

March 4, 1997

BILL ANALYSIS

TO: Members, Committee on Trade and Economic Development
FROM: Kenny Pittman, Research Analyst (786-7392)
RE: **HB 2087 - Providing community empowerment.**

BACKGROUND:

The Community Empowerment Zone program was created in 1993 to coordinate the efforts and resources of government, business and the community to create an environment in which reinvestment could occur. The Department of Community, Trade, and Economic Development was authorized to designate up to six areas for participation in the program by March 1, 1994. Only five areas submitted applications for designation as a community empowerment zone: Seattle, Tacoma, Bremerton, Yakima, and White Center in King County. Currently, the only incentives targeted to businesses located in Community Empowerment Zones are a tax incentive for investments and business and occupation tax credit for job creation.

Business and Occupation Taxes. Washington's major business tax is the business and occupation (B&O) tax. This tax is imposed on the gross receipts of business activities conducted within the state. Businesses are taxable according to the activities they engage in and therefore may be subject to more than one tax rate.

Retail Sales and Use Taxes. The sales tax is imposed on retail sales of most items of tangible personal property and some services. The state rate is 6.5 percent and is applied to the selling price of the article or service. In addition, local sales taxes apply. A use tax is imposed on the use of an item in this state, when the acquisition of the item has not been subject to the sales tax. Use tax is equal to the sales tax rate multiplied by the value of the property used. The total sales or use tax rate is between 7 percent and 8.6 percent, depending on the location.

Real Property Taxes. Property taxes are based on the assessed value of real property, including the land itself, and all buildings, structures, or improvements or other fixtures sitting upon such land. In 1995, the Legislature created a ten-year property tax exemption for new, rehabilitated or converted multiple-unit housing in urban areas. The exemption applies to housing-related improvements made to the property, but not to the value of the land or nonhousing-related improvements or increases in assessed valuation on nonqualifying portions of the building or the value of the land. The multiple-unit housing property tax exemption program is limited to cities with a population of at least 150,000, that are planning under the state's Growth Management Act.

SUMMARY:

The state's Community Empowerment Zone program is expanded and additional incentives are created to encourage public and private reinvestment in the area.

Community Empowerment Zones. The designation process for community empowerment zones, through the Department of Community, Trade, and Economic Development (department), is extended to January 1, 2000. The number of areas that can be designated a community empowerment zone is increased from six to ten. An area that receives federal designation as an empowerment zone or enterprise community can apply to the state for dual designation under the state's community empowerment zone program.

The department is authorized to approve or disapprove proposed amendments by local governments to alter the boundaries or terminate the designation of an area as a community empowerment zone. The department is required to monitor and submit reports evaluating the effectiveness of the community empowerment zone program. The evaluation reports are due to the Governor and Legislature by December 1, 1997 and every December 1 thereafter.

Empowerment Zone Hiring and Training Tax Credit. A business and occupation tax credit or public utility tax credit is provided to employers who agree to hire and train public assistance recipients that reside in a community empowerment zone. A two-level tax credit is provided for both hiring and training of public assistance recipients.

The hiring tax credit may not, in a calendar year, exceed the lesser of: (1) eight percent of the employee's gross annual wages or \$ 1,200 for a category 1 employee; (2) sixteen percent of the employee's gross annual wages or \$2,400 for a category 2 employee; or (3) twenty-four percent of the employee's gross annual wages or \$3,600 for a category 3 employee. The tax credit can be claimed for one to three years, depending on the employee qualifications and training needs.

The employee training tax is equal to 120 percent of the tuition paid by an employer to a community college or other qualified training institution under an approved training plan. The Office of Financial Management is responsible for making annual adjustments to the tax credit amounts to reflect the rate of inflation. The total tax credits allowed to all businesses claiming the credit may not exceed \$10 million in any biennium.

New Business Tax Reduction. A business and occupation (B&O) tax exemption is provided to a new business that is located in a community empowerment zone. The business is exempt from all B&O tax liability for the first three years (36 months) of operation. In the fourth year of operation, the business is exempt from 50 percent of its B&O tax liability. The B&O tax exemption is then reduced 25 percent per year. The business is not eligible for the exemption after six years (60 months) of operation.

A new business- is defined as a business with less than 50 employees and that has obtained a certificate of registration as a business the first year they claim the exemption. The term new business- does not include a business that has been restructured, reorganized, transferred, a new branch location unless by an existing out-of-state business, or a business that is similar to a business operating or operated within the past five years by the same owners.

Sales and Use Tax Exemption on Consumables. A sales and use tax exemption is provided on consumables sold to or used by a business located in a community empowerment zone that is involved directly in a manufacturing operation or research and development operation. Consumables are defined as chemicals and materials.

To be eligible for the sales tax exemption the purchaser must provide the seller an exemption certificate with a copy of the Department of Revenue (department) or provide an annual summary of exempt sales to the department. To be eligible for the use tax exemption the user must provide an exemption certificate to the department within 60 days or provide an annual summary of exempt sales to the department.

International Services Employment Tax Credit. A business and occupation (B&O) tax credit is provided to businesses that are located in a community empowerment zone and provide services on an international basis. Businesses are eligible for a tax credit of \$1,000 per qualified employee. To claim the tax credit at least 10 percent of the qualified employment positions must be filled with residents from a community empowerment zone. The business cannot use the tax credit to relocate existing jobs from any part of the state to the community empowerment zone. The total amount of tax credits in a biennium cannot exceed \$5 million.

Business income derived from sales to other businesses that provide direct international services is not subject to B&O taxation. To qualify for the B&O tax deduction, the supportive business must be located in a community empowerment zone.

Excise Tax Increment Financing. A program to allocate a portion of state and local retail sales and use taxes generated within a community empowerment zone is created. The program is designed to assist in the financing of: (1) needed health and safety improvements; (2) improvements to publicly owned or leased facilities; (3) professional management of retail trade activities; (4) improvements to mitigate the negative impacts caused by the siting of a major public facility; (5) maintenance and security for public areas; or (6) historic preservation activities.

The revenues which may be allocated by the city or county to the community empowerment zone are limited to an amount equal to 50 percent of the increase in tax revenue generated the year proceeding the formation of the allocation district. The revenue must be used to pay part or all of project costs, pay into bond funds to pay the principal and interest on general obligation bonds issued to finance a project, or a combination of the two.

Tax Credits for Contributions. A business and occupation (B&O) tax credit is provided to businesses that make a contribution to a nonprofit organization that are undertaking community empowerment activities in a community empowerment zone. These activities include affordable housing, community service, crime prevention, education, and job training.

The tax credit is based on 75 percent of the approved amount contributed to a nonprofit organization. The tax credit is taken at a rate of 20 percent per year for a 5-year period. The Department of Revenue cannot allowed credits under the tax credit program to exceed \$10 million per biennium. No tax credit can be granted for a contribution of amount less than \$250. A tax credit may not be issued after December 31, 2005. The business must submit a request for approval of the contribution before the contribution is made.

Property Tax Exemptions for Improvements to Commercial Buildings. A 10-year property tax exemption is provided on improvements made to commercial buildings located in a community empowerment zone. The tax exemption applies to the increased valuation of the property due to the improvements to an existing building. The exemption would be for a 10-year period after completion of the improvements. In the eleventh year, the buildings would be assessed based on the improvements.

The taxpayer must file notice of their intent to make

improvements before the improvements are made on forms prescribed by the Department of Revenue and furnished by the County Assessor. The exemption could only be claimed once in a 15-year period.

Property Tax Exemption for Multiunit Dwellings. The 10-year property tax exemption is provided on new construction of or improvements to residential buildings with four or more dwelling units that is located in a city or town with a community empowerment zone. The housing units must be built within a community empowerment zone. The original administrative requirements apply to projects in community empowerment zones.

State Purchases from Empowerment Zone Businesses. State agencies, departments, and the Legislature is required to purchase at least 10 percent of their goods and services, on an annual basis, from businesses with less than 50 full-time employees and that are located in a community empowerment zone.

Appropriation: None.

Fiscal Note: Requested February 25, 1997.

Effective Date: Ninety days after adjournment of session in which bill is passed.