Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Community & Economic Development & Trade Committee

ESSB 5901

Brief Description: Modifying provisions of the local infrastructure financing tool program.

Sponsors: Senate Committee on Economic Development, Trade & Innovation (originally sponsored by Senator Kastama).

Brief Summary of Engrossed Substitute Bill

- Expands limitations on the local sales and use tax rate set by sponsoring and cosponsoring local governments.
- Sets a September 1, 2009 deadline for certain sponsoring local governments to select a local sales and use tax rate.
- Eliminates requirements for "base year" and annual "measurement year" calculations of state and local excise tax revenues.
- Requires that before imposing the local sales and use tax, a sponsoring local government must estimate that certain revenues will equal or exceed the amount awarded to the project by the Community Economic Revitalization Board.
- Makes various technical changes and adds reporting and notice requirements.

Hearing Date: 3/16/09

Staff: Meg Van Schoorl (786-7105)

Background:

Traditional Tax Increment Financing.

Traditional "tax increment financing" is a method of allocating a portion of property taxes to finance economic development in urban areas. Typically, under tax increment financing, a local government issues bonds to finance public improvements. To repay its bondholders, the local

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government is permitted to draw upon regular property tax revenue collected from property owners inside a special district surrounding the site of the public improvements. Construction of public improvements tends to increase the market values of nearby properties. Increases in value can result in increased property taxes for each taxing district that includes property near the public improvement. Under tax increment financing, the local government making the improvement gets all of the resulting tax revenue increase. For example, if a city makes an improvement that raises nearby property values, the city gets all of the resulting increase in property taxes, rather than sharing that increase with the state, county, and other local districts under the normal property tax allocation system.

1982 Tax Increment Financing Act.

Washington's original tax increment financing legislation was adopted by the Legislature in 1982. The 1982 Community Development Refinancing Act (Act) followed the general contours of traditional tax increment financing, as described above. At the same time the original tax increment financing legislation was adopted, the Legislature also adopted Senate Joint Resolution (SJR) 143, a proposed constitutional amendment that expressly authorized the financing methods described in the Act. The voters rejected SJR 143 in the November 1982 state general election. However, the legislation authorizing tax increment financing was not contingent on the proposed constitutional amendment, and remained on the books. In 1985 the Legislature passed House Joint Resolution 23, another proposed constitutional amendment authorizing tax increment financing, and placed it on the ballot. It was also defeated at the polls.

Legislative history for the Act shows that the Legislature thought tax increment financing might violate the uniformity requirement for property taxes under Article VII, section 1 of the state Constitution. The City of Spokane attempted to use the Act to finance re-development of the area surrounding Bernard Street in downtown Spokane. A lawsuit challenging the use of tax increment financing to fund these improvements was filed by a property owner in the apportionment district. In 1995 the Washington Supreme Court (Supreme Court) invalidated Spokane's use of the Act, ruling that the Act violated article IX, section 2, of the state Constitution, in that it allowed diversion of property tax revenues away from the common schools. That section of the Constitution requires that the state tax for common schools be applied exclusively to the support of the common schools. By ruling under the school funding clause of the Constitution, the Supreme Court did not reach other property tax uniformity issues. Therefore, the constitutionality of tax increment financing under the uniformity clause is still an open question.

2006 Local Infrastructure Financing Tool (LIFT).

Under the LIFT program, state sales taxes collected within a sponsoring jurisdiction are diverted to the jurisdiction for the purpose of funding public improvements within a designated "revenue development area." A sponsoring jurisdiction can be a city, town, county, or federally recognized Indian tribe. The maximum state contribution that a sponsoring local government can receive each year is limited to the lesser of:

- $1 million;
- The state excise tax allocation revenues and state property tax allocation revenues received by the state during the preceding calendar year;

- The amount of local matching funds dedicated to payment for the public improvements in the preceding calendar year; or
- The amount the LIFT award approved by the Community Economic Revitalization Board (CERB).

State sales taxes cannot be diverted for more than 25 years. Sponsoring local governments must issue bonds by the end of the fifth fiscal year that the taxes have been diverted.

The maximum statewide contribution for all of the LIFT projects is capped at $7.5 million per year ($2.5 million for demonstration projects, $5 million for competitive projects.) Nine projects have been awarded under the LIFT program. Three of them are demonstration projects designated by the Legislature: Bellingham; Vancouver; and, Spokane County. Six of them were approved through two competitive application processes administered by the CERB: in 2007 Bothell, Everett, and Federal Way; and, in 2008 Yakima, Mt. Vernon, and Puyallup. The CERB may not approve use of the LIFT within more than one revenue development area per county, with two exceptions: cities located in more than one county, and counties that include demonstration projects. The window for the application process is currently closed. Approval of additional projects requires future legislative action. The expiration date for the LIFT program is June 30, 2039.

During the first calendar year following the CERB's approval of a LIFT project, a "base year" measurement is taken by the Department of Revenue (DOR) and the sponsoring local government of the amount of state and local sales and use taxes derived from the designated revenue development area. Beginning with the calendar year following the "base year", and each calendar year thereafter, a "measurement year" calculation is made and compared to the base year measurement to identify the increases in state and local sales and use tax revenues from taxable activity within the revenue development area.

Sponsoring local governments must report annually by March 1 to the DOR on revenues received and expended during the preceding calendar year, names of businesses locating within the revenue development area as a result of the public improvements undertaken, the number of permanent jobs created, and the average wages and benefits received by all employees of these businesses.

Summary of Bill:

“Base year” and “measurement year” definitions and requirements are removed. The requirement that the sponsoring local government's receipts from the local sales and use tax each year be no more than the state excise tax allocation revenues and state property tax allocation revenues received by the state in the preceding year is removed. However, before imposing the local sales and use tax, a sponsoring local government must estimate that the state excise tax allocation revenues and state property tax allocation revenues for the preceding calendar year must equal or exceed the amount of LIFT award approved by the CERB.

The maximum state contribution that a sponsoring local government can receive each year is limited to the lesser of:

- $1 million;
- The amount of local matching funds dedicated to payment for the public improvements in the preceding calendar year; or,

- The amount of LIFT award approved by the CERB.

A sponsoring local government must estimate increases in annual state and local sales and use tax revenues due to taxable activity within the revenue development area in its initial application to the CERB and must update the information in a written report to the CERB and the DOR at least once every three years. Upon request by the local government, the DOR must assist in preparing these revenue estimate updates.

Beginning on March 1, 2010, the following additional information is required to be submitted by a sponsoring local government in its annual report to the CERB and the DOR: A list of public improvements financed on a pay-as-you-go basis in previous calendar years and those financed by indebtedness; the expected retirement date for the LIFT indebtedness; and any other information required by the CERB or the DOR. At least once every three years, the sponsoring local government must include in its report the updated estimates of increased tax revenues.

A sponsoring local government that has designated a revenue development area and has been authorized to use the LIFT may incur general indebtedness as long as it includes that intention and the maximum amount of indebtedness contemplated in either an ordinance and related notices, or in a resolution adopted after public comment.

Sponsoring and cosponsoring local governments may impose the local sales and use tax at a rate not to exceed the lesser of:
- the state sales and use tax rate (6.5 percent) less the aggregate rates of all other local taxes imposed as credits against the state sales and use tax, and those authorized but not yet imposed for hospital benefit zones and other of the LIFT projects; or
- the rate reasonably necessary to receive the state contribution over ten months.

Sponsoring local governments whose projects were approved by the CERB prior to October 1, 2008 must select a tax rate no later than September 1, 2009. Upon request, the DOR must assist them. Once the rate is selected, it may not be increased.

Various additional technical changes are made related to the DOR administration.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.