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Now is Not the Time to Raise Taxes in Seattle

Briefly

Seattle's tax revenues have held up remarkably well, and the city is under much less financial stress than the state or King County.

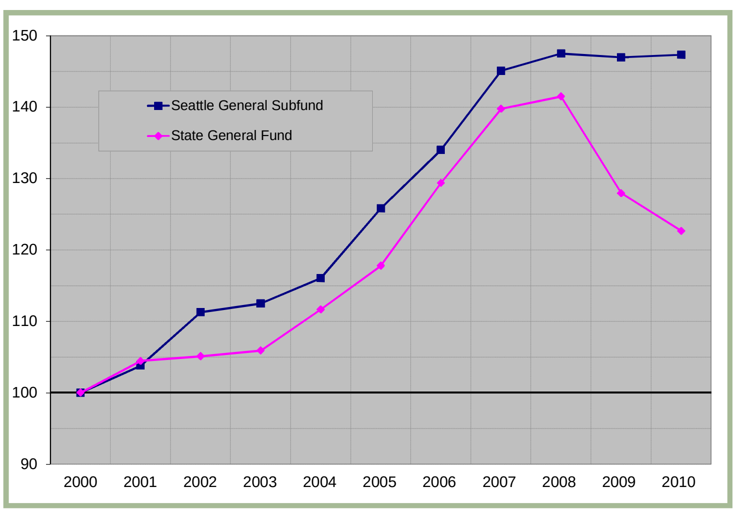
On September 27, Seattle Mayor Mike McGinn released his budget proposal for 2011 and 2012. Adjusted for accounting changes, the mayor's proposed 2011 budget spends 0.3 percent more money than the adopted 2010 budget. City Budget Office staff project a $67 million gap between available resources and the cost of carrying forward existing programs. The mayor's proposal balances the city's budget without imposing any general tax increases, but does propose a number of tax and fee increases in specific areas. Taken as a whole, the task facing Seattle's budget writers is easy relative to those faced by the state Legislature or the King County Council because the city's revenue situation is not as dire. City revenue grew 27 percent from 2004 to 2008 and has been essentially flat since then. Modest growth is forecast in 2011 and 2012.

Recovery Will Be Slow

The arbiters at the National Bureau of Economic Research have marked June 2009 as the last month of the recession. While downward movement in the economy has stopped, recovery has been nearly invisible, and it is likely to take three or more years for economic activity to regain 2008 levels.

Locally, the recession has been severe. From August 2008 to August 2009, King and Snohomish Counties lost 116,500 jobs. Over the period, the two-county unemployment rate rose from 4.7 percent to 8.4 percent. From March 2008 to March 2009 (the most recent month for which the Puget Sound Regional Council has released city employment estimates) the city of Seattle lost nearly 23,200 private sector jobs (WRC 2010). Seattle has clearly lost many more jobs since March 2009. According to Grubb and Ellis, the office vacancy rate in the Seattle central business district was 18.4 percent during the April–June quarter of this year. Revenues from the city's economically sensitive retail sales, business and occupation, and amusement taxes fell by 10.3 percent from 2008 to 2009 and are forecast to fall another 1.3 percent in 2010.

Chart 1: Growth in Seattle General Subfund and Washington State General Fund Revenues 2000 to 2010



Property and Utility Tax Gains Offset Other Revenue Losses

In the longest and deepest recession since the Great Depression, the City of Seattle's overall revenue collections have held up remarkably well. Declines in economically sensitive business and sales taxes have been offset by gains in property and utility taxes. Chart 1 compares, for the period 2000 to 2010, revenue growth experienced by Seattle's General Subfund to revenue growth of the state's General Fund. (Note: Data are for fiscal years. The city's fiscal year begins on January 1 and ends December 31. The state's fiscal year begins on July 1 and ends June 30.) From 2000 to 2008 revenue on both levels grew considerably. Seattle's growth (47.5 percent) exceeded that of the state (41.5 percent) by a comfortable margin. Seattle revenues fell by 0.4 percent in 2009 and are ex-

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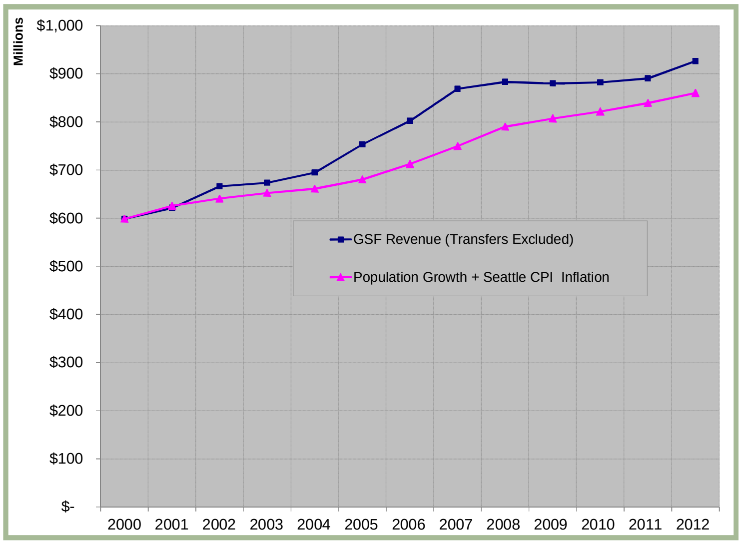
Chart 2: City of Seattle General Subfund Revenue, 2000 to 2012



pected to increase by 0.3 percent this year. For the state, revenues fell by 10 percent in 2009 and by a further 4 percent in 2010.

Altogether, the city's revenues for 2010 are expected to be 47.3 percent greater than 2000. For the state, the ten-year growth is 22.7 percent.

Chart 2 provides a second perspective on Seattle's revenue growth. The upper curve on the chart is actual city general subfund revenue for 2000–2009 and forecast revenue for 2010–2012.

The lower curve is constructed so that its value for the year 2000 is city revenue for that year. For each subsequent year, the percentage growth in the curve is equal to the sum of the city's population growth rate and the inflation rate measured by the Seattle consumer price index. Thus, along the lower curve *real*, (i.e. inflation-adjusted) per capita city revenue remains constant at the 2000 level.

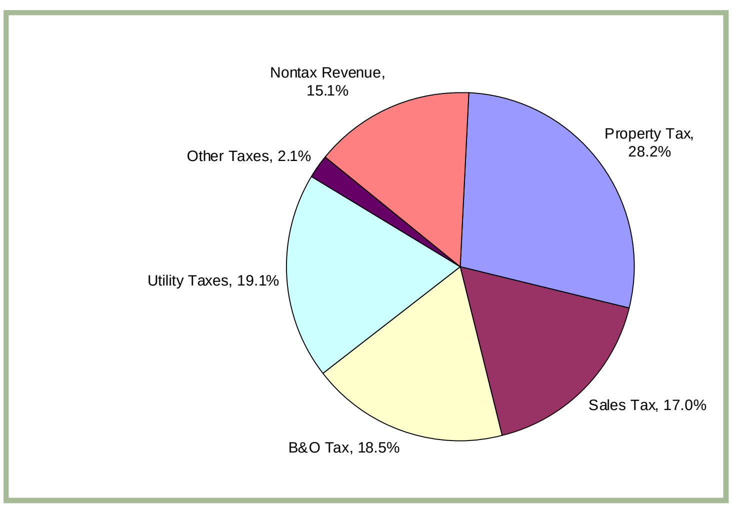
We have used consumer price inflation forecasts from the state Office of the Forecast Council and population estimates from the state Office of Financial Management. We assume that for 2011 and 2012 the population growth rate equals the average rate from 2000 to 2010.

City revenue grew much more rapidly than population plus inflation from 2004 to 2007. The 2008 rate was slower and the 2009 rate was negative. For 2010 and 2011 revenue is expected to grow at a rate a bit less than population plus inflation; for 2012, a bit more. Inflation adjusted per capita revenue is expected to be 8 percent higher in 2012 than it was in 2000, the peak year of the dot com bubble.

WHERE THE MONEY COMES FROM

Most of the monies for general government services pass through the General Subfund of the city's General Fund. Excluding transfers from other city accounts, General Subfund (GSF) revenues totaled about $871.0 million in 2009. We have estimated that 54 percent of city taxes are paid by businesses (WRC 2007b).

Chart 3: Seattle General Subfund Revenue Shares, 2009



(The city charter dedicates "ten percent of the gross receipts of the City from all fines, penalties and licenses" for parks and recreation [Article XI, Section 3]. In 2009 these monies were deposited directly to the GSF. In prior years, such monies were deposited to the Parks and Recreation Fund. All historical trends data presented in this brief have been adjusted to reflect the current practice.)

Chart 3 provides a high-level view of the sources of GSF revenue for 2009. Taxes provided 85 percent of this revenue. The remainder came from license and permit fees; federal, state and interlocal grants; fines and forfeitures; interest; parking meters; service charges; interfund charges and operating transfers; and other miscellaneous sources.

The city's tax revenues come mainly from four taxes, the property, sales, business and occupation (B&O), and utility taxes.

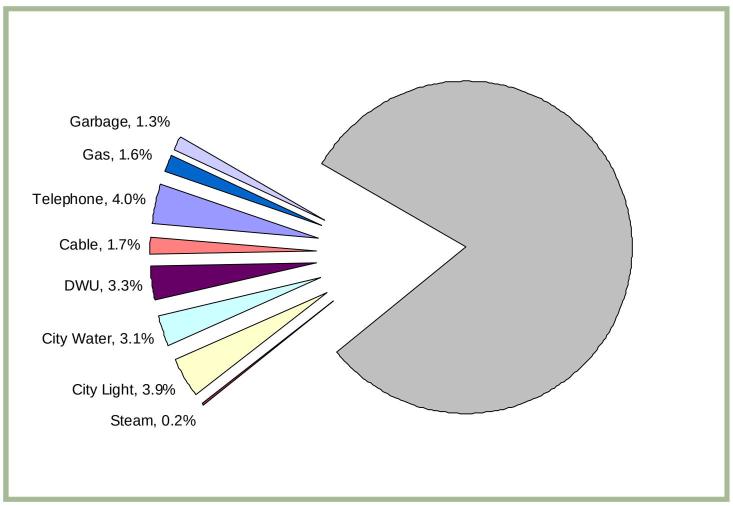
Property taxes provided 28.2 percent of GSF revenue in 2009. The GSF receives two slices of property taxes: The city's regular tax ($1.55 per $1,000 assessed value in 2009) yielded $208.4 million. The city's share of the countywide Medic One levy (12 cents per $1,000 assessed value) was $37.2 million.

Sales tax provided 17.0 percent of GSF revenue. The sales tax comes in two slices: the regular sales tax (at the rate of 85 cents per $100 taxable sales) yielded $136.6 million, while the city's share of the countywide criminal justice sales tax (at the rate of 10 cents per $100) was $11.7 million.

The B&O receipts reported by the city include revenue from the complementary square footage tax. B&O receipts were 18.5 percent of GSF revenue in 2009, $161.0 million.

The B&O tax rate is 21.5 cents per $100 of gross receipts in the retail, wholesale, manufacturing, extracting, printing and publishing sectors, and 41.5 cents per $100 of gross receipts in the service and other sectors. Beginning in 2008, the city augmented the existing gross receipts tax on business with a square footage tax. State legislation (HB 2030, enacted in 2003) limiting the ability of the city to collect gross receipts tax on out-of-city activities of Seattle-based businesses became fully effective on January 1, 2008. The square footage tax is designed to recoup the lost revenue from those businesses whose taxes were reduced by HB 2030. The rates are $1.56 per square foot annually for office, retail or production space and 52 cents per square foot annually for space with other usages (such as warehousing and storage). The fraction of a firm's space subject to the tax is equal to the fraction of its Seattle-based revenue that escapes the B&O tax because of HB 2030. The amount of square footage tax any firm owes is capped at the amount of B&O tax savings it receives from HB 2030.

Chart 4: Utility Tax Revenue Shares, 2009



Utility taxes on a wide range of services provide 19.1 percent of GSF revenue. The utility tax is a gross receipts tax imposed on municipally-owned and private utilities at varying rates: $19.87 per $100 of revenue for water; $12.00 per $100 for wastewater; $11.50 per $100 for drainage and solid waste; $10.00 per $100 for cable; and $6.00 per $100 for City Light, telephone, natural gas and steam. In total, utility taxes provided $166.5 million in 2009. Chart 4 shows the distribution of revenue across the various utility services. (The abbreviation DWU stands for the city's drainage and Wastewater utility.)

Tax Revenue Trends

Charts 5, 6, 7 and 8 show trends from 2000 to 2009 in revenues from the property, sales, B&O and utility taxes.

Property Tax. In November 2001 voters passed Initiative 747, which tightened the annual limit on regular property tax revenue growth to the lesser of 1 percent or the rate of inflation, plus the rate of growth in assessed value due to new construction. In 2002, with the economy slipping into recession and revenues from other taxes constrained, Seattle used all of its "banked" capacity, which allowed regular property tax revenue to grow by 5.3 percent ($8.5 million). In addition, renewal of the Emergency Medical Services levy provided a $2.6 million bump in that slice of property tax. From 2002 to

Chart 5: Property Tax Revenue

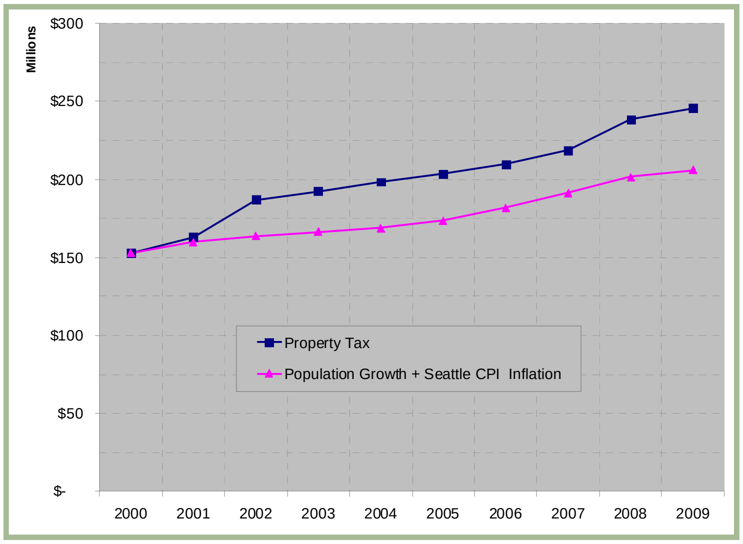


Chart 6: Sales Tax Revenue

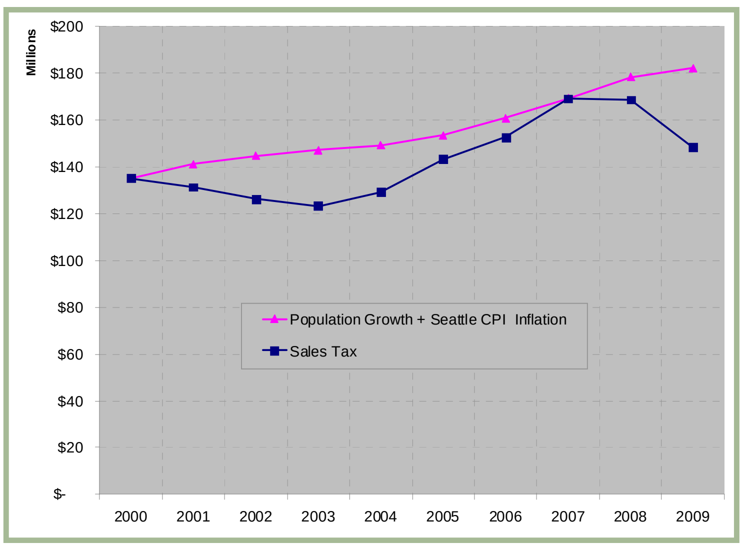
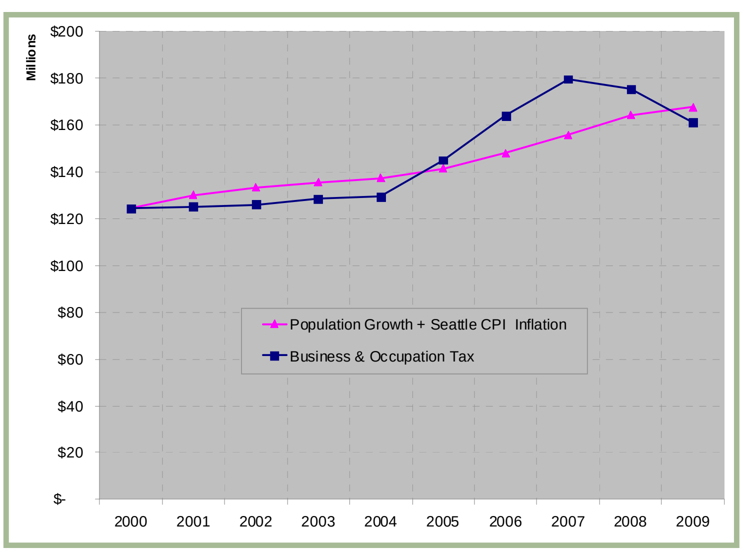


Chart 7: B&O Tax Revenue



2009, with the I-747 limit binding, the annual increase in revenues from the city's regular property tax averaged 3.1 percent.

Overall property tax revenue increased 9.2 percent from 2007 to 2008 with voter approval of a $14.2 million bump up in the Medic One levy. Overall revenue in 2009 was 56 percent greater than in 2000. From 2000 to 2009, the population plus inflation benchmark grew 32 percent.

Sales Tax. City sales tax revenue surged during the late 1990s as a result of the dot-com boom and the resurgence of the downtown retail core. After peaking in 2000, sales tax revenue fell for three years in a row, with a cumulative decline of nearly 9 percent. Revenues finally turned upwards in 2004, with the rate of growth accelerating to 11.3 percent in 2005. In that year, revenues finally surpassed the 2000 level peak. It took until 2007, however, for inflation adjusted per capita sales tax revenue to regain the 2000 level. Sales tax revenue continued to grow through 2008, benefitting from a high level of construction activity. (Construction activity peaked later in Seattle than elsewhere in the state providing 25 percent of Seattle's sales tax revenue during 2008, compared to 21 percent for the state as a whole.)

Sales tax revenue fell 12 percent in 2009, at which point it was 10 percent greater than in 2000.

B&O Tax. B&O tax revenue grew by 23.6 percent during the boom years from 1997 to 2000. The subsequent recession greatly slowed the growth in B&O revenue, from 2000 to 2004 it grew by only 4.0 percent. But unlike the sales tax, B&O revenues did not decline during the recession. The years 2005, 2006 and 2007 were stunning, with B&O revenue up by $50.1 million (38.7 percent). Construction and manufacturing were particularly strong.

B&O receipts dropped 2 percent in 2008 and 8 percent in 2009, so that 2009 revenue was $18.5 million less than 2007. B&O revenue in 2009 was 29 percent greater than in 2000.

Utility Taxes. As noted above, the city collects utility tax on a number of different activities. Between 2000 and 2009, the city's utility tax revenues increased by $65.8 million, 65.3 percent. This growth was concentrated in four years: 2001, 2005, 2006, and 2009.

Between 2000 and 2001, utility tax revenues grew by $12.6 million (12.5 percent). Much of this growth was due to taxes on City Light (which grew from $23.3 million to $29.4 million), telephones (from $32.5 million to $35.8 million) and natural gas (from $6.9 million to $9.7 million). The growth in City Light tax rev-

Chart 8: Utility Tax Revenue

Chart 9: Specific Utility Tax Growth, 2000 to 2009

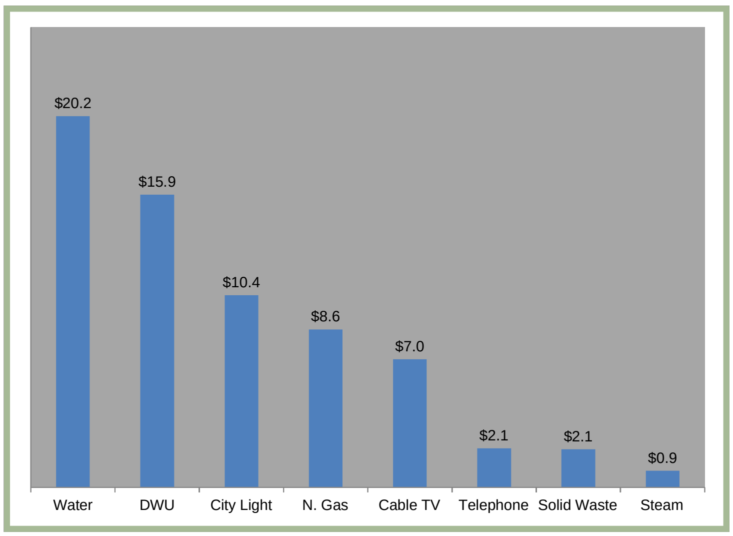


Table 1: Major Seattle Tax Rates, 2010

Property Taxes *($ per $1,000 of Assessed Value)*		**Utility Taxes**	
General Property Tax	$1.78	City Light	6.00%
Emergency Medical Services	$0.30	Water	19.87%
Families & Education	$0.14	Drainage	11.50%
Parks and Open Space	$0.20	Wastewater	12.00%
Low Income Housing	$0.17	Solid Waste	11.50%
Fire Facilities	$0.09	Cable TV	10.00%
Transportation	$0.31	Telephone	6.00%
Pike Place Market	$0.10	Natural Gas	6.00%
City Excess GO Bond	$0.14	Steam	6.00%
Business and Occupation Tax		**Retail Sales and Use Tax**	0.85%
Retail/Wholesale	0.215%		
Manufacturing/Extracting	0.215%	**Admissions tax**	5.00%
Printing/Publishing	0.215%		
Service, other	0.415%	**Parking Tax**	10.00%

enues stemmed from the electricity rate increases that accompanied the western electricity crisis. Similarly, the growth in natural gas tax revenues stemmed from the spike in natural gas prices that accompanied the electricity crisis.

Between 2004 and 2006 utility tax revenues grew by $24.6 million (20.8 percent). In this period taxes on the city's water utility and its drainage and wastewater utility (DWU) accounted for over half of the rise. In 2005 the city raised the utility tax rates on water, drainage, wastewater and solid waste.

Between 2008 and 2009, revenues rose by $16.2 million. Again, much of the revenue increase come from water and DWU, where tax revenues were up 42 and 12 percent, respectively. The large increase for water was the product of both an increase in the rates charged to customers by the utility and a temporary increase in the utility tax rate from 15.54 percent to 19.87 percent.

Chart 9 shows the revenue increase from 2000 to 2009 for each of the utility taxes. Taxes on the city's water utility (up $20.2 million, 293 percent) and DWU ($15.9 million, 123 percent) contributed more than one-half of the $65.8 million increase over the period. Over the period, the tax rate on water went from went from 10 percent to 19.87 percent. The tax rate on wastewater went from 10 percent to 12 percent and the tax rates on drainage and solid waste went from 10 percent to 11.5 percent.

TAX RATES

The table below shows the current tax rates for the city's major taxes. Most of these taxes have been discussed earlier, as the proceeds are deposited to the general subfund. The exceptions to this are property taxes other that the general property tax, the EMS property tax and the parking tax.

All together, the rates on the city's these non general subfund property taxes totaled $1.14 per $1,000 of assessed value, which is 36 percent of total property tax that the city receives. The largest of these property taxes is the one for transportation, which was imposed as part of the funding for the Bridging the Gap transportation program.

The other major tax not dedicated to the general subfund, the parking tax, was also introduced as part of the Bridging

Table 2: Taxes imposed in Seattle by Other Local Governments

Local Sales Tax Rates Levied in Seattle ,2010	
City of Seattle	0.85%
Criminal Justice Levy	0.10%
King County General	0.15%
King County Mental Health	0.10%
King County Metro	0.90%
Sound Transit	0.90%
Total	3.00%

Local Property Tax Rates Levied in Seattle, 2010	
City of Seattle, GSF	$1.78
City of Seattle, Other	$1.14
Emergency Medical Services	$0.30
King County*	$1.39
Port of Seattle	$0.22
Seattle School District	$1.98
Total	$6.82

*Includes Flood and Ferry Levies

the Gap Program. The City Council recently voted to increase the rate on this tax from 10 percent to 12.5 percent, beginning January 1, 2011. Mayor McGinn has proposed to add another 5 percent to the tax.

As Table 2 shows, other local governments impose sale and property taxes within Seattle's city limits.

The overall sales tax rate in the city is 9.5 percent (10 percent for restaurant meals). Of this 6.5 percent goes to the state, while the remaining 3 percent goes to local governments. The city takes 0.85 percent the local tax directly and also gets a share of the 0.1 percent criminal justice levy. The county fund gets 0.15 percent for its general fund, 0.1 percent for mental health programs, and 0.9 percent for the Metro bus system. Sound Transit gets 0.9 percent. All together, these jurisdictions will get about $323 million in sales tax from transactions in Seattle in 2010.

For most of the city, the overall property tax rate for 2010 is $9.04 per $1,000 of assessed value. The state takes $2.22 of this. The city, as it happens, also takes $2.22. Of the remainder, the Seattle School district takes $1.98, King County takes $1.39 and the Port of Seattle takes $0.22. These local jurisdictions will get about $430 million in property taxes from property in Seattle this year.

Discussion

As we said earlier, Seattle's overall revenue collections have held up remarkably well during the Great Recession, especially in comparison with the state of Washington. The two city taxes that are most sensitive to the level of economic activity (sales and B&O taxes) account for less than 36 percent of city General Subfund Revenue. The stable property and utility taxes account for more than 47 percent.

City revenue grew 27 percent from 2004 to 2008 and has been essentially flat since then. Modest growth is forecasted in 2011 and 2012. Inflation adjusted per capita city revenues for 2012 are expected to be 8 percent greater than those for 2000, which was the peak year of the dot-com boom.

As we have previously noted, the city faces stiff competition for jobs from suburban cities, which tax businesses less heavily than Seattle does (WRC 2007, 2009). City Council must strive to write a 2011–2012 budget that does not does not increase the costs providing jobs, commuting to work or driving to stores in the city.

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