

CORPORATE SUBSIDIES IN OUR COMMUNITIES: A DELICATE BALANCE

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CURRENT LEAGUE POSITIONS
PUBLIC-PRIVATE PARTNERSHIPS

- **Support measures to ensure accountability and adequate citizen participation/oversight in public-private partnerships. Our vision recognizes that public-private partnerships may serve as a mechanism for cities to work in concert with the private sector to achieve public objectives if the following elements are present:**
 - A. Citizen involvement at the earliest possible point in the process: Prior to any city commitment or negotiation about a possible project, citizen involvement should be solicited and required to assess the benefits, if any, and risks, both tangible and intangible, of any proposed public/private partnership.
 - B. Periodic public hearings should be held in which there is an opportunity for citizens to comment at the initiation of a project and at key stages of project development.
 - C. **Any proposed public-private partnership involving a substantial commitment of public funds should be reviewed by an advisory body that will provide advice and direction to the city council, the mayor and the public.**
 - D. **Criteria should be developed to enable the public and any designated advisory body to weigh the public benefit and cost of public-private partnerships.**
 - E. **Any advisory body should be empowered to develop additional criteria to ensure:**
 1. **Accountability to the citizenry;**
 2. **An adequate cost/benefit analysis; and**
 3. **An adequate return on the public investment.**
 - F. **To ensure a successful public-private partnership, the cities should develop a set of standards prior to entering into a contractual agreement with a private partner that includes the following:**
 1. **A competitive selection process;**
 2. **Identification of financial exposure, public objectives and contract safeguards;**
 3. **Investment in the necessary expertise for negotiating the contract;**
 4. **Establishment of contractual performance standards, including exit provisions and methods to enforce the standards; and**
 5. **Development of methods to assure adequate oversight and accountability at every stage of the project. (2002)**

ECONOMIC DEVELOPMENT (ready for adoption at LWVS 2006 Annual Meeting)

- Support the use of public funds for economic development that benefits the public, and that
 - A. Provides sustainable, living-wage jobs
 - B. Supports the development goals and economic vitality of the community
 - C. Encourages good business practices, fair and safe treatment of employees, and protection of the environment.
- Support the evaluation of publicly-funded economic development activities to ensure that stated goals are achieved.
- Support business regulation that is clear and consistent, and that protects public health, worker safety, and the environment.

SCOPE OF THE STUDY

This study will examine the impact of corporate tax breaks and subsidies on the citizens of Greater Seattle. It identifies the types of incentives that exist at the state and local level, provides examples of corporations that have benefited, identifies some of the trade-offs in economic impacts, and looks at attempts to achieve corporate accountability.

THE STATE'S TAXING (AND EXEMPTION) AUTHORITY

In Washington, the state holds most of the taxing authority and therefore, almost all of the tax exemptions and incentives originate at the state level.

The majority of taxes collected are for sales and use, property, public utilities and business and occupation (B&O). Exemptions are provided on all of these taxes in the form of deductions, deferrals, differentials and credits. Some examples of exemptions include:

- Retail/Use Differential on the construction of Qwest Field and Safeco Field;
- B&O Tax Differential on Certified Aircraft Repairs;
- Property Tax Exemptions on low-income housing and multi-unit housing facilities; and
- Preferential B&O Tax Rate for Manufacturers of Nuclear Fuel Assemblies.

The stated purposes of the exemptions are to help create jobs and generate revenue, and to relieve burdens on industries with typically low profit margins.

The B&O tax is Washington's main corporate income tax and generates the second highest level of revenue after sales tax. It is considered onerous for business because it taxes gross receipts rather than profits. Since Washington has no income tax the burden falls more heavily on those paying B&O, sales and property taxes, especially the smaller and lower profit companies. As compensation for the business tax burden, the state legislature has adopted and extended many B&O tax exemptions.

THE STATUS OF EXEMPTIONS

As of 2004 the state had 503 tax exemptions on the

books, totaling more than \$64 billion. There are three categories of exemptions. First are those which are not subject to repeal because of constitutional provisions for things like interstate commerce, business activity on behalf of government, and business activity on Indian tribal lands. The second category consists of exemptions which would result in realized revenue if repealed, but they will likely be left to stand because they are popular and therefore, considered politically untouchable, i.e., supports for the agricultural and fishing industries, nursing homes and non-profit organizations. All other exemptions fall into a third category where, according to a 2004 study published by the state's Department of Revenue (D.O.R.), approximately \$13 billion could be recovered in revenue if exemptions were repealed.

About 70 percent of the exemptions date back to the 1930s and are targeted to the agricultural industry, which no longer plays the same large role in the state's 21st century economy. Many exemptions are adopted and never revisited for evaluation, but are simply extended indefinitely.

The D.O.R. study defines the year each exemption was enacted, its stated purpose - usually to encourage a specific type of business activity - and the dollar amounts, at state and local levels, that the industries save as a result. In a few cases, such as the B&O differential on certified aircraft repair, no taxpayer savings amount is listed. This is due to a confidentiality requirement put into motion when less than three companies receive the exemption. The same holds for the preferential B&O tax rate for manufacturers of nuclear fuel assemblies, where the confidentiality requirement kicks in for the sole company receiving the benefit.

The D.O.R.'s Summary of 2005 Tax Legislation shows that eleven exemptions have since been repealed when it was found they had no fiscal impact whatsoever, and that list includes the preferential B&O tax rate for manufacture of nuclear fuel assemblies. However, another fifteen exemptions for business were signed into law.

BUDGET AND SPENDING CONSTRAINTS

The passage of I-601 in 1993 put strict limits on Washington State spending by linking it to population growth and inflation. I-695, the anti-tax initiative, drained even more money (\$1.2 billion per biennium) from state funds. Meanwhile, the state still lists more than 500 tax breaks on the books. These tax breaks, which are targeted to particular groups of individuals or corporations,

are sometimes referred to as “tax expenditures” because they are essentially government spending programs that happen to be administered through the tax code. The Institute on Taxation & Economic Policy argues that because expenditures are not given a line item in the state’s budget, we can’t really know how much is lost in revenues.

DO EXEMPTIONS AND INCENTIVES SPUR ECONOMIC GROWTH?

In April of 2003, former State Senator Dino Rossi wrote an opinion piece for the Seattle Post-Intelligencer which made the case for continuing tax exemptions on behalf of Washington’s businesses. “Tax exemptions are an issue of competitiveness,” Rossi wrote. “We must remain competitive or suffer the consequences – more companies moving out of state like Boeing did when it moved its headquarters to Chicago.” The piece cautions against repealing any tax exemptions, and points to an April 15, 2003 policy brief produced by the Washington Research Council which reported that, “each high-tech job created through the B&O tax exemption resulted in the creation of nearly three other jobs.” Rossi suggests that the jobs created resulted in almost \$60 million in state revenue.

Rossi’s position echoed with influence in the 2005 legislative session when the Senate failed to pass HB 1069, a bill requiring periodic reviews of tax preferences. A year later, in March of 2006, the bill was resubmitted, passed both the House and Senate and was signed into law. HB 1069 provides for the Joint Legislative Audit and Review Committee (JLARC) to consider if public policy objectives are being met by continuing exemptions. It will determine the feasibility of modifying, sunseting, or immediately terminating certain exemptions in order to recapture revenue. A seven-member citizen’s commission will compile the JLARC’s findings and make recommendations with respect to the extension or termination of exemptions. The commission will be comprised of individuals with expertise in performance management, fiscal analysis, strategic planning, economic development and performance assessments. Some business exemptions – the sales and use tax exemption for research and development and for manufacturing equipment and machinery, as well as the B&O tax credit for small business – will be omitted from review.

Washington College economics professor Robert Lynch, who authored a study for the Economic Policy Institute in Washington D.C., finds little ground to support tax

cuts and incentives as the best means to expand employment and spur economic growth. He contends that state and local taxes may be largely irrelevant to business investment decisions and that other factors – the cost of hiring qualified workers, the proximity to customers, and the quality of public services – are more critical than taxes. Lynch concludes that any jobs that might be gained by cutting taxes can be more than offset by the jobs and revenues lost as a result of cuts in public services. Puget Sound economist Dick Conway (Dick Conway & Associates) adds that the best approach to economic development is to focus spending on schools, infrastructure, transportation systems, health and safety, and cultural amenities.

STATE & LOCAL BENEFICIARIES OF SUBSIDIES AND TAX BREAKS

THE BOEING AGREEMENT

In 2003, the Boeing Company reached agreements with the State of Washington that secured the city of Everett as recipient of the much-coveted assembly plant for the new 7E7 Dreamliner. The core of the deal was a 20-year B&O tax cut. Approval was also given for Boeing to reduce its workers compensation and unemployment insurance contributions by millions of dollars. The tax breaks totaled approximately \$3.2 billion in savings for the company. Questions were raised when it was discovered that, in addition to the tax breaks approved by the Legislature, Governor Gary Locke had, on his own, negotiated behind the scenes for another \$45 million in incentives for the aerospace giant.

Washington State’s constitution includes a restriction against giving tax preferences on behalf of a single company. There is some controversy surrounding the legality of the Boeing deal, with public interest groups and some public officials concluding it breaks the constitutional restriction because, while not naming one company specifically, it clearly benefits Boeing the most. In particular, the “extra” deals were reached solely on Boeing’s behalf. Others, like David Walsh, former Deputy Attorney General, say it will all stand up in court because the tax breaks are for the entire aerospace industry.

Boeing had actively courted other states for favorable deals, and invited what amounted to a bidding war. At the time, the details of those deals were kept confidential but after Boeing chose to stay in Washington, news reporting showed the other states’ offers didn’t even come

close. Subsequently, questions have arisen regarding the seriousness of Boeing's threat to leave Washington, and whether the company might have built the 7E7 for less than the final deal promised.

CONFLICTING JOBS NUMBERS/ CONFLICT OF INTEREST

It has become common for corporations to make relocation threats, whether implied or explicit, and state and local governments feel obliged to appease them into staying put. One current example of this is the threat by owners of the Seattle Supersonics to leave the area unless hotel and restaurant taxes – originally put into place for the construction of Safeco Field and Qwest Field – are extended to fund a \$200 million makeover of the Key Arena.

Notwithstanding economists' estimates of indirect jobs, direct employment can be readily measured. The cost to states that lose corporate jobs can be daunting. Boeing has a century-long history in the Northwest and, despite its "bust" periods, the company has engendered a great deal of loyalty. Boeing may periodically lay off hundreds and even thousands of workers at a time, but they seem to come right back into the fold during hiring periods. During the months before contracts were signed, varying jobs numbers were projected by Boeing, Deloitte Consulting (the firm hired by the state to help craft an agreement), and the Governor. 800-1200 projected jobs of direct employment for the 7E7 changed into 1000-2500 jobs. Deloitte reported that new indirect and induced jobs could total anywhere from 4,800-14,790 by year 2012. Governor Locke and Deloitte cautioned that if Boeing didn't choose Washington for its 7E7 assembly, as many as 200,000 total jobs could be lost forever.

Economist Dick Conway thinks the company would have agreed to the 7E7 deal for less than the State offered. All the other states in competition were offering incentives packages in the \$100-200 million range, far less than the package agreed upon in Washington. "Boeing", says Conway, "could find cheaper labor in the South, but would it have been more productive? And if Boeing moves the 7E7 project what happens to the morale of the remaining work force? What's morale worth?" Even with the generous tax breaks and other incentives, the 7E7 will still be manufactured at other plants in the U.S. and around the world, where labor is cheaper. Only final assembly will take place at the Everett facility. After Boeing relocated its headquarters to Chicago in 2001, Governor Locke and the Legislature decided that the im-

THE BOEING AGREEMENT

TAX CUTS

- \$3.2 billion, includes:
40% reduction in B&O tax over 20 years and reforms to state unemployment and workers compensation programs.

THE 'EXTRAS'

- \$10 million to design, build and operate an Employment Resource Center
- \$14 million to hire "workforce development coordinators" through Department of Community, Trade and Economic Development to develop recruitment, screening, and training program to help Boeing and its suppliers hire workers
- \$15.5 million for improvements at Port of Everett rail-barge facility
- \$4.2 million in transportation improvements (includes extending HOV lanes on I-5 and widening lanes on Hwy 527 for 20 blocks)
- \$5 million to help company develop 747-based "Large Cargo Freighter" to fly in 7E7 components
- State hires employees to help expedite Boeing's environmental permits, advise about possible future tax breaks, seek new grants
- State agrees to withhold or blackout information from public record "to the fullest extent permitted by law"
- Future lawmakers may not revoke or change tax breaks; may not modify unemployment and insurance rate changes signed into law in 2003

Sources: *Seattle Times*; *Spokesman-Review*; *King County Journal*; *Seattle Weekly*

plications of losing final assembly were too great to risk. Although Conway didn't believe in the imminent loss of Boeing without a 7E7 deal, he thought it more likely the company would eventually have moved out of state over the next two or three decades.

The deal produced another nagging issue: the involvement of Deloitte Consulting and its perceived conflict of interest. The state paid Deloitte \$715,000 to help put together an analysis of the overall economic impacts of both securing and not securing the 7E7 project. The conflict was that since 1932 Deloitte Consulting and its parent company, Deloitte & Touche, have earned millions of dollars in fees as Boeing's own auditor and consultant.

“CASH COW”

What are the ramifications of the 7E7 deal with respect to future corporate behavior and the policy objectives of state governments?

Less than four months after Boeing and Washington State signed the 7E7 contracts, the consulting firm Ernst & Young began offering some of America's largest corporations – Alcoa, Goodyear, Wal-Mart, Home Depot, Verizon and Microsoft, among them – a power point presentation entitled, “*How to Turn Your State Government Relations Department from a Money Pit into a Cash Cow*”. The consulting firm conducts seminars modeled on the Washington State / Boeing agreement, promoting key strategies for success, such as directing companies to identify “public benefits”, while making a threat of dire consequences if the deal is not made. Ernst and Young's Michael Press delivered a *Cash Cow* presentation in Savanna, Georgia in March 2004, alongside co-presenter Robin Stone, the former vice-president of state and local government relations for Boeing.

Ernst & Young also advises businesses to “control publicity” and “avoid legislation if possible”. The final 7E7 contracts required that all of the state's press and publications relating to the “extra” deals be coordinated directly with Boeing. Governor Locke had negotiated and signed the 76-page contract, keeping much of the information secret by erecting barriers to public disclosure, such as: forcing interested parties to file complaints with the Attorney General's office, and letting the Attorney General decide whether or not to pursue a court challenge; and by making available only redacted (blacked-out) documents. A law suit was filed by the Evergreen Freedom Foundation, an Olympia-based watchdog organization, which successfully sued for access to the documents by using the state's Public Disclosure Act.

The one thing public disclosure can't solve is the Boeing contract's stipulation that future Washington State legislatures “shall not suspend, revoke, or require repayment” of its incentives and tax breaks in the absence of promised jobs. Apparently, that's one of the most appealing aspects of the deal: Ernst & Young's presentation mentions it specifically, and promotes it as part of the overall strategy to milking the *Cash Cow*.

HIGH-TECH TAX BREAKS

The Washington State Legislature believes that stimulation of research and development (R&D) in the high-tech industry sector creates jobs and economic diversity. B&O tax credits and sales tax deferrals have been tailored for the following industries: advanced computing, advanced materials, biotechnology, electronic device technology and environmental technology. The legislature considers these industries - which are characterized by high-wage, high-skilled jobs - as vital to the state's economy.

The legislature voted in 2004 to extend to 2015 certain B&O and sales tax breaks for the high-tech industry. Some disclosure will be required from companies, but not until 2009, and the information will be provided only to the D.O.R., not to the public.

The 2003 D.O.R. High-Tech Tax Incentive Programs Study examined whether tax incentives increased jobs, company growth, geographic diversification, growth in R&D investment and new patents. Results have been mixed. More high-tech firms are taking the tax breaks, but the number of high-tech jobs has remained virtually unchanged. While R&D spending has grown in Washington over the last decade and the number of patents has increased, most of the firms are still located in urban counties throughout Western Washington.

Incentives to businesses do not necessarily buy their loyalty. Some companies register in other states so that their dollars escape taxation at home, and some respond to global market conditions by opening offices in other countries. A local example of this is Microsoft Corporation. Microsoft has registered over 40 companies with more than 400 employees in Nevada, a state which does not have a B&O tax. In the seven years since Microsoft has been operating there, it has sheltered more than \$60 billion in royalty revenue, thus costing Washington State an estimated \$327 million in unrealized revenue (“Citizen Microsoft”, Jeff Reifman).

CITY OF SEATTLE – AUTHORITY IN GIVING INCENTIVES

The City of Seattle has an interest in giving local business incentives, and the reason is the same as for other government entities – increased jobs and revenue. Its taxing authority is often linked to state activity, so exemptions are only given where already provided for by state law. The city does provide direct subsidies and incentives, and the power of the purse rests with the city council.

The city has joined with the county, port and state to provide subsidies to specific businesses. In 1998 when Immunex Corporation moved from downtown Seattle to Pier 91 in Magnolia, the company asked for a separate road to be built for its use, leading from 15th Avenue West to the facility. The city complied by paying the lion's share of what is now known as the Galer Street Flyover. The total cost was \$19 million. Another example of a subsidy is the city's acquisition of the Pacific Place Garage in November 1998. Large cash outlays taken from the General Fund are often controversial because it can take many years for positive results to show. In the case of the garage purchase, the economic strength of Seattle's business climate proved positive in a short time. Downtown retailing added over \$800,000 of new B&O and sales tax revenues in a year, which allowed the General Fund subsidy of \$400,000 to be totally eliminated for 2000.

One common incentive the city offers, with respect to land use, is making changes to zoning laws. Currently, the city is engaged in allowing double density on single lots, particularly in the South Lake Union neighborhood, thereby increasing the value of the property. Businesses developing there and in the downtown core are also being offered incentives which trade certain amenities - creation of affordable housing and mixing retail and residential within a building - for increased building heights.

The city has the authority to raise sales taxes, but has not done so. Because Washington's total sales tax is one of the highest in the nation, increases to the city's portion would probably come in the form of a citizen's voter initiative.

DEVELOPMENT AT SOUTH LAKE UNION – CREATING AN URBAN VILLAGE

The following case study raises issues regarding the trade-offs at stake with burgeoning local development. The state is providing tax breaks to companies locating at South Lake Union and the city is providing infrastructure and land-use incentives, all with the expectation that jobs and revenue will result.

In 1995 and 1996, a citizen's initiative to build a park in the South Lake Union (SLU) neighborhood called "The Commons" was proposed and rejected by Seattle voters. Microsoft co-founder Paul Allen had contributed \$20 million to the city for the purchase of the property. When the project suffered defeat at the polls the property reverted to him. In 2000 the city acquired 12 acres of future park property that had previously housed the Naval Armory. Partial funding for the park was secured through passage of the Pro Parks Levy. In the ensuing years, Allen and his development company, Vulcan Inc., acquired 58 acres in the area.

By December 2003 there were already major plans underway for a much more ambitious venture: the creation of a nationally-recognized biotechnology hub in the SLU neighborhood. Many of the key players in Seattle's public and private arenas – from politicians to businesspeople to leaders in the medical and life sciences fields – had long dreamed of a way to create a real "urban village" on one of the city's most centralized pieces of real estate. The SLU and adjoining Cascade neighborhood had served as a largely industrial area, interspersed with some small businesses and lower-income housing. In the last two decades, with the changing nature of Seattle's economy, the neighborhood seemed more like an area to pass through than a destination in itself. Arterials running alongside it gave even more of a stand-alone feel because it was flanked on the east corridor by Interstate 5 and on the west by Aurora Avenue. Tapping into a highly educated, tech-savvy workforce and coupling it with developers seemed the perfect antidote to the perceived isolation and unused potential of SLU.

BIOTECH – THE PROMISE OF EXCELLENCE

The University of Washington's medical school, life sciences division and hospital have become top choices for students, patients and medical professionals alike due, in no small part, to Senator Warren Magnuson's talent for bringing federal dollars to the school. The UW goes on record as the public institution consistently receiving the most National Institutes of Health (NIH)

funds in the country.

The Fred Hutchinson Cancer Research Center sited its first facility on the southeast edge of SLU in 1993. By then, Seattle already had Immunex Corporation and start-up biotech companies like Zymogenetics popping up in the region. The biotechs are primarily funded by venture capital, although the R&D tax breaks provided by state government are a big helping hand because start-up biotechs don't know if or when they're going to be making any money from the development of drugs. It takes an average of ten years for a drug to make it to market, due to a lengthy R&D process and a series of successful drug trials. Seattle generally ranks fifth or sixth nationally in the life sciences field and the biotech business.

A great deal of activity is already underway at SLU. The UW, long-interested in expanding its research work off campus, has built a new facility called UW Medicine-Lake Union. On the south side of the lake, Vulcan has put up a building for the Seattle Biomedical Research Institute (SBRI). The *South Lake Union Agenda*, devised by the mayor's office in 2003, assumes that the UW, Fred Hutchinson, Zymogenetics and SBRI will act as anchors of the hub and attract other biomedical activity to the neighborhood. Our local region is already home to over a dozen biotech companies, many of which are immersed in the research and development of cancer drugs and treatments for infectious diseases.

It would seem the stage is set for the grand opening of Seattle's biotech century. Or is it? The unknown factor upon which the entire plan hinges is: jobs.

THE MAGIC BULLET?

Economic development means jobs, growth and ultimately, revenues. But the strength of the biotech industry, famously dependent on the success of those process-heavy drug trials, cannot realistically be considered a sure thing. Successes guarantee jobs and investment dollars for the future, just as failures can bring companies right back to square one, forcing layoffs and cutbacks.

In 2003 the mayor's office commissioned a study by economist and UW professor Paul Sommers on the proposed development at SLU. Predictions of jobs and revenues were extremely favorable: at least 16,000 direct jobs and between 32,000 and 39,000 indirect jobs to the SLU area by the year 2020 ("full build-out"

WHAT COULD BE FUNDED WITH \$25 MILLION IN REVENUES?

- 400 full-time Seattle elementary school teachers for one year, with full healthcare and retirement benefits;
- Large city garden in Belltown, two smaller ones on Capitol Hill and First Hill;
- Half-rent subsidies to 1,200 households or individuals for two years;
- Emergency one-time rent assistance to 17,800 households or individuals for one year;
- Case management to 3,500 youth for drug use prevention for five years;
- Child care subsidies to 6,250 children from low-income families for one year (this would eliminate current waiting list).

AMOUNT OF REVENUE NEEDED TO FUND 25,000 SLOTS IN WASHINGTON STATE'S BASIC HEALTH PLAN

- \$47,846,054 (Includes benefit, communications and administrative costs - based on December 2005 model).

Sources: *City of Seattle School District; Seattle Office of Planning; Seattle Department of Human Services; Washington State Health Care Authority*

scenario) along with \$247 million in new revenues to the city by 2025. In February 2004 Mayor Nickels projected eventual jobs numbers to reach as high as 76,000 as a result of developing SLU as a biotech hub. The Sommers jobs numbers have since been revised down to about 30,000 in most media publications, although the original revenue predictions remain unchanged. Seattle City Council member Nick Licata cautions that the "full build-out" numbers don't represent actual jobs, but the *capacity* for jobs in the neighborhood. The projected number of direct biotech jobs purported to fuel the boom is between 4,730 and 6,300.

Many experts in the biotech field dismiss huge jobs predictions as over-hyped. Bruce Montgomery, CEO of Corus Pharma, told Luke Timmerman of *The Seattle Times* that taxpayers should not expect biotech to produce anything like the number of jobs Nickels touted in the South Lake Union area. Most biotechs stay small, relying on big pharmaceutical companies to take care of their manufacture and national sales.

Fred Hutchinson has a bigger payroll than the region's top seven biotech companies combined. These biotechs

collectively added a total of 187 jobs from 2001 to 2003. Overall, most biotechs succeeding with drug trials and bringing those drugs to market would be lucky to add as much as 100 employees in a single year.

LIFE SCIENCES/DEFENSE FUND

Some of the money coming to research institutions will be distributed in the form of competitive grants from the Life Sciences/Defense Fund. This fund, set up by the State of Washington, is a direct result of the \$500 million that Washington received for its leadership on the settlement won by the states from the major tobacco companies. The State Legislature approved \$350 million to be used as seed money, and it's expected that amount will be matched by private investment over a ten year period, beginning in 2008.

VULCAN, INC.

In 2001 Mayor Paul Schell's administration signed a contract with Vulcan, Inc., Paul Allen's development company. Adding to the properties Allen already owned via the failed Commons plan, the City of Seattle sold him another eight parcels for the price of \$20.2 million. That money is slated to be re-invested in the SLU neighborhood for transportation and infrastructure improvements, some required by law, some desired by Allen. But those transportation improvements – lowering Aurora Avenue North, reconfiguring both Valley Street and Fairview Avenue, transforming Mercer Street into a widened two-way boulevard, and construction and operation of a streetcar line – will cost many times that amount. The city's conservative estimate for reconstructing Mercer Street alone is \$90 million. While fixing the "Mercer Mess" has long been a goal for Seattle residents, the \$350,000 study commissioned by the city concluded that Mayor Greg Nickels' transportation improvement plan might not be an improvement at all, but could actually make the congestion worse. The city may end up buying back some of the eight parcels in order to reconstruct Mercer Street. The entire transportation and infrastructure package could cost anywhere from \$420 million to \$1 billion.

THE PARK

The 2001 contract required that Paul Allen contribute toward the development of some cultural amenities in

the neighborhood. In March 2005 Allen agreed – with conditions – to donate \$10 million for the construction and development of a 12-acre park. He will contribute the first \$5 million in exchange for a rewrite to the 2001 contract that allows him to wait until 2013 before starting construction on some of his parcels instead of by 2008, as originally mandated. The second \$5 million contribution is contingent upon the Seattle Parks Foundation raising its \$10 million portion first, and that Allen's donation be listed as a credit against future development impact fees. The city must also commit to narrowing Valley Street before receiving the second \$5 million donation.

SOUTH LAKE UNION STREETCAR

Mayor Nickels, Paul Allen and many of the new business owners in the development at SLU have been heralding a streetcar line as the city's answer to jump-starting economic development in the area by providing clean, frequent transit service. The neighborhood currently has 12 different bus routes serving it, which generally run on the half hour. Despite the existing bus service, the city has opted for a streetcar transit system based upon the successful Portland, Oregon model. In 2004 the Seattle Department of Transportation (SDOT) applied for federal funds to cover some of the capital cost of a streetcar line. SDOT's application describes the intended project's purpose as: providing local transit service; connecting to the regional transit system scheduled to come online in 2009; encouraging economic development; and creating a vibrant, pedestrian-oriented urban center, which will connect SLU to the existing transit hub at Westlake Avenue and Fifth Avenue. To date, SDOT has obtained \$12.3 million in committed funds for the project.

In June 2005 the Seattle City Council voted (7-2) to approve funding for the construction, operation and maintenance of the streetcar. Roughly 53 percent of the capital cost is covered by the creation of a local improvement district (LID), whereby the property owners along and adjacent to the route will pay a fee based on the city's estimates of increasing property values. Many of the larger developers along the route lobbied for the LID, seeing benefits to their properties and the neighborhood in general. Others, particularly older small businesses, objected, saying they saw no benefit to more walk-by traffic as their businesses are industrial and rely on truck or car pick-ups. They are

also worried that increases on their property taxes will drive them out of the area or force them to close. The city's promise on capital funding is that no General Fund money would be used, but a minimum of \$700,000 for administrative costs on the LID has been earmarked.

Councilmembers Nick Licata and Peter Steinbrueck opposed the overall plan, partly because of the unknown factor of how many future Metro bus hours will be needed to feed the streetcar operations. Licata envisioned 9,000 hours being taken from other neighborhoods and wanted more study before committing to an unforeseen loss. That amendment was rejected by the majority of the council. Now that the monorail plan has been shut down, the issue of bus hours becomes more crucial, as there is no longer a second transit link to take up the slack.

When the final vote on the LID was taken on October 3, 2005, Steinbrueck was the lone dissenter, questioning the streetcar as a priority in a neighborhood that doesn't yet have sidewalks or traffic synchronization. He expressed concerns about the ongoing availability of federal funds and the wisdom of tying up revenues from the sale of city property. He also noted that the issue of future Metro bus hours had still not been resolved.

A NEW ELECTRICAL SUBSTATION

It is the city's obligation to provide money for infrastructure improvements on economic development projects, and an estimated \$30 million has already been committed to SLU. The amount of planned development will inevitably require a new electrical substation in the area. The city estimates about a \$100 million investment over 10 years for the substation project, but there are currently no answers to the questions of how it will be paid for, where or when it will be built, and the date it will need to be up and running. Councilmember Jean Godden told the *Seattle Post-Intelligencer* (April 29, 2005) that there's only speculation about where it might be built because property at SLU is appreciating, and because there are geological factors to consider due to the marshiness of the lake. As for how it would be paid for, Godden said the options include a voter approved levy, councilmanic bonds (the city's credit card) which the council can issue without voter approval, or borrowing by City Light. City Light spokesman Bob Royer confirmed that the schedule on building the substation is unknown. "It

could be 10 years, it could be 30", he said.

AFFORDABLE HOUSING AND PROPERTY TAX EXEMPTIONS

While the city doesn't give direct tax breaks to business, it does participate in the Multifamily Property Tax Exemption (MFTE) program. Developers receive tax exemptions on the entire property by setting aside a certain percentage of units with affordable rents. Vulcan's contract with the city requires that it reserve at least 50 rental units for affordable housing at SLU. City Investors, Vulcan's real estate arm, was approved for the MFTE program on March 7, 2005. One year earlier the same exemption was directed to other apartment developers who may save about \$30 million in taxes over 10 years for setting aside 25 percent of the studio units to rent as low as \$886 per month. City Investor developments will save about \$3 million. Councilmember Richard Conlin has stated, "The city does not actually lose any money, as the property tax foregone is spread to other property tax payers".

The Cascade neighborhood, historically the area's residential zone, had a 33-unit low-income apartment building called the Lillian Apartments, where the lowest rents were about \$250 per month. The Lillian was torn down in 2002 and is being replaced with a 35-unit building for affordable housing, where the minimum rents will be \$740 per month.

The concern for low-income housing advocates is that, because the area's land values have risen considerably since development began, many of SLU's previous low-income residents will be permanently driven from the neighborhood and into low-income areas outside the city's core. Developers contend that property values are increasing anyway and it's simply becoming more expensive to develop in all areas of the city, so keeping rents at previous levels is impossible.

COMMUNITY INVOLVEMENT/CORPORATE ACCOUNTABILITY

One of the ways that public-interest advocates can help guide development projects toward mutually beneficial goals is by creating a Community Benefits Agreement (CBA) with the developers. CBAs have been successful in other cities, especially with big-box superstores.

Beginning in 2004, Seattle's Coalition for Healthy

Communities hoped to negotiate such an agreement with Vulcan, Inc., using a model that worked for community groups in California. Those groups had won enhanced labor rights and environmental standards for the development of Los Angeles' Staples Center sports complex. The Seattle coalition included organizations such as the Transportation Choices Coalition, the Housing Development Consortium of Seattle, and the Hotel Employees & Restaurant Employees Union. Among its goals were: the adoption of environmentally friendly practices, building affordable housing, and rights to unionize for hotel and security staff. The group first approached Vulcan directly, but unsuccessful there, turned to the mayor's office. The three entities held private negotiations for nine months. With millions of dollars coming out of the General Fund for infrastructure and transportation improvements, much was riding on the coalition's ability to reach an agreement on tangible public benefits. In the end, the coalition concluded that Vulcan and the mayor's office were on the same team and the talks ended in a failure to reach any agreements.

MINNESOTA LEGISLATION TO CREATE ACCOUNTABILITY

While tax exemptions and incentives are provided in the name of economic development at the state and local level, it's unclear how public benefits are verified. Neither has it been demonstrated whether the jobs created and the revenues generated result from the incentives given. The Good Jobs First Minnesota study illustrates how public benefits can be measured by requiring accountability through reporting and tracking. The study also links lack of performance with consequences.

Minnesota's first-in-the-nation economic development accountability reforms were born of civic engagement according to a study by Good Jobs First. Controversial business deals in the late 1980s and 1990 attracted public attention and laid the groundwork for citizen activism. For example, in 1987 the U.S. Department of Justice found that a major Minnesota employer, Amhoist, had violated the terms of its \$4 million grant from the U.S. Department of Housing and Urban Development. Amhoist had used the subsidy to relocate crane production from St. Paul to Wilmington, North Carolina, dislocating hundreds of Minnesota workers. After a lengthy series of protests by U.S. Representative Bruce Vento, the company was required

to repay the \$2.8 million it had already received.

Minnesota activists involved in the living wage and welfare reform debates of 1994 argued that corporations receiving subsidies ought to be subject to at least the same accountability being demanded of recipients of welfare programs. The initial state law in 1995 had four major components:

- Any business that received state or local government assistance for economic development or job growth purposes must create a net increase in jobs within two years of receiving assistance.
- Assistance was defined as a grant or loan exceeding \$25,000 of any amount of tax increment financing.
- Recipients who failed to meet wage and job creation goals within two years were required to repay the assistance.
- It required that the government agency providing assistance report the wage and job goals and the results for each project in achieving those goals to the state, which was required to publish the results.

This initial legislation and the data collected during its implementation revealed conflicting interpretations of the law as compliance with reporting and goal-setting requirements was spotty, communities were not well informed about the law, job and wage goals were infrequently met and there was lack of clarity on how the law should be enforced and how goals should be met. To address these problems, a bipartisan Corporate Subsidy Reform Commission was created by the State Legislature in 1997. This Commission held statewide hearings and over the next year developed a series of recommendations that would better define the existing accountability law. The recommendations to strengthen the Minnesota legislation included the following:

- require the business subsidies meet a stated public purpose,
- clarify which subsidies were covered under the law, the date for reporting requirements and the time period that a business has to satisfy job and wage goals,
- require all communities and agencies to develop criteria for subsidies that would apply to all future deals,
- require detailed reporting from local governments,
- require communities and agencies to provide

- public notice and hold public meetings before awarding subsidies, and
- impose a financial penalty (known as a “clawback”) for non-compliance with a business subsidy agreement including a prohibition against future subsidies being granted to non-complying businesses.

The impetus behind the corporate accountability legislation was not just the creation of jobs but “living wage” jobs. Analysis revealed that almost half of the 525 deals examined were providing jobs that paid wages 20 percent or more below the market.

Spurred by research findings, the Minnesota Legislature enacted a new subsidy reform bill in 1999, which replaced the original 1995 law with a detailed, comprehensive law that implemented almost all of the recommendations. While subject to subsequent amendments, the law remains in effect in substantially similar form today.

WHAT WORKED – PUBLIC VISIBILITY

Initiated by a public interest group hoping to hold corporate America accountable, the Minnesota accountability law set a precedent that generates public information about subsidy deals and holds businesses accountable for the creation of living wage jobs or they face “paying back” the public investment. Because public officials are aware the public is watching, and because the accountability law’s processes encourage communities to define their criteria up front, local city policies have changed substantially. Communities now seek higher wage deals and high wage industries. The study showed that Minnesotans are no longer willing to accept a costly deal-by-deal economic development process.

WHAT DIDN’T WORK – FULL ACCOUNTABILITY FOR RESULTS

Minnesota’s accountability law continues to be a work-in-progress. If further amended, it could create still more effective accountability by:

- simplifying the business reporting forms to focus on results,
- evaluating all subsidy strategies by weighing costs against public benefits,

- more closely aligning economic development expenditures with land-use planning and transportation goals, and
- redirecting funding from large single-company deals to skills and infrastructure that benefit all employers.

CONCLUSION

In Washington, state and local granting of exemptions raises the question of how foregone revenue might otherwise have been allocated. What government programs have been overlooked?

Public disclosure about tax incentives and economic development deals has been lacking at both the state and local level. Community involvement efforts in the South Lake Union neighborhood have been discouraged by developers and the city. Good economic development decisions benefit from public involvement at all levels early on in the process.

The heavy focus of public investment in one part of the city can occur at the expense of needs in other neighborhoods. Tax breaks for certain companies may result in shifting the burden onto other tax payers.

There isn’t a demonstrated correlation between exemptions or incentives given and jobs and revenue created. Would the jobs have been created as a natural result of economic growth? In some cases, the number of projected jobs includes both new jobs and existing jobs that are being moved to a new location. Without additional information, the public may assume that the projections reflect only new jobs.

PRECEDENTS SET/FOUNDATIONS LAID FOR ACCOUNTABILITY MEASUREMENT

The Minnesota Economic Development Accountability Law mandated public hearings as well as disclosure of public deal costs and benefits, job creation requirements and job quality standards, and money-back guarantees or “clawback” measures.

Washington State has attempted to adopt legislation implementing oversight of tax preferences, however, between 1989 and 2005 none of the bills achieved a majority vote. HB 1069, which passed the House but died in the Senate in the 2005 legislative session, was resubmitted and adopted into law March of 2006.

EXAMPLES OF AFFORDABLE RENTS				
Household size	Annual Income	% of area median income	Affordable unit size	Affordable monthly rent
1 to 3 persons	\$16,350 to \$21,050	30%	Studio to 2 bedrooms	\$408 to \$526
1 to 3 persons	\$27,250 to \$35,050	50%	Studio to 2 bedrooms	\$681 to \$876
1 to 3 persons	\$32,700 to \$42,060	60%	Studio to 2 bedrooms	\$817 to \$1,051
1 to 3 persons	\$40,600 to \$52,200	80%	Studio to 2 bedrooms	\$1015 to \$1305

Source: *City of Seattle Office of Housing*

This bill calls for periodic performance audits of tax preferences. The audits are intended to serve the public through the reporting of findings by a joint legislative committee to a citizen's commission.

Locally, the Seattle City Council had created a citizen oversight commission to review incentive deals that exceeded a specific amount of public investment. It failed due to lack of direction by the council over how early in the process the commission would become involved and what criteria the commission should apply in their review. It last met in 1999.

GLOSSARY

CLAWBACK: a provision in a law or a contract that limits or reverses a payment or distribution for specified reasons.

CREDIT:

1) a dollar for dollar reduction in the amount of tax that a taxpayer owes. Unlike deductions or exemptions, which reduce the amount of income subject to tax, a CREDIT reduces the actual amount of tax owed.

2) adjustments in the customer's favor or increase in equity.

DEDUCTION: amount allowed to taxpayers under the Internal Revenue Code as an offset against gross income, or adjusted gross income.

DEFERRAL OF TAXES: postponement of tax payments from the current year to a later year. Deferring taxes is worthwhile because interest can be earned on money not yet paid in taxes; moreover, the deferred amount can often be offset by subsequent losses or ended in a year when the taxpayer is in a lower tax bracket.

DIFFERENTIAL: partial deduction allowed one taxpayer in a specified group of taxpayers. For example: manufacturers of raw or frozen seafood products are provided a preferential B&O tax rate of 0.138 percent, while other manufacturers continue to pay the standard rate of 0.484 percent.

DIRECT LABOR: cost of personnel that can be identified in the product, such as the salary of the person who works at the production machine, but not the administrator's or janitor's salary.

EXCLUSION: taxation: amount that would otherwise constitute a part of gross income, but is excluded under a specific provision of the Internal Revenue Code.

EXEMPTION: deduction allowed a taxpayer because of the taxpayer's status or circumstances rather than because of specific economic costs or expenses during the taxable year.

INCENTIVE: feature of the taxation system that encourages or discourages certain economic activities. Common tax incentives are: depreciation allowances and tax credits.

INDIRECT LABOR: wages and related costs of employees, whose time is not charged to specific finished products; sometimes combined with indirect materials costs, such as supplies.

ROYALTY: share of the product, or of the proceeds therefrom, reserved by an owner for permitting another to exploit and use his property

SUBSIDY: payment or other favorable economic stimulus (such as remission of taxation) given by government to certain individuals or groups of economic entities, usually to encourage their continued existence, growth, development and profitability. In the United States, subsidies are given to the agricultural industry, the very poor, and many other groups.

VENTURE CAPITAL: important source of financing for *start-up* companies or others embarking on new or *turnaround* ventures that entail some investment risk, but also offer the potential for above-average future profits; also called *risk* capital.

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**WASHINGTON STATE LEGISLATIVE
HISTORY FOR CORPORATE
ACCOUNTABILITY, TRANSPARENCY**

1989 – The Washington State Compact would have required businesses that apply for public assistance like grants, loans, development subsidies and tax deferrals to agree to some social and economic standards including basic health care coverage for employees and wage levels no less than state's average wage. Introduced again in 1991 and 1993. *Failed in legislature all three times.*

1996 – SB 6479 Corporate Welfare Reform Bill would have required establishing job creation/maintenance, wage and benefits standards for businesses that receive tax breaks and incentives. *Passed Senate, amended in House to set up advisory committee to establish "goals", but was never voted upon.*

2000 – SB 6541 would have required the Department of Community, Trade and Economic Development to publish an annual report listing subsidies, tax cuts or other incentives offered to private business by state and local governments. *Died without a hearing.*

2003 – HB 1869 in its original form, would have subjected tax expenditures to review by a legislative committee. *Gutted and passed the House.*

2004 – HB 2762 provided mandatory disclosure and accountability standards for tax expenditures; **HB 2654** required a tax expenditure report as part of the biennial budget process; **HB 2930** set a cap on tax expenditures. *All three bills received hearings but were not voted upon.*

2005 – HB 1069 would have required periodic performance audits of tax preferences, with findings to be reported to a citizen commission for performance measurement of tax preferences by August 30 each year. *Passed the House but died in the Senate.*

2006 - HB 1069 was resubmitted, passed both the house and the senate and was signed into law in March of 2006.

Source: *Washington State Labor Council (2006)*

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(Discussion)

- 1) List some benefits and trade-offs that result from government giving corporations subsidies, tax preferences and incentives.
- 2) Under what circumstances are subsidies, tax preferences and incentives appropriate?

(Consensus)

- 3) Is the Minnesota law a good model for legislation? Why or why not?
- 4) a) Should our local governments adopt legislation that links the granting and continuation of subsidies and tax preferences and incentives to specific criteria?

b) What criteria should be included?
(Examples: established company and community goals; tracking of new jobs and revenue; accountability measures in case goals aren't met.)
- 5) Should a citizen oversight commission be created? What authority would it have?

INTERVIEWS

Luke Timmerman, Seattle Times business reporter
– March 2005

Helen Sommers, Washington State Representative
– June 2005

Marilyn Watkins, Ph.D., Policy Director, Economic
Policy Institute – June 2005

Julie Sexton, Legislative and Policy Division,
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Seattle City Councilmembers:

Richard Conlin – September and November 2005

Jean Godden – October 2005

Nick Licata – October 2005

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