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MEMORANDUM

TO: Spokane Transit Authority

FROM: Roy J. Koegen
Jason R. Whiteley

DATE: June 27, 2006

RE: Local Financing Options for Light Rail

Spokane Transit Authority (“STA”), a public transportation benefit area created under chapter 36.57A RCW, is exploring the acquisition and construction of a light rail system. This memorandum addresses the financing mechanisms available to construct such a system (excluding direct state and federal funds) including (i) public benefit transportation area authority to levy taxes and issue bonds under chapter 36.57A RCW, (ii) supplemental authority to construct high capacity transportation systems under chapter 81.104 RCW, (iii) transportation benefit districts under chapter 36.73 RCW, (iv) the transportation authority of cities, towns and counties, (v) other local revenue sources, (vi) port districts, (vii) interlocal cooperation and (viii) IRS 63-20 financings.

1. Public Transportation Benefit Areas (Spokane Transit Authority – RCW 36.57A)

a. *Authority to establish a light rail facility.* STA, as a public transportation benefit area, is authorized to design, construct and operate a light rail system under its general authority to design, construct and operate “transportation facilities.” RCW 36.57A.080, 35.58.2721.

b. *Taxing authority.* Two provisions of the RCW permit STA to levy taxes to pay for the design, construction and operation of transportation facilities. The first—RCW 82.14.045—authorizes STA’s legislative body, with the approval of a majority of the STA electors, to impose a local option excise tax of up to .9 percent (in .1 percent increments). STA currently relies on this authority for its .6 percent excise tax levy so an additional excise tax of up to .3 percent (in .1 percent increments) could be levied with a majority vote of the STA electors.

In lieu of the .9 percent excise tax, STA has the authority to levy (i) an excise tax up to \$1 per month for each housing unit in the benefit area and (ii) a business and occupation tax upon approval of a majority vote of the qualified electors. RCW 82.14.045(2)(c). Since STA has already levied the .6 percent excise tax, it may not levy either of these taxes unless and until the current excise tax is repealed or expires.

c. *Authority to issue bonds and pledge revenues.* As a public transportation benefit area, STA may issue non-voted and voted general obligation bonds. RCW 35.58.2721. Each type of bond may have a term of up to 40 years.

(1) Non-voted general obligation bonds. STA may issue general obligation bonds without a vote of the STA electors if the principal amount of the bonds, when added to STA's other outstanding non-voted indebtedness, does not exceed three-eighths of one percent of the value of taxable property within STA boundaries. Wash. Const. Art. 8, § 6; RCW 35.58.2721(1); RCW 39.36.020(1). Such bonds are commonly referred to as "councilmanic bonds" or "limited tax general obligation bonds." One of the primary benefits of councilmanic bonds is that they can be issued without an authorizing vote of the STA's voters. This decreases both the time necessary to consummate the financing (bonds can be issued as soon as the authorizing resolution is effective) and the initial financing costs (there are no election expenses).

(2) Voted general obligation bonds. To preserve STA's non-voted debt capacity, or to issue bonds in an amount that is greater than STA's existing non-voted debt capacity, STA can submit for voter approval a proposition to issue general obligation bonds.¹ Such bonds are commonly referred to as "voted bonds" or "unlimited tax general obligation bonds," and must be approved by 60 percent of STA's voters voting on the proposition at an election in which the total votes cast upon the proposition exceeds 40 percent of the total number of voters voting at the preceding general election. Wash. Const. Art. 7, § 2(b); RCW 39.36.020(1); 84.52.056. The maximum principal amount of STA indebtedness—both voted and non-voted—cannot exceed one and one-fourth percent of the value of taxable property within STA. RCW 39.36.020(1). The major shortcoming of unlimited tax general obligation bonds is self-evident—they must be approved by a supermajority vote of the STA voters.

STA may pledge any taxes levied by it "for the payment or security of the principal of and interest on" either voted or non-voted bonds issued by it. RCW 35.58.2721(1).

d. *Interlocal cooperation.* STA may also enter into contracts with other public entities or with private persons or entities to provide public transportation services for a fee and, in turn, may pledge those revenues as well as "all other revenue derived from the ownership or operation of publicly owned transportation facilities to pay and to

¹ The proceeds of such bonds must be used for capital purposes and cannot be used to replace equipment. Wash. Const. Art. 7, § 2(b); RCW 35.58.2721; RCW 84.52.056.

secure the payment of [STA] general obligation bonds and/or revenue bonds.” RCW 39.33.050. There is no express authority which would permit STA to issue revenue bonds despite the reference to such bonds in RCW 39.33, though we believe RCW 36.57.080 which says that a public benefit transportation area can "secure loans or advances . . . for the design, construction or operation of transportation facilities" could probably serve as the basis for this authority. Finally, cities and towns within STA’s boundaries are permitted to “contribute such sums toward the expense for *maintaining and operating* the public transportation system” as they see fit. RCW 36.57A.130. Spokane County may also be authorized to issue bonds to facilitate the construction of a light rail system by STA under RCW 35.58.2721 which states that “the governing body of any municipality shall be authorized . . . to issue general obligation bonds for public mass transportation capital purposes.”

2. High Capacity Transportation Systems (RCW 81.104)

a. *Authority to establish high-capacity transportation systems.* “Transit agencies” in certain counties, including Spokane, “may elect to establish high capacity transportation service.” RCW 81.104.030. The term “transit agencies” includes “city-owned transit systems, county transportation authorities, metropolitan municipal corporations, and *public benefit transportation areas.*” RCW 81.104.015(4). The term “High-capacity transportation system” is broadly defined as “a system of public transportation services within an urbanized region operating principally on exclusive rights of way . . . [which] provides a substantially higher level of passenger capacity, speed, and service frequency than traditional public transportation systems operating principally in general purpose roadways.” RCW 81.104.015(1). The term “high-capacity transportation system” clearly includes light rail. Thus, if it complies with the procedures set forth in RCW 81.104, STA may rely on chapter 81.104 revenue sources to construct a light rail system in Spokane County.

b. *Taxing authority.* RCW 81.104 gives STA, as a “transit agency,” the authority to levy three different taxes, all of which must be approved by a majority of the STA electors, to establish a light rail system. They include an employer tax, a retail car rental tax and a general sales and use tax. RCW 81.104.140. The employer tax is a tax of up to \$2 per month per full-time employee on all employers located within STA boundaries. RCW 81.104.150. The car rental tax is a sales and use tax of up to 2.172 percent on retail car rentals within STA boundaries that are taxable by the state under RCW 82.08 and 82.12. RCW 81.104.160. The general sales and use tax is a local option sales and use tax of up to one percent, except that if Spokane County has imposed the .1 percent criminal justice tax authorized by RCW 82.14.340, which it has, the tax imposed may be up to .9 percent. RCW 81.104.170. This .9 percent sales and use tax is in addition to the sales and use tax of up to .9 percent that may be imposed by STA under RCW 82.14.045.

Before a high-capacity transit tax may be placed on the ballot, STA must undertake the planning process described in RCW 81.104.100(1) & (2) and the proposition must reference the detailed “system plan” referred to in RCW 81.104.100(2)(d).

STA may also apply to receive funds from the state high capacity transportation account. RCW 81.104.090. Revenues allocated to this account were eliminated in 2000, however, and no balance remains. Accordingly, additional appropriations will have to be sought before STA may receive such funds.

c. *Authority to issue bonds and pledge revenues.* STA is authorized to issue bonds to establish a high-capacity transit system under RCW 35.58.2721, which is described in subsection 1(c) above. RCW 81.104.180 and 35.58.2721 both authorize STA to pledge revenues from high-capacity transit taxes to retire bonds issued to finance a light rail system.

d. *Intergovernmental cooperation.* Under RCW 81.104.140, “[l]ocal option funds may be used to support implementation of interlocal agreements with respect to the establishment of regional high capacity transportation service. Except when a regional transit authority exists (and none does in STA’s case), local jurisdictions shall retain control over moneys generated within their boundaries, although funds may be commingled with those generated in other areas for planning, construction, and operation of high capacity transportation systems as set forth in the agreement.”

3. Transportation Benefit Districts (RCW 36.73)

a. *Formation and authority to finance light rail systems.* Under RCW 36.73.020, a city or county—or a combination of cities and counties—may establish a transportation benefit district (a “TBD”) “for the purpose of acquiring, constructing, improving, providing, and funding a transportation improvement within the district that is consistent with any existing state, regional, and local transportation plans and necessitated by existing or reasonably foreseeable congestion levels.” The term “transportation improvement,” which used to refer only to highways, streets and roads, was expanded in 2005 to include “high-capacity transportation.” RCW 36.73.015. Tax benefit district revenues can therefore now be used to finance a light rail system.

A TBD is a quasi-municipal corporation and independent taxing authority that, in the case of a TBD formed by more than one jurisdiction, is governed by interlocal agreement, provided that the governing body must be comprised of at least one representative from each jurisdiction in the TBD. RCW 36.73.040, 36.73.020(3). A TBD has the power to condemn to the same extent as the entity that created it. RCW 36.73.130. While the improvements constructed are normally owned by the jurisdiction in which they are located, the county may elect to have a participating “transit district”—such as STA—own them. RCW 36.73.020(1).

The TBD statute used to require that TBD boundaries be coextensive with the boundaries of the participating jurisdictions but this requirement was dropped in the 2006 legislative session. HB 2871.

b. *Taxing authority.* Upon the approval of a majority vote of the TBD electors, a TBD may impose the following taxes, fees and charges:

- A .2 percent sales and use tax
- An annual vehicle fee up to \$100 per vehicle²
- A development impact fee
- Vehicle tolls on highways, streets and roads within the TBD

A TBD may also levy property taxes in excess of the one percent state limit in certain cases with approval of 60 percent of the TBD electors.

The .2 percent sales and use tax may be imposed for a *10 year period* except that voters may approve a ten year extension by majority vote. RCW 82.14.0455. If TBD taxing authority is to be used to support a light-rail bond issue, this provision would likely need to be extended to 20 or even 30 years.

The annual vehicle fee of up to \$100, which was adopted in 2005, applies to vehicles subject to license tab fees under RCW 46.16.0621 as well as to vehicles subject to gross weight fees under RCW 46.16.070. RCW 82.80.140.

The development impact fee is a charge on essentially any development occurring within the TBD. The fees imposed must be “reasonably necessary as a result of the impact of development, construction, or classification or reclassification of land on identified transportation needs.” RCW 36.73.120. Developments consisting of 20 or fewer residences are exempt.

The Department of Transportation administers tolls on state routes or federal highways and the TBD administers tolls on county roads and city streets, with the amount of the toll being approved by the transportation commission. The tolls must not be prohibited by another provision of Washington law.

A TBD may also levy ad valorem property taxes in two instances. In the first, a TBD may levy property taxes in excess of the aggregate one percent state limit for a one-year period if approved by 60 percent of the TBD electors. In the second, a TBD may levy property taxes in excess of the aggregate one percent limit for a period of more than one year to retire voter-approved general obligation bonds issued for capital purposes. RCW 36.73.060.

c. *Local improvement district.* A TBD may also form a local improvement district within its boundaries and “impose special assessments on all property specially benefited by the transportation improvements.” RCW 36.73.080. Such local improvement districts must be created and administered in the manner set forth in RCW 35.43-54, as applicable. The TBD is also authorized to issue special assessment bonds or revenue bonds to fund the costs of the transportation improvement funded by the local improvement district assessments. 36.73.080(1).

d. *Authority to issue bonds and pledge revenues.* A TBD may issue non-voted general obligation bonds, voted general obligation bonds and revenue bonds (in

² If Initiative Measure 917 passes, this per-vehicle fee will be repealed.

addition to the special assessment bonds referenced in subsection (c) above), provided that such bonds mature within 40 years. The total outstanding non-voter approved indebtedness of a TBD must not exceed 1.5 percent of the value of taxable property within STA boundaries. RCW 36.73.070(1). *This limit is much higher than STA's non-voted debt capacity and could play an important role in the formulation of STA's financing plan—especially since voted debt must be approved by a supermajority.* A TBD may issue voted general obligations with the approval of 60 percent of the TBD electors if the principal amount of the bonds, when added to the TBD's other outstanding general obligation indebtedness (voted and non-voted), does not exceed 5 percent of the value of taxable property within the TBD boundaries. RCW 36.73.070(1).

Excess property tax levies may be used to retire voter-approved general obligation bonds, RCW 36.73.070(1), and revenues, fees and special assessments generated by specific projects may be pledged to pay bonds issued to finance those projects, RCW 36.73.070(3). RCW 36.73.070(3) also states that “the district may also pledge any other revenues that may be available to the district.” The meaning of this sentence is not entirely clear because it doesn't indicate what the “other revenues” may be pledged for. One interpretation is that the “other revenues” may be pledged only to pay bonds issued to finance revenue generating projects. Another interpretation is that the “other revenues” may be pledged to pay any bonds issued by the TBD. If the former is true, then TBD's ability to pledge tax revenues for the repayment of bonds will be circumscribed.

A TBD may also issue revenue bonds. RCW 36.73.070(4). Bonds issued by a TBD may not have a maturity in excess of forty years. RCW 36.73.070(2).

4. Cities, Towns, Counties and Metropolitan Municipal Corporations

a. *Authority to establish a light rail facility.* In Washington, cities, towns and counties are authorized to “acquire, construct, operate, and maintain a public transportation system and additions and betterments thereto, and to issue general obligation bonds for public mass transportation capital purposes.” RCW 35.58.2721 *see also* RCW 35.92.060, 35.95.030. Note that there is no requirement in RCW 35.58.2721 that proceeds of bonds issued under RCW 35.58.2721 be used for mass transportation facilities owned by the city or county issuing them. This suggests that Spokane County could issue bonds to finance a light rail system owned by STA or some other public entity.

Counties are authorized to form County Public Transportation Authorities and Unincorporated Transportation Benefit Areas for public transportation purposes. RCW 36.57.030 and 36.57.100. The taxing authority of these public entities, however, is the same as that of a public transportation benefit area, subject to the requirement that the tax may only be imposed once. Since the excise tax has already been imposed by STA, it may not be imposed by any other entity. Metropolitan Municipal Corporations may also be formed to provide transportation services under RCW 35.58.030 but they suffer from the same problem; namely, they cannot tax if STA has already imposed the tax under RCW 82.14.045.

b. *Debt capacity.* The non-voted debt capacity of a city, town or county is equal to 1.5 percent and the total debt capacity (including voted and non-voted debt) of a city, town or county is equal to 2.5 percent.

c. *Local revenue sources*

The following local revenue sources are available for transportation purposes in addition to the general taxing authority of cities, towns and counties.

1. Local Option Fuel Tax. A county, with the approval of a majority of the voters, may levy local option motor vehicle fuel tax at a rate up to “ten percent of the statewide motor vehicle fuel tax rate under RCW 82.36.025.”³ RCW 82.80.010. The tax, though levied by the county, is levied on incorporated and unincorporated areas. Proceeds from the tax may only be used for “transportation purposes” which again was recently amended to include the “development and implementation of public transportation and high-capacity transit improvements and programs; and planning, design, and acquisition of right of way and sites for such transportation purposes.” RCW 82.80.010(8), 82.80.070.

2. Commercial Parking Tax. A city or county may impose a tax, at the city or county’s election, on either (1) all persons engaged in a commercial parking business within its respective jurisdiction or (2) the act of parking a motor vehicle in a facility operated by a commercial parking business. The tax referred to in subsection (1) above may be based upon gross proceeds or the number of vehicle stalls. The tax referred to in subsection (2) above may be imposed on a per vehicle basis or measured by the parking charge. The proceeds must be used for “transportation purposes,” which are described in Section 4(a) above or for “transportation improvements” under the transportation benefit district provisions. The definitions of both terms include high-capacity transportation. There is no statutory limit to the amount of the tax.

3. Impact Fees. Counties, cities, towns and transportation benefit districts may adopt impact fee programs for the purpose of financing transportation improvements. Detailed requirements for such a program are outlined in RCW 39.92.020.

4. Local Improvement Districts. Cities are authorized to impose special assessments on benefited property to construct “systems of surface, underground, or overhead railways, tramways, buses, or any other means of local transportation, except taxis” including necessary passenger terminal and parking facilities. RCW

³ Article II, Section 40 of the Washington State Constitution requires “all excise taxes collected by the State of Washington on the sale, distribution or use of motor vehicle fuel” to be used for highway purposes. Since the term “highway purposes” has long been interpreted to exclude high capacity transit such as light rail, there is some question about whether proceeds from a local-option fuel tax can be used for non-highway purposes. While the question has never been tested in court—indeed, to our knowledge, no local government has ever imposed this tax—Attorney General Opinion 1974 Number 6 concludes that Article II, Section 40 relates only “to taxes collected by the state of Washington and does not reach those imposed and collected by local units of government.”

35.43.040(16); *see also* RCW 35.84.060. Local improvement districts may be formed and assessments imposed without a vote of the people.

5. Tax Increment Financing.

(i) *Community Revitalization Financing.* Under RCW 39.89, a local government—including a county, city, town or port district—may establish an “increment area” within its boundaries to capture a portion of the future increase in property taxes to finance public improvements. To create an increment area, a local government must first enter into a written agreement for the use of community revitalization financing with taxing districts that levy at least 75 percent of the “regular property taxes” levied in the proposed increment area. RCW 39.89.050(1). With certain exceptions, the term “regular property taxes” refers to all property taxes levied in the increment area except the state portion that is dedicated to schools. RCW 39.89.080(6). The sponsoring local government must also obtain the approval of any fire district with territory in the proposed increment area. RCW 39.89.030(5). Once the approvals are obtained, the sponsoring local government holds a hearing and then adopts an ordinance creating the increment area.

After the increment area is created, the sponsoring local government receives, depending on the content of the agreements with the various taxing districts, up to 75 percent of the increase in regular property taxes (i.e., the “tax increment”) levied in the increment area to finance certain public improvements. Among other things, the tax increment or bonds paid for by the tax increment may be used to finance “[p]arking [and] terminal . . . facilities . . . [as well as] park and ride facilities of a transit authority.” RCW 39.89.020(4).

(ii) *LIFT Legislation.* House Bill 2673 (“HB 2673”), which was signed into law following the 2006 legislative session, expands a local government’s ability to use tax increment financing by giving a local government the right to a sales tax increment and state matching funds in addition to a property tax increment to finance public improvements. The increment areas created under this legislation are referred to as revenue development areas or “RDAs”. Only one RDA per county is permitted. HB 2673 § 204(3). In addition, HB 2673 identifies three demonstration projects, each of which must be approved for state matching funds before any other RDA is approved. HB 2673 § 203. One of the three demonstration projects is the Spokane river district project in the newly annexed portion of Liberty Lake just north of the Spokane River. Since one of the demonstration projects is located in Spokane County and only one RDA is permitted per county, any light rail improvements constructed with RDA financing will have to be located in the river district demonstration project.

Creation of an RDA is accomplished through a somewhat more elaborate process. First, the sponsoring local government designates the RDA. The sponsor then obtains the written consent of any participating local government or taxing district. A public hearing is then held and the ordinance creating the RDA is adopted. The sponsor then submits an application to the state community economic revitalization board (the “CERB”). CERB approval is required before the sales tax increment and state matching funds can be obtained.

The sales tax increment is equal to 100 percent of the increase in sales from local governments and taxing districts that have agreed to dedicated the increment to the sponsor, provided the agreements don’t provide for some lesser amount. HB 2673 § 301. The property tax increment is equal to 75 percent of the increase in property taxes levied on the RDA assessed value, so long as the increase is due to new development. HB 2673 § 302. The state match is an amount approved by CERB up to \$1,000,000. HB 2673 § 401. Spokane County will most likely be submitting its CERB application later this year. STA will therefore need to act quickly to have light rail or transit-related funds included in the river crossing RDA plans.

As with community revitalization financing, RDA financing or bonds paid for with RDA financing can be used to construct “[p]arking [and] terminal . . . facilities [as well as] . . . park and ride facilities of a transit authority.” HB 2673 § 102(21).

6. Port Districts (RCW 53)

A port district is a municipal corporation authorized to be created and operated by RCW Title 53. Thirty-two of the 39 counties in the state of Washington currently have one or more such districts. A port district’s authority to construct a light rail system is limited to the construction of “rail . . . transfer and terminal facilities.” RCW 53.08.020.

The creation of a port district may be initiated either by a resolution of the board of county commissioners or by a petition signed by ten percent of the registered voters of the county based on the total vote cast in the last general election. If the petition method is used, it must be submitted to the county auditor who, within 15 days, must examine the signatures and certify its sufficiency or insufficiency. Once the petition is certified as being sufficient, the board of county commissioners must adopt a resolution submitting the question to form a port district at either a special or general election. A majority vote is required for the formation of such district.

A port district has the statutory authority to levy an ad valorem property tax of up to 45 cents per \$1,000 of assessed value of all taxable property within the district. This levy does not require a vote. A port district may issue limited tax general obligation bonds without a vote of its qualified electors in an amount not to exceed one-fourth of one percent of its assessed value. Such bonds must be repaid from the levy described

above or from other legally available sources. In addition, with the assent of three-fifths of the voters voting thereon at a general or special election, a port district may issue unlimited tax general obligation bonds in an amount not to exceed three-fourths of one percent of the value of taxable property within the district. Based on Spokane County's current assessed value, a port district's nonvoted debt capacity would be approximately \$65,455,034 and the voted debt capacity would be approximately \$196,365,104. The term of the bonds cannot exceed 50 years. A port district may also issue revenue bonds and special assessment bonds.

7. Interlocal Cooperation.

Under Washington's Interlocal Cooperation Act, any power that may be exercised by a public agency may be exercised jointly with another public agency with the same power. RCW 39.34.030. As an example, a group of municipalities that formed a transportation benefit district could work together with STA (with its high capacity transportation system authority) to finance, construct and operate a light rail system. Indeed, the transportation benefit district and public transportation benefit area provisions of the Washington code contemplate, and even require, interlocal cooperation in certain circumstances. See RCW 81.104.140(5) (authorizing local option funds to be used to support "implementation of interlocal agreements [for] the establishment of regional high capacity transportation service) and RCW 36.73.020(3) (requiring governance by interlocal authority where the TBD includes territory in more than one jurisdiction). Perhaps STA could combine its taxing authority under the high capacity transportation system provisions of RCW 81.104 with the expanded non-voted debt capacity of a transportation benefit districts to achieve the optimal combination of revenue sources and debt capacity.

STA might also consider relying on the debt capacity of Spokane County to finance light rail. RCW 35.58.2721 (giving cities and counties the authority issue "general obligation bonds for public mass transportation capital purposes"). However, any interlocal agreement involving high capacity transportation system funds will have to take into account the requirement that "[a]gencies providing high capacity transportation service shall retain responsibility for revenue encumbrance, disbursement, and bonding."

8. "Private, Non-profit 63-20 Financings"

IRS Revenue Ruling 63-20 also permits a non-profit corporation to issue tax exempt bonds on behalf of a public entity to finance certain projects with a public purpose. To qualify to issue tax exempt debt under ruling 63-20, a non-profit corporation must satisfy the following criteria:

- The corporation must engage in activities which are essentially "public in nature;"
- The corporation's income must not inure to any private person;
- A state or political subdivision must have a 'beneficial interest' in the corporation while the indebtedness remains outstanding;
- The state or political subdivision must approve the specific obligations issued by the corporation; and

- Unencumbered legal title in the financed facilities must vest in the governmental unit after the bonds are paid.

63-20 financings have been an important part of the following high-profile transportation projects: the Las Vegas Monorail, the Tacoma Narrows Bridge, California's SR 125 toll road projects and Virginia's Pocahontas Parkway. While Revenue Ruling 63-20 provides a vehicle for a certain type of financing, revenue streams will still need to be identified to retire the credit facility associated with the financing.