MEMORANDUM

DATE: July 7, 2009

TO: Councilmember Jan Drago, Chair, Transportation Committee

FROM: Dwight Dively, Director of Finance

RE: Effects of Repeal of Employee Hours Tax on Transportation Projects

As you know, Mayor Nickels, Council President Conlin, and Councilmember Burgess recently proposed to repeal the City’s employee hours tax (EHT) effective as of January 1, 2010. The EHT was imposed in 2006 and became effective on July 1, 2007. The EHT is one revenue source for the “Bridging the Gap” (BTG) program, which is also supported by a commercial parking tax (CPT) and a voter-approved property tax levy lid lift.

The Department of Finance (DOF) currently projects the EHT to generate about $4.6 million in 2010, with the amount growing slowly in future years. The total projected EHT revenue for the remaining term of “phase 1” of the BTG program is about $31 million (phase 1 corresponds to the nine-year period of the levy lid lift).

The EHT has produced less revenue than originally expected. Employers are not required to pay the tax for employees who commute using modes other than single occupancy vehicles. There was little reliable information available to calculate the potential effect of this exemption, and its effect appears to be larger than expected. In addition, compliance is always an issue with a new tax and few audits have yet been done that cover the EHT. Finally, the severe economic recession has reduced employment below levels originally anticipated.

The proposal to repeal the EHT is intended to help stimulate Seattle’s job market. The tax is a deterrent to hiring and is complicated for businesses to calculate.

In your June 29 letter to Grace Crunican, you expressed support for repealing the EHT but concern about the effect of the lost revenue on transportation projects during BTG’s phase 1. DOF has analyzed this issue and believes all currently-planned BTG phase 1 projects can be funded. There are at least four reasons for this:

1. Commercial parking taxes have exceeded estimates. The original BTG plan (as described in Resolution 30915) assumed the CPT would generate about $123 million during phase 1. Our most recent estimate is $182 million, even allowing for the effect of the current recession. Most of this higher revenue is due to there being more parking
operators than originally estimated. The additional $59 million over the nine-year period more than offsets the difference between the originally assumed EHT revenue and the actual EHT revenue if the tax were repealed starting in 2010.

2. **Debt service costs have been lower than planned.** The BTG plan assumed that bonds would be issued for several major projects, such as Spokane Street, the Mercer Corridor, King Street Station, and bridge upgrades and rehabilitation. The bonds issued to date have had lower interest rates than originally assumed, resulting in lower debt service. In addition, the original plan had assumed that principal repayments would be structured to match a growing revenue stream, but higher-than-expected revenues have allowed more principal to be paid earlier in the term of the bonds. These effects mean that the City has considerable flexibility to structure future BTG bond issues to match a revenue stream that does not include the EHT. We will still use maximum terms of 20 years or less, which is conservative given that the expected lifespan of most of the improvements is 30 to 50 years.

3. **Construction costs have fallen during the last year.** The recession has resulted in significantly lower bids for many construction projects over the last year. These savings will allow more projects to be funded than originally planned.

4. **Much of the surplus CPT revenue has not been allocated to specific projects.** The 2009 Adopted Budget and the 2009-2014 Adopted CIP did not show full use of the expected revenues from the CPT and EHT. The Mayor and Council have made annual decisions about the use of such funds and have typically devoted them to smaller projects such as paving or sidewalk development.

The combined effects of these four considerations mean that all currently planned projects can be funded even if the EHT is repealed starting in 2010. The current “pay as you go programs” of smaller phase 1 projects can be held harmless. DOF staff have provided a detailed projection of this information to Council Central Staff for their review.

Of course, it is true that more transportation projects could be funded in the future if the EHT were kept in place. However, the challenge for the Mayor and the Council is to balance the benefits of these projects with the adverse effects of the EHT.

The Mayor has not yet proposed specific projects to be budgeted in 2010 and beyond. This will be done through the 2010 Budget and CIP presented to the Council in late September. The SDOT capital budget will also factor in the effects of other funding sources, such as the General Fund, Cumulative Reserve Subfund (real estate excise taxes), grants, and federal recovery funds.

Finally, it is worth noting that BTG has met or exceeded its goals in every category. The Committee will be briefed on this later in today’s meeting.

I hope this information addresses the concerns outlined in your June 29 letter. Please let me know if you have additional questions.

cc: Grace Crunican, Anne Fike-Zuniga, Lenda Crawford, Steve Viney – SDOT
    Cameron Keyes, Steve Barham, Dave Hennes – DOF
    Andrew Glass-Hastings - OPM