








EXECUTIVE SUMMARY

Governor Gary Locke convened the Washington Competitiveness Council to examine Washington's ability to compete in the global economy of the 21st century. The council met five times during the summer and fall of 2001. The council identified competitiveness issues of greatest concern and developed recommendations to address them.

The council will actively seek to implement the recommendations and will meet in early 2002 and annually to assess progress in its drive to make Washington a more competitive place to do business.

The council divided its work into five issue areas:

-  **Taxes and Fees**
-  **Regulatory and Permitting Issues**
-  **Physical Infrastructure**
-  **Human Capital and Innovation**
-  **Benchmarks and Performance Measures**

This section summarizes the primary findings and recommendations of the council within these five issue areas. It also summarizes the minority opinions expressed by several council members. Of all the issues considered by the council, the transportation problems facing our state stand out as the issue with the broadest mandate for action. The statement below summarizes the council's position about the urgency of this recommendation:

The most important competitive investment the state of Washington can make is to improve its transportation infrastructure. Washington's currently overwhelmed transportation system threatens jobs and economic vitality, wastes people's time and money, diminishes quality of life, and degrades our environment. To ensure Washington State's prosperity in the future, given the interdependence of the economies both east and west of the Cascades, we **must** improve our ability to move people and products.

A complete list of the council's recommendations concludes the Executive Summary.



Taxes and Fees

Council Findings

- Taxes and fees significantly affect Washington business's ability to compete. As businesses become increasingly mobile, they decide where to locate or expand based increasingly on the tax burden in a given locale. Physical and social infrastructure and quality of life also play a role.
- In its tax policy, Washington State must balance two competitiveness issues – the need to provide essential state services and the need to minimize the relative tax burden on business. Currently, Washington State's initial tax burden on business is one of the highest in the nation.

Council Recommendations

- Washington should avoid increasing the tax burden on business and should maintain existing exemptions and incentives. However, transportation improvements will require new revenue, and these can be generated through user fees, regional taxes and alternative financing mechanisms.
- Washington should clarify and simplify a number of its tax provisions. The council focused on several specific areas of the law that need attention and clarification. They include manufacturing machinery and equipment sales and use tax exemptions, municipal taxation, and deduction of investment income from the business and occupation (B&O) tax.
- Washington should reform its unemployment insurance (UI) system. Eliminating a number of inequities in its structure will make the system more fair, predictable, and stable.
- The state should consider ways to develop and use tax incentives to keep and grow businesses in Washington. Currently, the state's unique tax system combined with equally unique provisions of the Washington Constitution, limit the state's ability to offer tax incentives to new and expanding companies.
- The Governor should adopt key performance measures to better judge Washington's overall competitiveness, and the effect of its tax system on the state business climate. The measures should track Washington's performance over time and compare it to other states. The data used for benchmarking should be timely and include both state and local taxes, unemployment insurance taxes, and worker compensation taxes.

Regulations and Permitting

Council Findings

- Washington's environmental regulations are important to the environment and the health of citizens. The competitiveness council does not seek to weaken Washington's environmental safeguards. Instead, it seeks a culture change within the regulatory agencies to help businesses get things done.
- Washington's current environmental regulatory system is a tangled structure that evolved in piecemeal fashion, resulting in an uncoordinated and inefficient regulatory regime. This contributes to regulatory problems that damage Washington's competitiveness.
- The current regulatory structure unnecessarily delays projects, increases project cost, creates unnecessary uncertainty, reduces operating flexibility, and increases barriers to business growth. It stirs hostility toward government. It wastes resources, increasing government costs. It leads to angry applicants and it encourages project opponents to manipulate the permitting system.
- Washington's inadequate water systems impose uncertainty on businesses and growing communities.
- A lack of affordable housing impedes a company's ability to attract a quality workforce. Regulatory requirements that are overly burdensome can add cost to a home, and delays in obtaining permits can delay the availability of new housing.

Council Recommendations

- Washington should create leadership to streamline and generally oversee the environmental regulatory process. This leadership should have the authority to coordinate the work of different agencies, reprimand agencies when they act improperly, and demand accountability. Most council members recommend a cabinet position for this function. However, some members believe that, given the current fiscal environment, these functions can be performed by the Governor and his staff.
- The Department of Ecology must adopt a greater service ethic to improve employees' attitude in dealings with business and to improve the agency's accountability to those it serves.

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Regulations and Permitting (cont.)

- Washington should consolidate and/or coordinate permitting to simplify procedures for obtaining permits for a development project. An independent official should oversee this process, and there should be a mechanism to enforce project timelines. Some committee members feel that inflexible project timelines will actually further delay the projects by leading to more permit denials.
- Washington should create a single state-government contact with which businesses can work as they decide whether to locate or expand in the state. This would reduce the problem of regulatory agencies that are found by businesses to be unresponsive and unaccountable.
- The Washington Administrative Procedures Act (APA) should be tightened to reduce agency discretion in the process for adopting rules that implement legislation. Currently, some provisions of the APA give too much discretion to agencies in their rule-making process. Several members of the council feel that sweeping changes to the APA are premature until the results of recent statutory changes in the APA are evaluated.
- The state must continue to move toward a system of water law that reduces uncertainty, encourages conservation, and provides funding for capital improvements. During the 2001 legislative session, significant progress was made in amending the water code to address some of these problems, but more is needed.
- Washington should increase funding to make the Growth Management Act work in a timely and effective manner. Successful implementation of the act requires increased funding for infrastructure needed to support growing communities. It also requires funding and technical assistance for communities engaged in planning and environmental review.
- Washington should find ways to streamline the adjudicative processes related to land use. The state should address problems with duplicative appeals, consolidate the land use code, and consolidate the five formal hearings boards overseeing land use and environmental protection. Some council members believe that this type of charge must maintain environmental protections and acknowledge regional issues.
- The Department of Labor and Industries should delay implementation of its proposed ergonomics rule until questions about its cost and effectiveness are answered. Some council members disagree with this recommendation. They recommend that any changes to the rule reflect the evaluation of the blue ribbon panel of experts that is currently reviewing the rule.
- Washington should find ways to ease regulatory pressures to make it easier to build affordable housing in Washington.

Physical Infrastructure



Council Findings

- Transportation, utilities, and telecommunications systems provide the basic support structure essential to a functioning economy. The state's infrastructure must ensure assure the fluid movement of people, products, and information.
- The most important competitive investment the state of Washington can make is to improve its transportation infrastructure with secure long-term funding and efficient operations. Washington citizens currently lose \$2 billion per year because traffic congestion wastes time and fuel and causes shipping delays.
- Washington should build more water storage capacity. Water laws and infrastructure do not adequately provide the capacity to meet 21st century demands and responsibilities.
- The state must reduce unnecessary delays in the siting of telecommunications and energy facilities.
- Low-cost and reliable electricity is a critical element of Washington's economy. Washington needs an energy strategy designed to ensure the availability of low-cost and reliable electricity. The recent energy crisis has financially weakened many of Washington's utilities. Their financial viability and access to capital are essential to their ability to provide for Washington's energy needs.
- The Pacific Northwest needs additional electrical transmission lines to meet expected growth in energy demand.

Council Recommendations

- Washington must secure long-term, stable, reliable funding for its transportation system. The state must put in place performance measures to provide evidence that transportation investments are effectively addressing the most important needs. Regional funding authority and alternative financing mechanisms are critical, and must be part of any transportation funding solution. Washington must continue work to solve the growing water shortage by building more water storage capacity.
- State agencies that manage public lands and rights-of-way must do a better job of reducing unnecessary delays in siting telecommunications and energy facilities that are essential to economic development projects.
- Washington State should promote a regulatory and political environment that supports the financial health of the state's utilities. This includes helping to ensure the BPA has the ability to invest in new transmission capacity in the Pacific Northwest.



Human Capital and Innovation

Council Findings

- Human capital and innovation are fundamental to gaining a competitive advantage in the modern economy. The success of companies, industries, and states increasingly depends on an educated, flexible workforce, their access to new technology, and their ability to rapidly innovate.
- Strength in education, research and development, and technology commercialization is essential to cultivating and nurturing a growing, competitive economy. Other states and regions are investing massively in these areas, so Washington must act decisively or risk falling behind.

Council Recommendations

- Washington must increase support of research, development, and technology commercialization in strategically important industrial clusters. Research universities have contributed significantly to the formation of existing strategic industries. They must be given the tools and flexibility they need to continue to attract top talent and federal funding.
- Washington should expand capacity at its colleges and universities, particularly in strategically important fields of science and engineering.
- Washington should accelerate training of workers for high-demand fields. This requires not only training new workers but also upgrading the skills of existing workers and retraining displaced workers so that they can reenter the workforce.
- Washington must continue to invest in a modern education system to improve still-lagging academic standards. Washington must address the challenge posed by a growing number of students who speak English as a second language, and it must reverse a severe shortage of science and math teachers at all levels.

Benchmarks and Performance Measures

Council Findings

- Many studies that benchmark Washington’s business climate and competitiveness against other states are currently available. So many statistics of such varying quality are available that it is difficult to determine which few measures are best used to determine whether Washington is making the right policy choices for improving its business climate.
- The Washington State Office of the Forecast Council is required by statute to publish an annual Economic Climate Study. This study, which contains nine indicators of economic performance and 24 economic climate benchmarks, provides a credible assessment of Washington’s economic climate. However, the Economic Climate Council, which selects the benchmarks, has not met within the last several years to reconsider and update these benchmarks. Furthermore, it is unclear to what extent these benchmarks are used to evaluate policy options or to assess state agency performance.

Council Recommendations

- Reconvene the Economic Climate Study Advisory Board to revisit the indicators and benchmarks published in the Economic Climate Study to ensure current and appropriate indicators. Consider the summary measures contained in this report if they are not already included. The Economic and Revenue Forecast Council should then reconvene to consider the Advisory Board’s recommendations, and they should then reconvene on an annual basis to review and discuss the indicators.
- Employ the Competitiveness Council’s/Economic and Revenue Forecast Council’s performance measures for state policy analysis and performance reviews for all state agencies.



Minority Views

- **The business community in Washington State needs to shoulder some of the burden** for making up the \$1.2 billion revenue shortfall that we currently face taking some pressure off cutting services, jobs and benefits to poor and working families. This can be done by closing some corporate tax loopholes and exemptions and by enacting subsidy disclosure legislation that will allow us assess the return we get for public dollars forgone.
- **Our fiscal crisis goes well beyond this recession.** It is rooted in our regressive tax system and its inability to generate sufficient funds to meet the growing needs of our economy and society. The passage of two anti-tax initiatives show us we need to take these issues seriously. If we want to accomplish many of the recommendations in this report then we need to increase our revenue base in a fair way and we need to enact legislation extending collective bargaining rights to state employees so that true bargaining over efficiencies in state government can take place.
- **Although the business community has legitimate issues** about the poor customer service they experience from permitting agencies, the environment community believes that permitting agencies sometimes do not fully or properly enforce existing regulations in an effort to satisfy business interests. These differences in perceptions call for benchmarking the performance of state regulatory agencies to provide a common understanding of the dimensions of problems related to permitting.
- **Some of the Council's recommendations related to environmental regulations and permitting focus on symptoms** rather than addressing the causes of the problems cited in the report. Creating negative incentives for quick permit decisions and reducing public participation in these decisions address symptoms. It would be more productive to focus on the causes of these problems by identifying cultural and management reforms of agencies, simplifying and streamlining laws, and implementing permitting efficiencies. Above all, staff professionalism should be demanded, encouraged, and rewarded.



COMPETITIVENESS COUNCIL RECOMMENDATIONS

Taxes and Fees

Issue	Recommendations
Balance revenue needs with tax burden	<ul style="list-style-type: none">• Avoid general tax increases and protect existing exemptions• Pay for transportation improvements with user fees and alternative funding mechanisms—consider regional taxes• Focus the efforts of the Tax Structure Study Committee on the following:<ul style="list-style-type: none">✓ Modernization✓ Equity✓ Certainty✓ Flexibility✓ Volatility
Clarify vague and complex tax provisions	<ul style="list-style-type: none">• Review the M&E Exemption• Enact legislation for municipal tax simplification• Enact legislation to clarify investment income
Unemployment insurance tax burden and inequities	<p>Apply the following guiding principles when considering changes in UI:</p> <ul style="list-style-type: none">• Fairness• Predictability• Stability
System dissimilarity with other states	<ul style="list-style-type: none">• Explore the use of tax increment financing• Consider eliminating sales tax on construction contracts• Change the taxation of start-up businesses• Consider providing some kind of incentives for capital intensive firms• Consider tax credits and exemptions to stimulate investments in innovative strategies for energy development and conservation
Need for benchmarking	Incorporate benchmarks into the state’s internal evaluation and review process

Regulations and Permitting

Issue	Recommendations
Establishing state leadership for comprehensive regulatory reform	<ul style="list-style-type: none"> • Appoint a Secretary of Regulatory Reform • Establish benchmarks for timely permit decision-making • Provide positive and negative incentives to state agencies and local governments that issue permits in a timely manner • Eliminate the practice of changing previous regulation through permitting processes • Enter into binding contracts with federal agencies
Reinventing the Department of Ecology	<ul style="list-style-type: none"> • Institute regulatory reform at the Department of Ecology following the city of Renton’s example • Require DOE to formally promulgate its 401 Certification rules • Require DOE to publish reliable TMDL requirements • Require DOE to promulgate regulations regarding isolated wetlands • Obtain full delegation of Clean Air Act permitting • Consider transferring responsibility for water rights to a Washington Water Resources Commission
Improving the relationship between state agencies and the business community	<ul style="list-style-type: none"> • Create a business ombudsman and business sector managers • Expand the master business license program to cities
Amend the Administrative Procedures Act	<ul style="list-style-type: none"> • Remove the provision placing the burden of proving invalidity of a rule on the challenging party • Permit a request for declaratory judgment on the validity of an agency rule to be filed in any county in the state • Require submission of proposed rules to the Governor’s office prior to final promulgation
Consolidate and/or coordinate permit processes	<ul style="list-style-type: none"> • Create a pilot program modeled on the California Permit Consolidation Zone program • Administratively adopt some elements of the PCZ concept • Develop an executive director for coordination of multiple agency permits
Improving Washington’s water rights system	<ul style="list-style-type: none"> • Become more aggressive in defending state water law • Define “Waters of the State” more fully • Appoint an Eastern Washington water representative • Continue making progress on reform of water law

Regulations and Permitting (cont.)

Issue	Recommendations
Meeting the goals of the Growth Management Act	<ul style="list-style-type: none"> • Fund the infrastructure required to make GMA workable • Annually and adequately fund the PERF program • Provide local governments with procedural and substantive guidance for the environmental review of comprehensive plans and development regulations • Include an economic development element in the GMA (HB 2056; SB 6070) • Strengthen the positive incentives for complying with GMA • Amend the statute on duplicative appeals so that the appellants are required to post a bond in the amount of estimated attorney's fees • Create a consolidated land use code that maintains environmental protections • Reduce the number of environmental adjudicative bodies by developing a unified hearings board system • Benchmark and enforce local government permitting timelines and require permits to be issued within 120 days
Challenge of L&I's Ergonomics Rule	<ul style="list-style-type: none"> • Delay the implementation of the ergonomics rule
Address Housing regulatory issues	<ul style="list-style-type: none"> • Establish model ordinances and best practices for municipal development • Search for and support a remedy to legal issues facing condominium developers

Physical Infrastructure

Issue	Recommendations
Transportation	<ul style="list-style-type: none">• Pass a long-term comprehensive solution for Washington’s transportation solution that includes long-term funding and accountability measures• Secure long-term predictable funding for the Community Economic Revitalization Board (CERB)
Shortage of water storage	<ul style="list-style-type: none">• Support bipartisan solutions to address current and anticipated shortages of water storage• Invest in water infrastructure to match local, federal, and private sources to assure affordable, safe drinking water• Address and coordinate inter-state issues affecting water in the state’s current effort to reform Washington’s water law
Siting and construction of telecommunications and energy facilities on public lands	<ul style="list-style-type: none">• Establish processes—including firm timelines, clearly-stated criteria, and fair compensation—for handling requests for placement of energy and telecommunications facilities on public lands and aquatic lands• Consider the impact and cost of utility infrastructure easements on the construction of facilities and delivery of utility services to energy and telecommunications consumers
Protection of Washington’s competitive advantage in energy	<ul style="list-style-type: none">• Assist in restoring the financial health of the state’s utilities and ensure that the political and regulatory climate in Washington is supportive of its utilities• Press Congress and the federal administration to increase BPA’s borrowing authority to ensure the completion of needed upgrades to the region’s transmission infrastructure• Ensure the state’s updated energy strategy focuses on maintaining Washington’s competitive advantage in supplying low-cost, reliable electricity to the region’s energy-dependent businesses

Human Capital and Innovation

Issue	Recommendations
<p>Better support research, development, and technology commercialization in strategically important industrial clusters</p>	<ul style="list-style-type: none"> • Identify and support industry clusters that are strategically important to the state’s economic future • Provide universities with greater flexibility in setting tuition, so that they may increase faculty salaries and make other investments in strategically important fields • Authorize the issuance of revenue bonds to finance the construction of new facilities through indirect cost recovery from federal research grants • Upgrade the technology commercialization function at the state’s research universities • Systematically examine the impact of current and new taxes on public and private research and development • More vigorously market the federal Small Business Innovation Research (SBIR) grant program to Washington businesses • Exempt sales tax on research expenditures by universities, including expenditures for construction • Authorize purchase of land by universities through real estate contracts • Clarify the applicability of ethics law exemptions to faculty financial interest in commercialization of university-based research • Exempt SBIR grants from the B&O tax • Invest strategically in top-ranked university research programs in science and engineering fields and create more such programs to support strategic industry clusters • Establish one or more university-based science and technology centers, with facilities for research, technology commercialization, and new company incubation
<p>Increase the supply of top-quality bachelors and masters graduates in science and engineering</p>	<ul style="list-style-type: none"> • Allocate university enrollment increases to high-demand fields, with a preference to programs that are of demonstrable top quality by national standards and/or obtain private sector matching funds • Develop a mechanism to finance higher education enrollments, fund educational scholarships, and provide training to upgrade incumbent worker skills (e.g., per employee, per hour set-aside) • Improve articulation between four-year institutions and community and technical colleges, based on best practices here in Washington and from other states • Encourage businesses to establish multi-year internship programs for university students • Fund FTEs (enrollments) based on the cost of education in specific fields • Develop scholarship programs to encourage the most talented high school graduates to attend college in-state • Expand bachelors and masters capacity in science and engineering

Human Capital and Innovation (cont.)

Issue	Recommendations
Expand the pool of educated workers in high-demand fields	<ul style="list-style-type: none"> • Expand the Worker Retraining Program by funding additional enrollments to enable community and technical colleges to match the state and federally funded tuition they will collect from unemployed workers seeking retraining • Allocate community and technical college enrollment increases to high-demand fields, with a preference to institutions that obtain private sector matching funds • Develop a mechanism to finance higher education enrollments, fund educational scholarships, and provide training to upgrade incumbent worker skills (e.g., per employee, per hour set-aside) • Increase the capacity of the Job Skills Program to provide customized training for business recruitment or expansion • Deploy federal and state workforce training dollars more strategically, with priority to local training partnerships aimed at preparing people to meet high demand occupations and the workforce needs of local industry clusters • Develop applied technology bachelors programs, which enable community and technical college graduates to increase their skills to meet industry needs; begin with one or more pilot programs • Increase the role of registered apprenticeship in expanding and renewing the pool of skilled workers • Require workforce development councils to demonstrate that their strategic plans address current workforce needs. • Encourage regional partnerships among community and technical colleges and industries in strategically important clusters to better match curriculum with industry need • Increase funding for vocationally oriented English as a Second Language and Adult Basic Education programs at community colleges
Enable all high school graduates to achieve high academic standards	<ul style="list-style-type: none"> • Maintain focus and accountability for K-12 educational reform • Develop a long-term strategy for enabling all students to achieve high academic standards, including those who speak English as a second language • Extend the school day and school year to leverage assets • Create options for expanding the pool of qualified math and science teachers (e.g., differential pay, alternative routes to certification, faculty loaned from the private sector) • Better link K-12 academic standards and assessments to college admissions and business hiring • Increase professional development support for teachers to obtain advanced credentials in science and math • Increase student access to advanced placement education in science, math, and English • Create smaller, more personalized learning environments • Develop means of addressing the impending shortage of teachers (e.g., increased pay, retraining of workers displaced from other fields, scholarships for college students who agree to pursue teaching careers)

Benchmarks and Performance Measures

Issue	Recommendations
Establishing benchmarks	<ul style="list-style-type: none">• Reconvene the Economic Climate Study Advisory Board to revisit the benchmarks published in the Economic Climate Study• Reconvene the Economic and Revenue Forecast Council annually to discuss the benchmarks
Performance reviews	<ul style="list-style-type: none">• Employ the resulting list of performance measures for state and policy analysis and agency performance reviews