

# HOUSE BILL REPORT

## HB 2857

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**As Reported by House Committee On:**  
Agriculture & Natural Resources

**Title:** An act relating to tax incentives that will promote the manufacturing and use of sustainable wood materials.

**Brief Description:** Concerning tax incentives that will promote the manufacturing and use of sustainable wood materials.

**Sponsors:** Representatives Blake, Harris, Rossetti, Walsh, Wilcox, Fey and Kilduff.

**Brief History:**

**Committee Activity:**

Agriculture & Natural Resources: 1/26/16, 2/2/16 [DPS].

**Brief Summary of Substitute Bill**

- Exempts the portion of gross receipts derived from the wholesale, retail, or manufacture of cross-laminated timber (CLT) from the business and occupation tax, in the form of a deduction.
- Exempts certain qualifying construction containing CLT as a major design component from the sales and use tax, in the form of a remittance.

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### HOUSE COMMITTEE ON AGRICULTURE & NATURAL RESOURCES

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 12 members: Representatives Blake, Chair; Walkinshaw, Vice Chair; Buys, Ranking Minority Member; Dent, Assistant Ranking Minority Member; Chandler, Hurst, Kretz, Lytton, Orcutt, Pettigrew, Schmick and Van De Wege.

**Staff:** Jason Callahan (786-7117).

**Background:**

Cross-Laminated Timber.

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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.*

According to generally accepted industry terms, cross-laminated timber (CLT) is a form of massive timber product. Massive timber products are factory-produced, structural wood panels of two inches or greater thickness and typical widths of four feet or more. Cross-laminated timber is a large-scale, prefabricated, solid engineered wood panel. Finished panels are typically between 2 and 10 feet wide, with lengths up to 60 feet and thickness up to 20 inches. It is sometimes used as an alternative to conventional materials like concrete, masonry, or steel, especially in multifamily and commercial construction, and as long spans in walls, floors, and roofs.

### Business and Occupation Tax.

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. The tax is imposed on the gross receipts from all business activities conducted within the state. Revenues are deposited in the State General Fund. There are several rate categories, and a business may be subject to more than one B&O tax rate, depending on the types of activities conducted. Current law authorizes multiple exemptions, deductions, and credits to reduce the B&O tax liability for specific taxpayers and business industries. The rates are as follows: 0.471 percent for retailing; 0.484 percent for wholesaling and manufacturing, and 1.5 percent for service and other industries.

### Sales and Use Tax.

Retail sales taxes are imposed on retail sales of most articles of tangible personal property, digital products, and some services (including construction). A retail sale is a sale to the final consumer or end user of the property, digital product, or service. If retail sales taxes were not collected when the user acquired property, digital products, or services, then use taxes apply to the value of property, digital product, or service when used in this state. The state, most cities, and all counties levy retail sales and use taxes. The state sales and use tax rate is 6.5 percent; local sales and use tax rates vary from 0.5 percent to 3.1 percent, depending on the location.

### Taxation of Manufacturing Activities.

Persons who manufacture products in this state are subject to the manufacturing B&O tax upon the value of the products, including by-products, at a rate of 0.484 percent, unless the activity qualifies for a special preferential rate. Manufacturers who sell their products at retail or wholesale in this state are also subject to either the retailing (0.471 percent) or wholesaling (0.484 percent) B&O tax. In such cases, the manufacturer must report under both the "production" (manufacturing) and "selling" (wholesaling or retailing) classifications of the B&O tax. Manufacturers who report B&O tax on multiple activities in Washington may qualify for the multiple activities tax credit (MATC). The MATC is a B&O tax credit that is available to certain manufacturers, extractors, and sellers doing business in Washington. Businesses are eligible for this credit against the state B&O tax for gross receipts taxes paid in another jurisdiction or for taxes paid on multiple activities within Washington.

### Tax Preferences for Wood Manufacturers.

Until June 30, 2024, manufacturers of wood products are subject to a preferential B&O tax rate of 0.3424 percent. This is comprised of a base rate of 0.2904 percent plus a surcharge of 0.052 percent. "Wood products" are defined as paper and paper products; dimensional lumber; engineered wood products such as particleboard, oriented strand board, medium density fiberboard, and plywood; wood doors; wood windows; and biocomposite surface products.

### Taxation of Construction Activities.

Prime contractors must collect retail sales tax from the purchaser of the construction project on the gross contract price (without deduction of costs incurred). Billing invoices must separately state the sales tax. If the contract requires retainage, sales tax must be computed before deducting such amounts. Retail construction services are sourced to the location where the construction takes place. A contractor is considered the consumer of items purchased for use in the construction process and not used as component parts of the finished structure, and therefore, retail sales tax must be paid to the vendors of such items. The purchase of materials by custom contractors that will become part of the completed project are purchases for resale (wholesale). Such purchases are not subject to retail sales tax. Reseller permits allow businesses to purchase items or services for resale without paying retail sales tax. Use tax is due if sales tax has not been paid on items the contractor uses as a consumer. Use tax is generally due (if sales tax has not been paid) on the following: equipment, tools, supplies, and rentals of equipment, even if the cost for these items is passed along to the purchaser of the construction project.

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

#### Business and Occupation Deduction for Cross-Laminated Timber Sale or Manufacture.

Wholesalers, retailers, and manufacturers of cross-laminated timber (CLT) may deduct receipts from the sale or manufacture of CLT from their total gross receipts, for the purposes of calculating B&O tax liability. Taxpayers must file an annual survey with the Department of Revenue (Department), listing the amount of tax preference claimed for the calendar year covered by the Department. Deductions for the sale of CLT may only be claimed for sales by the manufacturer.

"Cross-laminated timber" means a prefabricated engineered wood product consisting of not less than three layers of solid-sawn lumber or structural composite lumber where the adjacent layers are cross oriented and bonded with structural adhesive to form a solid wood element.

The B&O tax deduction begins on July 1, 2016, and expires on July 1, 2023.

#### Sales and Use Tax Rebate for Qualifying Buildings Using Cross-Laminated Timber.

Taxpayers who have paid sales or use tax on the construction of a qualifying building using CLT as a major structural component are eligible for an exemption in the form of a remittance, based on both the state and local shares of the tax.

A building may qualify if the appropriate city or county authority verifies at permitting that it meets the following conditions:

1. For buildings that exceed three stories: The CLT structural roof and floor components or the CLT structural wall components are incorporated into the design in a way that allows them to resist at least 75 percent of lateral forces above the second floor.
2. For buildings with three or fewer stories: The CLT structural roof and floor components or the CLT structural wall components are incorporated into the design in a way that allows them to resist at least 75 percent of lateral forces above the first floor.

The sales and use tax provisions begin on July 1, 2016, and expire on July 1, 2023.

#### Joint Legislative Audit and Review Committee Review.

The bill contains a tax preference performance statement requiring the Joint Legislative Audit Review Committee to evaluate the number of businesses claiming the B&O tax deduction; the number of taxpayers who benefit from the sales and use tax exemptions; and the number of construction projects that qualify for the sales and use tax exemptions.

#### **Substitute Bill Compared to Original Bill:**

The substitute bill limits the sales and use tax exemption in the bill to just the construction of the CLT buildings, and not to the repairing, decorating, or improving, of CLT buildings, clarifies that the business and occupation tax deduction only applies to the actual manufacturer of CLT product, and adds in proper cross-references.

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**Appropriation:** None.

**Fiscal Note:** Available.

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

#### **Staff Summary of Public Testimony:**

(In support) There is currently not a CLT market in Washington, but supporting one would have multiple benefits, including an opportunity to keep forests working and to address the ongoing forest health crisis. The manufacturers of CLT need access to small diameter fiber, which is often the wood that is removed in forest health treatments. An active CLT market will save the state money in forest fire prevention and suppression costs. A tax preference for CLT is not a silver bullet, but is a good step forward.

Potential CLT manufacturers are doing their due diligence in deciding if it makes sense to invest in a Washington-based manufacturing facility. Washington is well positioned to take advantage of the growing market in CLT, but a tax preference will help justify the needed investments.

Improving the outlook for using alternative construction materials helps the entire forest products industry, including the growers, harvesters, and transporters. Washington is falling behind the rest of the world, including Canada, in the use of these materials. Cross-laminated timber product merges nicely in projects with traditional brick and masonry construction.

(Opposed) No one construction material should be given a preference or incentive over other materials. When one is, it puts the other materials at a competitive disadvantage. This includes masonry, steel, and aluminum. Construction experts and local building codes should dictate which materials are the best suited for a project and not have that expertise colored by an artificial incentive in the market.

The brick and masonry industry is an industry that is proven in the market and creates jobs. The reality of what masonry is, and that it is extremely heavy, means that it is almost always created locally and has minimal shipping costs. Less shipping means less transportation impacts and less greenhouse gas emissions. Masonry is an environmentally friendly product, especially when compared with timber products that necessarily have to kill trees in order to be produced. Masonry is frequently recycled and is as sustainable of a product as there is on the market, compared to wood products which will ultimately rot and release carbon into the atmosphere.

A tax preference for CLT does not support local forestry businesses. Instead it supports large, out-of-state businesses that produce the product.

**Persons Testifying:** (In support) Representative Blake, prime sponsor; Lauren Burnes, Washington Department of Natural Resources; and Tim Boyd, Vaagen Brothers Lumber.

(Opposed) Tonia Sorrell-Neal, Masonry Institute of Washington and Rick Crooks, Mutual Materials.

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