CENTER CITY DISTRICT

A Small Down-Payment On Growth

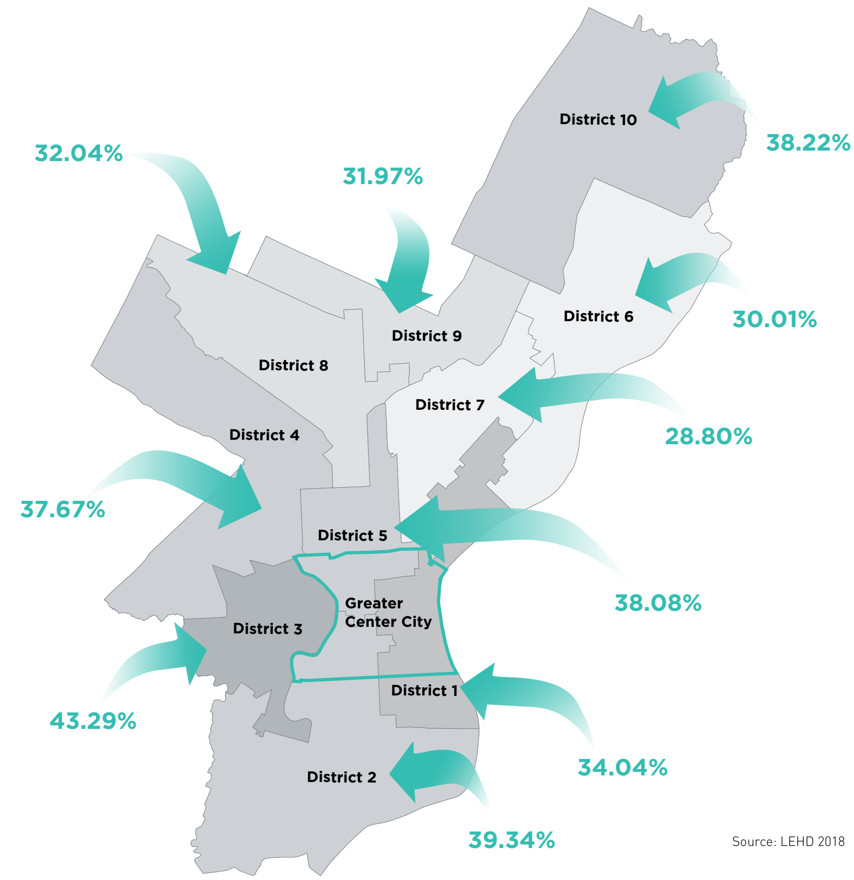
How Tax Policy Shapes Opportunity and Equity

This is a transformational moment for Philadelphia, when investments in economic development funded by the American Rescue Plan (ARP) can be combined with the long-recommended changes to Philadelphia's tax structure to prompt faster and more equitable citywide job growth.

We've lived so long with Philadelphia's wage tax that we've lost the ability, after 82 years, to see how it takes money out of the pockets of lower-income workers, weakens the City's financial stability, pushes businesses, jobs and residents out of the city and now constrains opportunity and economic recovery.[1]

The Chief Financial Officer of the District of Columbia calculated that of 51 major U.S. cities, Philadelphia has highest combined state and local tax burden for a family earning $25,000/year.[2] Families with annual incomes of $25,000 or less comprise 28% of all Philadelphia households. For them, the math is clear: 3.8% of $25,000 is $950 per year. That covers much of a month's rent in most Philadelphia neighborhoods. In 50 other cities, low-income workers keep more take-home pay.

Figure 1: Percentage Of Workers In Each City Council District Who Commute In From Surrounding Suburbs



Source: LEHD 2018

The Pandemic's Wake-Up Call:

With the loss of 120,000 jobs at the start of the pandemic, Philadelphia experienced in just one year what two tax commissions warned about for decades: the perils of funding government with wage taxes when digital technology enables many workers and businesses to locate almost anywhere. The two cities that suffered the largest revenue losses and service cuts during the pandemic, according to the Pew Charitable Trusts, were Detroit and Philadelphia, both heavily reliant on wage tax revenues that plummeted with job losses. Boston suffered less because it funds local government primarily through the more stable property tax.[3]

We've regained one-third of the jobs lost in March and April of 2020, but the wage tax may retard full recovery. Pre-pandemic there were 284,500 suburban residents who commuted into Philadelphia. Should they continue to work remotely, as during the last 15 months, they remain exempt from the City's wage tax. In short: stay home, get a raise and let your employer save money

1: Philadelphia's wage tax debuted in 1939 as a 1% temporary stopgap to compensate for lost real estate values in the Great Depression. It slowly crept up to 1.5% by the early 1960s and then, as the city hemorrhaged people and jobs in the 1970s and 1980s it was doubled and doubled again until it peaked at 4.96% in the late 1980s, where it remained through 1995. A study by Wharton professor Robert Inman and colleagues found that Philadelphia lost 172,000 jobs due to wage tax increases between 1971 and 2001. In 1996, Mayor Edward Rendell, persuaded by Inman's analysis, began a series of incremental cuts that continued through his second term and for eight years during Mayor John Street's administration but were suspended by Mayor Michael Nutter in 2010 during the Great Recession. The reductions made in the last decade were much smaller than those made from 1996 to 2008 – with the average rate cut less than one-fifth of the average from 1996 to 2010.

2: *Tax Rates and Tax Burdens: - A Nationwide Comparison*, April 2021

3: "How the Pandemic Has Affected Municipal Budgets in Philadelphia and Other Cities" Pew Charitable Trusts. March 30, 2021 on office costs. If just 15% remain remote, as the City's budget director estimates, $100 to $120 million will be lost annually in wage tax revenues to support municipal services. When office space stays vacant, there's less need for thousands of building janitors, security staff, mechanical operators or transit workers and fewer customers for nearby restaurants and retail. Diverse employment sectors are interconnected.

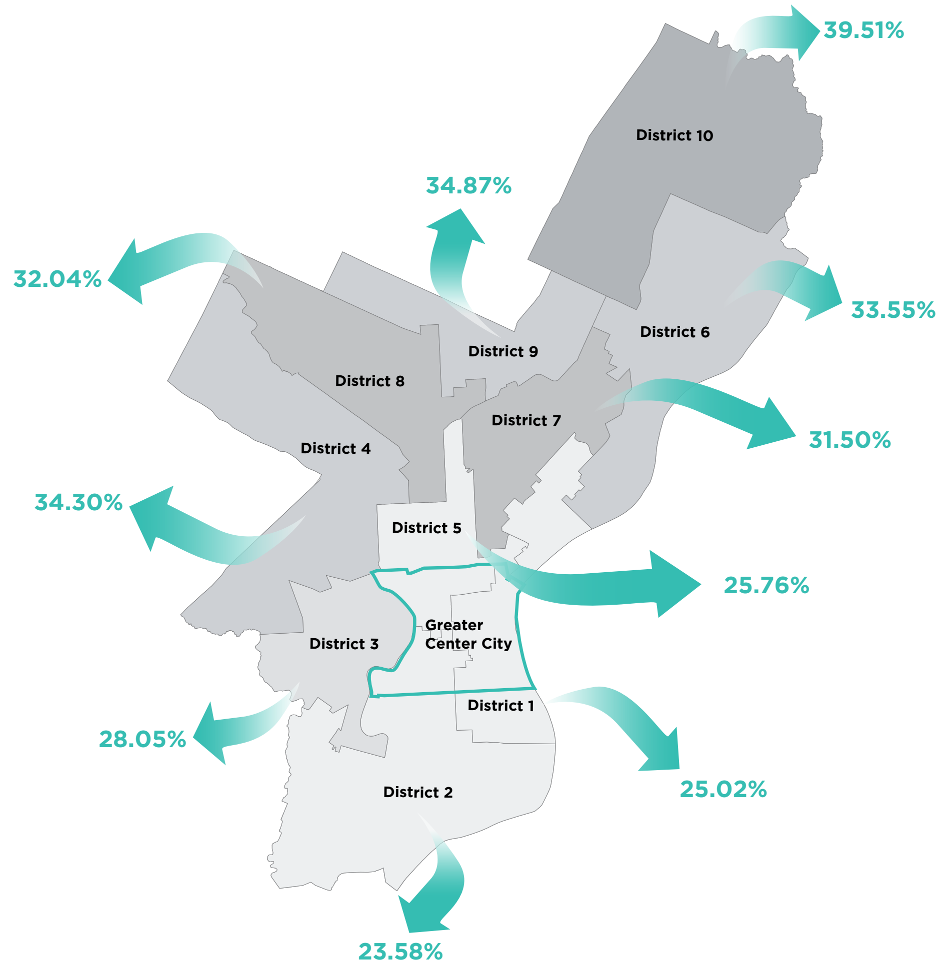
Political Borders Aren't Economic Boundaries:

It may come as a surprise to some, but this isn't just a downtown issue. One-third of those who work in Philadelphia live in Philadelphia. But pre-pandemic, another *30% of those employed at businesses and organizations in each City Council district were suburban residents commuting into the city* (Figure 1). Lose them and nearby neighborhood businesses — dry cleaners, auto mechanics, sandwich shops — lose purchases made by commuters at lunch and after work.

Commuting within the region is a two-way street (Figure 2). Between 30% and 40% of the working residents of each City Council district *reverse commute* to the suburbs each day. These 224,500 reverse-commuters still pay Philadelphia's 3.8% wage tax. But they work alongside suburban peers who pay a wage tax of just 1% or less to their municipality, where a stronger property tax base provides more funding for schools. This creates a potent combination of incentives to move to the suburbs: a shorter commute, a pay raise and better-funded schools.

This isn't just theory. While the population has grown in Center City, more Philadelphians moved in the last decade from the city to suburbs than moved the other way. IRS data suggest that from 2011 to 2018, 128,000 households moved from the city to the suburbs, while only 100,000 moved in the other direction, a net loss of 28,000 city households. Overall, Philadelphia had been gaining population each year since 2007, due to local births and immigration. However, recent Census data suggests that pre-pandemic, 2018 to 2020, Philadelphia's population actually declined. The losses were from our neighborhoods.

Figure 2: Percentage of Employed Population Living in the Council District and Working in the Suburbs



30% to 40% of the working residents of each City Council district *reverse commute* to the suburbs each day

SEE APPENDIX A FOR WORKFORCE LOCATION AND COMMUTING PATTERNS FOR EACH CITY COUNCIL DISTRICT

One reason why Philadelphia has such a high poverty *rate* is that we keep losing the working and middle class from neighborhoods outside Center City. IRS data shows that out-movers have higher average incomes than in-movers. When a Council district loses population, it not only loses customers for its small businesses, it loses representation in Harrisburg and Washington.

Philadelphia is also unique among all major cities in having a business income and receipts tax (BIRT) that takes a bite out of both gross and net income. There is no counterpart in the suburbs. Several years ago, when suburban and downtown office rents were both around $30 per square foot, a CCD analysis of Revenue Department data found that BIRT added from $6 to $16 per square foot to downtown occupancy costs, depending on the type of firm. Combine BIRT's bite with the impact of the wage tax and what comes into focus is the distorting effect of Philadelphia's tax mix on where residents and businesses choose to locate in the region. Wage and business taxes in the proposed 2022 budget account for 65% of local tax revenue; the real estate tax brings in just 18%. In Boston, it accounts for close to 70%.

Too Few Businesses:

The Philadelphia region holds 17.3 businesses per 1,000 adults. The city has just 12.1 businesses per 1,000 adults – 30% less business concentration than the region (Figure 3). Low business density means fewer job opportunities and lower workforce participation.

By contrast, a more auto-dependent region like Atlanta has 17.5 business per 1,000 adults, while the city's businesses density is 40% greater than the region: 24.6 businesses per 1,000 adults. Compared to Philadelphia, Atlanta has double the density of businesses in the city. None of our East Coast peers lag so far behind the business density of their regions. This limits accessible opportunities for Philadelphia's residents, especially those without cars, and encourages out-migration of other workers to more job-dense suburbs. For residents seeking family sustaining jobs, it doesn't help that in the decade before Covid, only 26% of jobs added in the city were family-sustaining, while in the suburbs, it was 62%.

Across the nation, there are pronounced disparities between Black- and brown-owned businesses and all other businesses. In Philadelphia these disparities are further compounded by lower business density overall (Figure 4). Washington has 2.8 times Philadelphia's number of Black-owned businesses per 1,000 Black adults; Atlanta has 2.5 times our Black business density; and New York's Black business density is 1.9 times ours.

A Unique Moment for Change:

The American Rescue Plan (ARP) gives Philadelphia the means to invest in Black and brown businesses, in neighborhood commercial corridors and in all forms of economic development. But we require more fertile ground for these business to grow. Many minority businesses start by serving their neighborhoods. Grocery stores, hair and nail salons may stay focused there, but they're constrained if the neighborhood's income is low and its population is declining. Accountants, architects, contractors, lawyers and public relations firms can take on more employees if they expand market share. They can do this in multiple ways, but the most convenient is to sell products and services to other businesses in the city. There is good work now being done by large businesses and institutions diversifying their purchase of services and supply chains by connecting with local Black, brown and Asian businesses. But slow growth and low business density within the city, limit the quantity and buying power of existing firms.

Figure 3: Businesses Per 1,000 Residents, City and Region, 2017

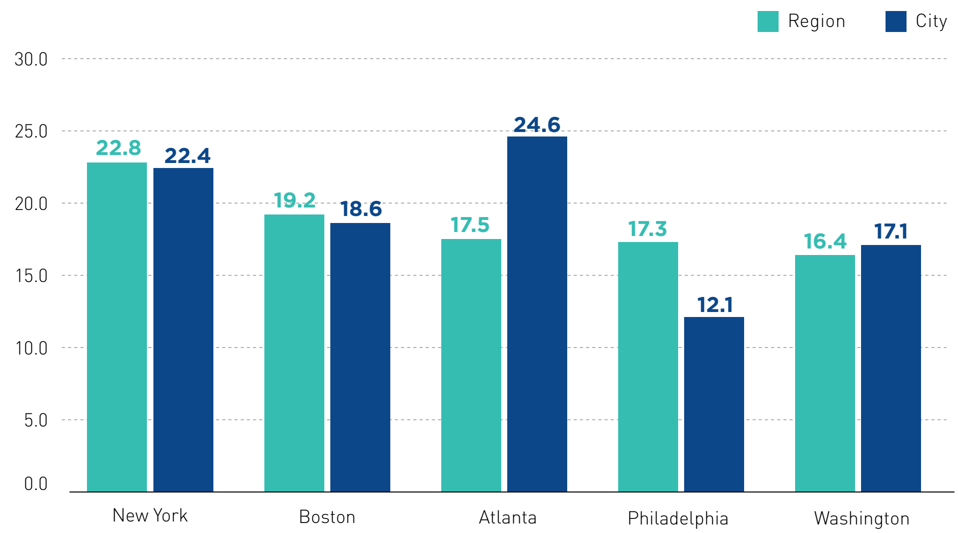
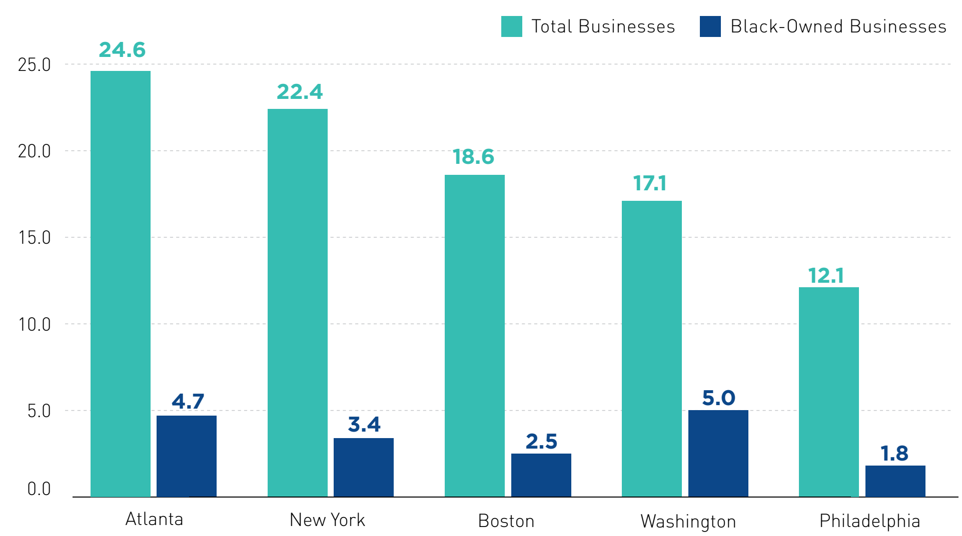


Figure 4: Total Businesses and Black-owned Businesses per 1,000 Residents, Major Cities 2017



Low business density limits local job opportunities

Reshaping the Location of Opportunity in the Region:

Pocket-book politics matter. But tax-policy is a critical tool for reshaping the location of jobs and opportunity within the region. When Philadelphia was in decline, our suburbs expanded, factories departed, neighborhoods were redlined and property values fell. That's what drove the dependence on wage and business taxes in the 1970s and 1980s. Yet, the more these taxes were raised, the more sensible it was for workers and employers to move beyond our boundaries. Business density, employment opportunity and regional wealth all relocated to the suburbs (Figures 5, 6). The tax base that remains to underwrite our schools on a per student basis is just one-third that of our western suburbs.

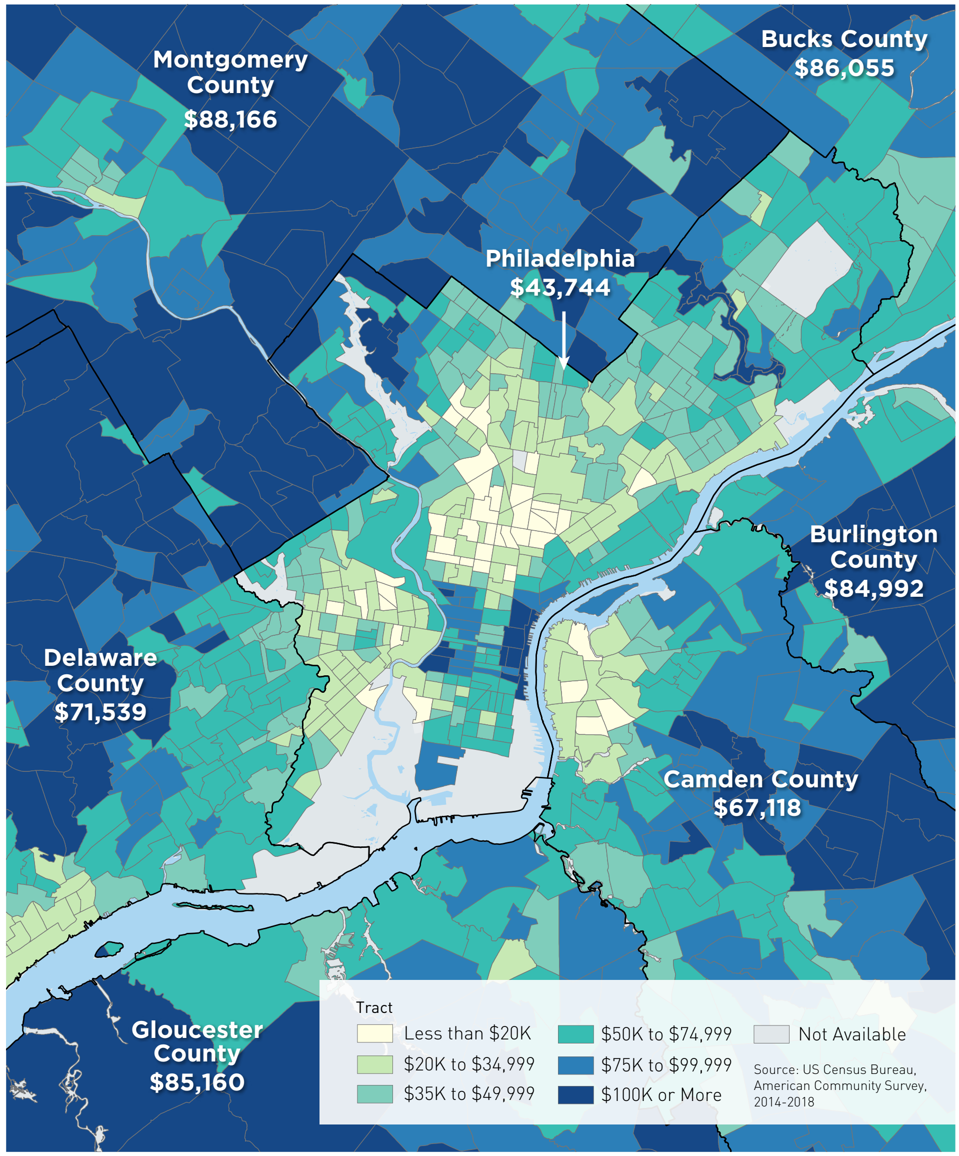
The New Value Proposition for Cities:

What's changed in the last quarter century is the value proposition for cities. Factories and railroads no longer dictate the location of jobs. Mobile employers are drawn by a diversified workforce: skilled laborers, immigrant and local entrepreneurs, tech-savvy millennials and college-educated professionals. Make our costs for doing business comparable to those in the region and our extraordinary advantages come to the fore: an accessible international airport, strong transit connectivity, diverse, affordable and walkable neighborhoods and an abundance of parks, arts, educational, research and cultural organizations.

Invest in these assets and amenities as we invest in Black and brown businesses, in economic development and in our schools and more people and business will choose to locate here. The American Recue Plan is an opportunity not just to restore the status quo, but to address long unresolved challenges that have held Philadelphia back.

This is a city built for 2.1 million residents that currently houses just 1.5 million with huge amounts of unused, old industrial land. Encourage businesses to make productive use of this land and the real estate tax base of the city will expand as many more shoulder a burden currently carried by too few. A local government supported by taxes on things that don't move – land and improvements – is a government more sheltered from future storms, a government that lowers the barriers to entry and accelerates opportunity for all. Tax policy is a potent lever for change largely within local control. When strategic investments are combined with tax policy changes that benefit all, Philadelphia can embark on path toward more expansive and inclusive growth.

Figure 5: Median Household Income, City and Suburbs



Current Budget Choices:

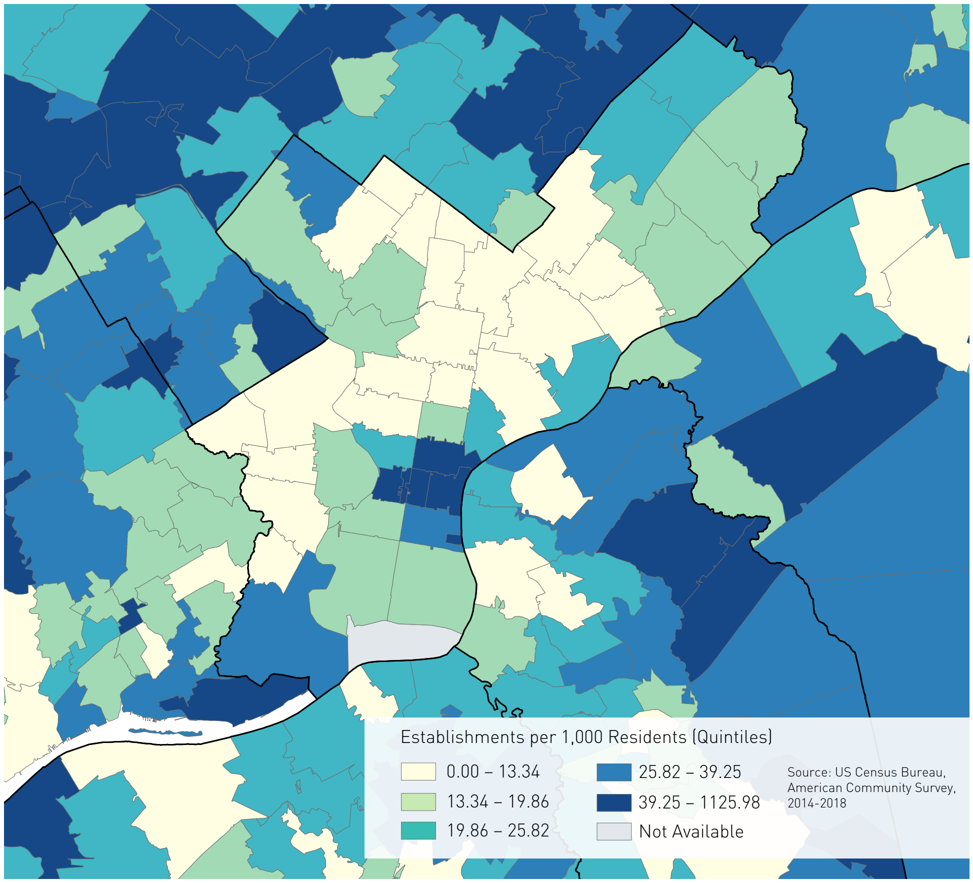
Mayor Kenney's proposed budget for fiscal year 2022 devotes 30% of general fund spending to public safety: police, fire and the criminal justice system; 28% goes to employee benefits and pension liabilities; 10% to administration; 10% to debt service; 8% to economic development, streets, sanitation, libraries, parks and recreation; 7% to health and human services and 7% to education, not counting funding the School District receives directly from the property tax. So more than 50% of the budget is devoted to direct services to Philadelphia residents.[4]

4: Housing, homeless programs, community development and social services are also supported by block grants from the federal government, over and above the General Fund.

The proposed budget rolls back last year's increase in the wage tax on suburban residents, resumes wage tax reduction for residents and restarts cuts in business taxes. Add these up and the administration is proposing to commit just 0.64% of General Fund expenditures to wage and BIRT reduction. In subsequent years, the proposed cuts become more modest. So the appropriate comparison is 52% for direct services to residents and 0.64% for tax reduction.

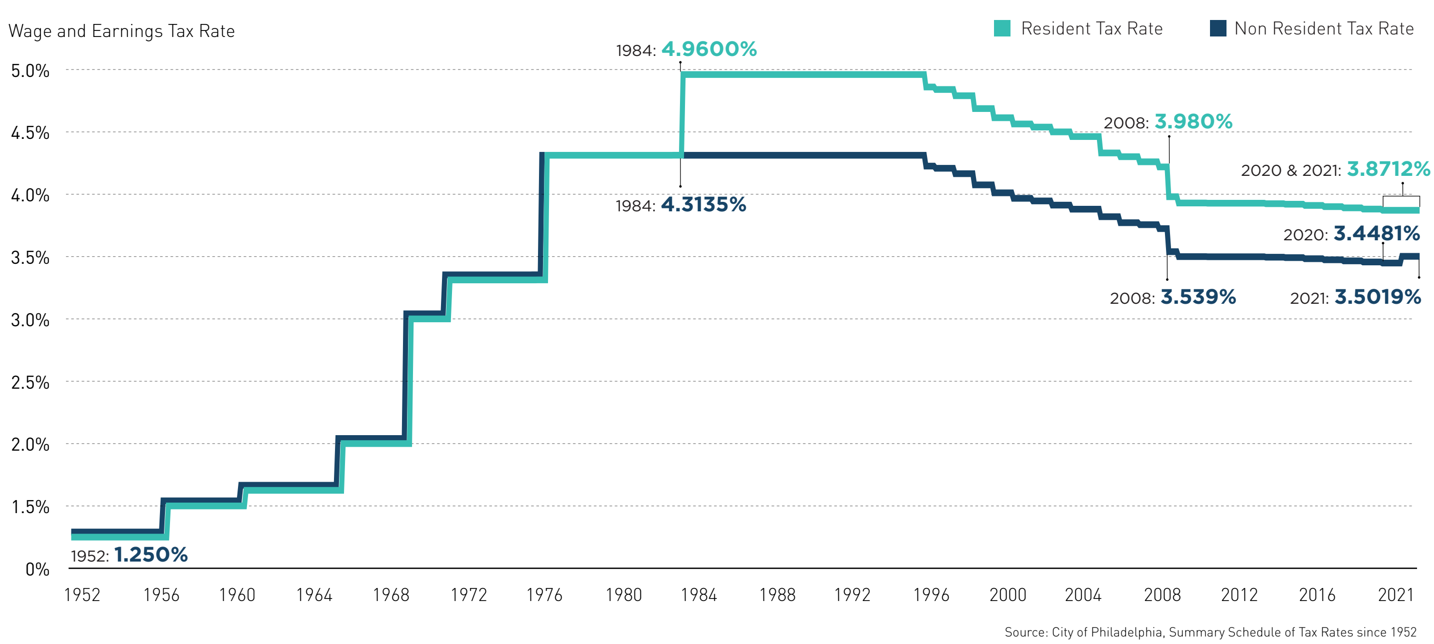
Through recurring, annual wage tax cuts from 1996 to 2010, the City significantly reduced the resident wage tax from 4.96% to 3.93%, steadily increasing the take-home pay for residents (Figure 7).[5] Similarly, the gross receipts portion of the BIRT declined by 56% (from 3.25 mills to 1.415 mills). What followed, in the recovery from the Great Recession, was the longest period of job growth in Philadelphia since the 1920s and the first increase in population in seven decades.

Figure 6: Where Businesses are Located Within the Region



Through annual reductions from 1996 to 2010, the City significantly reduced wage and businesses taxes. What followed, in the recovery from the Great Recession, was the longest period of job growth in Philadelphia since the 1920s.

Figure 7: Wage and Earnings Tax Rate History, 1952-2021



5: Through subsequent, more modest cuts between 2010 and 2019, the rate was further reduced to 3.87%.

Setting a New Course for Faster Growth:

Think of what can be achieved in a rebound from the pandemic if ARP-funded investments in economic development are combined with a sustained stepping down of tax rates, similar to the trajectory from 1996 to 2010. If the City devotes just 1% of budgeted spending annually to tax reduction, or about $50 million out of a $5 billion budget in each of the next five years, allocating 70% to wage tax reduction and 30% to reduce the net income portion of BIRT, it can ignite a new, broader cycle of growth.[6]

Wage tax reduction is the most direct, broad based stimulus since it puts money directly in pockets of more than 670,000 resident wage earners (plus sole proprietors not included in that number) and 284,500 suburban commuters. It frees money up to spend on housing, food and consumer purchases that radiate throughout the local economy. BIRT reductions benefit about 30,000 businesses. Cuts can encourage new businesses to start, Black and brown businesses to expand and major firms to stay here and grow.

Unlike the federal stimulus, these reductions deliver benefits each year and build upon themselves. A five-year plan that commits 1% of general fund revenues to wage and BIRT reduction also sends a signal to those considering locating in Philadelphia that they can count on predictable, steadily declining costs (Figure 8).

This tax schedule does far more than put dollars into the hands of residents and businesses. It alters our competitive position and the location of opportunity in the region. This happens in two fundamental ways: First, by lowering costs that consistently push residents, businesses and family-sustaining jobs out of the city, the competitive advantages of Philadelphia can come to the fore. We can leap from the back of the pack in job creation among major American cities to become one of the fastest growing. Second, by undoing damaging decisions made in the 1970s and 1980s and weaning the City from its dependence on wage and business taxes, it creates a climate for Black and brown businesses, new life-sciences industries and tech startups to expand, while making it easier for existing firms to remain and grow. All of this creates demand for more real estate and new construction jobs.

In the coming decade, we can fill many of the job deserts in the city, shown in Figure 6, with new and expanding businesses and more accessible employment opportunities for residents. As more firms make improvements on unused real estate, the City's tax *base* grows. Many more shoulder the costs so *rate* increases are not required as real estate's share of city taxes steadily rises from a meager 18%, expanding at the same time resources for public schools.

This is a transformational moment not likely to come again soon. The American Rescue Plan's $1.4 billion can fill budget gaps. But it can also fund multimillion-dollar equity and economic development investments, while covering transition costs from a tax structure that has constrained opportunity to one that supports robust and inclusive prosperity. One percent of $5 billion is a small down payment on accelerated and equitable growth.

Figure 8: Proposed Tax Rate Schedule

Resident Wage Tax	
FY21	3.8712%
FY22	3.8079%
FY23	3.7446%
FY24	3.6813%
FY25	3.6180%
FY26	3.5547%
Non-Resident Wage Tax	
FY21	3.5019%
FY22	3.4446%
FY23	3.3874%
FY24	3.3301%
FY25	3.2728%
FY26	3.2156%
BIRT Net Income Tax	
TY2020/FY2021	6.200%
TY2021/FY2022	5.928%
TY2022/FY2023	5.656%
TY2023/FY2024	5.384%
TY2024/FY2025	5.112%
TY2025/FY2026	4.840%

> **This is a transformational moment not likely to come again. ARP's $1.4 billion can fill budget gaps, fund multimillion-dollar equity and economic development investments and expedite long-recommended changes to our tax structure**

6: There has been some debate in legal circles as to whether ARP funds may be used to reduce taxes. The legislation limits states abilities to do this but not cities. Even so, while this report refers to a commitment of general fund revenues, tax reduction does not entail an expenditure of revenues but rather a foregoing of collecting revenues through the reduction in rates.

Appendix A

Council District 1

	2008	2018	DIFFERENCE	% CHANGE	% DISTRICT RESIDENTS BY WORK LOCATION IN 2018
Total employed population living in the 1st District	56,031	73,459	17,428	31.10%	—
Living and Employed in the 1st District	13,005	15,739	2,734	21.02%	21.43%
Working in Greater Center City	21,008	25,410	4,402	20.95%	34.59%
Working in Philadelphia outside both 1st District & Center City	3,599	5,706	2,107	58.54%	7.77%
Working in the suburbs	13,764	18,383	4,619	33.56%	25.02%
Working outside of the Region	4,655	8,221	3,566	76.61%	11.19%
Total employees regardless of residence working in the District	119,875	146,930	27,055	22.57%	% District workers
Living in the suburbs and working in the District	39,048	50,019	10,971	28.10%	34.04%

Council District 2

	2008	2018	DIFFERENCE	% CHANGE	% DISTRICT RESIDENTS BY WORK LOCATION IN 2018
Total employed population living in the 2nd District	54,505	68,484	13,979	25.65%	—
Living and Employed in the 2nd District	8,081	9,489	1,408	17.42%	17.41%
Working in Greater Center City	11,602	13,621	2,019	17.40%	24.99%
Working in Philadelphia outside both 2nd District & Center City	18,340	22,037	3,697	20.16%	40.43%
Working in the suburbs	14,461	17,519	3,058	21.15%	32.14%
Working outside of the Region	4,515	6,587	2,072	45.89%	12.09%
Total employees regardless of residence working in the District	75,842	92,639	16,797	22.15%	% District workers
Living in the suburbs and working in the District	28,079	35,222	7,143	25.44%	39.34%

Council District 3

	2008	2018	DIFFERENCE	% CHANGE	% DISTRICT RESIDENTS BY WORK LOCATION IN 2018
Total employed population living in the 3rd District	47,901	55,783	7,882	16.45%	—
Living and Employed in the 3rd District	7,631	8,802	1,171	15.35%	15.78%
Working in Greater Center City	11,602	13,621	2,019	17.40%	24.42%
Working in Philadelphia outside both 3rd District & Center City	10,081	11,910	1,829	18.14%	21.35%
Working in the suburbs	13,984	15,647	1,663	11.89%	28.05%
Working outside of the Region	4,603	5,803	1,200	26.07%	10.40%
Total employees regardless of residence working in the District	67,890	89,523	21,633	31.86%	% District workers
Living in the suburbs and working in the District	28,260	38,754	10,494	37.13%	43.29%

Council District 4

	2008	2018	DIFFERENCE	% CHANGE	% DISTRICT RESIDENTS BY WORK LOCATION IN 2018
Total employed population living in the 4th District	59,565	65,448	5,883	9.88%	—
Living and Employed in the 4th District	4,919	4,979	60	1.22%	7.61%
Working in Greater Center City	15,297	15,694	397	2.60%	23.98%
Working in Philadelphia outside both 4th District & Center City	14,793	16,652	1,859	12.57%	25.44%
Working in the suburbs	19,886	22,450	2,564	12.89%	34.30%
Working outside of the Region	4,670	5,673	1,003	21.48%	8.67%
Total employees regardless of residence working in the District	28,474	35,929	7,455	26.18%	% District workers
Living in the suburbs and working in the District	10,136	13,535	3,399	33.53%	37.67%

Council District 5

	2008	2018	DIFFERENCE	% CHANGE	% DISTRICT RESIDENTS BY WORK LOCATION IN 2018
Total employed population living in the 5th District	47,466	61,099	13,633	28.72%	—
Living and Employed in the 5th District	9,394	11,796	2,402	25.57%	19.31%
Working in Greater Center City	15,301	18,857	3,556	23.24%	30.86%
Working in Philadelphia outside both 5th District & Center City	6,163	8,557	2,394	38.84%	14.01%
Working in the suburbs	12,381	15,742	3,361	27.15%	25.76%
Working outside of the Region	4,227	6,147	1,920	45.42%	10.06%
Total employees regardless of residence working in the District	145,386	162,364	16,978	11.68%	% District workers
Living in the suburbs and working in the District	54,767	61,821	7,054	12.88%	38.08%

Council District 6

	2008	2018	DIFFERENCE	% CHANGE	% DISTRICT RESIDENTS BY WORK LOCATION IN 2018
Total employed population living in the 6th District	61,053	63,774	2,721	4.46%	—
Living and Employed in the 6th District	6,613	6,192	-421	-6.37%	9.71%
Working in Greater Center City	11,572	11,535	-37	-0.32%	18.09%
Working in Philadelphia outside both 6th District & Center City	17,540	17,998	458	2.61%	28.22%
Working in the suburbs	20,227	21,399	1,172	5.79%	33.55%
Working outside of the Region	5,101	6,650	1,549	30.37%	10.43%
Total employees regardless of residence working in the District	34,839	38,399	3,560	10.22%	% District workers
Living in the suburbs and working in the District	10,188	11,522	1,334	13.09%	30.01%

Council District 7

	2008	2018	DIFFERENCE	% CHANGE	% DISTRICT RESIDENTS BY WORK LOCATION IN 2018
Total employed population living in the 7th District	45,197	55,101	9,904	21.91%	—
Living and Employed in the 7th District	4,172	5,170	998	23.92%	9.38%
Working in Greater Center City	6,668	6,377	-291	-4.36%	11.57%
Working in Philadelphia outside both 7th District & Center City	16,314	21,059	4,745	29.09%	38.22%
Working in the suburbs	13,637	17,355	3,718	27.26%	31.50%
Working outside of the Region	4,406	5,140	734	16.66%	9.33%
Total employees regardless of residence working in the District	29,522	34,287	4,765	16.14%	% District workers
Living in the suburbs and working in the District	9,181	9,874	693	7.55%	28.80%

Council District 8

	2008	2018	DIFFERENCE	% CHANGE	% DISTRICT RESIDENTS BY WORK LOCATION IN 2018
Total employed population living in the 8th District	58,429	61,512	3,083	5.28%	—
Living and Employed in the 8th District	4,466	4,739	273	6.11%	7.70%
Working in Greater Center City	13,512	13,461	-51	-0.38%	21.88%
Working in Philadelphia outside both 8th District & Center City	16,583	18,380	1,797	10.84%	29.88%
Working in the suburbs	19,086	19,711	625	3.27%	32.04%
Working outside of the Region	4,782	7,240	2,458	51.40%	11.77%
Total employees regardless of residence working in the District	24,822	30,455	5,633	22.69%	% District workers
Living in the suburbs and working in the District	7,563	9,579	2,016	26.66%	31.45%

Council District 9

	2008	2018	DIFFERENCE	% CHANGE	% DISTRICT RESIDENTS BY WORK LOCATION IN 2018
Total employed population living in the 9th District	63,843	66,320	2,477	3.88%	—
Living and Employed in the 9th District	3,429	3,749	320	9.33%	5.65%
Working in Greater Center City	13,362	13,040	-322	-2.41%	19.66%
Working in Philadelphia outside both 9th District & Center City	19,687	20,588	901	4.58%	31.04%
Working in the suburbs	22,251	23,128	877	3.94%	34.87%
Working outside of the Region	5,114	5,815	701	13.71%	8.77%
Total employees regardless of residence working in the District	19,711	26,420	6,709	34.04%	% District workers
Living in the suburbs and working in the District	5,356	8,447	3,091	57.71%	31.97%

Council District 10

	2008	2018	DIFFERENCE	% CHANGE	% DISTRICT RESIDENTS BY WORK LOCATION IN 2018
Total employed population living in the 10th District	67,908	68,721	813	1.20%	—
Living and Employed in the 10th District	9,577	9,865	288	3.01%	14.36%
Working in Greater Center City	11,852	11,367	-485	-4.09%	16.54%
Working in Philadelphia outside both 10th District & Center City	9,831	6,891	-2,940	-29.91%	10.03%
Working in the suburbs	25,897	27,153	1,256	4.85%	39.51%
Working outside of the Region	10,751	13,445	2,694	25.06%	19.56%
Total employees regardless of residence working in the District	54,241	57,317	3,076	5.67%	% District workers
Living in the suburbs and working in the District	19,892	21,906	2,014	10.12%	38.22%