SENATE BILL REPORT
2SHB 1425

As of March 29, 2023

Title: An act relating to facilitating municipal annexations.

Brief Description: Facilitating municipal annexations.

Sponsors: House Committee on Finance (originally sponsored by Representatives Berg, Low, Eslick, Ryu, Stonier, Duerr, Ortiz-Self, Cortes, Peterson, Fosse, Donaghy and Pollet).

Brief History: Passed House: 3/3/23, 96-0.
Committee Activity: Local Government, Land Use & Tribal Affairs: 3/21/23, 3/23/23 [DP-WM].
Ways & Means: 3/31/23.

Brief Summary of Bill

- Requires an interlocal agreement for annexed areas in which a sales and use tax is imposed to address certain criteria.
- Removes the requirement that a city commence annexation prior to January 1, 2015, to be eligible for the sales and use tax credit for annexed areas.
- Changes population thresholds for imposing the sales and use tax for annexed areas.

SENATE COMMITTEE ON LOCAL GOVERNMENT, LAND USE & TRIBAL AFFAIRS

Majority Report: Do pass and be referred to Committee on Ways & Means.
Signed by Senators Lovelett, Chair; Salomon, Vice Chair; Torres, Ranking Member; Kauffman and Short.

Staff: Karen Epps (786-7424)

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

SENATE COMMITTEE ON WAYS & MEANS

Staff: Jeffrey Mitchell (786-7438)

Background: Urban Growth Areas. Under the Growth Management Act (GMA), counties that fully plan must designate urban growth areas (UGAs) within which urban growth must be encouraged and outside of which growth can occur only if it is not urban in nature. Planning jurisdictions must include within their UGAs sufficient areas and densities to accommodate a 20-year population projection range provided by the Office of Financial Management. Cities must include sufficient areas to accommodate the broad range of needs and uses that will accompany the projected urban growth, including as appropriate, medical, governmental, institutional, commercial, service, retail, and other nonresidential uses. Each city located within a planning county must be included within a UGA.

Annexation of Territory Within Urban Growth Areas. The legislative body of a county, city, or town planning under the GMA is authorized to initiate an annexation process for unincorporated territory by adopting a resolution commencing negotiations for an interlocal agreement between a county and any city or town within that county. The territory proposed for annexation must meet the following criteria:

- it must be within the city or town UGA; and
- at least 60 percent of the boundaries of the territory proposed for annexation must be contiguous to the annexing city or town.

The interlocal agreement must describe the boundaries of the territory to be annexed and a public hearing must be held by each legislative body. Following adoption and execution of the agreement by both legislative bodies, the city or town legislative body must adopt an ordinance providing for the annexation. The annexation ordinance is subject to referendum for 45 days after passage.

Annexation Sales and Use Tax Credit. Any city within a county with a population greater than 600,000 that annexes an area may impose a sales and use tax in addition to other authorized taxes collected. The tax may only be imposed by a city if:

- the city has commenced annexation of an area with a population of at least 10,000, or at least 4000 in certain circumstances, prior to January 1, 2015; and
- the city determines that the projected cost to provide municipal services to the annexation area exceeds the projected revenue the city would otherwise receive from the annexation area on an annual basis.

The tax is a credit against the state sales and use tax. The Department of Revenue must collect the taxes on behalf of the city, at no cost to the city, and must remit the tax to the city.

The maximum rate that may be imposed by a city is:

- 0.1 percent for each annexed area with a population between 10,000 and 20,000, or

between 4000 and 10,000 for a city with a population between 115,000 and 140,000 located within a county with a population over 1,500,000 and may be imposed for no more than ten years;
- 0.2 percent for an annexed area with a population over 20,000 and may be imposed for no more than ten years; and
- 0.85 percent for an annexed area with a population over 16,000 if the area was, prior to November 1, 2008, officially designated as a potential annexation area by more than one city, if at least one of those cities has a population over 400,000 and may be imposed for no more than six years.

Maximum cumulative rates are specified. All revenue collected may be used solely to provide, maintain, and operate municipal services for the annexation area. The revenues may not exceed revenue necessary to equal to the difference between the city's cost to provide, maintain, and operate municipal services for the annexation area and the general revenues that the cities would otherwise expect to receive from the annexation during a year. If the revenues exceed the costs to the city to provide municipal services for the annexation area during a given year, the city must notify the Department of Revenue and the tax distributions must be suspended for the remainder of the year.

Summary of Bill: Annexation of Territory Within Urban Growth Areas. If an interlocal agreement is used for a sales and use tax credit for annexed areas, the interlocal agreement must address:
- the balancing of annexations of commercial, industrial, and residential properties so that any potential loss or gain is considered and distributed fairly, as determined by tax revenue;
- development, ownership, and maintenance of infrastructure; and
- the potential for revenue-sharing agreements.

Annexation Sales and Use Tax Credit. The requirement that a city be within a county with a population of at least 600,000 to impose the tax is removed. The requirement that an annexation area must have a population of at least 10,000, and in some circumstances 4000, to impose the tax is removed. The timeline for commencing annexation prior to January 1, 2015, to be eligible for the tax credit is removed. A city may not begin to impose the authorized tax after July 1, 2028. To impose the tax, a city must have entered into an interlocal agreement with the county regarding the proposed annexation area.

The maximum levy amount that may be imposed based on population is changed to:
- 0.1 percent for each annexed area in which the population is between 2000 and 10,000; and
- 0.2 percent for each annexed area in which the population is above 10,000.

Maximum cumulative rates and other requirements related to an annexed area with a population over 16,000 if the area was, prior to November 1, 2008, officially designated as a potential annexation area by more than one city, if at least one of those cities has a population over 400,000, are removed.

Appropriation: None.

Fiscal Note: Available.

Creates Committee/Commission/Task Force that includes Legislative members: No.

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

Staff Summary of Public Testimony (Local Government, Land Use & Tribal Affairs): PRO: This bill will help with the housing crisis and will incentivize cities to annex unincorporated portions that are within their UGA. This bill provides cities with a credit against the state sales tax for a set period of time to allow cities to provide infrastructure and other immediate fiscal needs that will not be taken care of by the increased revenue from unincorporated areas becoming part of the city. This bill builds on the work of the GMA, which assumes that over time more developed unincorporated areas would gradually be annexed by cities. This bill will have an impact on density and the availability of housing supply. This bill addresses concerns regarding the unequal annexation of revenue generating areas and non-revenue generating areas, since commercial/revenue generating areas tend to be annexed by cities while counties are left providing services to generally residential areas, which often have higher needs with less revenue. The bill also requires counties and cities to consider infrastructure and revenue sharing. The sales tax tool in the bill will incentivize annexations, promote efficient service delivery, and ensure that residents of dense unincorporated urban areas receive urban-level services. This tool was a game-changer in King County when it was authorized in 2006 and led to six large urban island annexations into cities. This bill provides a valuable financing tool and structure to facilitate annexations. The bill requires an interlocal agreement between the city and the county regarding annexation and the credit against the state sales tax is key to discussions around cost sharing. Without the credit in this bill, it is unlikely that some annexation could occur, limiting cities' ability to grow. Financial circumstances are a factor in preventing annexations and reinstating this sales tax could be a tipping point for some cities and towns to move forward with annexations.

Persons Testifying (Local Government, Land Use & Tribal Affairs): PRO: Representative April Berg, Prime Sponsor; Megan Dunn, Snohomish County Council; Brian Enslow, Cities of Vancouver, Lacey, Ferndale, and College Place; Karen Meyering, King County; Paul Jewell, Washington State Association of Counties; Ben Wick, Councilmember, City of Spokane Valley.

Persons Signed In To Testify But Not Testifying (Local Government, Land Use & Tribal Affairs): No one.