Special Report

Washington Research Council June 22, 1999

With New Cities, New Concerns for Business

Introduction

An unintended – if not unanticipated – consequence of the state's nine-year old Growth Management Act (GMA) has been a spate of new incorporations in the Puget Sound region. These new cities, formed within the GMA-established urban growth area (UGA) have increased the number of political and administrative players in the region. And they have created the potential for increases in the cost and reach of government.

Briefly

Formation of new municipalities creates additional concerns for businesses, particularly firms operating in several jurisdictions or involved in regional and statewide affairs.

"Financially fragile" cities – those relying to an extraordinary extent on state revenues – could see those revenues shrink over time, forcing service reductions or major tax increases.

With more cities, intergovernmental disputes are apt to increase, decision-making will be further fragmented, and solutions to regional problems may be delayed.

County government faces the loss of significant tax bases and will be forced to rely more heavily on intergovernmental service contracts.

Civic and business leaders must be involved in defining the new governance structures in Pierce County that will assure a positive business climate in an increasingly urban county challenged by emerging cities and regional infrastructure requirements.

The emergence of new cities and the likelihood of further incorporation initiatives has generated concern among some members of the Pierce County business community who question the impact of new cities on the business climate and on regional governance. Their particular interests included the effect of new cities on infrastructure financing, regional cooperation, and the cost of government.

For the Tacoma-Pierce County Chamber of Commerce, the Washington Research Council has conducted an initial exploration of these issues, interviewing regional leaders in business and government and reviewing relevant planning and fiscal reports. (The Council did not attempt to evaluate the efficiency or effectiveness of the new cities, of Tacoma or of Pierce County government.) Based on this review, the Research Council believes the business community's concerns are justified.

The Council's general conclusions and observations are presented at the end of this report. Briefly, they can be stated as follows:

- ❑ Additional incorporations are likely to increase the cost of government within Pierce County.
- ❑ Pierce County government will face increasing challenges as a result of new incorporations and annexations.
- ❑ Fragmented decision-making, reduced revenues for infrastructure investment, and potentially higher costs will eventually hurt the business climate in the county.

New cities form in response to growth management.

Of the twelve new cities (Sammamish in King County will make it thirteen this August) created in the four-county Central Puget Sound Region this decade, three are in Pierce County and nine in King County. "The new incorporations during this decade represent the fourth largest number of incorporations by decade since statehood. Only between 1890-1900, 1900-1910, and 1950-60 were more new cities formed."[1]

Under GMA, urban areas seem destined to become cities,[2] either through incorporation or annexation. As Mary McCumber, executive director of the Puget Sound Regional Council, observes, the GMA does not indicate a preference for annexation over incorporation. This, she believes, is a shortcoming of the Act. "I personally think there should be a preference for annexation," she says.[3]

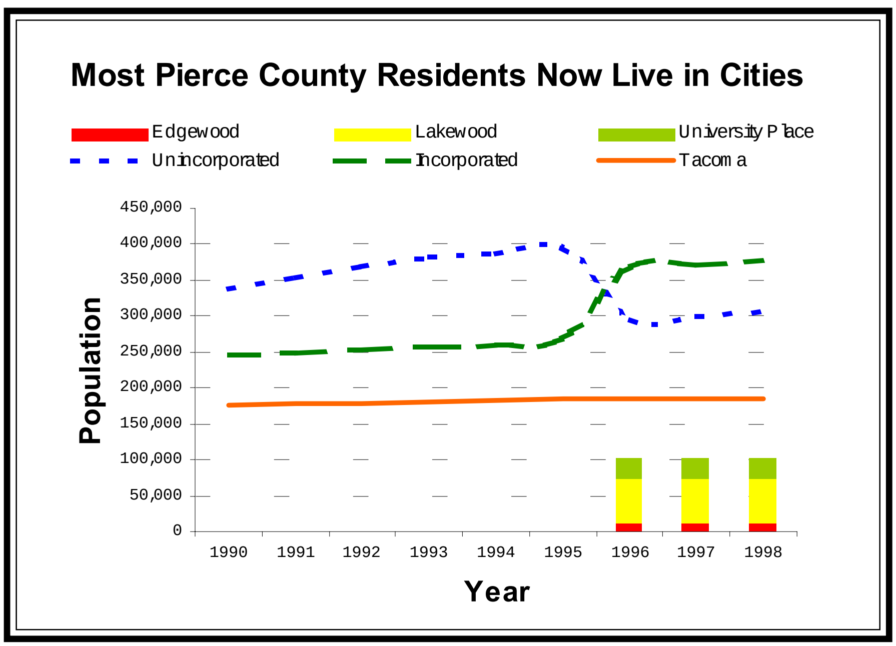
According to the PSRC, "King County has adopted countywide planning policies that call for incorporation of the entire UGA into cities over the 20-year comprehensive planning period. Snohomish County calls for 'orderly transition of unincorporated to incorporated.'"

Pierce County has no plan to encourage either incorporations or annexations. Incorporation is neither inevitable nor essential for communities in the Pierce County UGA, says county executive Doug Sutherland,[4] who believes that the county can provide all necessary services.

Most Pierce County residents now live in cities.

The three new cities in Pierce County – Edgewood, Lakewood, and University Place – comprise 103,000 people (about 15% of the county's population) and $4.8 billion in assessed valuation. Fundamental to the decision to incorporate was a desire to control land use and to manage growth.[5] Incorporation also offered certain financial advantages, in particular eligibility for state funds and avoidance of the local B&O tax that would be imposed were an area annexed to Tacoma.

FIGURE 1



In 1995, prior to the recent incorporations, 57 percent of the county's assessed valuation (AV) could be found in unincorporated Pierce County where 60 percent of the county's population lived. By 1998, the total population of Pierce County was 687,000, with 45 percent living in unincorporated areas. The total assessed valuation of the county was $33.8 billion, 42 percent in unincorporated areas.

Lakewood and University Place were likely candidates for incorporation or annexation before passage of the GMA. Both were urban without being cities. With 62,500 people, Lakewood is now Pierce County's second largest city and one of the larger municipalities in the state. University Place is a well-established, primarily residential, community with an independent identity. Edgewood, on the other hand, describes itself as "a residential neighborhood, rural in character, for persons employed in Seattle, Bellevue, Tacoma and Olympia."

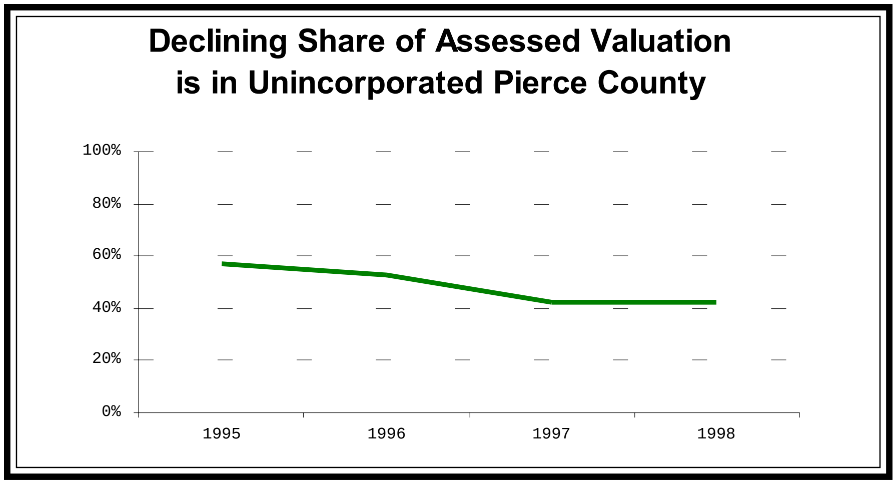


FIGURE 2

Although the three cities are still relatively new – University Place incorporated in August 1995, Lakewood and Edgewood in February 1996 – they provide some clues as to the effect of new incorporations on the business climate and on regional governance in Pierce County. The implications of new city development in the county will be discussed in three parts: local and multi-jurisdictional considerations affecting regional development and the business climate, the economic viability of new cities, and the effect of a declining revenue base on county government.

More Cities, More Decision-makers

As the number of cities in the region grows, more decision-makers are involved in the process of developing and coordinating solutions to regional problems. When the issues involve major infrastructure, resolution can become laborious and expensive, adversely affecting the regional business climate.

Infrastructure concerns - transportation, surface water management and sewer - dominate business discussions of the effect of the new incorporations. Business leaders often express frustration with the slow pace of governmental decision making. They believe the emergence of new cities will further fragment decision-making authority and accountability. With fragmentation comes delay and uncertainty. The DuPont sewer example, discussed below, frequently arises in this context.

Given the emergence of salmon recovery efforts and the demand for new and improved highways, small cities may impede the development of regional solutions.

The following examples serve to illustrate the issues involved. The first, the DuPont sewer project, shows how intergovernmental squabbles can negatively impact the business climate. In contrast, the development of the Boeing plant at Frederickson shows the advantages a large jurisdiction can bring to bear, as county government was able to expedite a major industrial development

Intergovernmental disputes impede development.

"What can go wrong will go wrong." It's an old expression. With respect to intergovernmental agreements, the point is valid. The more opportunities that there are for a decision to be delayed, for disputes to arise, the lengthier will be the process.

Pierce County's executive director of administration, Patrick Kenney, acknowledges that now, with the new incorporations, major land-use planning and capital improvements are "probably more complicated than before. Roads and sewers come to mind."

The example most frequently cited is the DuPont sewer project. John Trent, Pierce County Public Works director, says. "We are absolutely at loggerheads with Lakewood on this issue."[12]

Six years ago, the county signed an agreement with the City of DuPont to provide sewer service to the Weyerhaeuser property that the city was annexing. The county's intent was to run a sewer line north from DuPont to the sewage treatment plant at Chambers Creek, Trent says. That was before Lakewood incorporated.

By the time an early challenge to the project had been cleared up, the City of Lakewood had formed. The county did an environmental impact study. Lakewood contributed comments. The EIS was finished and approved.

But when the county asked Lakewood for a permit to do sewer-line work on the city's streets, the city demanded the county obtain a franchise to operate the sewer line and pay mitigation costs of about $3 million.

Trent says Lakewood wants 8 percent of the gross revenue of the sewer service charge on Lakewood residents. But the city does not want its residents to pay it. "They wanted everyone else to pay it," he said. Trent believes insistence on a franchise is illegal. "Lakewood is a difficult organization to deal with," Trent said.

For his part, Scott Rholfs agrees that Lakewood has had "a lot of difficulties with the county. There's no two ways about that."

Trent says the city could impose a utility tax, but it would show up as a city tax, and Lakewood residents would have to pay it. The courts will resolve the matter.

This example might appear to be unique. As likely, it could be a harbinger of things to come. While Trent and Rholfs agree that the relationship between Lakewood and Pierce County government is good in other areas, like the road maintenance contract, with regard to the sewer project the issues are different and relations are strained.

Service contracts are relatively straightforward, routine business transactions. For services previously provided by county government, contractual agreements should be easily negotiated, as they generally have been with the new cities.

When large infrastructure projects are involved, however, the issues are complex and the payoffs great. Major revenues are at stake in the sewer dispute.

Large projects confer large benefits. The allocation of those benefits among government jurisdictions provides ample fodder for disagreement. As those disagreements are resolved, patterns and precedents may be established, albeit inadvertently. Governments – like businesses – learn from one another. If one jurisdiction succeeds in recovering mitigation costs, for example, other jurisdictions are apt to follow suit. Such attempts will become more common, as will the wrangling associated with the effort.

Fast track development is a county strength.

Regional planning and infrastructure development require cooperation from all affected parties. Within the unincorporated area, Pierce County government has the ability to move with relative speed. That ability, a plus for the business climate, diminishes as the unincorporated area within the county shrinks.

According to Brian Winslow, a planner with The Boeing Company, the Frederickson site was developed for three reasons. First, it was in an unincorporated area. Second, Canyon Road, the only major north-south highway from the site to SR 512, provided effective transportation. Third, it was the last large parcel of land available.

Most important to this analysis, however, is the ability of the county to "fast track" the new plant. "Fast-track" means the plant would be designed and built simultaneously. Permitting departments would not get the entire design all at once. For instance, Boeing would submit the foundation design first, and permitters would not yet know what the company planned to build on top.

The county was willing to go along with Boeing, but lacked the staff to support the effort. So Boeing paid for a new staff member, who worked exclusively on the company's project.

Given the size of the new plant, occasionally it was difficult to build exactly according to code. But Boeing figured it could meet the intent of the code, so it submitted proposals to the county for their approval. The county then decided whether the proposals were satisfactory and gave or withheld its approval.

"From our experience in the Puget Sound region, this could not have happened if the county had been a city," Winslow said. "Most smaller cities are uncomfortable with fast-tracking, and are not geared up for it."[11]

Winslow emphasized that this is especially true of the smaller jurisdictions. For want of experience and manpower, they would be hard-pressed to work out innovative permit processes. So construction of big projects would take longer.

Since the Frederickson project, Winslow noted, Boeing has been able to work cooperatively with officials from smaller jurisdictions involved in the Washington Association of Building Officials. Through these efforts, progress on such matters as "fast track" permitting is being made.

Although Winslow's comments apply most directly to the challenge of working with a small city, they are even more applicable to the difficulties facing businesses concerned with regional infrastructure projects, projects that necessarily involve several jurisdictions.

Mary McCumber believes the provisions of the Growth Management Act and the requirements for regional transportation planning serve to keep local officials working together. Doug Sutherland assigns more of the credit for collaborative planning to the carrot represented by federal transportation funding. Clearly, there are incentives, including the wishes of their respective constituents, to keep local officials working together. But there are also instances in which intergovernmental disputes can delay action and inhibit cooperation.

Jurisdictional disputes damage the business climate.

Such disputes unquestionably work to the detriment of the regional business climate. David Fisher, Intel manger, perceives the issue as political. He believes Lakewood used the sewer pipe that was to serve to serve Northwest Landing as leverage on other issues. And he is concerned that as the county is carved up into more jurisdictions, it's increasingly complicated to get anything done.

Erling Mork, head of the Economic Development Board for Tacoma-Pierce County and long-time Tacoma city manager, is a veteran of multi-jurisdictional planning scraps. He recalls it took eleven years to build 19th Street because of the need to coordinate among several jurisdictions – city, county, and state. He notes succinctly, "It doesn't get better the more incorporations you have, it gets worse."[13]

With respect to the DuPont sewer line, he notes, "Intel comes in under one set of conditions. Two years later they're at the mercy of a government that wasn't here when they made their commitment."

He cites the problems with intergovernmental contracts (sometimes cited as solutions to jurisdictional problems) confronted by Diane's Foods, which wanted to build a tortilla plant in Fife. In order to build, the company needed a letter from Pierce County indicating Diane's could hook up its plant to a Pierce County sewer line running through Fife. According to Mike Barrett, Diane's director of facilities development, obtaining the necessary approval took three months and the intervention of the Economic Development Board.

As soon as Diane's got the permit, four companies in Fife sued Pierce County because the permit was issued to Diane's ahead of them. Mork believes that because the new cities lack infrastructure they, like Fife, will have to contract for services they cannot provide, opening the door to similar conflicts.

While good contracts can reduce uncertainty, unanticipated situations will arise, affording disputants the opportunity to confound orderly processes, leading to delay and frustration. When the county is the exclusive provider of services in an area, there is less likelihood of intergovernmental disagreement over costs, revenue allocation or priorities. That's one of the strengths of regional service provision, a point underscored by Erling Mork.

It's not the details of the individual hassles that matter, he says. Most important is the impression such disputes give of the region. Business looks for ease of permitting and adequacy of infrastructure. The more common the system, the better it is.

Cities, says Mary McCumber, need to recognize they are a part of regional economic units. The trick is to get "everyone going in the same direction on large projects." She says the ideal might be a combination of cities responsive to their residents but acting in concert with a regional strategy. That, of course, still begs the question of how regional policy can be enforced effectively. When cities form in reaction against county policies (e.g., the siting of commercial or multi-family housing developments), then it's unlikely the new city officials are going to embrace those same county or regional policies after incorporation.

Impact of new cities on local business climate will vary and may be positive.

There will be instances where the regional interest, including the collective interest of business and economic development proponents within the region, will be at odds with the particular interests of local businesses. At times, the new cities may provide specific benefits to local businesses.

Sutherland has been mayor of an older, established city (Tacoma), city manager of a new city (SeaTac), and now serves as the elected head of Pierce County government. He maintains that the business impact of new incorporations will "vary from city to city depending on the personalities of the individuals involved." And the same will, of course, be true of intergovernmental conflicts.

The advantage cities have rests in their ability to focus benefits in a smaller geographical area while having more revenues – own source as well as state – to work with, he observes. That can be, and often is, a significant benefit to the business community locally.

Differences in internal procedures among the cities and the county can frustrate business activity for firms operating in several jurisdictions. Inconsistent regulations, as well as inconsistent application of uniform regulations, can complicate day-to-day transactions. In interviews with business people in the county, such occurrences are occasionally cited. Generally, however, the evidence is anecdotal and the problems are manageable.

Businesses operating primarily in a single jurisdiction may experience little change in their operations from municipal incorporation. Indeed, they may benefit from a more "local" and responsive city government.

Lakewood's new sign ordinance, for example, created a significant initial furor as several thousand illegal signs were removed. Scott Rholfs, Lakewood city manager, says it was the biggest single business issue. According to Rholfs, the county's sign ordinance "did not amount to much" and was not really enforced.[6] Rholfs said the city has reworked its ordinance and "business thinks it's a lot better."

Such initial problems are typical, according to Roland Dewhurst, district manager of Associated General Contractors in Tacoma. "There are hiccups at the start," he says. Overall, however, he says the effect of new cities on the business climate "is not that big a deal." Things like the sign ordinance, while problems at the beginning, "are not real permanent draw-backs."[7]

Even skeptics like Mike Tucci, Sr., of Tucci Construction agrees. Tucci originally opposed incorporation out of concern that it would mean more bureaucracy. And though that concern still lingers, he says, "generally, I'm not unhappy with incorporation."[8] Echoing some of the sentiments of new city boosters, he says that smaller cities have a lot of good things going for them – identity, beauty, local committees. Tucci said he initially had some trouble getting a permit from the new city to fix up his old asphalt plant and to add a new plant, but ultimately, "we got the permit without much trouble."

Complexity is not a marketing virtue.

From sewer lines to sign ordinances, multiplication of jurisdictions adds complexity to the regional business climate. And complexity is not a marketing virtue. As noted in the Pierce County Strategic Economic Development Action Plan, "The processes for planning, prioritizing, funding, and building infrastructure must be predictable and accomplished in partnership with jurisdictions around the county." As well, the Action Plan called for "consistent guidelines and regulations for permitting and to set consistent development standards."[14]

More simply, business wants certainty. New cities increase uncer-tainty.

To minimize the problem, the Pierce County business community may be well served by embracing the bias toward annexation that the legislature failed to place in the Growth Management Act. Either annexation or incorporation of new cities will shrink the county revenue base – and annexation may result in a loss of the intergovernmental service contracts that the new cities have generally signed with the county (see below). Nonetheless, annexation will permit cities to take advantage of some economies of scale, particularly with respect to major facilities development and maintenance, and not add to the number of governmental actors involved in regional affairs.

Transportation funding may be jeopardized by new cities, hurting regional mobility.

There is also a transportation infrastructure argument against new incorporations. The formation of new cities has a direct, negative, financial impact on available funding, as stated in the Puget Sound Regional Council's (PSRC) discussion of the issue. A recent PSRC analysis points out that "the major transportation-related revenue source for cities is the local share of the state gas tax…. An interesting feature of the portion of the cities' share (that is passed on directly) is that it is fixed – the more cities there are, the less each one gets."[9] (As will be shown later, similar factors affect another major source of new city revenues, the sales tax equalization pool.)

Further, it notes that the counties' share is also fixed by formula. "… as county population and road miles get absorbed into newly-formed and annexing cities, the funding that used to support them does not go to these cities but is reallocated to other, less urbanized counties elsewhere in the state."[10]

As well, the incorporation of an area, whether by annexation or incorporation, reduces the assessed valuation subject to the county road levy. The city gains taxing authority for general government, but the dedication for transportation purposes is lost. While currently much of the revenue continues to be spent for transportation maintenance as the new cities contract with Pierce County government, continuation of those contracts could be jeopardized by changes in the financial health of the new cities, as will be discussed in the next section.

Financially Fragile Cities

Established cities often have higher taxes and fees than unincorporated places. They have greater taxing authority, principally in their ability to levy B&O and utility taxes. As well, the cost of providing an urban level of services will often be more expensive than that identified with the lower service levels associated with rural living (although, to be sure, communities within the UGA are, by definition, not rural).

The GMA-sparked wave of incorporations, while largely to control growth and development, also represents a choice not to be annexed to an established city. The new cities have a financial incentive to incorporate. Revenue distributions from the state are generous to communities with limited sales tax revenues. And incorporation allows the cities to avoid annexation to an established city with higher business and property taxes. This observation was made by several local business people in University Place with respect to the relative advantage of incorporation over annexation to Tacoma.

Gary Lowe, Executive Director, Washington Association of Counties, predicts Washington will experience a "spread of inappropriate cities across the map of urban counties. It's going to be LA County all over again."

At the same time, he doubts it will damage the business climate. "I don't think it's going to be bad for the private economy. They're going to compete for investment."

For the most part, new cities do not emerge in reaction against commercial development. More often, the impetus is the desire to avoid residential development, particularly, large, multi-family

New Cities in Pierce County Lead State in Receiving Sales Tax Equalization Money

	CITY	1999	1998	1997	1996	1995
1	Lakewood	3,045,010	3,360,790	3,099,635	3,046,639	N/A
2	University Place	2,255,697	2,250,496	2,135,044	2,188,956	N/A
3	Des Moines	1,863,691	1,947,744	1,502,831	1,296,267	1,539,485
4	Shoreline	1,660,835	1,842,543	1,930,315	2,065,262	N/A
5	Mountlake Terrace	1,259,997	1,237,996	1,087,954	1,082,698	1,366,992
6	Lake Forest Park	1,091,335	1,065,266	983,969	440,752	194,162
7	Richland	998,693	806,001	594,368	269,989	45,493
8	Edgewood	965,636	971,520	898,443	715,710	N/A
9	Mercer Island	926,135	894,354	966,245	857,539	1,107,887
10	Pullman	733,563	634,721	584,823	635,843	923,739
	Top 10	14,800,592	15,011,430	13,783,628	12,599,655	5,177,758
	ALL CITIES	35,034,443	32,486,056	30,178,370	28,083,998	26,261,929

FIGURE 3

Sales Tax Equalization Money Still Represents One-fifth of University Place Revenues

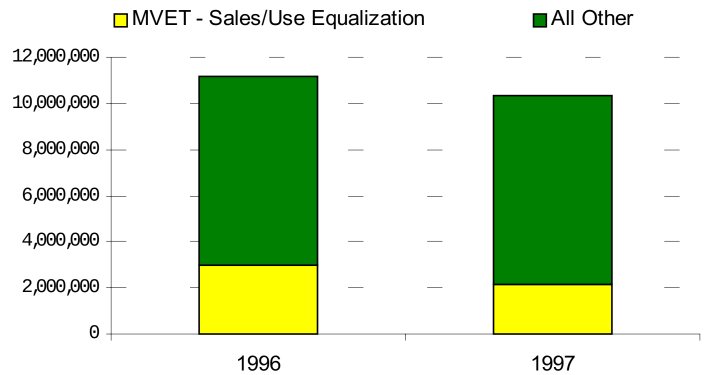


FIGURE 4

Edgewood Gets 30% of Its Revenues from the Sales Tax Equalization Pool

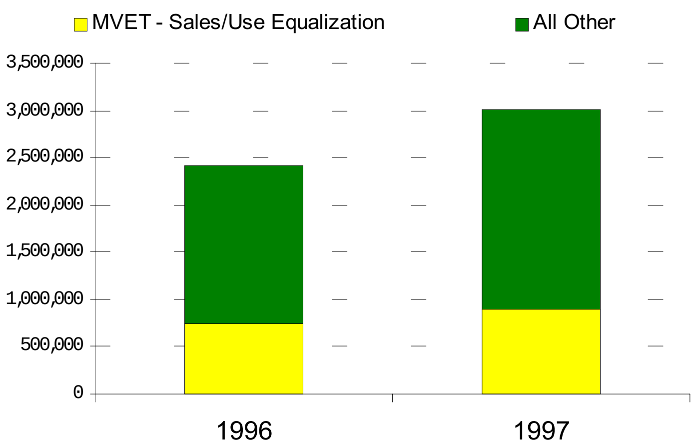


FIGURE 5

Fifteen Percent of Lakewood Revenues Come from the Equalization Pool

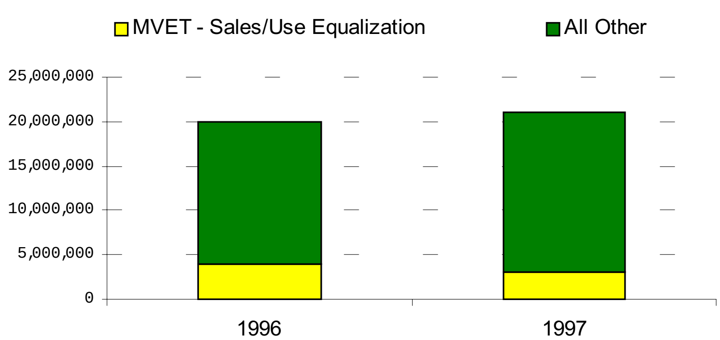


FIGURE 6

housing complexes. These communities want to avoid additional traffic congestion and population density.

Some of the new "rural cities," however, have made it clear that they intend to exercise strict control over the development in their communities. And because they can tap the sales tax equalization pool, they are somewhat insulated from the need to generate commercial investment to support municipal operations.

Excessive reliance on "imported dollars" signals potential problems for new cities.

Sales tax equalization funds. What makes a city "inappropriate"? The criteria vary – area, population, geography, ability to be self-sustaining are generally cited – depending on whom you ask. But a key benchmark seems to be financial viability.

And here, many new cities, including Lakewood, University Place, and Edgewood, might be considered "financially fragile" except for the significant subsidy provided by state government, the sales tax equalization fund, which provides a perverse incentive for communities to incorporate. This provision of Washington State Law, adopted in 1982 in part as a response to the loss of federal revenue sharing and rampant inflation, distributes money to cities with per capita sales tax revenues falling below 70 per cent of the statewide average per capita sales tax collections for cities.

The account is funded by the Motor Vehicle Excise Tax (MVET). In essence, cities with relatively low sales tax collections – a consequence of limited retail activity in the cities – receive a revenue bonus from the state. As the following table shows, the three new cities in Pierce County are among the top ten cities in the state in receiving sales tax equalization funds. Shoreline, also in the top ten, is also a new city, incorporated in 1995.

The Pierce County new cities rely to a significant degree on these funds. For Edgewood, equalization dollars represent thirty percent of the operating budget; University Place, about twenty percent; and, Lakewood, fifteen percent. Annexation to a more populous city with healthy retail sales, of course, would not draw substantial equalization money to the city.

If equalization dollars shrink, new taxes likely or services may be cut.

Clearly, without this subsidy, the three cities would face significant revenue shortfalls. Costs would have to be reduced or local revenues increased.

Equalization Funds for Pierce County Cities

CITY	1999	1998	1997	1996	1995
Lakewood	3,045,010	3,360,790	3,099,635	3,046,639	N/A
University Place	2,255,697	2,250,496	2,135,044	2,188,956	N/A
Edgewood	965,636	971,520	898,443	715,710	N/A
Fircrest	463,738	458,467	416,433	397,204	489,828
Steilacoom	452,767	523,590	437,876	403,112	405,497
Bonney Lake	282,192	277,535	313,049	351,228	420,386
Orting	207,427	191,726	153,952	111,738	110,799
Buckley	158,707	181,802	129,074	180,180	207,406
Ruston	65,773	61,599	55,565	36,486	30,900
Carbonado	55,933	58,862	53,741	52,504	50,207
South Prairie	36,739	41,320	34,769	34,581	28,668
Wilkeson	32,382	33,920	25,479	26,068	30,605
Du Pont	0	0	0	0	751
Eatonville	0	0	0	0	1,997
Fife	0	0	0	0	5,675
Gig Harbor	0	0	0	0	4,789
Puyallup	0	0	0	0	34,258
Roy	0	0	0	0	437
Sumner	0	0	0	0	9,816
Tacoma	0	0	0	0	234,719

FIGURE 7

The reliance on this funding source raises two important issues of concern: 1) the stability of the pool and 2) the security of the funding source. First, as stated in The New City Guide: "Groups contemplating incorporation should note that as more cities incorporate, the per capita distributions will grow more slowly than they have in the past, or actually decline, depending on the relation between the growth in the funding source and the growth in population in incorporated areas. The effect of incorporations on the distribution of the sales and use tax equalization funds is particularly severe."[15]

The point is reinforced in the City of Lakewood budget for 1999. "The more there are '**NEW**' cities, the less the pot for distribution."[16] (Emphasis in the original.) And, the distribution is a zero-sum game. If Lakewood were to succeed in having population from a military base annexed for the purposes of calculating distributions of shared revenues, the city's gain would reduce the pool for other communities.

Referendum 49, approved in November 1998, increased the MVET for equalization by about $4 million a year. Nonetheless, new city incorporations may over time place significant pressure on the program.

The second issue is perhaps of greater concern. The future of the MVET is not secure. Referendum 49 reduced the tax slightly, but there remains significant grassroots political opposition to Washington's relatively high motor vehicle excise tax. Two campaigns are currently attempting to

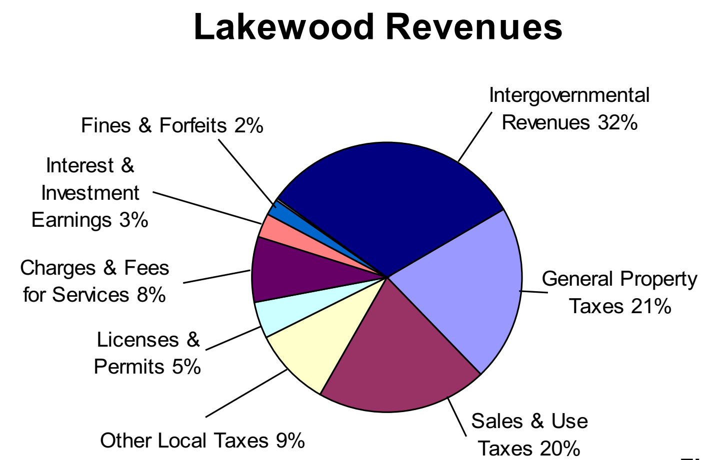


FIGURE 8

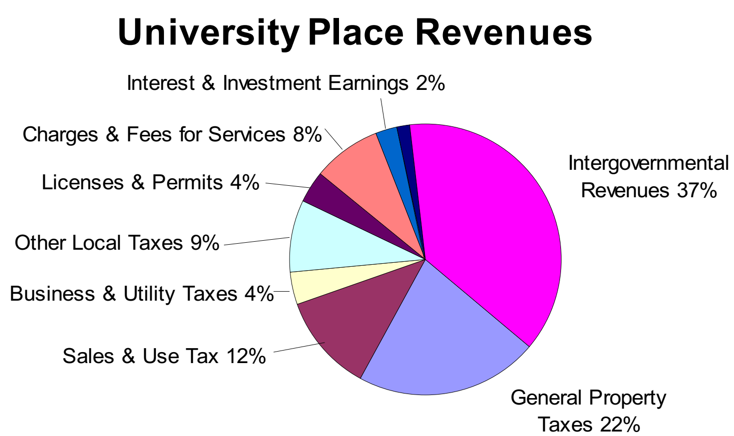


FIGURE 9

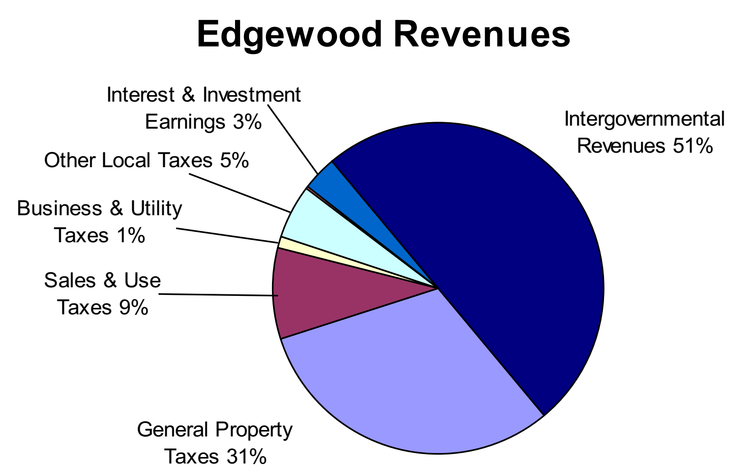


FIGURE 10

gain signatures to place on the 1999 ballot initiatives that would eliminate or radically reduce the tax. Should that occur, those cities relying on the funds for operations would face either severe program reductions or find themselves proposing major tax and fee increases.

The three new cities are not the only Pierce County communities relying on sales tax equalization money, although their reliance is greatest. Before 1996, that is before the incorporation of several new cities, money in the pool was distributed on a per capita basis to all cities in the state after each eligible city was brought up to the 70% level. There has been no excess to distribute since 1995.

Property Taxes. Cities and counties in Washington rely heavily on property tax revenues. The primary levies for county government are the general levy, which is applied countywide, to property in both incorporated and unincorporated areas, and the county road levy, applied only in the unincorporated area.

For general county purposes, counties may levy up to $1.80 per $1,000 of assessed valuation (AV); for Pierce County, the regular county levy rate for 1999 is about $1.65 per $1,000 AV.

For county roads, they may levy $2.25 per $1,000 AV. For 1999, Pierce County is levying the maximum, which includes $0.44 per $1,000 AV for the law enforcement levy, collected only from the unincorporated area.

When a city incorporates, its taxpayers no longer pay the county taxes levied exclusively in unincorporated areas. Cities, generally, are able to levy a maximum of $3.60 per $1,000 AV.

Cities and towns belonging to fire districts or library districts cede to those special districts a share of their statutory $3.60 levy rate. The maximum regular levy rate that can be levied by a fire district is $1.50; by a library district, $0.50. Each of the three new cities belongs to both fire and library districts and therefore has a balance of $1.60 available. Lakewood and University Place are levying a regular property tax rate of $1.58. Because the fire district for Edgewood is levying below the maximum ($1.255 rather than $1.50) Edgewood is able to exceed the $1.60 rate and it has chosen to levy $1.834.

The revenue distributions for each of the three cities are shown in Figures 8, 9 and 10.

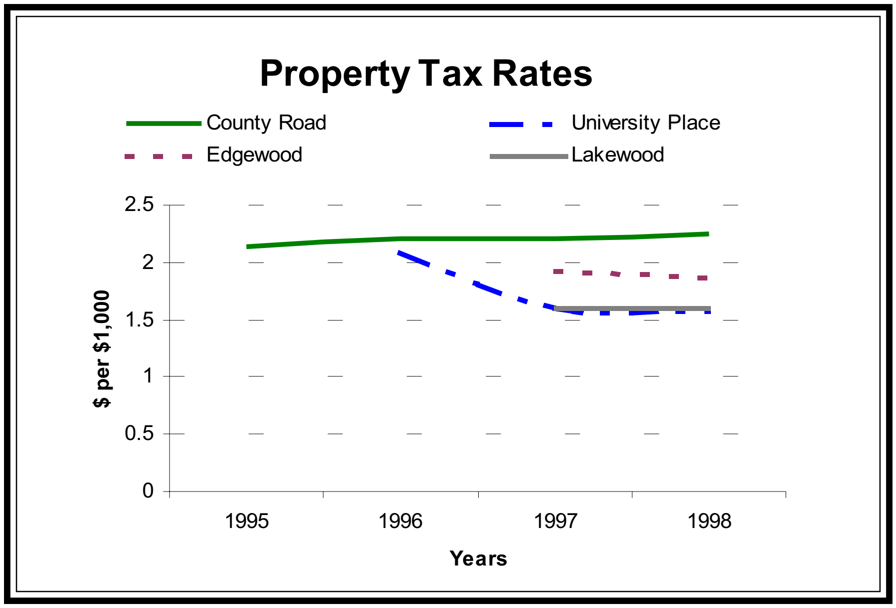


FIGURE 11

The comparison between property tax burdens before and after incorporation can best be seen by looking at the relationship between the county road levy and the regular property tax levy of the new cities. That's the comparison emphasized in the budget documents for University Place and Lakewood, and a comparison that is favorable for the new cities (see Figure 11). Each of the new cities is levying a property tax well below the county road tax rate of $2.25. The new cities are contracting with Pierce County for road maintenance and the overall investment in transportation infrastructure does not appear to have been affected.

Retail Sales & Use Taxes. Cities and counties may also impose a local sales and use tax. Essentially, they share a 1.0% tax, technically levied as two 0.5% shares. Pierce County, along with thirty-four other counties in the state, levies the tax countywide. Cities can, and nearly always do, levy the two 0.5% shares as well. Because the county levies a sales tax, the municipal sales tax does not represent an additional tax burden in the new cities. It's simply a shift from the county treasury to the city.

Cities retain about 84% of the local sales taxes collected within their jurisdictions. The county gets about 15% and the state takes a 1% administrative fee.

For 1999 Lakewood estimates collections of $3.6 million, University Place, $925,000 and Edgewood $182,000. These collections, then, represent a shift from Pierce County to the cities of about $4.7 million.

Other Revenue. No one interviewed by the Washington Research Council cited objections to current license and permit fees, although there were concerns that such fees may increase in the future. The new cities are roughly comparable in the share of revenues received from these sources, and none collects a local B&O tax.

Scott Rholfs acknowledges that Lakewood has increased development standards, resulting in higher costs. The city requires infrastructure – curbs, gutters, sidewalks and, sometimes, street lights and underground utilities – with development. And Lakewood has tightened zoning, restricting multi-family complexes in single-family neighborhoods. City Manager Robert Jean points to the University Place comprehensive plan, which “largely validates existing uses.”

Other Concerns. What cannot be readily determined at this time is the potential for financial problems in the future. When the Boundary Review Board considers incorporations, the attention is focused on operations and maintenance. Capital budget items are not scrutinized. As older communities incorporate, they acquire some aging infrastructure. To the extent that maintenance and replacement costs fall to them, these costs can represent a significant burden, particularly on communities with limited financial resources and narrow tax bases.

Pierce County government faces new challenges.

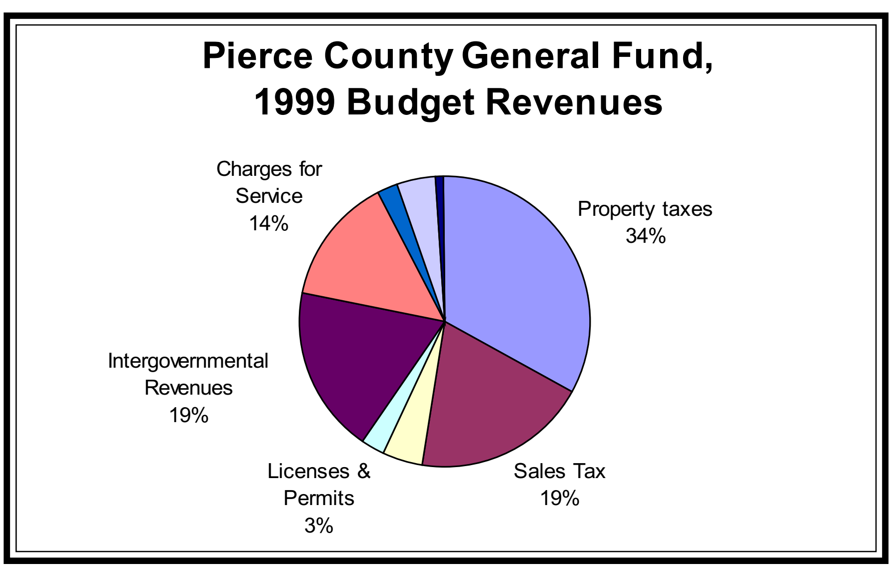
Historically, counties were discouraged from extending urban services to unincorporated areas. Special purpose districts often formed to provide specific services to unincorporated urban areas. Over time, however, particularly in the fast growing Puget Sound region, counties began to extend services and allow growth outside cities. For so doing, the counties have been criticized for creating the conditions resulting in growth management legislation. The new cities regularly cite the desire to control sprawl, “inappropriate development,” and preserve a sense of community. The county, they believe, failed to protect their interests.

The GMA endorses the goal of having urban services provided by municipalities. Cities, however, do not fully substitute for county governments. Pierce County officials point out that, in addition to serving as a “city government” to the unincorporated area, the county provides a number of unique services countywide, from assessor and auditor to juvenile justice and superior court.

Doug Sutherland says, “There are no services provided by a city that are not provided by a county. There are services provided by a county that are not provided by a city.” As well, economy-of-scale considerations make the county a logical provider of certain services (e.g., road maintenance, law enforcement, sewer, jail) that may be less efficiently delivered by small municipalities. And the county does provide such services under contract to cities in the region.

Lost revenue base will increase financial strain on county government.

FIGURE 12



Incorporations and annexations will increase the fiscal stress on Pierce County government. Property taxes make up about a third of the county general fund, with the sales tax making up nearly one-fifth. Incorporations and annexations directly impact each of these revenue sources, although in somewhat different ways.

As mentioned above, by incorporating, a community not only gains access to the equalization pool and other shared revenues distributed by state government, it also retains about 84% of the local share of sales taxes collected inside the city limits. The sales tax collected by the three new cities, for example, has cost Pierce County about $4.7 million in the 1999 fiscal year.

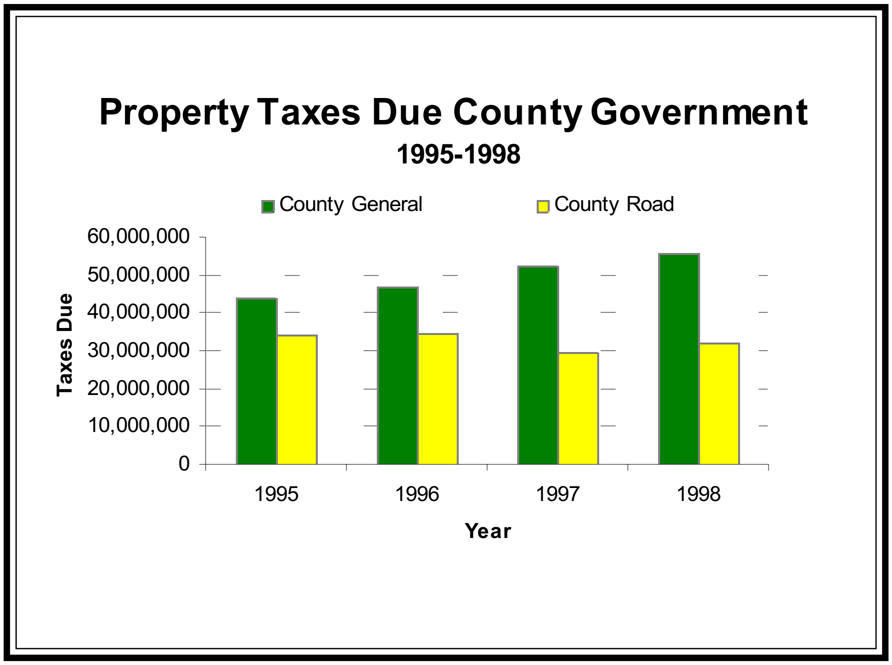


FIGURE 13

While there has been steady economic growth countywide, the assessed valuation in unincorporated Pierce County declined significantly, primarily as a result of the incorporations, with only a slight return in 1998. The loss of nearly $5 billion in AV to the county road fund represents about $10 million annually in tax collections. Figure 13 compares taxes due from the general Pierce County levy (applied countywide) with the county road levy, paid only by owners of property in the unincorporated area. A small illustration: The Law Enforcement Fund, a property tax levy collected only in unincorporated Pierce County, dropped by nearly a million dollars, from $6.62 million in 1995 to $5.66 in 1996, primarily as a result of incorporations. The services it pays for are provided countywide.

Contracts with the new cities have mitigated the impact of the property tax loss. Therefore, the new incorporations have not negatively affected county operations so far, according to Patrick Kenney, executive director of administration for Pierce County. Because the cities contract with the county for such services as roads, sewers, utilities, corrections and sheriff's patrol, the effect has been manageable. With respect to revenue flow, he says, "there's been no major impact on operations."[17]

Francea McNair, deputy county executive, observes, however, that there are services that the new cities now provide that had previously been provided by the county. And in those cases, the county has reduced personnel. Particularly impacted has been the planning office, which has cut back substantially, about 40 people.[18] Ironically, last year saw a substantial increase in permits from the South Hill area, an increase perhaps fueled by the area's potential for incorporation.

Nearly three-fourths of the county general fund budget is allocated to public safety and justice services. Increasing demand for public safety and justice services has limited the county's ability to cut back on internal services (e.g., personnel), according to McNair.

Revenue mismatches and lost economies-of-scale pose problems.

The county faces two potential problems. First, there is a revenue mismatch as the sales tax, traditionally a source of funding for general county purposes, shrinks with no offsetting decline in the responsibility of county government. (Other funds, notably the Law Enforcement Fund, will also represent a continuing mismatch between revenue source and intended use, but the sales tax is most significant.) Second, the economies-of-scale that the county can bring to bear on major operations exist only insofar as it continues to provide services broadly. For example, the planning expertise that allowed expeditious handling of the Frederickson project required a large department accustomed to dealing with major projects.

Doug Sutherland observes that the "only way the county can survive in this process is by contracting for services." And in general, with respect to the financial impact of new cities on county government, Gary Lowe of the counties' association agrees. "As long as contracts remain in place," he says, "it's pretty much a wash."

When money gets tight, though, cities may look first to service contracts as a source of cost reduction. That could increase the pressure on county government, which has fewer revenue options. Pierce County is not yet at its maximum property tax levy rate and is constrained by the provisions of Referendum 47, adopted by the voters in 1997.

To the extent general revenues, primarily the sales tax, stagnate or decline as a result of incorporations and annexations, counties are likely to seek additional revenues. And, as mentioned previously, the replacement of the county road levy with a general city levy inevitably reduces transportation infrastructure development.

New roles for county government imply new governance structure.

Mary McCumber sees the day when counties will need new revenue sources. While the case has yet to be made by local officials, the loss of tax revenues from traditional resources combined with continued demand for county provision of public safety, corrections, juvenile justice and court services creates a potential revenue shortfall. If Sutherland and Lowe are correct, that the key to the county's survival is in contracting for services, then success will be tied to a series of intergovernmental agreements that will be more or less stable depending on the availability of more efficient competitors. As reported earlier, however, intergovernmental agreements can be the source of costly wrangling as well.

The issue is considerably more complex than just rearranging county responsibilities and identifying additional funding sources. The role of county government in urban areas increasingly dominated by incorporated cities is changing. Business leaders have a tremendous stake in helping develop new and responsive structures for local and regional governance.

Conclusions

1. New incorporations heighten the potential for significant increases in the cost of government. Cities have broader revenue-raising powers than counties, primarily because they can levy B&O and utility taxes. Whether from incorporation or annexation, the municipal share of the population and tax base within Pierce County is likely to increase. More residents and businesses will be subject to the greater taxing authority of cities. While state-shared revenues, primarily sales tax equalization funds, have eased significantly the pressure on city government to finance internally the full cost of municipal operations, those funds are unlikely to grow in the future. As new cities continue to form, the pooled revenues will be shared more broadly, reducing the amounts available to existing recipients. As subsidies drop, cities may be expected to seek additional funding from traditional revenue sources, e.g., property taxes, business taxes and fees.
2. Pierce County has experienced revenue loss from the new incorporations. That negative impact, however, has been mitigated by the new cities' pattern of maintaining contracts with the county for specific services, including roads, sewers and law enforcement. In addition, sustained economic activity in the county has contributed to positive revenue growth for county government despite the loss of property and sales tax base. Changes in contractual agreements or an economic downturn will affect the county's ability to maintain services without tax or fee increases, which could have a disproportionate impact on businesses located in unincorporated Pierce County.
3. Infrastructure investment in the region may be negatively affected in two ways. First, the incorporation of new cities in the county has increased the complexity of intergovernmental decision-making. Intergovernmental arguments may delay the development of large public or private projects that span jurisdictional boundaries. The more jurisdictions, the more potential for conflict and protracted negotiation. Second, funding for maintenance and development may be affected by both the loss of revenue to the county road fund and by the redirection of state transportation money.
4. The incorporations of Lakewood and University Place have not created significant new challenges for strictly local businesses operating in those cities. Business representatives express satisfaction with the level of service they are receiving and the costs of doing business remain acceptable. These local businesses may face increased costs, however, when the cities are no longer able to import shared revenues to the extent required to maintain adequate service levels.
5. The business climate may be damaged by a pattern of fragmented decision-making, rising costs and underfunded infrastructure. The region may appear to be an uncertain and "unfriendly" place to do business. Pierce County business and government leaders should begin now to prepare a coordinated response to the pressure for additional incorporation and annexation. The issues involved extend well beyond reshuffling the responsibilities of city and county government. Coordinated systems of intergovernmental agreements may be required.
6. Beyond that, however, is the need to take a fresh look at the local governance structures operating in Pierce County. The emergence of

new cities affects not only Pierce County; all urban counties will ultimately face similar challenges. As well, the multiplication of municipalities will affect Tacoma and other urban centers providing regional commercial, cultural and recreational services. At a minimum, these older cities are losing the ability to add revenue capacity by annexation. Pierce County civic and business leaders can play a critical role in advancing the regional and statewide consideration of the appropriate fiscal and governance structures for local governments in a changing urban landscape.

End Notes

[1] Puget Sound Regional Council, 1998 Regional Review, December 1998, page 52.

[2] "In general, cities are the units of local government most appropriate to provide urban governmental services." RCW 36.70A.110(4)

[3] Interview with Mary McCumber.

[4] Interview with Doug Sutherland.

[5] Lakewood Incorporation Study Part B: City of Lakewood Fiscal Impact Assessment prepared by The Georgette Group; Notice of Intention for Incorporation of the City of Edgewood, Washington.

[6] Interview with Scott Rholfs.

[7] Interview with Roland Dewhurst.

[8] Interview with Mike Tucci, Sr.

[9] "The Effects of the Current Transportation Finance Structure," Transportation Pricing Task Force, Puget Sound Regional Council, March 11, 1999, page 28.

[10] Ibid., page 29.

[11] Interview with Brian Winslow.

[12] Interview with John Trent.

[13] Interview with Erling Mork.

[14] Partnerships for the 21st Century, Pierce County Strategic Economic Development Action Plan, Summary of Recommendations, July 1997, page 5.

[15] The New City Guide, Municipal Research & Services Center of Washington, June 1993 (Revised November 1994), Report No. 25. Page 26.

[16] City of Lakewood, 1999 Budget, page 103.

[17] Interview with Patrick Kenney.

[18] Interview with Francea McNair.