016 and 2020. Even in the Great Recession, DC’s revenue growth did not stay this low for so long. Each 1 percent growth equals about \$80 million in revenue. See Figure 2.

- **Tax triggers make it hard to keep up with DC’s growing needs:** DC’s revenues are projected to increase by just 3 percent per year for the foreseeable future, largely due to the tax triggers.¹ Over the last five years, population has grown 2.3 percentⁱⁱ and inflation 1.5 percent on average. This means that we need at least 4 percent revenue growth just to maintain the status quo. But other needs are growing even faster. For example, over the last five years, on average: Medicaid enrollment has grown 4.5 percent per year; homeless services has grown 28 percent per year; and debt payments have grown 8.6 percent per year (to pay for school modernizations and other capital projects. **See Figure 3.**

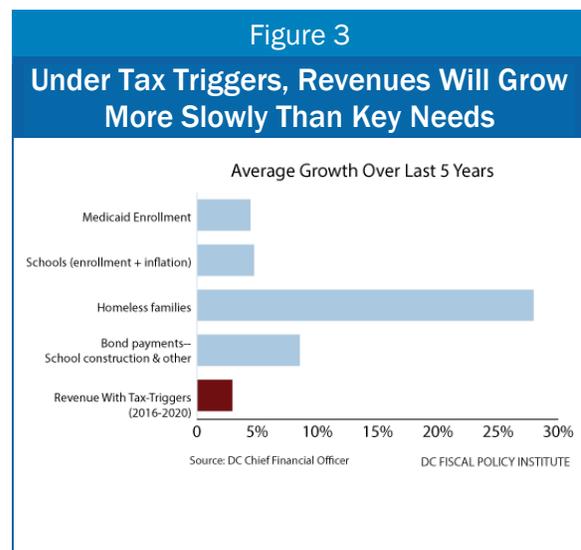


Table 2

In 2014, Tax Revision Commission Cuts Cost Us \$46 Million

Tax Commission Policy Changes	FY 2017 Fiscal Impact (In Millions)
Established a new individual income bracket of \$40-60,000, reducing rates from 8.5% to 7.0%	(\$39.5)
Expanded the local earned income tax credit to childless workers	(11.4)
Raised the standard deduction to \$5,200 for singles, \$8,350 for married residents	(16.5)
Eliminated certain tax expenditures	3.9
Expanded the general sales tax rate to certain services	16.8
Phased out the personal exemption by 2% for each \$2,500 above \$150,000, with a complete phase out at \$275,000	4.9
Exempted passive investment vehicles from the unincorporated business franchise tax	(4.6)
Reduced the business franchise tax from 9.975% to 9.4%	20.8
Changed the franchise tax apportionment method to a single weighted sales formula	(20.8)
Tax Triggers Have Cost Us \$47 Million This Year	
Tax Commission Policy Changes	FY 2017 Fiscal Impact (In Millions)
Further reduced the rate on the new middle income tax bracket to 6.75%	(\$7.5)
New income tax bracket - \$350,000 to \$1M at 8.75%, income greater than \$1M at 8.95%	(5.0)
Further reduce business franchise taxes to 9.2%	(10.1)
Finish reducing the rate on middle income tax bracket to the new rate of 6.5%	(7.5)
Reduce unincorporated & incorporated business franchise tax from 9.2% to 9.0%*	(10.1)
Raise the estate tax threshold from \$1 million to \$2 million*	(6.5)
\$139 Million in Additional Cuts Will Go Into Effect Via Triggers	
Tax Commission Policy Changes	FY 2017 Fiscal Impact (In Millions)
Further increase the standard deduction to \$5,650 for single and \$10,275 for married residents	(\$9.4)
Increase the personal exemption to \$2,200	(\$13.8)
Finish raising the standard deduction and conform to federal levels	(\$9.8)
Further increase the personal exemption to \$2,700	(\$16.7)
Further reduce business franchise taxes to 8.75%	(\$11.9)
Further increase the personal exemption to \$3,200	(\$16.2)
Finish increasing the estate tax threshold to conform to the federal level	(\$12.3)
Further reduce the business franchise taxes to 8.5%	(\$11.9)
Further increase the personal exemption to \$3,700	(\$15.6)
Finish reducing business income taxes to 8.25%	(\$11.9)
Finish increasing the personal exemption to conform to the federal level	(\$9.1)
*Tax cuts "triggered" in most recent budget forecast but not yet implemented.	
Source: Mayor's Office of Budget and Finance, March 2016.	

Rather than automatically reducing taxes using all new revenue growth, additional revenues could instead have been used to fund additional services that went underfunded in FY 2017 budget. For example, the \$45 million in tax cuts implemented this year could have fully funded the Public Assistance Amendment Act of 2015, which would reform DC's Temporary Assistance for Needy Families (TANF) time limit to ensure that the basic needs of low-income children are met. This money could have been further used to provide funding to reduce the DC Healthcare Alliance six-month interview requirement to an annual interview, which would ease long lines and wait times at DC's social service intake centers.

ⁱ The Mayor's proposed FY 2017 Budget. Chapter 3: Revenue.

ⁱⁱ American Community Survey. Annual Estimates of the Resident Population: April 1, 2010 to July 1, 2015.