

# HOUSE BILL REPORT

## ESHB 1346

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### As Passed Legislature

**Title:** An act relating to making changes to laws administered by the department of revenue that do not create any new or broaden any existing tax preference as defined in RCW 43.136.021 or increase any person's tax burden

**Brief Description:** Making tax law changes that do not create any new or broaden any existing tax preferences as defined in RCW 43.136.021 or increase any person's tax burden.

**Sponsors:** House Committee on Ways & Means (originally sponsored by Representative Hunter; by request of Department of Revenue).

### Brief History:

#### Committee Activity:

Ways & Means: 1/25/11, 2/10/11 [DPS].

#### Floor Activity:

Passed House: 3/5/11, 58-39.

#### First Special Session

Passed House: 5/22/11, 53-38.

Passed Senate: 5/25/11, 43-0.

Passed Legislature.

### Brief Summary of Engrossed Substitute Bill

- Clarifies that a person who has a substantial nexus in Washington in any tax year will be deemed to have a substantial nexus with the state for the following tax year.
- Clarifies a seller has no obligation to collect use tax if the United States Constitution or federal law prohibits Washington from requiring the person to collect use tax.
- Repeals two redundant tax incentive annual study and report statutes.
- Requires the Department of Revenue to update the January 2012 tax exemption report only for tax exemptions impacting state revenue.

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### HOUSE COMMITTEE ON WAYS & MEANS

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 19 members: Representatives Hunter, Chair; Darneille, Vice Chair; Hasegawa, Vice Chair; Orcutt, Assistant Ranking Minority Member; Carlyle, Cody, Dickerson, Haigh, Hinkle, Hudgins, Hunt, Kagi, Kenney, Ormsby, Parker, Pettigrew, Seaquist, Springer and Sullivan.

**Minority Report:** Do not pass. Signed by 8 members: Representatives Alexander, Ranking Minority Member; Bailey, Assistant Ranking Minority Member; Dammeier, Assistant Ranking Minority Member; Chandler, Haler, Ross, Schmick and Wilcox.

**Staff:** Jeff Olsen (786-7175).

### **Background:**

#### Business and Occupation Tax and Nexus.

Washington's major business tax is the business and occupation (B&O) tax. The B&O tax is imposed on the gross receipts of business activities conducted within the state without any deduction for the costs of doing business. Nexus is the level of connection with a state necessary under the United States Commerce Clause to permit a state to impose a tax or collection duty on out-of-state businesses doing business in the state.

In 2010 the Legislature enacted Engrossed Substitute Senate Bill 6143, specifying that for service-type activities, a business will have substantial nexus in Washington if it has a certain threshold amount of property, employees, or income in the state. The 2010 changes also provide that a business with substantial nexus in the current year is deemed to have substantial nexus the following year. This is referred to as trailing nexus.

#### Sales and Use Taxes.

Retail sales and use taxes are imposed by the state, most cities, and all counties. Retail sales taxes are imposed on retail sales of most articles of tangible personal property, digital products, and some services. The use tax applies to the acquisition of tangible personal property, digital products, and some services that are not subject to sales tax. Generally, a person or business acquiring property in another state is responsible for the payment of Washington use tax when the property is brought into the state. However, under certain circumstances, an out-of-state seller may be required to collect and remit use tax to Washington even if the property is transferred to the buyer outside the state. This requirement would apply only if the seller has some connection to the state.

#### Tax Incentive Reporting Requirements.

The Citizen Commission for Performance Measurement of Tax Preferences (Commission) was established by the 2006 Legislature (Engrossed House Bill 1069). The Commission develops a schedule to review nearly all tax preferences at least once every 10 years. The Commission also schedules preferences with expiration dates for reviews two years before the tax preference expires. Tax preference reviews are conducted by the Joint Legislative Audit and Review Committee (JLARC) according to the schedule established by the

Commission. For each tax preference, the JLARC provides recommendations to continue, modify, schedule for future review, or terminate the preference. The Commission reviews and comments on the JLARC report.

In 2005 the Legislature created a Cost-Recovery Incentive Payment Program to promote renewable energy systems that produce electricity from solar, wind, or anaerobic digesters. The Department of Revenue must measure the impacts of the program and provide a report to the Legislature by December 2014. The JLARC is also scheduled to review the tax incentive in 2013.

Businesses claiming tax incentives are required to provide data on annual accountability reports or surveys filed with the Department of Revenue. In general, accountability reports and surveys require information about employment and economic activities related to the tax incentives. In prior years, it was common to create an entirely new accountability report or survey statute for each new tax incentive even though the requirements of each new annual report or survey largely duplicated existing report or survey statutes. In 2010 Substitute House Bill (SHB) 3066 repealed most of these duplicative tax incentive annual report and survey statutes and replaced them with a uniform annual survey and a uniform annual report. However, duplicative annual report and survey statutes were also amended in other bills that passed during 2010. These other bills did not take cognizance of the repealed sections in SHB 3066.

#### Exemption Study.

The Department of Revenue (DOR) must produce and submit to the Legislature a tax exemption report every four years. The report includes a listing of the estimated revenue lost from the exemption and the beneficiary of the exemption. The next report is due in January 2012.

#### **Summary of Engrossed Substitute Bill:**

The trailing nexus statute is clarified by specifying that a person who has a substantial nexus with this state in any tax year will be deemed to have a substantial nexus with the state for the following tax year.

Two redundant annual tax incentive accountability report and survey statutes are repealed.

For purposes of collecting use taxes, it is explicitly clarified that a seller has no obligation to collect use tax if Washington is prohibited under the United States Constitution or federal law from requiring the person to collect use tax.

For the January 2012 tax exemption study, the DOR does not have to prepare or update the report for any tax exemption that is not likely to increase state revenue if the exemption was repealed.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill takes effect 90 days after adjournment of the session in which the bill is passed.

**Staff Summary of Public Testimony:**

(In support) The DOR is proposing housekeeping changes to clarify language for trailing nexus and use tax collection. In addition, redundant reporting requirements are repealed. The exemption study is proposed to be suspended in response to budget reductions as directed by the Governor. Research positions have been reduced in higher levels to prioritize revenue generating positions.

(In support with concerns) There are inconsistencies in the nexus definition between physical and economic nexus standards that should be made consistent. There are other housekeeping issues that should be considered with this bill.

(With concerns) The tax preference study should not be suspended. Tax preferences should continue to be measured, and should be considered like expenditures of public funds. Suspending the exemption study makes it more difficult to compare the cost of tax preferences with other budget expenditures.

(Opposed) None.

**Persons Testifying:** (In support) Drew Shirk, Department of Revenue.

(In support with concerns) Amber Carter, Association of Washington Business.

(With concerns) Nick Federici, Rebuilding our Economic Future Coalition.

**Persons Signed In To Testify But Not Testifying:** None.