Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Local Government Committee

HB 1628

Brief Description: Increasing the supply of affordable housing by modifying the state and local real estate excise tax.

Sponsors: Representatives Chopp, Macri, Peterson, Alvarado, Taylor, Reed, Pollet, Lekanoff, Fitzgibbon, Berg, Riccelli, Davis, Street, Ramel, Duerr, Senn, Doglio, Cortes, Stonier, Gregerson, Mena, Berry, Fosse, Goodman, Bergquist, Slatter, Ormsby, Thai, Farivar, Simmons and Wylie.

Brief Summary of Bill

- Adds a new state real estate excise tax threshold of $5,000,000 on January 1, 2025, with the portion of the selling price that is above the threshold taxed at a rate of 4 percent.
- Provides for the distribution of the increase in revenue from the new threshold over what would have been collected had the new threshold not been imposed, including to a newly created Developmental Disabilities Trust Account that can be used for housing support for individuals with developmental disabilities.
- Allows a county or city to impose an additional 0.25 percent real estate excise tax for the construction and support of affordable housing beginning on January 1, 2024.
- Removes the expiration date on the ability to use certain local government real estate excise tax funds for facilities for those experiencing homelessness or for affordable housing, and removes a $1,000,000 limit on the annual use of such funds in larger jurisdictions.
- Creates a real estate excise tax exemption for certain sales or transfers of properties that qualify for a property tax exemption that will be used for a community purpose.

Hearing Date: 2/7/23

Staff: Kellen Wright (786-7134).

Background:

Excise Taxes.
Excise taxes are taxes imposed on a specific good or activity. Cigarettes, syrup, and aircraft are all subject to excise taxes in Washington.

So too is real estate. The sale, or transfer of a beneficial interest for consideration, of real estate is subject to a state excise tax, and may be taxed by counties and cities (local governments) as well.

State Real Estate Excise Tax.
The state imposes a graduated real estate excise tax on the sale of property that is not timberland or agricultural land. The portion of the selling price up to $525,000 is taxed at 1.1 percent; the portion that is more than $525,000 but less than or equal to $1,525,000 is taxed at 1.28 percent; the portion that is more than $1,525,000 but less than $3,025,000 is taxed at 2.75 percent; and any portion of the selling price over $3,025,000 is taxed at 3 percent. A property that sold for $3,525,000 would therefore be subject to $74,825 in taxes: $5,775 for the first $525,000 portion of the selling price; $12,800 for the next $1,000,000; $41,250 for the next $1,500,000; and $15,000 for the final $500,000.

The Department of Revenue is required to adjust the first price threshold every four years by the lesser of the growth in the consumer price index for shelter or 5 percent, rounded to the nearest thousand dollars. The consumer price index is a measure of the change over time in prices for certain goods, and is often used as a measure of inflation. If the change in the consumer price index for shelter is zero or negative, then the price threshold must remain the same. If the first threshold does increase, then the remaining thresholds must increase by the same amount. The first update to the price thresholds occurred on January 1, 2023; it resulted in an increase of 5 percent to the first price threshold, which translated to an increase of $25,000 at each threshold. Timberland and agricultural land is taxed at a flat rate of 1.28 percent.

Until June 30, 2023, the revenue from the state real estate excise tax is deposited as follows: 1.7 percent into the Public Works Assistance Account, which is used to make loans and grants to local governments for public works projects; 1.4 percent into the City-County Assistance Account, which provides funding to local governments on their size and how their sales and property tax revenue compared to the statewide average; 79.4 percent to the State General Fund; and 17.5 percent into the Education Legacy Trust Account, which is used to support education. After July 1, 2023, the portion going to the Public Works Assistance Account increases to 5.2 percent, while that going to the Education Legacy Trust Account decreases to 14 percent.

The tax imposed is due at the time of sale, and is subject to monthly interest if paid more than a month after the sale. The tax is a lien on the property, and its payment is the responsibility of the seller. The Department of Revenue may foreclose on the property if the tax remains unpaid.

Local Government Real Estate Excise Tax.
Local governments are also authorized to impose real estate excise taxes. There are five varieties of real estate excise tax that counties are authorized to impose, three of which can also be imposed by cities. The taxes differ both in the rate that may be imposed and in the uses to which the revenue can be put.

First 0.25 Percent Real Estate Excise Tax.
First, any local government can impose a real estate excise tax of up to 0.25 percent. This tax is imposed by the legislative authority of the local government. This revenue can be used in two ways, depending on the size of the local government and on whether the county or city plans under the Growth Management Act (GMA). If the local government has either 5,000 or less population, or does not plan under the GMA, then it can use the revenue for any capital purpose identified in a capital improvements plan or for local capital improvements. If the local government has more than 5,000 people and plans under the GMA, the revenue can only be used for certain capital facilities specified in the capital facilities element of the comprehensive plan and for housing relocation assistance.

Until December 31, 2023, a local government can annually use the greater of $100,000 or 35 percent of revenue for maintenance and support for existing capital projects. After 2023, the local government can use the greater of $100,000 or 25 percent of revenue, up to $1,000,000, for maintenance if the local government writes a report that:

- demonstrates that the local government has sufficient funding to pay for the capital projects over the next two years;
- demonstrates that the local government has not adopted requirements related to the listing or sale of property, or to requiring landlords to provide improvements or modifications to property that are not required to address an immediate threat to health or safety unless specifically authorized by state or federal law;
- identifies how real estate excise tax funds were spent in the previous two years;
- identifies how the funds will be spent in the succeeding two years; and
- identifies what proportion of the funds for capital projects come from real estate excise taxation as compared to other sources.

Second 0.25 Percent Real Estate Excise Tax.
The second local government real estate excise tax can only be imposed by local governments planning under the GMA. This tax can be imposed legislatively if the local government is required to plan under the GMA, as 18 counties are. In the 10 counties that have chosen to plan under the GMA, the tax can only be imposed after voter approval. It cannot be imposed by the remaining 11 counties. This tax can be imposed at a rate of up to 0.25 percent of the selling price.

These funds can be used for financing certain capital infrastructure projects identified in the capital facilities element of the comprehensive plan; for parks; and, until January 1, 2026, and under certain conditions, for the acquisition, construction, repair, or improvement of facilities for those experiencing homelessness and for affordable housing projects. The funds available for use related to homelessness and affordable housing are limited to the greater of $100,000 or 25 percent of revenue, up to $1,000,000. This dollar limitation does not apply if the local government used the revenue from this second real estate excise tax to provide housing facilities for the homeless prior to June 30, 2019. A local government must also demonstrate that it has sufficient funds during the next two years for its capital infrastructure projects in order to use the funds for homelessness or affordable housing purposes.

Until December 31, 2023, the greater of $100,000 or 35 percent of revenue can also be used for maintenance of existing capital infrastructure projects and for capital projects for which the first 0.25 percent tax could be used. After 2023 the amount that can be used for these purposes is the greater of $100,000 or 25 percent of revenue, up to $1,000,000, and the revenue can only be used upon the completion of a report with the same information that was required to use a portion of the first 0.25 percent for maintenance.

<u>Real Estate Excise Tax in Lieu of Sales Tax</u>.
The state has authorized local governments to impose two 0.5 percent sales taxes. A local government that has not imposed the second of these taxes can instead impose an additional real estate excise tax of up to 0.5 percent. Any imposition of this tax, or increase in the rate of the tax, can be subjected to a referendum within a short time after the passage of the ordinance imposing or increasing the rate of the tax if at least 15 percent of the registered voters within the local government sign a referendum petition.

The first three real estate excise tax options share some traits that the fourth and fifth do not. With each of the first three options, the responsibility for paying the tax falls on the seller of the property. Additionally, with each of the first three options, a county can only impose the tax in the unincorporated areas of the county, while a city can only impose the tax within city limits.

<u>Conservation Area and Affordable Housing Real Estate Excise Tax</u>.
The fourth and fifth real estate excise taxes can only be imposed by counties. The first of these final two taxes can be imposed at a rate of up to 1 percent. Revenue from the tax can be used only for the purchase and maintenance of conservation areas. A conservation area is land or water that has environmental, agricultural, aesthetic, cultural, scientific, historic, scenic, or low-intensity recreational value. The tax can only be imposed if approved by voters. The payment of this tax is the obligation of the purchaser.

The final tax can only be imposed in a county that imposed the maximum conservation areas real estate excise tax prior to January 1, 2003. The imposition of the tax also requires voter approval. This tax can be imposed at a rate of up to 0.5 percent, and the revenue must be used exclusively for the development of affordable housing through grants and loans. The county legislative authority can determine the division of responsibility for paying the tax between the buyer and the seller, though at least half of the obligation must be the buyer's.

The five real estate excise tax options share some common characteristics. In each of the options, the payment is due at the time of the sale, and the tax operates as a lien on the property. Additionally, with each tax, if the tax is not paid, the local government can foreclose on the property.

Real Estate Excise Tax Exemptions.
Some transfers of property are exempted from being considered a sale. Because these transfers are not considered sales, they are not subject to real estate excise taxation. These exemptions include, among other things, transfers made by gift or through inheritance, transfers made pursuant to a dissolution of marriage, or the transfer of a mortgage interest in property.

Certain sales or transfers related to low-income housing are also exempt from being considered sales. These exemptions cover low-income housing developments that qualify for federal low-income housing tax credits or for tax credits from the Washington State Housing Finance Commission. The exemptions also include sales of self-help housing to households that have an income of less than 80 percent of the median income, adjusted for house size, of the county in which the dwelling is located.

Also exempted are sales or transfers to certain entities that use the property for low-income housing, as long as certain conditions are satisfied. First, the property must qualify for a property tax exemption related to certain properties owned by a qualified entity. A qualified entity is a nonprofit organization that provides low-income rental housing or develops properties for sale to low-income households; a housing authority; a public corporation; or the United States, Washington State, a county, or a municipal corporation. Second, the property must actually be used as housing within one to five years by a household that has an income of less than 80 percent of the median income, adjusted for house size, of the county in which the dwelling is located, with the time frame dependent on whether the organization is operating existing housing, renovating housing, or constructing new housing on the site. If this deadline is missed, then the organization must pay the tax that would have been due at the time of the transfer, plus interest.

The Washington Housing Trust Fund, The Apple Health and Homes Account, and The Affordable Housing for All Account.
The Washington Housing Trust Fund is used to provide grants and loans for local government, housing authority, behavioral health service organization, nonprofit community, tribal, and regional or statewide housing assistance projects that will provide housing to those with special housing needs and with incomes at or below 50 percent of the median family income for the county or standard metropolitan area where the project is located. It is administered by the Department of Commerce.

The Apple Health and Homes Account is also administered by the Department of Commerce. It is used to support permanent supportive housing programs.

The Affordable Housing for All account is used to fund affordable housing programs.

Summary of Bill:

Beginning January 1, 2025, a new threshold is added for state real estate excise tax. This tax applies at a rate of 4 percent to the portion of the sale price that is over $5,000,000. The increased revenue of this portion of the state real estate excise tax over what would have been collected without the new price threshold must be deposited separately from the other portions. The revenue must be deposited as follows: 30 percent to the Washington State Housing Trust Fund, 30 percent to the Apple Health and Homes Account, 15 percent to a new Developmental Disabilities Trust Account, and 25 percent to the Affordable Housing for All account for operations, maintenance, and service for permanent supportive housing.

The Developmental Disabilities Trust Account is created. This account may be used for providing grants and forgivable loans to housing programs to support people with developmental disabilities. These grants and loans can be used for operations and maintenance costs, housing-related services, technical assistance to nonprofit organizations serving or housing populations with intellectual or developmental disabilities, and rental subsidies.

Beginning on January 1, 2024, the legislative authority of a local government may impose an additional real estate excise tax at a rate of up to 0.25 percent. If a city does not impose the tax at the full rate by June 30, 2024, the county may impose the tax within the city up to a combined rate of 0.25 percent. At least half of the revenue from the tax must be used for the capital construction or acquisition of affordable housing; any remainder may be used for operations, maintenance, and services related to the affordable housing, and may only be used for permanent housing, rather than temporary, transitional, or shelter housing. Housing is affordable if the monthly costs of the housing do not exceed 30 percent of the income of a household making 60 percent of the county median income, adjusted for housing size, if the housing is rental housing; or do not exceed 35 percent of the income of the same household if the housing is owner-occupied.

The expiration date of January 1, 2026, for the use of revenue from the second of the 0.25 percent local government real estate excise tax options on facilities for those experiencing homeless or for affordable housing projects is removed. Up to $100,000 or 25 percent of the revenue from this tax option, whichever is greater, can be used on homeless or affordable housing facilities; and the $1,000,000 cap on the maximum amount of the revenue that could be used in this way is removed.

Beginning January 1, 2024, the sale of any portion of an affordable housing development by a qualified entity to an organization that meets the requirements for a property tax exemption as a nonprofit organization, housing authority, or public corporation, for use for a community purpose is exempt from real estate excise taxation. A community purpose includes, but is not limited to, the provision of services to affordable housing development tenants, health clinics, senior day cares, food banks, community centers, and early learning facilities.

Appropriation: None.

Fiscal Note: Requested on January 27, 2023.

Effective Date: The bill contains multiple effective dates. Please see the bill.