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Happy Holidays!!!

Tax Increment Financing Re-interpretation

Many recent discussions have illustrated that there are some ambiguities in certain statutes, leading to differing interpretations as to tax increment financing issues. The statutes needing interpretation are RCW 39.114.010, RCW 39.114.050 and RCW 84.55.010.

Some commentators, city officials, and maybe even the Washington State Department of Revenue, seem to think that the junior taxing districts will receive some tax revenue generated by new construction in a tax increment area (TIA) during the time that the TIA is in effect. Having reviewed the three above statutes in an effort to harmonize them if they conflict, we think that now we clearly see the ambiguity that may have resulted in their confusion. We have concluded that it is incorrect to argue that the junior taxing districts will receive a “bump” in revenue (taxes) due to the new construction in TIAs attributable to the public improvements of the sponsoring city or other qualified entity.

Perhaps before diving into the merits of the two differing interpretations of these statutes, I should discuss some well-established concepts used in statutory interpretation. First, there is a rule known as the “plain meaning” rule. Essentially, this rule or canon of construction holds that if the meaning of a statute is clear and unambiguous, then the courts and attorneys need not resort to any of the secondary rules or canons of construction. In other words, the statute means what it says, literally! Only when a statute is ambiguous—capable of at least two different meanings—do we need to dig deeper into the various rules.

A second rule is that the legislature is presumed to know of its prior enactments and then it legislates against that backdrop.

A third rule is that a specific statute is preferred over a general statute, when the two are in apparent conflict and deal with the same subject matter.

Now let's see how these three canons of construction might be used to construe or interpret the three above-cited statutes. First, let's discuss RCW 39.114.010.[1] Specifically, I would like to focus on RCW 39.14.010(3), which provides: "'Increment value' means 100 percent of **any** increase in the true and fair value of real property[2] in an increment area **that is placed on the tax rolls** after the increment area **takes effect**. The increment value shall not be less than zero." (emphasis added).

I would argue that this statute is clear and unambiguous. In fact, it seems to rather explicitly provide that "100%" of *any* value increase in the increment area is within the definition of increment value. It does not seem to matter why there is an increase in value—the property needs to be in the TIA and the TIA needs to be in effect. And the definition does not exclude "the value of new construction." I see no real ambiguity. Now, apply that definition of "increment value" in the context of RCW 39.114.050[3]:

This statute has two noteworthy concepts: First, RCW 39.114.050(1)(a) states that each taxing district shall receive that portion of the taxes produced by the current levy rate of taxes, "on the tax allocation **base value**…." By the way, "tax allocation base value" is defined in the definitions at RCW 39.114.010(10). "Base value" means the value as of the year in which the TIA is formed. In other words, for those other taxing districts, the value is stuck in the same amount all during the term of the TIA for purposes of generating taxes for those districts.[4]

Thus, it seems clear, at least to me, that the other taxing districts only get the base value times their current tax rate during the TIA's existence, which can be up to 25 years. The sponsoring city, county or port district that created the TIA is allocated the rest of the taxes levied, as they are allocated (diverted) to the sponsoring entity. That is what RCW 39.114.050(1)(b) rather clearly states: "The local government that designated the increment area shall be entitled to receive an additional amount equal to the amount derived from the regular property taxes levied by or for each taxing district upon the **increment value** within the increment area." (emphasis added). That sentence well describes the allocation or

[1] https://app.leg.wa.gov/RCW/default.aspx?cite=39.114.010

[2] "Real property" is also a statutorily defined term: https://app.leg.wa.gov/RCW/default.aspx?cite=84.04.090

[3] https://app.leg.wa.gov/RCW/default.aspx?cite=39.114.050

[4] Although there is newly enacted language at RCW 39.114.050 (5) regarding adjustments to base value on the basis of "private developments" on "publicly owned land," we do not view that as impacting the base value except under narrow circumstances.

diversion, does it not? The statute goes on to say that the sponsoring jurisdiction only gets back the funds that it spent on the public works it completed for the purpose of facilitating the projected growth in the TIA. For example, it might mean that the city recoups the equivalent amount of what it spent on infrastructure, and therefore the TIA ends even before the end of the term set out in the ordinance establishing the TIA.

Now let us discuss RCW 84.55.010[5] because it may well be causing some of the confusion of certain consultants and others. That statute, which was amended somewhat when chapter 39.114 was adopted, is a law relating to limitations on tax increases from one year to the next. The law limits the increases in revenue (regular property taxes) to a limit factor, which quite often is a 1% increase over the prior year. For several years, that statute has excluded from the 1% calculation certain items such as new construction (that added to the tax rolls since the previous year); increase in assessed value due to construction of facilities such as wind turbines, solar, biomass and geothermal facilities; "improvements to property," and increases in the AV of state-assessed property. (We call these collectively "NC&I").

When the TIF statute was added, the legislature added one more to these exclusions from the calculation of the tax increase. Now RCW 84.55.010 also excludes from the calculation any increase in AV in a TIA. Since any value increases in a TIA are most likely due to new construction or improvements to property within the TIA, that addition to the law was probably unnecessary or obviously covered already. Some people seem to think that means somehow the other taxing districts get some of that money as it would not be included in the "increment value" for that tax year. I think otherwise.

Let us analyze the problem from the vantage point of the typical levy worksheet, often used by county assessors and supplied by them to the taxing districts. On those worksheets, the "new construction" and the other exclusions from the limit factor calculation are listed on separate lines from the calculation of the limit factor increase. But in the end, all of these various lines on the worksheet are added together so that normally the taxing districts get their percentage increase by applying the limit factor, plus the money generated by multiplying the levy rate by the value of new construction or the like NC&I.

Now let us go back. "Increment value means 100% of any increase in the true and fair value of real property in an increment area <u>that is placed on the tax rolls</u> after the tax increment area takes effect." As you can see from my discussion of the levy worksheet process, all of that new construction and other such items (which we call "NC&I") do get added to the tax rolls and taxes are collected by someone!! In the case of the TIA, they get collected by the assessor or treasurer of the county and then they get allocated (diverted) to the sponsor, not to the junior taxing districts, under the TIF statutes.

How do the above rules or canons of construction come into play? While we could argue that only the "plain meaning" rule applies as there is no ambiguity here, what if we assume some ambiguity in one or more of these statutes? Under rule #2, I would argue that the legislature knew of RCW 84.55.010, when it enacted the TIF law at a later date. Indeed, it is clear that they did because they simultaneously amended RCW 84.55.010(1) by adding (e) to make reference to

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5 https://app.leg.wa.gov/RCW/default.aspx?cite=84.55.010

RCW 39.114.010. It does not matter that the change may have been unnecessary; it shows they considered the limitation law when they enacted the TIF law. In that regard, they could have said somewhere in one of these statutes that the junior taxing district would receive some of the taxes generated by improvements in the TIA, but instead they provided in RCW 39.114.010(10) a definition of "base value." Clearly, the intent of the legislature was to limit the other taxing districts to the base value at inception of the TIA, multiplied by their current levy rate.

Finally, we apply rule #3. RCW 39.114.010 and .050 are both very specific statutes relating to tax increment financing, and how the monies are distributed. RCW 84.55.010 as now amended is a generally applicable tax limitation statute, that only tangentially now mentions tax increment financing in RCW 84.55.010(1)(e). It is pretty obvious to me that the TIF law controls questions of how the tax monies derived from the TIA are allocated (diverted). No matter how you "slice it and dice it" there is no statutory basis to conclude that the other taxing districts get any benefit from a TIA. Any statutory recital to the contrary is window dressing, or is not based in reality. As indicated by a prior article,[6] we believe the TIF statute—and the way it really works to divert funds intended for junior taxing districts—is totally inconsistent with RCW 43.09.210(3), which provides that no institution shall benefit in any financial manner whatever by an appropriation or fund made for the support of another. In our view, the TIF statute contravenes that law.

6 https://www.firehouselawyer.com/Newsletters/October2023FINAL.pdf

But let's make sure we understand how the allocation process and the redistribution of property taxes derived from the TIA affect total valuation and the "highest lawful levies" (HLL) of the other taxing districts. Here is a rather simple hypothetical situation that we think well illustrates how this should work in the assessor's office:

City A enacts a TIF ordinance applicable to about 190 parcels in a designated TIA, effective June 1, 2023. The total valuation of properties within the TIF at that time was $100 million. This is the "base value." Public improvements including water and sewer systems worth $25 million are installed at city expense (supported in part by municipal bonds) in a project completed in 2023 and 2024. The goal is to facilitate private development within some or all of the 190 parcels due to the new water and sewer infrastructure, the lack of which is what impeded development in the first place. Development starts right away in 2024, but the first project is not completed until 2025—a new office and light industrial project. So the assessor gets that "new construction" on the tax rolls for 2025-2026 for levy and collection respectively. That is shown as property on both the junior taxing district's schedule of values and the city's schedule of values, on a separate line on the tax worksheet, so it is not included in the limit factor calculations mandated by RCW 84.55.010.

Did we mention that the TIA is also included within a fire district and a hospital district? Let us assume the hospital district has a regular levy of $0.50 per thousand. Let us assume that the fire district has a regular levy rate of $1.25 per thousand and a total AV of $3 billion. Remember that later; that total value of $3 billion is vital to understanding this.

I am going to assume that the limit factor (the amount by which the levy revenue can increase year over year) is 1% for both of those junior taxing districts, for the sake of simplicity. Let us just calculate then that the fire district's total levy, levied in 2022 and collected in 2023 was about $3,750,000 and the hospital district's will be assumed to be $1,000,000.

Let's assume that the new construction of the office/industrial development is valued at $50 million, increasing the AV in the TIA, but that all other parcels remain about the same so the increment value is $50 million. In that year, the city's worksheet will not include that $50 million in the calculation of its HLL, but it will go on the tax rolls on a separate line for new construction. It will be taxed at the current rates (2025 rates, by the way) for ALL applicable taxing districts, but let us say that is just the city, fire district and hospital district to keep it simple. The city then gets allocated by the county treasurer all of the taxes levied on the aggregate increment value generated in the TIA for all three of these taxing districts. The fire and hospital districts just get the base value (remember that is the AV in the TIA as of 2023!) times their current rates, whether those rates went up or down since the TIA went into effect. In other words, the TIA base value stays the same but tax levy rates of all taxing districts fluctuate from year to year. Indeed, if the total AV of any district goes up more than 1% or so (the limit factor) the rates will go down. We call this rate compression. By contrast, as noted in the recession some ten years ago, if deflation of real estate values is occurring, levy rates will go up because the total AV begins to drop as all residential and commercial real estate values sink! In fact, some of our clients in about 2012 and 2013 were hitting that statutory limit of the $1.50 rate ceiling. But we digress.

The question that has many people confused is how does the new construction (or increases in value in any given year) figure into the valuation used the next year by the taxing district? Our conclusion is that it is added in just like all other new construction, such as that *outside* the TIA. After all, it is on the tax rolls just like other new construction, so the treatment under RCW 84.55.010 is no different than assessors have been treating NC&I in the past. (We use NC&I as shorthand for all of those items not included in the limit factor calculation that must be done every year to make sure the revenue increase year over year does not exceed the applicable limit factor. Typically, that factor is 1% so the levy can be 101% of last year since the HLL is most often whatever your levy was last year. So NC&I 'exclusions' are: new construction; increases in AV due to construction of wind turbine, solar, biomass and geothermal facilities; improvements to property; increases in AV of state-assessed property; and now… increases within TIAs if not covered already above.).

The amended version of RCW 84.55.010 just added the new subsection (1)(e), but did not change the purpose of this statute, which is just to ensure that all of those NC&I items are excluded from what we might call the 1% increase calculation. We conclude that new construction and increases in value in a TIA, just like those items listed above as exclusions before the TIF law was enacted, do get added to the total valuation dollar amount for each taxing district. Why would they not be included in the assessed value? The whole point of the TIF law is to allow sponsoring entities to gain the benefit of the new development facilitated by the public improvements financed by that entity.

So in our hypothetical example above, the $50 million value added to the total valuation of both the fire district and the hospital district due to the new construction does get added to their AV in the following year. We do not think that would have a huge effect, since the total AV (remember that, back about 1000 words ago?) of the fire district was about $3 billion and may well have increased by a few percentage points. We certainly do not see some sort of significant benefit to the fire district from this increase in value until the TIA expires or is fully paid off, whichever occurs first.

We disagree with those consultants who insist that the law allows for an "increment add-on value" that somehow mitigates the effects of the diversion of the taxes on the "increment value." We see nothing in the statutes that lays the foundation for such a statement. One consultant concluded that the junior districts would continue to receive the "new construction add-on values generated for all property inside and outside of the TIA in addition to the 101 percent increase in property tax." Well, obviously the value of new construction is added each year to the total valuation of each taxing district that includes the property in question. The only problem is that the value is not reflected in the revenues received by the junior taxing districts because those are all diverted to the city or other sponsoring jurisdiction that created the TIA. The junior taxing districts will not really benefit from the new construction until the TIF *expires*, one way or the other.

ANOTHER BID LAW EXCEPTION?

A very recent decision of Division II of the Court of Appeals, involving the University of Washington,[7] may be of interest to our readers. We will greatly simplify the fact situation to facilitate the discussion of what we view as issues relevant to municipal law clients like ours.

UW wanted to have built by a private contractor what they called the W27 development. Statutes provided UW with broad authority to manage property that it owned. Generally speaking, like fire districts, the UW is required to enter into publicly bid contracts when performing or having performed "public work" of a value greater than a statutory threshold. But in this case, the construction was not being done at the UW's cost, but rather the developer's cost. The UW did not contribute to the construction cost, but due to a complex lease/rent structure, the plaintiff (which was a disappointed potential bidder/construction company) claimed the UW was *indirectly* contributing to those upfront costs. UW was required to commit to a long-term lease of space. The plaintiff contended that the future promised rent payments meant that the work was being done at UW's cost. The Court of Appeals rejected this creative argument.

The Court of Appeals also held that the "disappointed bidder" had no standing because the law requires such a claimant to sue for an injunction promptly after a challenged contract award is made, or be forever barred. See *Dick Enterprises, Inc. v. Metro King County,* 83 Wn. App. 566,572, 922 P .2d 184 (1996), a case and doctrine we have mentioned in these pages before.[8]

We have started to see clients, however, ask us about arrangements where they will lease space in office buildings in which the landlord has made extensive "tenant improvements" specifically to

[7] https://www.courts.wa.gov/opinions/pdf/D2%2057985-5-II%20Published%20Opinion.pdf

[8] https://www.firehouselawyer.com/Newsletters/September2022.pdf

attract such municipal tenants. So what if your public agency wants to lease such space, but the landlord insists on your payment of a significant (more than the bid threshold amount for fire districts) part of the tenant improvement costs? Is this not a public work, to which the bid law applies? What if it was more subtle, but the future rent in the first 10 years was well above the going market rate for such space, because the landlord wanted to recover some of that upfront money? With no mention of why the rent is so high, would a court still conclude that the agency is doing indirectly what it could not do directly? By the way, the fact that in our scenario here the land is not even owned by the public agency does not mean that the work cannot be a public work. All RCW 39.04 requires is that the work be done "at the cost of" the municipality, so it does not address whether the local government has title to the land or the building, so it applies to leased property too. Isn't this fun?!

HIPAA SECURITY REVISITED

We lawyers who publish the *Firehouse Lawyer* free newsletter have long been subscribers to *The HIPAA Journal.* In every edition, there are articles about cybersecurity breaches and often fines resulting from not preventing ransomware attacks or more flagrant breaches. Many of these are in the healthcare field so they represent breaches of the HIPAA statutes or regulations. Let us know if you need advice about whether you are in compliance with, for example, the HIPAA Privacy Rule and/or the Security Rule. In fact, some fire departments probably think that HIPAA applies to them, but they may not even be a "covered entity."

IMPORTANT MEDICAL MALPRACTICE STATUTE OF LIMITATIONS CASE?

On December 7, 2023, the Washington State Supreme Court announced a decision in *Bennett v. United States of America*,[9] which was a medical malpractice case that must have been well received in the plaintiffs' bar, or at least those plaintiffs' lawyers that bring medical malpractice suits. The highest court in the state ruled that RCW 4.16.350(3)—which sets eight years after the professional negligence as the bar to lawsuits—is unconstitutional under Washington's privileges and immunities clause. See Washington Constitution, article I, section 12.

If the statute were valid, that would mean no medical malpractice action could be brought unless commenced within eight years after the alleged professional negligence. Of course, there is still another statute of limitations, requiring such actions to be commenced within three years of the negligence OR within one year after the plaintiff *discovers* that the injury or condition was *caused* by the act or omission in question, whichever is later. That statutory language remains in place in the same statute.

We do not think the decision is that critical for our fire district and regional fire authority clients, due to insurance coverage and due to the qualified immunity law that shields the employees of these entities (and therefore their employer) absent gross negligence. Nonetheless, it is good to be aware that the absolute bar or protection after eight years has gone away.

[9] https://www.courts.wa.gov/opinions/pdf/1013001.pdf