

State of Washington
Joint Legislative Audit & Review Committee (JLARC)



**Local Infrastructure Financing Tool (LIFT):
Lack of Data Hinders Evaluation and
Administration of the Program**

Report 13-4

December 11, 2013

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alternative formats for persons with disabilities.*

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Committee Action to Distribute Report

On December 11, 2013, this report was approved for distribution by the Joint Legislative Audit and Review Committee.

Action to distribute this report does not imply the Committee agrees or disagrees with Legislative Auditor recommendations.

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the Program**

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STATE OF WASHINGTON

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REPORT SUMMARY

LIFT Program Provides State Contributions for Local Infrastructure Projects

The Local Infrastructure Financing Tool (LIFT) is a state program designed to help local jurisdictions fund public infrastructure projects, which are in turn intended to foster economic development. LIFT projects may receive a state contribution of up to one million dollars per year for 25 years. Total state contributions are limited to \$7.5 million per year for all LIFT projects combined.

To participate in the LIFT program, local jurisdictions establish a revenue development area (RDA) and apply to the Community Economic Revitalization Board (CERB) for approval. There are currently nine LIFT projects around the state; the program is closed to further projects unless the Legislature increases the total amount of funding available for state contributions. The amount of state contribution each project receives per year is limited to the lowest amount of the following four caps:

- 1) One million dollars;
- 2) The amount of local revenue dedicated to the project;
- 3) The amount awarded to the project by CERB; or
- 4) The “state benefit” amount.

The “state benefit” amount is based on a complicated statutory formula intended to approximate increases to state property and excise tax revenues within the RDA. Statute directs each local jurisdiction to submit an annual report to CERB and the Department of Revenue (DOR) that contains the information necessary to calculate the state contribution, as well as information about the progress of its LIFT project.

Insufficient Data for JLARC Staff to Evaluate LIFT Program or Projects

In the LIFT enacting legislation (2006 E2SHB 2673), the Legislature directed JLARC to report every five years on changes to six different metrics within each RDA, and to also complete an analysis of the economic impact of expanding the LIFT program in 2028. However, the data necessary to accurately report on these metrics or to conduct an economic analysis of the projects either does not exist or may not be feasible to collect without significant additional resources. Even if the necessary data was readily available, there are significant challenges to isolating the impact of LIFT projects on the surrounding economy.

LIFT Statutes Do Not Assign Ongoing Oversight Responsibilities

The LIFT statutes do not assign either CERB or DOR with responsibility for ongoing oversight of the LIFT program. For example, there is no state agency responsible for verifying the information provided by the local jurisdictions that is used to determine the state contribution. Similarly, there is no state agency that can provide authoritative guidance to local jurisdictions if questions arise regarding statutory interpretation or program administration.

Formula for Calculating State Contributions Does Not Reflect Changes in Revenue or Economic Growth in the Project Areas

The formula to calculate the “state benefit” cap on state contributions does not measure actual changes to state tax revenues. For example, the formula captures increases in revenue from property and excise taxes, but not decreases. Additionally, the formula only captures a small portion of increases to property values, and is primarily based on whether there were large increases in retail sales. Furthermore, the amount of state contributions might depend less on the success of the project and more on the scheduling of project construction and the composition of the RDA. Finally, the data necessary to accurately calculate this formula does not currently exist.

Legislative Auditor Recommendations

The first recommendation is intended to address what JLARC staff observed about the lack of state agency oversight and guidance for the LIFT program and the operation of the current “state benefit” formula.

Legislative Auditor Recommendation 1

In consultation with local jurisdictions, the Department of Revenue and the Community Economic Revitalization Board should identify and recommend to the Legislature whether any statutory changes should be instituted that could improve: 1) oversight of the LIFT program; 2) state guidance to the local jurisdictions; and 3) the function of the “state benefit” cap to better serve the LIFT program’s purpose of encouraging economic development.

The second recommendation is based on the observation that JLARC staff will be unable to provide a meaningful evaluation of LIFT projects without substantial changes to data reporting, collection, and management practices by private businesses, local jurisdictions, and state agencies.

Legislative Auditor Recommendation 2

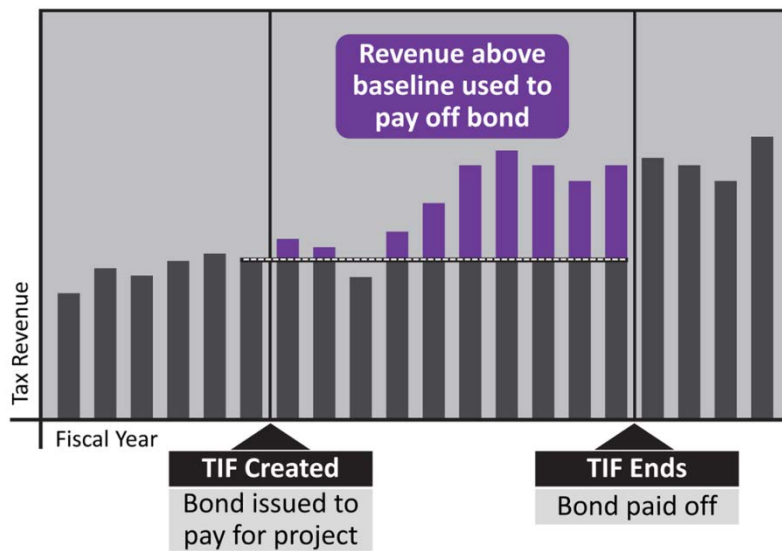
The Legislature should suspend future JLARC studies of the LIFT program.

CHAPTER 1 – DATA NECESSARY TO EVALUATE THE LIFT PROGRAM AND PROJECTS IS NOT AVAILABLE

How Does LIFT Compare to Traditional Tax Increment Financing?

The Legislature enacted the LIFT program in 2006 as one in a series of state programs that attempt to use tax increment financing (TIF) in Washington. TIF is a way of financing infrastructure projects that theoretically pay for themselves. In a traditional TIF project, a local jurisdiction issues a bond to pay for public infrastructure in a designated area, and then the jurisdiction pays off the bond using future increases in tax revenues from that area. It is important to note that only increases in revenues are intended to pay for the bond; the initial baseline amount of tax revenues are reserved for existing uses. See Exhibit 1 below for an illustration of traditional tax increment financing.

Exhibit 1 – Traditional TIF Projects in Other States Pay for Bond with Future Tax Revenue Increases



Source: JLARC staff analysis.

While all other states except for Arizona have some form of TIF programs, there are several constitutional and statutory provisions that constrain the implementation of a traditional TIF in Washington. This is especially true when a TIF relies on increases in property taxes, as is common in other states. For example, the Washington State Supreme Court struck down an earlier TIF-like program because it diverted state property tax funds, which are dedicated to support of public schools under the Washington State Constitution.

Even more restrictive to traditional TIF design is that Washington uses a levy-based property tax system. This means that increases in property values caused by economic development do not necessarily result in an increase in property tax revenues. Instead, only an increase to levy amounts will increase tax revenues. Several statutes limit the extent to which local jurisdictions may increase levy amounts (e.g., RCW 84.55.010).

How Does the LIFT Program Work?

While LIFT is similar to traditional TIF programs in many respects, it may operate differently than in other states due to the legal restrictions in Washington. Like a traditional TIF, the first step is for local jurisdictions to designate the geographic boundaries of the project. In the LIFT program, this project area is called a “revenue development area” (RDA).

The next step is for a local jurisdiction to apply to the Community Economic Revitalization Board (CERB), which approves projects and sets award amounts through a competitive process. There are several requirements for a successful application, including a committed private developer who intends to build within the RDA. The Legislature also included some specific projects in statute as demonstration projects. Between these demonstration projects and the competitive projects approved by CERB, there are currently nine LIFT projects in Washington that are eligible for state contributions.

Six of the nine LIFT projects may receive state contributions up to one million dollars per year for up to 25 years. CERB awarded the remaining three projects a maximum of \$500,000 per year for up to 25 years. Per statute, the total amount of state contributions to all LIFT projects combined in any single year is \$7.5 million, which is already accounted for in the nine current projects. Without further allocation of funding by the Legislature, the LIFT program is effectively closed to new projects.

Like in a traditional TIF program, the annual state contribution is intended to reflect the increase in state tax revenues in the RDA following approval of the project by CERB. However, due to state constitutional provisions, it is not permissible to simply give local jurisdictions state property tax revenues. Instead, local jurisdictions receive their state contribution by imposing a local sales and use tax (the “LIFT tax”), which is then credited against the state sales tax. Consumers do not see any increase in sales tax at the register, but instead some of the state portion of the sales tax is diverted to the local jurisdiction to pay for the LIFT project.

Per statute, the annual state contribution for each local jurisdiction is equal to the lowest amount of the following four caps:

- 1) **One Million Dollars:** The state may not distribute more than one million dollars to any LIFT project in a fiscal year.
- 2) **Local Match:** The state contribution is limited to the amount of local revenue the local jurisdiction dedicated to paying for the LIFT project in the previous year.
- 3) **CERB Award:** These amounts range from \$500,000 to one million dollars per year, and are specified in the award letter given to each qualifying jurisdiction.
- 4) **State Benefit:** The “state benefit” amount is based on a complicated statutory formula designed to approximate the increases in state property and excise taxes from within the RDA. The formula to calculate this amount has changed over the course of the LIFT program. See Appendix 3 for a more detailed explanation of the current formula.

What Are the Current LIFT Projects?

The nine current LIFT projects are located in eight different counties around the state. Exhibit 2 below provides a brief description of each project, as well as the project’s status as reported by the local jurisdiction. In addition, the boundaries of each RDA may be viewed on Google Maps at the following website address: <http://goo.gl/maps/bHYga> (address is case sensitive).

Exhibit 2 – Nine Current LIFT Projects Vary Widely in Scope and Goals, but All Report Being Behind Schedule

Project Description	Project Status
City of Bellingham – New Whatcom RDA	
<p>This is a multiphase redevelopment of the heavy industrial area along Bellingham’s downtown waterfront. The City’s goals include remediating environmental contamination and developing business, housing, and recreational opportunities in the downtown region. Early work has focused on project planning, constructing an interim access road, and clean-up of mercury-contaminated land and petroleum containment.</p>	<p>The City reports that progress is behind schedule due to economic conditions and the complexity of environmental clean-up.</p>
City of Bothell RDA	
<p>This project seeks to create new commercial land in the downtown region and provide better transit and pedestrian access, as well as improve access to the Sammamish River by relocating the intersection of State Route 522 and State Route 527 one block south of its current location. Early work has focused on demolishing buildings in anticipation of the road realignment and soil decontamination.</p>	<p>The City reports that litigation and economic conditions have slowed progress, but that it anticipates imposing the LIFT tax and issuing bonds sometime in 2014.</p>
City of Everett – Riverfront RDA	
<p>This project proposes to redevelop a reclaimed landfill, a former paper mill site, and a former logging yard while protecting a Wetland Enhancement Area. The City’s primary goal is to efficiently use this tract of land by developing it for commercial, residential, and recreational opportunities. Early work has involved design, completing the Environmental Impact Statement process, and relocating a portion of the railroad tracks that parallel the western border of the RDA.</p>	<p>The City reports that progress is behind schedule due to economic conditions and their impact on commercial credit and development markets.</p>

Project Description	Project Status
City of Federal Way – City Center RDA	
<p>The primary goal of Federal Way’s City Center Redevelopment Area is to convert its auto-oriented central business district into a high density, mixed use area with pedestrian-friendly and transit-oriented improvements. LIFT funds are anticipated for roadway upgrades intended to alleviate congestion, the creation of open spaces and trails, and public parking.</p>	<p>The City reports that this project is behind schedule because the original developer was unable to continue involvement due to economic conditions and subsequent developers have also been unsuccessful in significantly advancing their plans.</p>
City of Mount Vernon RDA	
<p>The primary goal of Mount Vernon’s multiphase RDA is to create a commercially viable riverfront district with high density residential options. The first phase of the project—constructing a flood wall, consistent with Federal Emergency Management Administration (FEMA) regulations, to protect the downtown area—is complete. The second phase will focus on a river walk plaza along the Skagit River, and the third phase includes the construction of a parking facility. The plaza is fully funded and scheduled to begin in 2013, and the parking facility will be financed in part by LIFT funds.</p>	<p>The City reports that it is waiting for FEMA to rule on moving the downtown area out of the floodplain and that it is still working on the financing for phase three.</p>
City of Puyallup RDA	
<p>This project concentrates on redeveloping city-owned parcels and infrastructure improvements for telecommunications, storm water runoff, drainage, parks, trails, and pedestrian bicycle access. The RDA includes a large portion of the downtown and South Hill areas along State Route 161. In 2012 the City completed a street realignment at SR 161 and 39th Avenue Southeast intended to reduce traffic congestion and improve safety for bicyclists and pedestrians. The City also reports the completion of storm drainage improvements and ongoing upgrades to high speed fiber optics lines.</p>	<p>The City reports that it has made progress on select parts of the project, while other plans were put on hold due to economic conditions.</p>

Project Description	Project Status
Spokane County – River District RDA	
<p>This project seeks to provide infrastructure, including access roads, water, sewer and storm water handling facilities, and highway interchange improvements to Interstate 90. One of the primary goals of the project is to develop a mixed-use area for residential, commercial, and recreational purposes.</p>	<p>The County reports that the project is behind schedule due to economic conditions, a pending Interchange Justification Report required under federal law, and the County’s desire to manage risks to taxpayers in terms of issuing bonds.</p>
City of Vancouver – Riverwest RDA	
<p>This project includes three distinct projects on one city block. The City has secured the involvement of a private developer who committed to be involved in all projects within the RDA. The first project, completed in 2011, consisted of a new public library funded by local bonds and private donations. The second project, an underground parking garage, will be financed using LIFT dollars but is currently on hold. The third project will also involve a parking structure for a proposed hotel and residential components, but will not be funded by LIFT dollars.</p>	<p>The City reports that development was put on hold due to economic conditions.</p>
City of Yakima – Cascade Mill RDA	
<p>This project seeks to create a development zone for commercial, light-industry, and entertainment purposes by cleaning up and repurposing an old municipal landfill and former paper mill site. The City’s primary goals include efficiently using land and improving the quality of life for residents. The project will involve various infrastructure improvements, connecting the Yakima River Greenway to a proposed employment and commercial center and transit lines, and modifying an existing highway interchange.</p>	<p>The City reports that the project is more than one year behind schedule, due in part to delays associated with a federally required Interchange Justification Report, environmental clean-up, and remediation studies.</p>

Source: JLARC staff interviews with local jurisdiction officials and local jurisdiction reports to CERB.

In addition to the individual project goals and progress, the nine LIFT projects vary on a number of different attributes. See Exhibit 3 below for a summary table of some of these differences. As of July 2013, five of the nine local jurisdictions had imposed the LIFT tax, but only three of these had received state contributions by the end of Calendar Year 2012.

Exhibit 3 – Summary of LIFT Project Attributes

RDA Jurisdiction (Year Approved)	RDA Size (Acres)	Has Construction Begun?	Max CERB Annual Award	LIFT Tax Imposed?	Total State Contribution (Through CY 2012)
Bellingham (2007)	137	Yes	\$1,000,000	July 1, 2013	\$0
Bothell (2008)	255	Yes	\$1,000,000	Not Yet (Expected 2014)	\$0
Everett (2008)	233	No	\$500,000	Not Yet	\$0
Federal Way (2008)	358	No	\$1,000,000	July 1, 2013	\$0
Mount Vernon (2009)	138	Yes	\$500,000	Not Yet (Expected 2015)	\$0
Puyallup (2009)	1,200	Yes	\$1,000,000	July 1, 2010	\$3,000,000
Spokane County (2008)	1,540	Yes	\$1,000,000	July 1, 2010	\$1,756,420
Vancouver (2008)	4	Yes	\$500,000	Not Yet (Expected 2019)	\$0
Yakima (2009)	556	No	\$1,000,000	July 1, 2011	\$757,194
Total	4,421	6 of 9	\$7,500,000	5 of 9	\$5,513,614

Source: JLARC staff analysis of data provided by the Department of Revenue and local jurisdictions.

Legislation in the 2013 Second Special Session removed a requirement that local jurisdictions issue a bond within five years of imposing the LIFT tax; projects may now complete their infrastructure projects on a pay-as-you-go basis. To date, none of the local jurisdictions have issued a bond.

Every year the sponsoring local jurisdiction of each project must submit a report to CERB detailing the goals and progress of the projects. CERB compiles these annual reports and presents a biennial report to the Legislature. The next CERB biennial report is due in 2014.

There Is Insufficient Data to Evaluate Either the LIFT Program or the Economic Impact of Individual Projects

As part of the LIFT enacting legislation in 2006, the Legislature directed JLARC to report every five years on changes to six different metrics within each RDA: sales and use taxes; employment; property taxes; property values; housing; and commercial activities. However, the data necessary to accurately report on these metrics either does not exist or may not be feasible to collect. For example:

- It is not currently possible to reliably determine the amount of sales and use taxes or employment from within an RDA. Data from the Department of Revenue and the Employment Security Department is not collected at the level of detail necessary to identify specific business locations within an RDA. Private businesses are not currently required to report at the level of detail necessary to isolate sales or employment within an RDA.
- Property values and taxes may be acquired from County Assessors and Treasurers, but collecting the data for each RDA may present significant challenges with data coordination, storage, and standardization. For example, not all Assessors maintain records of which parcels were located in an RDA in prior years. Since parcel boundaries may change or subdivide, this can present challenges in determining property values or taxes in prior years.
- The Legislature directed JLARC to measure housing and commercial activities based on the mitigation plans contained in each local jurisdiction's application to CERB. These mitigation plans were intended to preserve low-income housing and small businesses. However, none of the jurisdictions' plans included measurable targets. Furthermore, due to a lack of detailed data, it is not possible to reliably determine these amounts for an RDA.

In order to obtain the data necessary to complete a thorough analysis, there would need to be significant changes to data reporting, collection, and management practices by private businesses, local jurisdictions, and state agencies.

Beyond JLARC's requirement to issue regular five-year reports, the Legislature also directed JLARC to complete an analysis of the economic impact of expanding the LIFT program in its 2028 report. At a minimum, this would require resolving the data challenges referenced above. Additionally, it is unlikely that a conclusive economic analysis would be possible due to the significant challenges in isolating the impact of individual LIFT projects on the economy of an area.

CHAPTER 2 – LIFT STATUTES DO NOT ASSIGN OVERSIGHT RESPONSIBILITY OR BASE STATE CONTRIBUTIONS ON REVENUE OR ECONOMIC GROWTH

While gathering information about the LIFT program for this report, JLARC staff observed two aspects of the LIFT statutes that may be of interest to the Legislature. First, the LIFT statutes do not assign any ongoing oversight or guidance responsibilities to a state agency. Second, the statutory formula to calculate state contributions does not appear to reflect either revenue growth or economic growth from within an RDA.

Note: These observations are not intended to reflect any conclusion about the success or economic impact of any individual LIFT project.

Statutes Do Not Assign Ongoing Oversight or Guidance Responsibilities to a State Agency

The LIFT statutes in Chapter 39.102 RCW do not assign a state agency with any ongoing oversight responsibility after the LIFT projects have been approved. While the Community Economic Revitalization Board (CERB) has a well-defined role in the project approval process, it has no ongoing responsibility in statute. For example, statute does not direct CERB to review the accuracy of the local jurisdictions' annual reports. Further, CERB has no responsibility to assess the continued viability of a LIFT project, even if the circumstances have changed substantially since CERB initially approved the application.

Similarly, the Department of Revenue (DOR) has a well-defined role in the administration of distributing the LIFT tax revenues (see RCW 82.14.475), but it is not clear whether DOR has the responsibility to verify the information provided by local jurisdictions in their annual reports. For example, DOR must determine the state contribution for each local jurisdiction each year based on values reported in the local jurisdiction annual reports. However, there is no corresponding responsibility in statute to ensure that these values are accurate or that local jurisdictions understand how to calculate them correctly. As detailed in Appendix 3, these calculations are complex and require several pieces of information that may not be readily available.

Additionally, when questions arise among local jurisdictions about how to interpret statute or administer the LIFT program, it is unclear whether CERB or DOR can give authoritative guidance. For example, in interviews with JLARC staff, several local jurisdictions were unclear about how to comply with statutory reporting obligations. Statute does not specify to what extent CERB and DOR are authorized to provide guidance on these issues.

JLARC staff compared the LIFT program to other statutorily-established infrastructure/economic development programs. For example, the statute for the public facilities loans and grant program provides clear direction on oversight responsibilities. In that program, CERB is required to conduct biennial outcome-based evaluations of projects receiving state funds.

Formula for State Contributions Does Not Reflect Revenue Increases or Economic Growth in the Project Areas

Per statute, the amount of the state contribution for a particular LIFT project is equal to the lowest amount of four caps: 1) one million dollars; 2) the local match amount; 3) the CERB award amount; and 4) the “state benefit” amount. To determine the state contribution, the local jurisdictions and DOR must calculate the “state benefit” cap amount each year. This calculation is significant because it directly impacts how large or small the state contribution will be to the jurisdiction. See Exhibit 4 below for a simple example of how the calculation impacts the total amount the jurisdiction is eligible to receive. As mentioned earlier, the formula used to calculate the “state benefit” cap is complicated, and more details about how it works can be found in Appendix 3.

Exhibit 4 – Amount of State Contribution to LIFT Project May Be Highly Dependent on the “State Benefit” Calculation

State Contribution Caps	Hypothetical Scenario 1: Small “State Benefit”	Hypothetical Scenario 2: Large “State Benefit”
One Million Dollars	\$1,000,000	\$1,000,000
Local Match	\$750,000	\$750,000
CERB Award	\$1,000,000	\$1,000,000
“State Benefit”	\$50,000	\$800,000
State Contribution to Jurisdiction	\$50,000	\$750,000

Source: JLARC staff analysis of Chapter 39.102 RCW and RCW 82.14.475.

The “state benefit” cap was intended to approximate the revenue increases in state property and excise taxes within an RDA. However, unlike a traditional TIF program, the current “state benefit” formula does not measure actual changes in state revenues or actual economic development within an RDA. Below are four examples of how the formula may not accurately reflect state revenue increases or economic growth.

1) **Formula Captures Increases in Revenue, but Ignores Decreases in Revenue**

Instead of using the actual revenue change in the current year, the “state benefit” formula uses the highest amount calculated in *any one year* since the beginning of the LIFT project. This means the formula effectively ignores any decreases in state tax revenues, and does not adjust downward when increases are less than the “record high” increase.

In order for a jurisdiction to receive the amount awarded by CERB, the “state benefit” amount must meet or exceed the award amount only once. Since the formula ignores anything but record highs, once the “state benefit” amount equals the award amount, the “state benefit” cap is effectively removed from the calculation of the state contribution in all future years of the project. This means that the only remaining limitations on future state contributions would be the jurisdiction’s award amount (up to one million dollars) and the amount of local revenue dedicated to the project. Once

this happens, the LIFT program begins to function more like a state grant matching program rather than a traditional TIF program.

2) Formula Only Accounts for a Portion of Increases to Property Values

Unlike in some other states, Washington’s property tax revenues do not increase when property values rise; instead, property tax revenues only rise when the local taxing jurisdiction increases the levy amount. The property tax portion of the “state benefit” formula only captures the increases in property value that County Assessors designate as being due to “new construction.” The formula ignores increases due to any other reason (e.g., improved land value or any building improvements that do not qualify as “new construction”), which means that the “state benefit” formula only captures a portion of economic growth.

The result is that the amount of property tax increases measured by the formula will often be relatively small compared to the award amount. This means that for a local jurisdiction to receive their award amount, they will likely need to substantially rely on the other formula component: year-over-year increases in sales and use tax revenues within the RDA.

3) State Contribution Might Depend Less on Success of Project and More on Scheduling of Project Construction and Composition of RDA Boundaries

The emphasis on retail sales in calculating the “state benefit” formula means that the same infrastructure project could yield very different state contributions, based on factors unrelated to the effectiveness of the project itself. JLARC staff observed two ways in which a jurisdiction might have high year-over-year increases in sales tax revenue that are unrelated to long term economic growth:

Scheduling of Construction: If a jurisdiction schedules a large construction project (for example, the moving of a highway) over a short period of time, then the sales tax generated from that single project may be sufficient to remove the “state benefit” cap entirely. A jurisdiction that scheduled the same project over the course of 20 years might never achieve such a large year-over-year increase in a single year, and the “state benefit” cap may restrict the state contribution for the life of the LIFT program.

Composition of the RDA Boundaries: If a jurisdiction established the boundaries of its RDA to include a large amount of existing retail activity (e.g., its downtown retail core), then the natural fluctuations of retail sales in the area may be enough to produce a year-over-year increase in sales tax to remove the “state benefit” cap entirely. If the same jurisdiction had included only a small amount of retail businesses in its RDA, then even with the same infrastructure project the jurisdiction might never achieve such a large year-over-year increase in a single year, and the “state benefit” cap may restrict the state contribution for the life of the LIFT program.

4) Data to Accurately Calculate Formula Does Not Currently Exist

The complete set of data necessary to accurately calculate the “state benefit” cap amount does not currently exist. The information required to calculate the property tax portion of the formula must be tracked and supplied by County Assessors. Based on the data received by JLARC staff, it appears

Chapter 2 – LIFT Statutes Do Not Assign Oversight Responsibility or Base State Contributions on Revenue or Economic Growth

that Assessors do not currently organize their regularly maintained data in such a way as to allow all of this information to be extracted. This means that supplying this information would require a specially prepared report specifically for the purposes of the LIFT program. Of the eight County Assessors with LIFT projects in their counties, only one has provided a special report that would allow local jurisdictions to accurately calculate the property tax portion of the “state benefit” formula.

Furthermore, it is not currently possible to accurately calculate the sales and use tax portion of the “state benefit” cap amount, and it may not be possible for local jurisdictions to reliably estimate it. There are currently no separate tax codes for businesses to use that identify which sales are attributable to an RDA. The Department of Revenue estimates that the administrative costs to add these codes would be approximately \$250,000 for upfront implementation and \$90,000 per year for ongoing monitoring and administration.

CHAPTER 3 – LEGISLATIVE AUDITOR RECOMMENDATIONS

The first recommendation is intended to address what JLARC staff observed about the lack of state agency oversight and guidance for the LIFT program and the operation of the current “state benefit” formula.

Legislative Auditor Recommendation 1

In consultation with local jurisdictions, the Department of Revenue and the Community Economic Revitalization Board should identify and recommend to the Legislature whether any statutory changes should be instituted that could improve: 1) oversight of the LIFT program; 2) state guidance to the local jurisdictions; and 3) the function of the “state benefit” cap to better serve the LIFT program’s purpose of encouraging economic development.

Legislation Required:	None.
Fiscal Impact:	JLARC staff assume that this can be completed within existing resources. The agencies should identify if implementing any recommendations would require additional resources.
Implementation Date:	By September 1, 2014, in advance of the 2015 legislative session.

The second recommendation is based on the observation that JLARC staff will be unable to provide a meaningful evaluation of LIFT projects without substantial changes to data reporting, collection, and management practices by private businesses, local jurisdictions, and state agencies.

Legislative Auditor Recommendation 2:

The Legislature should suspend future JLARC studies of the LIFT program.

Legislation Required:	Yes, to repeal or modify RCW 39.102.200.
Fiscal Impact:	None; could free up JLARC staff capacity for future studies.
Implementation Date:	During the 2014 legislative session.

APPENDIX 1 – SCOPE AND OBJECTIVES

LOCAL INFRASTRUCTURE FINANCING

SCOPE AND OBJECTIVES

SEPTEMBER 19, 2012



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Why a JLARC Study of Local Infrastructure Financing?

In 2006, the Legislature passed ESHB 2673 creating the Local Infrastructure Financing Tool (LIFT) program. The goal of the program is to provide state matching funds to local governments to develop public infrastructure in defined areas. The underlying purpose is to use the public investment to attract private investment and improve the economic conditions of the selected areas. Currently, there are nine projects approved under LIFT.

The LIFT legislation requires the Joint Legislative Audit and Review Committee (JLARC) to report to the Legislature on the program every five years beginning in 2013. The program terminates in 2039.

What is LIFT?

LIFT is a variation on a type of program known as tax increment financing. LIFT projects are authorized on the assumption that local public infrastructure investment will result in increased local property values, tax revenues, and economic growth. LIFT projects are financed by locally approved bonds. LIFT projects that demonstrate increases in tax revenues from the project area qualify for state matching funds to help cover the cost of the project. LIFT projects must be approved by the state's Community Economic Revitalization Board (CERB).

The Legislature has also established other, similar financing programs, such as the Local Revitalization Financing (LRF) program. State law limits the total amount of state contributions for both the LIFT and LRF programs. Generally, new projects will require legislation authorizing additional state funding.

Study Scope

JLARC will report to the Legislature every five years for the life of the LIFT program.

In order to conduct its analysis, JLARC will require information on an annual basis from, at a minimum, cities and counties with tax increment financing projects, county assessors, the United States Census, and the departments of Revenue, Employment Security, and Commerce.

The initial report in 2013 will identify the resources and methodology JLARC will use to evaluate local infrastructure financing projects. Beginning in 2018, the reports will provide the descriptive measurements identified by the Legislature on all of the approved projects.

Study Objectives

Initial Report (2013)

The initial report to the Legislature will focus on establishing the data collection and analysis methodology for this large, multi-decade study. The study will address the following questions:

1. What is the current status of the LIFT projects?
2. What methodology does JLARC identify as appropriate to measure changes in employment, property values and taxes, sales and use taxes, housing, and existing businesses within the project areas?
3. Should other tax increment financing programs similar to LIFT be included in the analysis?
4. What methodology does JLARC identify as appropriate to evaluate the economic impacts of Washington’s tax increment financing programs?
5. Are any changes in the timing or nature of subsequent reports appropriate?
6. What resources will JLARC need to conduct this study?

Subsequent Reports

The 2013 report will identify the specific objectives for subsequent reports. The objectives will evaluate the effectiveness of the program by focusing on changes and impacts in the project areas. The evaluation will concentrate on the following topics listed in the enacting legislation:

- | | |
|-----------------------|--------------|
| • Property values | • Employment |
| • Property taxes | • Housing |
| • Sales and use taxes | • Businesses |

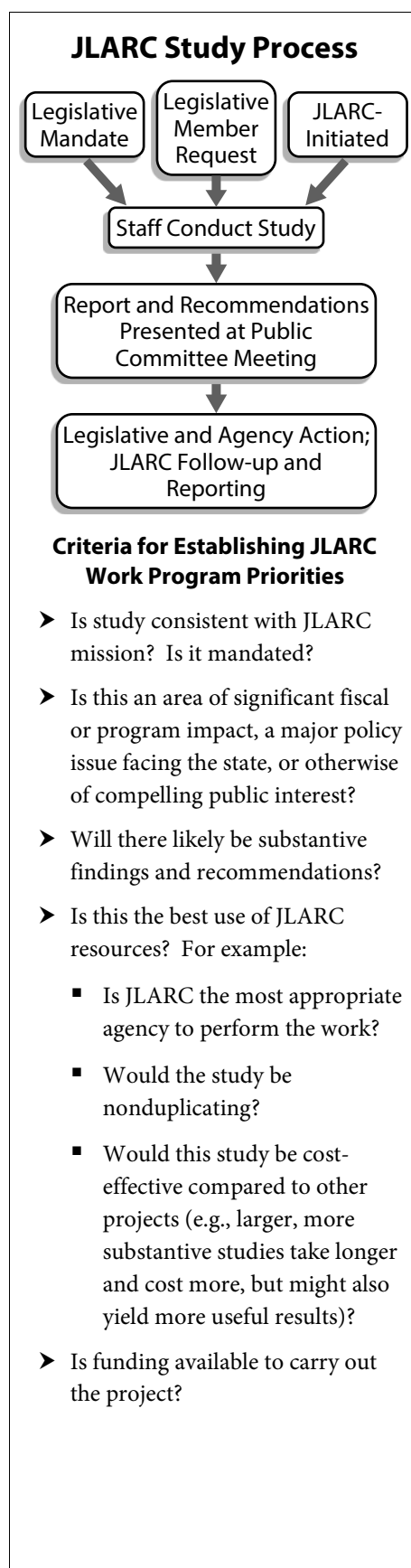
These subsequent reports will also address how projects’ interim results compare to their selection criteria. The Legislature specifically directed JLARC to report by 2028 on whether the program should be expanded and what impact the expansion would have on economic development in Washington.

Timeframe for the Study

This study requires reports every five years beginning in 2013. Staff will present the first report at the JLARC meeting in September 2013.

JLARC Staff Contact for the Study

Fara Daun (360) 786-5174 f.daun@leg.wa.gov
 Peter Heineccius (360) 786-5123 peter.heineccius@leg.wa.gov



APPENDIX 2 – AGENCY RESPONSES

- Department of Commerce
- Department of Revenue
- Office of Financial Management



STATE OF WASHINGTON
DEPARTMENT OF COMMERCE

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October 25, 2013

TO: Keenan Konopaski, Legislative Auditor
Joint Legislative Audit and Review Committee

FROM: Brian Bonlender *BB*
Director

SUBJECT: Joint Legislative Audit and Review Committee’s Local Infrastructure Financing Tool—Preliminary Report

Thank you for the opportunity to review and comment on the Joint Legislative Audit and Review Committee’s (JLARC) preliminary report titled, *“Local Infrastructure Financing Tool (LIFT): Lack of Data Hinders Evaluation and Administration of the Program.”*

The Department of Commerce (Commerce) appreciates the efforts of JLARC to review and thoroughly analyze LIFT. The Community Economic Revitalization Board (CERB) welcomes informed discussion about the original intent and assumptions underlying the LIFT structure to help state government evaluate the effectiveness of tax increment financing.

Commerce partially concurs with the report findings. Commerce will meet with Department of Revenue to identify possible statutory changes to assist in reporting and administration of LIFT.

JLARC recommended CERB identify and recommend to the Legislature whether any statutory changes should be instituted that could improve:	Commerce Response
1) Oversight of the LIFT program	Commerce agrees that clarity and delineation of oversight duties would strengthen the LIFT program.

Mr. Konopaski
 October 25, 2013
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<p>2) State guidance to the local jurisdictions</p>	<p>Because CERB does not receive funding to administer the LIFT program, additional support and guidance to local jurisdictions beyond what is already provided by CERB’s staff would mean other duties within the CERB programs would not be performed.</p> <p>If changes are made to the LIFT statute RCW 39.102.140 Local Infrastructure financing tool program reporting requirements, Commerce recommends removing the requirement for a biennial report to the Legislature. We suggest combining the required LIFT data with the biennial evaluation report stipulated by RCW 43.160.900 Community Economic Revitalization Board—Evaluations of financial assistance—Reporting of evaluations.</p>
<p>3) The function of the ‘state benefit’ cap to better serve the LIFT program’s purpose of encouraging economic development.</p>	<p>Commerce has no comment on this.</p>

We thank the JLARC staff for their thoughtful review and strong communication with us throughout the review process. With supplemental operating resources CERB could provide additional guidance on data collection and reporting to local governments, as recommended by JLARC.

We look forward to receiving the final report. If you have further questions, please feel free to contact Sonya Smith-Pratt, Internal Auditor, at (360) 725-4030.

cc: Dan McConnon, Deputy Director, Department of Commerce
 Kendee Yamaguchi, Assistant Director, Local Government and Infrastructure




STATE OF WASHINGTON
DEPARTMENT OF REVENUE
OFFICE OF THE DIRECTOR

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October 10, 2013

TO: Keenan Konopaski, Legislative Auditor
Joint Legislative Audit and Review Committee

FROM: Carol K. Nelson, Director 
Department of Revenue

**SUBJECT: JLARC PRELIMINARY REPORT – LOCAL INFRASTRUCTURE
FINANCING TOOL**

Thank you for the opportunity to respond to the Joint Legislative Audit and Review Committee's (JLARC's) preliminary report titled: *“Local Infrastructure Financing Tool (LIFT): Lack of Data Hinders Evaluation and Administration of the Program.”*

We appreciate JLARC's efforts to continuously review and analyze the state's tax programs and preferences. Informed discussion about the original intent, assumptions and requirements of current tax programs, such as LIFT, and legislative debate about their continuing effectiveness and relevance, can help state government maintain a fair and equitable tax system.

We appreciate your team's thorough analysis of the LIFT program and offer the following comment on the report item that pertains to the Department of Revenue.

Legislative Auditor Recommendation 1:

In consultation with local jurisdictions, the Department of Revenue and the Community Economic Revitalization Board should identify and recommend to the Legislature whether any statutory changes should be instituted that could improve: 1) oversight of the LIFT program; 2) state guidance to the local jurisdictions; and 3) the function of the “state benefit” cap to better serve the LIFT program's purpose of encouraging economic development.

Keenan Konopaski
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The Department of Revenue partially concurs with this recommendation. We will work with the Community Economic Revitalization Board and local jurisdictions to see if we can identify any statutory changes that could reduce reporting burdens and improve administration of the LIFT program. However, we do not believe we are in a position to make recommendations to the Legislature regarding the function of the “state benefit” cap.

JLARC could choose to recommend to the Legislature that separate tax codes be created for businesses to use to identify which sales are attributable to a revenue development area (RDA). However, as stated in the JLARC report, the Department estimates this would require funding of approximately \$250,000 for upfront implementation and \$90,000 per year for ongoing monitoring and administration. As indicated by JLARC staff in the last paragraph on Page 1 of the Report Summary, “Even if the necessary data was readily available, there are significant challenges to isolating the impact of LIFT projects on the surrounding economy.”

We appreciate the opportunity to review and provide comments on the report and JLARC’s recommendations. We continue to recognize the importance of consulting with state agencies that would be affected by possible changes to tax program statutes.




STATE OF WASHINGTON
OFFICE OF FINANCIAL MANAGEMENT

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October 7, 2013

TO: Keenan Konopaski, Legislative Auditor
 Joint Legislative Audit and Review Committee

FROM: David Schumacher 
 Director

SUBJECT: LOCAL INFRASTRUCTURE FINANCING TOOL (LIFT): LACK OF DATA HINDERS EVALUATION AND ADMINISTRATION OF THE PROGRAM – PRELIMINARY REPORT

Thank you for the opportunity to respond to recommendations put forth in the Joint Legislative Audit and Review Committee’s preliminary report titled: “Local Infrastructure Financing Tool (LIFT): Lack of Data Hinders Evaluation and Administration of the Program.”

Recommendation	Agency Position	Comments
1. In consultation with local jurisdictions, the Department of Revenue and the Community Economic Revitalization Board should identify and recommend to the Legislature whether any statutory changes should be instituted that could improve: 1) oversight of the LIFT program; 2) state guidance to the local jurisdictions; and 3) the function of the “state benefit” cap to better serve the LIFT program’s purpose of encouraging economic development.	Concur	No additional comments at this time.
2. The Legislature should suspend future JLARC studies of the LIFT program.	Concur	No additional comments at this time.

Again, thank you for the opportunity to comment. Please contact Sandi Triggs at 902-0562 with any questions.

cc: Tracy Guerin, Deputy Director, OFM
 Sandi Triggs, Senior Budget Assistant, OFM

APPENDIX 3 – STATUTORY FORMULA TO CALCULATE ANNUAL STATE CONTRIBUTIONS

State Contribution Amount

Under RCW 39.102.020(29), the annual amount of the state contribution to a particular LIFT project is calculated to be the lowest amount of the four following caps:

- a) One million dollars: however, it is worth noting that all CERB awards are already \$1 million or less, so this cap never actually comes into play.
- b) The local revenue dedicated to the project in the prior year: these can be local allocation revenues or any other source of money dedicated by local jurisdictions to pay for the bond or pay-as-you-go improvement costs. However, these cannot include any local funds derived from state grants, state loans, or any other state moneys including any local sales and use taxes credited against the state sales and use taxes.
- c) The amount awarded by CERB: this amount is contained in the approval notice that CERB sends to the local jurisdiction.
- d) The “state benefit”: this is a complicated formula (explained in detail below) that was intended to approximate the increase in state property and excise tax revenues in the RDA.

“State Benefit” Cap Calculation

“State benefit” is not a term used in statute, but how DOR staff refer to the cap in RCW 39.102.020(29)(d). The “state benefit” is determined to be the highest amount in any year (current or previous) of “state *excise* tax allocation revenues” (SETAR) and “state *property* tax allocation revenues” (SPTAR). The basic formula to calculate the current year “state benefit” value is:

$$\text{State Benefit} = \text{SETAR} + \text{SPTAR}$$

- **SETAR (State Excise Tax Allocation Revenues)** (RCW 39.102.020(30)): This is the single year-over-year increase in sales and use tax revenues from taxable activity “within” the RDA that is received by the state. In general, this would be 6.5% of this year’s taxable RDA sales less last year’s taxable RDA sales, minus any other state shared taxes. Note that this amount cannot be negative, because it only considers increases, not decreases.
- **SPTAR (State Property Tax Allocation Revenue)** (RCW 39.102.020(32)): The basic formula to calculate State Property Tax Allocation Revenue is:

$$\text{SPTAR} = \text{SPTR} * \text{PTARV}$$

- **SPTR (State Property Tax Rate)**: This is the rate of property tax imposed by the state for the support of common schools. This rate will vary county by county, due to adjustments DOR makes to convert the county assessed value to state market rate value. The average rate in 2012 was approximately \$2.40/\$1,000 of assessed value (see RCW 84.52.065). This rate is determined by DOR each year.

- **PTARV (*Property Tax Allocation Revenue Value*)**: This value is meant to approximate the increase in assessed property values due to new construction within an RDA. This value is to be determined by County Assessors under RCW 39.102.120(2) each year. According to RCW 39.102.020(19), the basic formula for PTARV is:

$$\text{PTARV} = 0.75 * (\text{NC} + \text{PTNC} + \text{IAVEB})$$

- **NC (*New Construction*)**: This is the increase in assessed value to a property within the RDA resulting from new construction (or other improvements, conversions, or rehabilitations deemed to be “new construction” by the Assessor for tax purposes). The “new construction” could be of an entire building or substantial changes to an existing building. Only new construction that was initiated after the RDA was approved by CERB applies. Note that this amount only applies to properties that are taxable (i.e., exempt properties such as government buildings and churches do not qualify). This value only counts in the year that the new construction is placed on the assessment roll. See RCW 39.102.020(19)(a)(i)-(ii).
- **PTNC (*Prior Taxable New Construction*)**: This value is the sum of prior NC values in each year following the approval of the RDA by CERB, but only for parcels that are still taxable (i.e., never became exempt). To be able to exclude exempt parcels, Assessors must necessarily keep a parcel by parcel breakdown of all prior NC values and indicate which parcels are taxable or exempt. See RCW 39.102.020(19)(a)(ii).
- **IAVEB (*Increased Assessed Value of Entire Buildings*)**: This value is any subsequent increase in assessed value of taxable properties in the RDA that once had new construction, but only if that new construction was of an entire building (i.e., not just an addition to an existing building). For these properties the initial increase in value when first placed on the roll would be captured by NC, and any increase in assessed value in subsequent years would be captured by IAVEB. Note that this value does not apply if the property is exempt. To be able to exclude subsequent exemptions and partial-building-new-construction, Assessors must necessarily keep a parcel by parcel breakdown of all prior NC values, and indicate which parcels are taxable or exempt, as well as which NC values were for entire buildings. See RCW 39.102.020(19)(b).

Appendix 3 – Statutory Formula to Calculate Annual State Contributions

To summarize, the formula to calculate “state benefit” can be expressed as follows:

$$\text{State Benefit} = \text{SETAR} + \text{SPTR} * 0.75 * (\text{NC} + \text{PTNC} + \text{IAVEB})$$

Note that if this value is lower than a prior year’s “state benefit,” then the prior year’s value will be used for purposes of calculating the state contribution. If any of these values are unknown (e.g., if a County Assessor has not maintained a record of whether prior new construction was of an entire building), it may not be possible to calculate the “state benefit.” This in turn means it may not be possible to accurately determine the state contribution.

