BORGER
management inc.

DC Tax Revision Commission
Public Hearing June 6, 2013

Testimony of G. Thomas Borger, Chairman, Borger Management, Inc.

My comments today will be directed at the Unincorporated Business Franchise Tax.

Borger Management, Inc. manages office buildings, apartment buildings and numerous retail locations in Washington, DC. As part of our property management services we pay taxes on behalf of our clients. In calendar year 2012, we paid to the DC Treasurer $15,132, 474 in real estate taxes and $2,193,349 in Franchise Taxes. This is clearly a considerable amount of money and very significant expense for the building owners. Therefore, tax policy is a serious matter to me and my clients.

In addition to taxes paid on behalf of clients and partners, Borger Management paid a significant DC Unincorporated Business Franchise Tax for our property management business. However, unlike our properties which obviously cannot be moved to Virginia to avoid this tax, our management business can relocate, and we have considered this in the past and it is a consideration in our future plans. Like many small businesses in DC, relocation to a neighboring tax jurisdiction is fact of life and a major factor in the decision making of the business owners.

Furthermore, I have always found the DC Franchise tax inequitable and inappropriate for real estate taxable entities for the following reason: the tax has no direct relationship to property values or gross income. Partnerships and LLC's pay the tax based upon the calculation of taxable income that conforms with the IRS calculations. As a result, interest is a deduction from the gross income.

The consequence of this fact is that property without debt will pay taxes while an identical property with an identical rental income with debt may pay no taxes. We have properties without debt that pay nearly as much for DC Franchise taxes as for real estate taxes. Property owners are effectively penalized for debt-free buildings. Therefore, when an ownership entity evaluates the capital structure and cash return of its investment, the relationship between debt service and DC Franchise tax becomes a major consideration.

This is further complicated by the fact that most real estate is owned by pass-thru entities. Therefore, the DC Franchise tax paid by the LLC or Partnership is passed thru as a paid income tax to the individual partners. For DC residents this tax is a 100% tax credit on their personal income tax. In Maryland, the tax is partially recognized as income tax paid, but in Virginia it is not recognized at all. As a result, the DC Franchise tax has a disproportionate impact dependent upon the domicile of the partner.

Please review the attached schedule for three apartment buildings for which we are general partners. Note that for each property, the 2012 DC Franchise tax was virtually the same amount, yet the properties differ markedly in size, market value, location, rental income, and gross income. The Franchise tax bears no relationship to any of these comparison points. Note that the property which happens to be an affordable rental apartment building has the lowest gross income yet pays the highest percent of gross income for DC Franchise tax. As noted earlier, this tax is then passed-thru to the partners and then subject to varying treatment on their tax return based upon the jurisdiction in which it is filed.

This system cannot be construed as an appropriate method for rationale taxation of income producing real estate. Although I would greatly prefer the tax completely eliminated, but assuming DC cannot meet its financial responsibilities without the Franchise tax income, perhaps a modest gross receipts tax would make more equitable tax policy and produce comparable revenues for DC.

Testimony G. Thomas Borger
June 24, 2013

Unicorporated Business Franchise Tax
Comparison of Tax Liability

Calendar year 2012	**122 unit garden NE apartment**	**108 unit Dupont Circle**	**230 unit hi-rise Mass. Ave. NW**
Gross Income	$ 1,705,070	$ 2,528,060	$ 4,465,092
Taxable Income	$ 458,573	$ 458,614	$ 443,504
Real Estate Tax	$ 63,386	$ 229,794	$ 266,018
Unincorporated Business Tax	$ 45,743	$ 45,747	$ 44,240
Business Tax as % of Gross Income	**2.7%**	**1.8%**	**1.0%**