

PUBLIC HEARING ON
BILL 17-0074, “STANDARD AND ITEMIZED
DEDUCTION FILING ELECTION ACT OF 2007”

Before the
Committee on Finance and Revenue
Council of the District of Columbia

The Honorable Jack Evans, Chairman

March 14, 2007, 11:00 a.m.
John A. Wilson Building, Room 120



Testimony of
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Good morning, Chairman Evans and members of the Committee on Finance and Revenue. I am Sherryl Hobbs Newman, Deputy Chief Financial Officer for the Office of Tax and Revenue (OTR). I am pleased to present testimony today on Bill 17-0074, the “Standard and Itemized Deduction Filing Election Act of 2007.”

Currently, under District law, taxpayers claiming itemized deductions on their federal tax returns must itemize on their District returns. Similarly, taxpayers claiming the standard deduction on their federal tax returns must elect the standard deduction on their District tax return. This is the standard practice for states that allow for itemized deductions on their state returns.

Bill 17-0074 would contradict this standard practice and allow taxpayers to elect either the standard deduction or itemized deductions on their District tax returns, regardless of whether taxpayers elected to itemize on their federal returns.

We recommend that the Council not enact this legislation. It reverses the 26-year-old policy of conforming District tax law to federal tax law, creates severe administrative problems, complicates the audit process, allows unintended tax benefits, and requires massive computer reprogramming.

First, federal conformity has made the District’s tax system more efficient, generating substantial administrative savings and promoting simplicity. This bill, however, will require the District to create new tax forms. For example, if a taxpayer claims the standard deduction for federal purposes and elects to itemize

deductions for District purposes, OTR will have to create its own Schedule A in order for the taxpayer to claim itemized deduction for District purposes.

Second, this bill will require taxpayers to keep separate records for District tax returns to support these itemized deductions claimed only for District tax purposes.

Third, the Internal Revenue Service monitors the reasonableness of itemized deductions claimed on Schedule A. The District frequently benefits from this monitoring process, while also performing its own check on these expenses. If a taxpayer electing the standard deduction at the federal level is allowed to claim itemized deductions for District tax purposes, then OTR will have to increase substantially its auditing resources and procedures to verify the taxpayer's entitlement to such itemized deductions.

Fourth, this bill will allow taxpayers to claim tax benefits not intended by the drafters of the legislation. For example, assume a District couple files a joint federal return and elects to itemize deductions in the amount of \$30,000, of which \$10,000 represents District income taxes. Currently, whether or not this couple files separately for District tax purposes, they could not claim more than \$20,000 in total in itemized deductions. This bill, however, would permit this couple to deduct a total of \$21,250 in itemized and standard deductions for District tax purposes, because the higher-income spouse could claim the entire \$20,000 of the itemized deductions and the other spouse could also claim a standard deduction of \$1,250.

Fifth, there are very extensive software and computer programming issues with implementing this legislation. Most electronic filing programs import information

directly from a taxpayer's federal tax return. These programs currently assume the taxpayer will elect to itemize for the state tax return if an election was made to itemize on the federal tax return. This bill will require OTR to rewrite its requirements for electronic filing programs.

There are very practical reasons for maintaining conformity with the federal income tax deduction elections. Such conformity eases the burden of compliance by taxpayers, reduces complexity, is likely to result in fewer filing errors, and reduces the cost of administration by the District.

Instead of modifying our conformity with the federal itemized deduction election, perhaps it would be more prudent to increase the District's standard deduction, such as currently proposed in Bill 17-0087 ("The Standard Deduction, Personal Exemption, and Homestead Deduction Increase Act of 2007").

There are also numerous technical defects and issues not addressed in the bill.

Fiscal Impact of Bill 17-0069

Funds are not sufficient to implement the proposed legislation. OTR will incur approximately \$800,000 in programming costs, \$258,830 in staffing costs, and \$150,000 in new form costs to implement the measure in FY 2007. Out-year costs are estimated to be approximately \$258,830 annually.

The proposed legislation would result in reduced revenue to the District of Columbia of \$3.1 million in FY 2008 and \$13.4 million in the FY 2008-2011 period.

Thus, for all of the above reasons, we recommend that the Council not enact this bill and, instead, consider alternatives.

Thank you, Chairman Evans, for the opportunity to comment on this bill. I would be happy to answer any questions you or other Councilmembers might have at this time.