

OCTOBER 1, 2008

UNDERGROUND CONSTRUCTION ACTIVITY AND LOCAL TAX REVENUE: AN EXAMPLE USING THURSTON COUNTY

The Task Force asked the Institute to estimate the impact of the underground construction economy on *local* business and occupation and sales tax revenue. The following example is an attempt at a crude estimate of this impact on *incorporated and unincorporated* Thurston County. The estimate illustrates the relative magnitude of tax losses associated with underground construction activity at a local level. However, available data and knowledge of local and statewide underground construction activity do not yet permit reliable estimates of local tax revenue impacts.

This estimate was generated as follows:

1. Previously, we reported that total taxes and premiums owed by the underground construction economy in Washington State were \$109,000,000.¹
2. About 88 percent of the taxes and premiums owed by the underground construction economy are owed to the Employment Security Department and the Department of Labor and Industries.² The remainder, \$13,000,000 comprises state B&O and sales taxes owed.
3. Next, total construction wages in Thurston County relative to the rest of the state are used to approximate the relative size of underground construction in Thurston County.³ Thurston County comprises 2.4 percent of total construction wages paid in Washington State.⁴ The entire county is therefore assumed to represent 2.4% of the State's underground construction economy.

Based on the above assumptions, underground construction activity in **Thurston County and its cities accounts for about \$312,000 in taxes owed to both the State and Thurston County.** Due to a variety of factors, we cannot decompose this estimate into state and local revenue. The gross estimate represents less than 1% of county and city B&O and sales tax revenue in 2006.⁵ The estimating procedure yields similar results, percentage wise, for other localities.

¹ All dollars represent the year 2006.

² State of Washington GMAP Presentation, September 12, 2007 (Department of Revenue, Employment Security Department, and the Department of Labor and Industries).

³ There are no estimates of the underground construction activity by locality. However, underground economic activity tends to shadow the above ground economy. Estimates based on building permits and population yielded grossly similar results.

⁴ Employment Security Department Workforce Explorer, Industry Report.

⁵ Total B&O and sales tax revenues in incorporated and unincorporated Thurston County, were \$7.8 million and \$44.4 million, respectively, in 2006. Source: Washington State Auditor's Local Government Financial Reporting System.