



Washington State  
Department of  
**Commerce**

We strengthen communities

# Multifamily Property Tax Exemption Audit Program Guide

**HOUSING PROGRAM  
GROWTH MANAGEMENT  
SERVICES**

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# Introduction and Context

The multifamily property tax exemption (MFTE) is a property tax waiver program enacted by cities and counties to support local housing goals. Under Chapter 84.14 RCW, local governments can give exemptions for new construction, conversion and rehabilitation of multifamily residential improvements with at least four units.

Under these exemptions, a property owner does not have to pay property taxes on the residential improvements for a given number of years. The property owner still pays tax on the land and on non-residential improvements like the commercial portion of a mixed-use building.

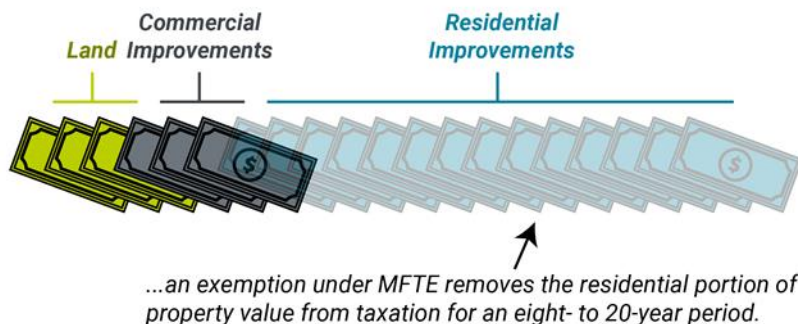
Originally designed as a tool to implement the Growth Management Act, MFTE was adopted in 1995 and codified as RCW 84.14. The initial program authorized a 10-year property tax exemption and focused on property tax exemptions for new and rehabilitated multiple-unit housing in urban centers. The legislature amended RCW 84.14 in 2007 to incorporate a focus on affordable housing, creating eight and twelve-year exemption programs, and clarifying that non-housing-related improvements did not qualify for property tax exemptions. The 2007 update also lowered the population threshold so more cities could offer the program.

In 2019, the Joint Legislative Audit Review Committee ([JLARC](#)) [issued a report](#) on the MFTE program. The report found that, between 2007 and 2019, the program incentivized production of 34,885 new housing units, with 21% of these units designated as affordable. The report identified some issues around a potential tax shift, inconsistent application of the program across jurisdictions, and problems with reporting and monitoring.

In 2021, [Engrossed Second Substitute Senate Bill 5287](#) amended RCW 84.14, requiring Commerce to "adopt and implement a program to effectively audit or review that the owner or operator of each property for which a certificate of tax exemption has been issued (with some exceptions<sup>1</sup>) is offering the number of units at rents as committed to in the approved application for an exemption and that the tenants are being properly screened to be qualified for an income-restricted unit."

Commerce analyzed comparable audit programs, MFTE audit program considerations and short, mid, and long-term steps to implement the audit program. This guide is intended to help Commerce and MFTE stakeholders successfully collaborate in the MFTE process and includes details on the MFTE audit program as proposed by Commerce. Commerce received funding to implement the MFTE audit program over the 2023-2025 biennium.

*For the annual property taxes collected on a development...*



<sup>1</sup> [RCW 84.14.100\(3\)\(a\)](#)

# Implementation Goals

Commerce has established the following goals for the audit program:

- Meet the requirements of [RCW 84.14.100](#).
- Maintain a database of all MFTE units.
- Create a self-funded audit program.
- Support jurisdictions and county assessors with a simple and efficient audit program.
- Increase access to data on the MFTE program to increase transparency.

# Audit Program Structure

Commerce will design and manage the audit program. We anticipate that the audit program will need to accommodate three types of MFTE projects:

- Private-sector properties audited by the Department of Commerce.
- Properties reviewed by their own jurisdiction as approved by the Department of Commerce.
- Properties operated by a non-profit or housing authority, or owned by private citizens.

The audit program will only audit whether owners are "offering the number of units at rents as committed to in the approved application for an exemption and that the tenants are being properly screened to be qualified for an income-restricted unit" as required by RCW 84.14.100(3)(a). The audit will not review other program aspects required by the RCW or locally adopted codes.

Commerce intends to develop a business application. The application will have a user interface where jurisdictions, not for profits, property owners, and auditors can input data. Commerce intends to contract with one or more auditors to complete on-site audits around the state. Commerce policy prohibits sending personal data of MFTE tenants electronically.

## Creating the audit program

Commerce has received state funds to launch the MFTE audit program during the 2023-2025 biennium. Commerce anticipates completing the following steps, many overlapping, to create the audit program.

- Develop database and business application.
- Develop inventory of current MFTE projects.
- Develop forms and processes for the audit.
- Pilot auditing process.
- Engagement with MFTE stakeholders.
- Contract with third party auditor(s).
- Establish fee structures.
- Develop materials and training on the audit program.
- Engage with MFTE enabling jurisdictions.
- Rulemaking for MFTE audit program.

## Program design

Building an effective program requires input from jurisdictions and other MFTE stakeholders. Commerce is sharing this preliminary guide to assist in creating meaningful feedback about the MFTE audit program.

All jurisdictions will continue the reporting required in RCW 84.14.100(2). To ensure accurate auditing, jurisdictions will submit the contract executed for projects that have received final certificates of tax exemption. Commerce will continue to check this data, confirming with county assessors. Commerce will enter this data into the MFTE audit database.

## Schedule

In January of each year, auditors will send certified letters to property owners whose project will be audited in that calendar year. Regional auditors will then schedule with each property owner. Auditing will be in-person and on-site. Auditors will provide a full list of what is required to be in tenant files and project files by the time they arrive on-site. However, the primary documents for review include the total list of units, the list of units that are rent-restricted, and the documentation of how rent-restricted rents are set, how tenants are screened, and how income is verified.

Requirements under RCW [84.14.100](#)(3)(a) specify that audits must occur at least once every five years. Audits will be scheduled as follows for new exemptions:

- For eight-year exemptions (where applicable), year five of the exemption.
- For 12-year exemptions, years five and 10.
- For 20-year exemptions (rental only), years five, 10 and 15.

For existing exemptions, auditors will schedule audits as if previous auditing cycles have already occurred. For example, audits during the first year of the audit program would be required for exemptions issued four or nine years before the current cycle. Auditors will also schedule return visits, if necessary, for sites with findings of noncompliance.

## Preparing records for auditing

During the audit itself, the files to check need to include:

- The MFTE contract with the local jurisdiction (for reference).
- The income verification worksheets submitted by the tenants.
- Supporting income and asset information for each worksheet, plus any other related information (e.g., student status, etc.).
- All leases for the project, including records of lease rates and requirements for payment of utilities.
- Vacancy rates for the project, including evidence of affirmative marketing if rates are unusually higher/longer than market expectations.
- Previous records from audits.

Jurisdictions that wish to enter their own auditing data and results will need a memorandum of understanding (MOU) with the Department of Commerce. This MOU will set the standard for review and the data to be entered into the MFTE auditing database.

Jurisdictions will confirm or correct:

- Site information (e.g., address, contact information, number and size of units, etc.).

- Property owner name and confirmation.
- Rents and vacancies recorded for market-rate units.
- Rents and vacancies recorded for income-restricted units, with confirmation that these leases meet affordability requirements under the MFTE program.
- Income and assets for individual households qualify under the terms of a specific lease.
- Affirmative marketing materials exist if vacancy rates for MFTE units are longer and/or higher than market-rate units.
- A summary of omitted or incorrect information, or other areas of noncompliance.

Jurisdictions will also provide an affidavit from the reviewer confirming the accuracy of the information provided.

## Noncompliance

There are several levels of potential findings of noncompliance during an audit:

- **Minor errors with negligible impacts.** Errors in calculations that result in small mistakes that do not have a substantive impact on the program should be noted in the auditing database. Commerce would not recommend assigning a penalty in these cases.
  - Examples include small errors in reported calculations that do not change household eligibility for MFTE units.
  - No notification of correction and follow-up audit would be necessary, but the city should ask that a follow-up letter of corrective action be provided with the next yearly report describing follow-up actions.
  - Corrective actions may include staff education, updated forms, or similar steps to reduce the likelihood of error.
- **Minor errors with impacts on program requirements.** Unintentional errors by property owners that result in nominal impacts may be required to follow a correction plan and participate in a follow-up audit within six months to determine compliance. In these cases, Commerce would recommend waiving any penalties unless these errors continue.
- **Major errors.** Clear errors that result from negligence and have a significant effect on the provision of rent-restricted units would result in a recommendation for penalties. In these cases, Commerce would recommend to:
  - Levy the sliding-scale penalty under [RCW 84.14.100\(3\)\(b\)](#) if rents were higher than required;
  - Require the property to follow a plan of correction; and
  - Participate in a follow-up audit within six months to demonstrate compliance.

If compliance is not demonstrated during the follow-up audit, Commerce would recommend cancellation of the exemption.

- **Bad faith noncompliance.** In cases of willful noncompliance or fraud, such as if the property owner intentionally failed to fulfill requirements under an MFTE program, Commerce would recommend immediate cancellation of the exemption, with collection of penalties as per RCW 84.14.110(1)(a).

Upon determination of noncompliance from completed audits and reports received, Commerce will provide a report to the local jurisdiction which specifies:

- Property information, including the address and contact information for the owner and/or property manager.
- The nature of noncompliance with affordability requirements.
- Recommendations for a follow-up audit or other review action.
- Recommendations for penalties to be pursued by the local government, including a sliding scale penalty under RCW 84.14.100(3)(b) or cancellation of the exemption under RCW 84.14.110(1).
- A copy of the auditing report provided to Commerce.
- Instructions on follow-up action for the local authority.

The recommendation for a sliding-scale penalty would include supporting guidance to local jurisdictions on the maximum amount of the penalty that can be levied on the property owner. This calculation would specify:

- The rent charged on each unit during each specific lease period.
- The maximum rent permitted under the MFTE affordability requirements.
- The total amount the rents charged exceeded the maximum rents permitted.
- The summation of all overages across the review period, as the maximum penalty that can be charged.

Commerce cannot levy penalties directly against property owners, and must work with local authorities to do so. Enabling jurisdictions have the discretion to change the penalty amount, but must impose and collect a penalty as required by [RCW 84.14.100\(3\)\(b\)](#).

Upon receipt of this report from the Department of Commerce, regardless of the approach used for auditing, the local jurisdiction should provide a certified letter to the property owner that includes a copy of this report and a letter from the local jurisdiction specifying:

- Final penalties to be levied on the property.
- Other corrective action required, including a plan of correction and follow-up audit.
- Options for appeal.

Local appeals should require an immediate follow-up audit, within 120 business days, at the owner's expense, detailing the issues specified in the previous audit and providing clear evidence that the property is in fact in compliance. Accepting the rationale of the appeal is at the discretion of the local jurisdiction, but follow-up action should be coordinated with Commerce.

Under no circumstances should actions to address noncompliance result in the eviction of a household from housing, even in cases where these households are not income eligible to be in an MFTE income-restricted unit. Jurisdictions are encouraged to allow unit floating, so tenants can stay in their unit and the next available unit within the project becomes an MFTE unit.

## Fees charged for auditing

The fees charged for the audit program will need to cover the following Commerce costs:

- Costs of contracting third-party auditing services.
- Staff costs for oversight and management.
- Overhead costs of maintaining the business application and back-end database.

Commerce will pilot the initial audit program to ensure that it is effective, efficient, and will increase MFTE program transparency. Commerce will then:

- Issue a request for proposals or qualifications to secure an MFTE auditor(s). These proposals will include quotes for cost.
- Commerce will set a range of fees for auditing.
- Jurisdictions running their own audit program will pay a fee to have access to and support maintenance of the MFTE audit database.
- Commerce anticipates that the greater number of rent-restricted units in a project the larger the fee for auditing.
- Commerce also anticipates that jurisdictions will collect the base auditing fee at the time the final certificate of tax exemption is issued. However, at this time, there is no process mapped out for transferring those funds from the jurisdictions to Commerce.

## Next steps and conclusions

MFTE stakeholders can expect engagement on the auditing program throughout late summer and early fall 2023. Commerce is in conversation with the Department of Revenue to begin the rule making process. Commerce's internal process to develop a database and business application is already underway.

We look forward to working with you to develop an audit program that will provide consistent support to MFTE programs.