The Billion-Dollar Pitch
An Analysis of the Ballpark Omnibus Financing and Revenue Act of 2004

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The city council is considering a bill that would exempt more small businesses from the stadium tax and direct new tax revenues from development around the stadium to finance bonds issued to fund community programs. This document is an analysis of the new bill. It finds:

- More than 100 businesses with 20-50 employees will pay the stadium tax, down from more than 500 under the previous plan. All businesses with 50-100 employees (almost 800) will pay the tax.

- The tax is based on gross receipts. Profits are a very small share of receipts, making the tax a significant share of profits. Businesses with $4 million to $50 million in revenues will probably pay 2-3 percent of profits. Because it is capped at $48,000 the tax is regressive: larger firms will pay a smaller share of profits.

- The proposed Community Benefit Fund is expensive and financially risky.
    - Its initial $30 million will be "transferred" from other District funds, meaning that it will come at the expense of other city priorities.
    - The city can issue up to $450 million in bonds to pay for community development projects, with payments on those bonds to be financed through new taxes raised from economic development around the stadium. In other words, the city would try to secure financing on the hope that in the future there will be economic development in the neighborhood. If the hoped-for development around the stadium does not occur, the city will have to repay the bonds by cutting existing city priorities or raising new taxes.

- The new bill increases the approved cost of bringing the Expos to Washington to over $1 billion, assuming no cost overruns in stadium construction.

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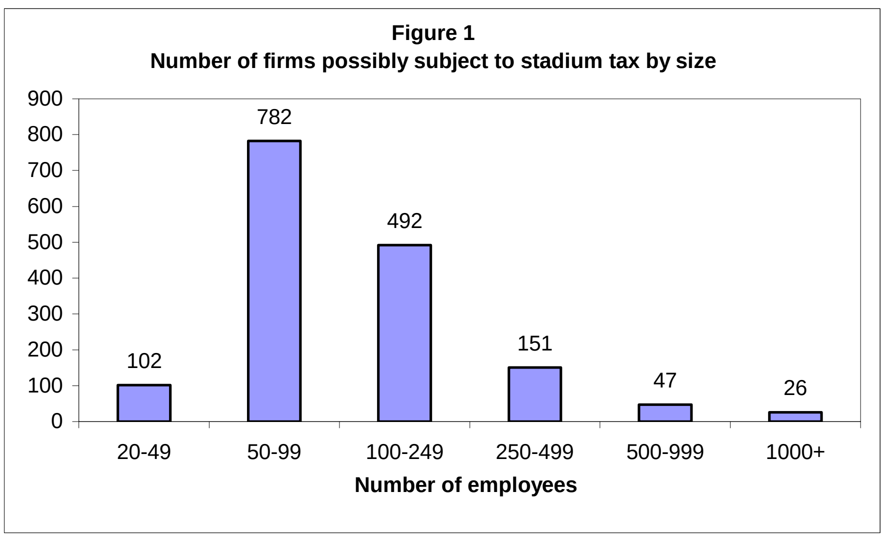
Fewer small businesses pay the tax, but it is a significant share of profits

The original stadium tax was to be levied on businesses with gross receipts of $3 million or more. In order to exempt more small businesses, the revised plan will levy a tax on businesses with gross receipts of $4 million or more. The D.C. Chamber of Commerce says this tax will apply to about 1,600 businesses.[1]

Who will pay the tax?

Although private businesses do not make their revenues public, US Census data allow us to estimate the types of firms likely to pay the tax by size and industry. Appendix 1 details our methodology.

Figure 1 reveals that the number of very large firms that will pay the tax is small, simply because there are few very large firms in the District. Approximately 100 businesses with 20-49 employees will be subject to the tax, while nearly 800 businesses with 50-99 employees will pay the tax.



Source: Authors' calculations from 2001 US Census County Business Patterns

These estimates are based on number of employees, while the tax is based on revenues. It is possible that there are many businesses with fewer employees but with revenues exceeding $4 million that will also pay the tax.

In short, while fewer small businesses will be subject to the tax, hundreds will still pay it. Many of those businesses will be restaurants and other entertainment venues that will lose some

[1] Personal communication with D.C. Chamber of Commerce (November 3, 2004). The Chamber estimates that 1,975 businesses would pay the tax if it is applied to all business with more than $3 million in gross receipts, and 1,596 if the tax is applied to all businesses with more than $4 million in gross receipts. These projections are based on 2001 data.

business as spending shifts to the stadium, meaning that these businesses will be taxed to subsidize their competition.

The tax can be a significant share of profits

The new tax is based on gross receipts. Profits, however, are much less than gross receipts—probably not much higher than five percent of gross receipts on average.[2] As a result, the tax as a share of profits can be substantial for many businesses.

Table 1 highlights this point. The table shows the proposed tax by gross receipts and translates the tax into share of profits for each size category. The data suggest that most businesses will pay 2 to 3 percent of profits as the stadium tax. Because the tax is capped at $48,000 the largest businesses pay a decreasing share of their profits as a stadium tax.

In other words, the tax is a significant share of profits for most firms and remains regressive: the largest firms pay relatively less than the smallest firms.

Stadium Tax as Share of Profits

Annual receipts (range)	Stadium Tax	Profits as share of sales before income taxes	Profits as share of sales after income taxes	Stadium tax as a percentage of profits
$4-8 million	$6,500	5.6	5.1	1.6 - 3.2%
$8-12 million	$11,800	5.3	4.7	2.1 - 3.1%
$12-16 million	$18,500	5.1	4.4	2.6 - 3.5%
$16-20 million	$25,000	5.1	4.4	2.8 - 3.6%
$20-25 million	$31,000	5.1	4.4	2.8 - 3.5%
$25-30 million	$39,000	5.3	4.3	3.0 - 3.6%
$30-50 million	$48,000	5.3	4.3	2.2 - 3.7%
$50-100 million	$48,000	4.4	3.2	1.5 - 3.0%
$100-250 million	$48,000	4.9	3.4	0.6 - 1.4%
$250 mil - $1 billion	$48,000	6.2	4.1	0.1 - 0.5%
$1 billion and over	$48,000	11.1	8.5	0.06% or less

[2] It is difficult to precisely calculate a firm's true profits without detailed knowledge of its accounts. This analysis is based on Census data on the manufacturing industry (data are for the 2nd quarter of 2004). There are few manufacturing firms in the District, meaning that this figure may not be representative. Unfortunately, profit margins by business size are not available for other industries. However, other information suggests that this estimate is reasonable. The Census reports that the average profit margin in wholesale trade is 2.2 percent. In addition, combining data from the Census economic survey with National Income and Product Accounts data from the Bureau of Economic Analysis yields an average profit margin across all industries of 3.2 percent. These additional pieces of information, though imperfect, suggest that our analysis may overstate profits for some firms in the District. According to Yahoo!Finance, profit margins for publicly-traded firms are higher: about 8.5 percent (unweighted) across industries most prevalent in the District. Few firms in the District that will pay the tax, however, are the headquarters of publicly traded companies.
Source: U.S. Census Bureau, Quarterly Financial Report for Manufacturing, Mining, and Trade Corporations (2004). Tables B and C.

The Community Benefits Project is Expensive and Risky

The proposed bill calls for a community benefit fund to “utilize the economic benefits that will be derived from the construction of the stadium for the benefit and well-being of the citizens of the District.”[3]

The Community Benefit Fund (CBF) will be funded by first by $30 million “transferred to the [CBF],” and up to $450 million in new bond issues. Payments on those bonds will be financed through taxes raised through creation of a “DC Ballpark TIF Area.”

Both of these financing schemes are problematic.

The initial $30 million will come from unnamed existing city services

The initial $30 million will be “transferred” into the CBF. To date the Mayor has not identified the source of the $30 million.[4] If the CBF actually funds projects that the city would not have otherwise undertaken, then the cost of the initial $30 million is the reduction of some existing city services plus new administrative costs of administering the fund. This transfer contradicts the spirit of the Mayor’s claim that the stadium will not affect any other aspect of the District’s budget.[5]

Bond-issue financed by a TIF

The District proposes to create a “DC Ballpark TIF [tax increment finance] Area” around the stadium. TIFs, authorized by the District in 1998, are geographic areas in which tax revenues above a baseline amount—typically the taxes paid the year prior to implementing the TIF—are designated for a particular purpose. TIFs are targeted at areas where the city projects growth from new development projects. The District issues bonds to pay for specified initiatives under the assumption that economic growth in the TIF area will generate sufficient new tax revenues to pay the interest on the bonds.

The TIF plan has several flaws and is risky.

First, a TIF itself generates no new net tax revenues. Instead, it simply designates that any new revenues in a specific area be used for a particular purpose—in this case, repaying bonds used for the CBF. Because the TIF does not generate additional tax revenues, in reality it is little

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[3] Bill 15-1028. Title II: Community Benefits Projects

[4] Personal communication, Cynthia Broch-Smith, Vice President of External Affairs at the D.C. Chamber of Commerce (November 4, 2004).

[5] Use of the funds is vague, intended for use in “the financing, refinancing, or reimbursing of costs incurred in the site acquisition for, and the development, design, construction, improvement, furnishing, and equipping of recreation centers, libraries, small business development incentives, job training and readiness programs, school athletic facilities and such other projects to be of benefit to any community of the District.”
Because of this vagueness, it is possible that the funds would be used for a project that would have happened without the CBF. In that case, the CBF did not occur at the expense of some existing program, but would simply have no effect at all except for the additional administrative costs the District would incur.

different from the city issuing new bonds without a TIF. One difference, though, is that the TIF will incur administration expenses, meaning that the TIF is more costly than if the new revenues from economic growth went directly into the general fund.

Second, under the plan the city will issue bonds under the assumption that tremendous economic growth will occur within the designated TIF geographic area. Indeed, TIF revenues can repay the bonds only if development occurs. This assumption is especially problematic in the case of the stadium. Independent research finds that stadiums create little economic growth in their surrounding neighborhoods.

That is, given past experience it is irrational and irresponsible to assume with 100 percent certainty that such development will occur, as the city is doing to finance these new bonds. And as discussed in a previous analysis, DC's stadium is designed to capture as much fan spending inside the stadium as possible, further reducing the chance of economic growth in the surrounding neighborhood.

Even if we assume that there will be economic growth inside the TIF area, it is unlikely that it could raise enough revenues to pay the debt service on $450 million. Debt service payments for that level of borrowing will be approximately $25 million per year. To fund stadium construction, the city may issue up to $550 million in bonds. To cover that debt service the city is relying on rent from the Expos, taxes on baseball-related sales, and a controversial new business tax (discussed above). Covering the debt service on the CBF bonds will require almost as much new tax revenue as the stadium bonds. The city has not produced any credible evidence that it can raise a similar amount solely from new taxes in this tiny geographic area.

If the city issues the bonds and, as past experience from other cities suggests, development around the stadium is less than expected, the city will have two choices to pay off the bonds. It could either expand the boundaries of the TIF to raise additional revenues, or it could finance the bonds through other means. In other words, the city would have to either divert revenues from other sources or increase other taxes.

The Community Benefits Project is ill-conceived and poorly-planned. The initial $30 million must come from existing city revenues, meaning some other city priority will suffer or taxes will be raised. The TIF plan assumes that there will be tremendous economic development around the stadium. If that development does not occur, or is less robust than expected, the city will be forced to find other ways to repay these bonds.

Conclusion

The proposed stadium financing plan would allow the District to issue $550 million in bonds for the stadium, another $450 million in bonds for the CBF, and reallocate $30 million from other city priorities.

In other words, rather than making the stadium agreement more beneficial to the District, baseball may now cost the city more than $1 billion, even assuming no construction cost overruns. By comparison, the Mayor's entire FY2005 budget is just over $4 billion.

If the stadium raises less tax revenues or costs more than expected, the mayor will be forced to increase the business tax to repay the construction bonds. Indeed, the baseball agreement requires the mayor to increase the business tax if revenues are insufficient. Likewise, if the city cannot raise enough tax revenues in the TIF area to pay its debt service on the CBF bonds, it will be forced to find other ways to pay it. Past experience suggests that both bad outcomes are likely to occur.

The criticisms of the baseball agreement raised in a previous analysis remain true; the city has not refuted a single argument made there. The new financing plan, while exempting more small businesses from the tax, makes the District's baseball gambit even more expensive and risky.

Appendix 1: Estimating the number of firms paying the stadium tax

County business patterns (CBP) provides an annual breakdown of firms by size range and industry.[6] Data for 2001 are the latest available. This is the same year of data used by the D.C. Chamber of Commerce in its projections. The data show a total of 19,689 non-government "establishments" employing 422,549 people in the District.[7]

The data show the number of firms in each size category in each industry represented in the District. It is therefore possible to estimate the size categories of the 1,600 largest firms, by employment, and their industry.

In 2001, 26 businesses had more than 1000 employees, 47 had 500-999, 151 had 250-499, 492 had 100-249, and 782 had 49-99 employees. This represents the 1,498 largest businesses.

The next smallest size category is 20-49 employees. In 2001 there were 2,014 businesses employing a number of workers in this range. If the largest 1,600 businesses in the District will pay the tax, then somewhat more than 100 firms in this group, or about 5 percent, will pay the tax.

Table A.1
Firms subject to stadium tax by industry and size

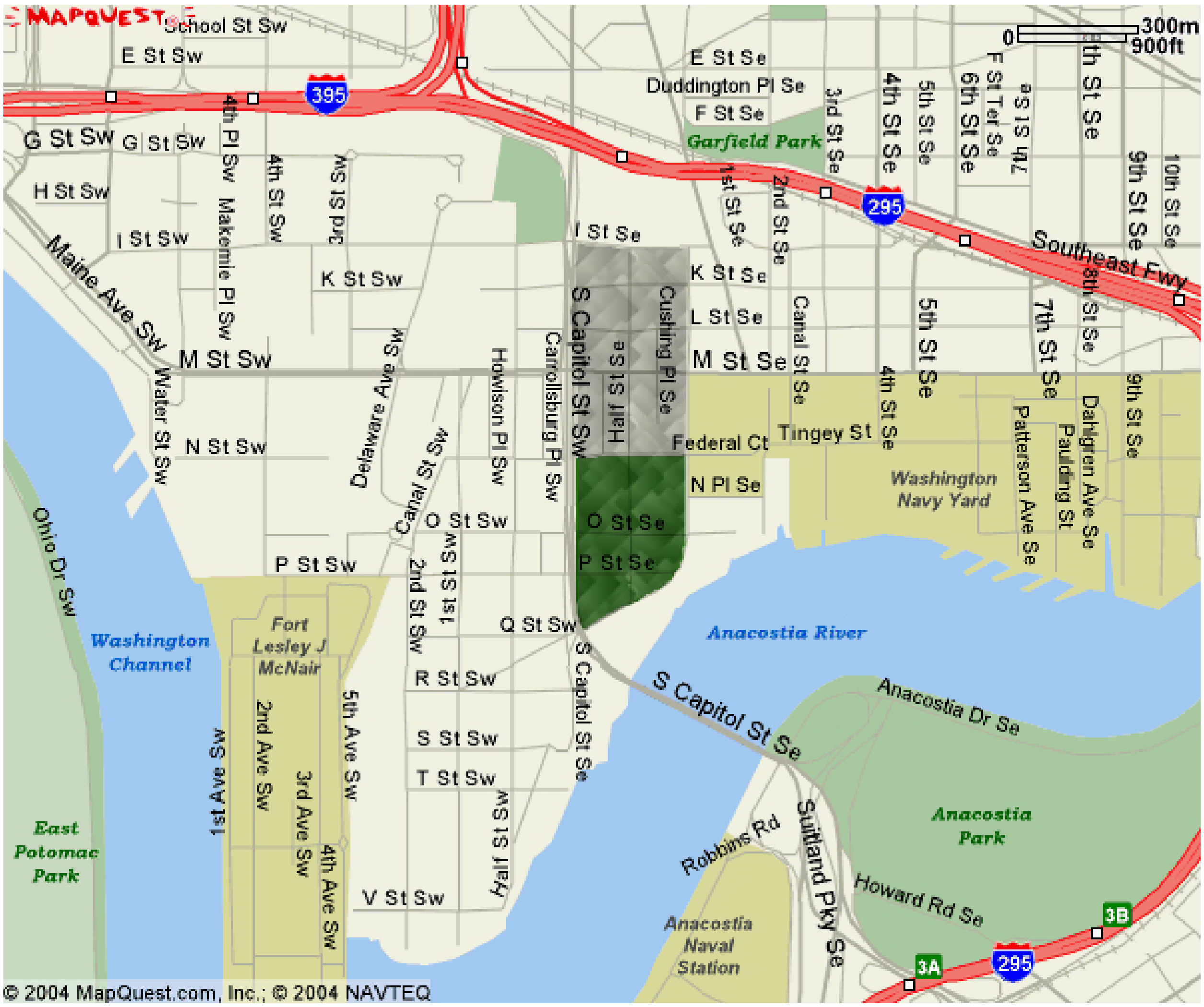
Industry	Number of establishments subject to tax with this range of employees						Total establishments in industry subject to tax
	20-49	50-99	100-249	250-499	500-999	1000+	
Utilities	0	0	1	2	1	0	4
Construction	2	23	11	1	1	0	38
Manufacturing	1	11	3	0	0	0	15
Wholesale trade	2	12	12	1	0	0	27
Retail trade	7	42	13	2	0	0	64
Transportation & warehousing	1	11	10	1	0	0	23
Information	5	38	29	16	6	2	96
Finance & insurance	5	25	19	3	1	2	55
Real estate & rental & leasing	2	19	11	5	0	0	37
Professional, scientific & technical services	21	172	119	32	16	1	361
Management of companies & enterprises	1	8	11	1	1	0	22
Admin, support, waste mgt, remediation services	6	69	55	18	4	1	153
Educational Services	3	32	18	8	1	7	69
Health care and social assistance	9	48	36	15	4	12	124
Arts, Entertainment, & recreation	1	17	5	2	1	0	26
Accommodation & food services	16	129	65	18	5	0	233
Other services	20	124	73	24	6	1	248
Auxiliaries (exc corporate, subsidiary & regional mgt)	0	2	1	2	0	0	5
Total establishments subject to tax	102	782	492	151	47	26	1600

Source: Authors' calculations from 2001 US Census County Business Patterns

[6] US Census County Business Patterns (http://www.census.gov/epcd/cbp/view/cbpview.html). Industry definitions based on North American Industrial Classification System: http://www.census.gov/epcd/cbp/download/naics.ref. Size ranges are 1-4, 5-9, 10-19, 20-49, 50-99, 100-249, 250-499, 500-999, and 1000+ employees.
[7] An "establishment" is not exactly the same as a "business." According to the Census, "An establishment is a single physical location at which business is conducted or services or industrial operations are performed. It is not necessarily identical with a company or enterprise, which may consist of one or more establishments. When two or more activities are carried on at a single location under a single ownership, all activities generally are grouped together as a single establishment. The entire establishment is classified on the basis of its major activity and all data are included in that classification." For clarity we will use the term "business" instead of "establishment." http://www.census.gov/epcd/cbp/view/genexpl.html

Appendix 2: Location of the Stadium and TIF

This map shows the proposed location of the new stadium and the proposed Ballpark TIF. The stadium will be bounded by N Street, SE, Potomac Avenue, SE, South Capitol Street, SE, and 1st Street, SE. The TIF area is bounded by I Street, SE, Potomac Avenue, SE, South Capitol Street, SE, and 1st Street, SE.



Note: The location of the stadium and stadium facilities is shown in green. The D.C. Ballpark TIF area includes the green as well as the grey shaded areas.