

# HOUSE BILL REPORT

## ESSB 5513

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### As Reported by House Committee On: Finance

**Title:** An act relating to increasing tax exemption transparency and accountability.

**Brief Description:** Increasing tax exemption transparency and accountability.

**Sponsors:** Senate Committee on Ways & Means (originally sponsored by Senators Frockt, Hasegawa, Miloscia, Rolfes, Saldaña, Keiser, Wellman, Conway, Chase, Billig, Kuderer, Hunt, McCoy and Darneille).

#### **Brief History:**

##### **Committee Activity:**

Finance: 2/22/18, 2/26/18 [DPA].

#### **Brief Summary of Engrossed Substitute Bill (As Amended by Committee)**

- Requires the Department of Revenue Tax Exemption Report to be updated more frequently.
- Directs the Office of Financial Management to engage in discussions with the House Finance Committee and the Senate Ways and Means Committee to determine how to incorporate more transparency and accountability on the impacts of the discretionary tax preferences in budget and outlook documents.

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### HOUSE COMMITTEE ON FINANCE

**Majority Report:** Do pass as amended. Signed by 6 members: Representatives Lytton, Chair; Frame, Vice Chair; Dolan, Pollet, Springer and Wylie.

**Minority Report:** Do not pass. Signed by 4 members: Representatives Orcutt, Assistant Ranking Minority Member; Condotta, Stokesbary and Wilcox.

**Minority Report:** Without recommendation. Signed by 1 member: Representative Nealey, Ranking Minority Member.

**Staff:** Tracey O'Brien (786-7152).

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

## **Background:**

### State Operating Budget.

The state government operates on a fiscal biennium that begins on July 1 of each odd-numbered year. A two-year biennial operating budget is adopted every odd-numbered year. Appropriations are made in the biennial budgets for the operation of state government and its various agencies and institutions, including higher education and kindergarten through twelfth-grade public schools.

### Governor's Budget Proposal.

The Budget and Accounting Act establishes various requirements for the budget documents that the Governor must submit to the Legislature before each regular legislative session. The required documents include: the Governor's budget message, which explains the budget and outlines proposed fiscal policies for the period covered by the budget; the budget bill; and other supporting information.

### Tax Preferences.

A tax preference confers reduced tax liability upon a designated class of taxpayer. Tax preferences include tax exclusions, deductions, exemptions, preferential tax rates, deferrals, and credits. Currently, Washington has over 650 tax preferences.

### Annual Surveys and Reports.

Over the last 10 years, the Legislature has required taxpayers to file the Annual Survey (Survey) or the Annual Report (Report) in order to qualify for a variety of new economic development-related tax preferences, or in some cases, to extend existing economic development-related preferences. There are currently 32 economic development-related tax preferences that require one of these supplemental filings.

### Exemption Study.

The Department of Revenue (DOR) must produce and submit to the Legislature a Tax Exemption Report every four years. The report includes a listing of all tax exemptions, including the estimated revenue lost from, and the beneficiary of, each exemption. The report also includes the estimated revenue lost for other tax preferences including preferential rates, deductions, and credits. The next report is due in January 2020.

### The Citizen Commission for Performance Measurement of Tax Preferences and Joint Legislative Audit and Review Committee: Tax Preference Reports.

The Citizen Commission for Performance Measurement of Tax Preferences (Commission) was established by the Legislature in 2006. The Commission develops a schedule to review nearly all tax preferences at least once every 10 years. The Commission also schedules preferences with expiration dates to be reviewed two years before the tax preference expires. Tax preference reviews are conducted by the Joint Legislative Audit and Review Committee (JLARC) according to the schedule established by the Commission. For each tax preference, the JLARC provides recommendations to continue, modify, schedule for future review, or terminate the preference. The Commission reviews and comments on the JLARC report.

### Budget Outlook.

A state budget outlook workgroup is required to prepare an official state budget outlook for the current and subsequent biennium. The outlook must estimate revenues to and expenditures from the State General Fund and related funds. The estimate must include maintenance items including, but not limited to, continuation of current programs, forecasted growth of current entitlement programs, and actions required by law, including legislation with a future implementation date.

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**Summary of Amended Bill:**

The DOR Tax Exemption Report must be updated every two years instead of every four years. The report must also include recommendations by the JLARC and the Commission if the tax preference has been reviewed.

The Office of Financial Management (OFM) must engage in discussions with the House Finance Committee and the Senate Ways and Means Committee to recommend the means to increase accountability and transparency in budgeting. The recommendations may include:

- how to set the minimum thresholds for inclusion based on the amount of revenue foregone by the tax preference in the biennia covered by the four-year budget outlook;
- whether there has been a JLARC or Commission review; and
- how best to determine and publicly share the return on investment for the identified tax preferences.

**Amended Bill Compared to Engrossed Substitute Bill:**

The amended bill removes the requirements:

- that the November outlook materials prepared by the Economic Revenue and Forecast Council (ERFC) must include the projected fiscal impact of discretionary tax preferences in the current biennium and subsequent biennium;
- that the ERFC, the Office of the Governor, and the OFM must maintain on their websites a current list of discretionary tax preferences; and
- that the Governor's budget documents must include a detailed listing of discretionary tax preferences.

The amended bill adds the requirement that the OFM engage in discussions with the House Finance Committee and the Senate Ways and Means Committee to recommend the means to increase accountability and transparency in budgeting.

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**Appropriation:** None.

**Fiscal Note:** Available.

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

### **Staff Summary of Public Testimony:**

(In support) This bill is intended to increase transparency around the state's tax expenditure policy. Increasing the frequency of the DOR Tax Exemption Report will allow for a more holistic approach when looking at reforms to the state's tax system. The updates will allow the public and legislators to keep tabs on the size of the exemption. Other states update their tax expenditure reports biennially as well.

There are three goals for effective corporate tax disclosure. First, the state must identify all the substantial tax deductions, exemptions, and credits claimed by each large corporation. Second, the state must evaluate the net impact of these tax breaks on the bottom-line tax payments of each corporation. Finally, the state must assess the effectiveness of these tax breaks in creating jobs and growing the state's economy.

This is a straightforward approach to making more information about tax preferences available to the public while leaving untouched the good work performed by the JLARC and the Commission. Indeed, this may highlight some of the challenges of reviewing tax preferences, including the lack of clear statements of public policy intent. There is often a race to the bottom among states competing for businesses.

(Opposed) None.

(Other) The changes made in the Senate address many of the concerns related to the budget provisions in the bill as it was introduced. However, more improvements can be made. The Legislature grants many of these tax preferences as a leap of faith. The need to validate that leap of faith is important.

The bill should be amended to require a description of the direct, indirect, and induced effects of each tax preference on the state's economy, workforce, and wages. In many instances, this information can be provided by those taxpayers taking advantage of the tax preferences.

As the result of earlier legislation, most tax preferences are subject to a performance review and expiration date. To increase the transparency of purposeful tax preferences, the state needs the full story. The bill in its current form does not reflect the full impacts of tax preferences.

**Persons Testifying:** (In support) Senator Frockt, prime sponsor; Nick Federici, All In for Action; Steve Clagett, Faith Action Network; Bruce Walker, Pacific County Assessor's Office and Washington State Association of County Assessors; Steve Zemke, Tax Sanity; and Melissa Taylor.

(Other) Tom Davis, Washington Farm Bureau; Clay Hill, Association of Washington Business; and Steve Gano, Gano and Associates.

**Persons Signed In To Testify But Not Testifying:** None.