HOUSE BILL REPORT
ESSB 5201

As Reported By House Committee On:
Trade & Economic Development

Title: An act relating to sales and use tax on manufacturing machinery and equipment, pollution control equipment, and high technology research and development.

Brief Description: Providing tax exemptions for manufacturing and processing.

Sponsors: Senate Committee on Ways & Means (originally sponsored by Senators Bauer, Cantu, McAuliffe, Haugen, Winsley, Snyder, Loveland, Sheldon, Fairley, West, Long, Palmer, Schow, Moyer, Sellar, Rasmussen, Deccio, Heavey, Quigley, C. Anderson, Oke, Roach and Hale; by request of Governor Lowry).

Brief History:
Committee Activity:
Trade & Economic Development: 3/29/95, 3/30/95 [DP].

HOUSE COMMITTEE ON TRADE & ECONOMIC DEVELOPMENT

Majority Report: Do pass. Signed by 10 members: Representatives Van Luven, Chairman; Radcliff, Vice Chairman; D. Schmidt, Vice Chairman; Sheldon, Ranking Minority Member; Backlund; Ballasiotes; Hatfield; Hickel; Sherstad and Skinner.

Minority Report: Do not pass. Signed by 2 members: Representatives Mason and Valle.

Staff: Kenny Pittman (786-7392).

Background: The state of Washington's tax structure imposes a sales tax on each retail sale of most articles of tangible personal property and certain services. Taxable sales include construction, repair, and the materials and labor used to alter or improve real or personal property. The state imposes a use tax on items used in this state, the acquisition of which was not subject to the retail sales tax, including purchases in other states, purchases from sellers who do not collect Washington sales tax and items produced for use by the producer.

The retail sales and use taxes are equal and is based on the value of the property or service. These taxes are imposed by both the state (6.5 percent) and the local government (up to 1.7 percent).

The state has developed retail sales and use tax relief programs and a business and occupation tax credit program as incentives to encourage the location or expansion of manufacturing and research and development firms in Washington.

Distressed Area Tax Deferral

The distressed area tax deferral program was created in 1985 to encourage economic development in areas with unemployment rates that are 20 percent higher than the state average. Businesses involved in manufacturing, research and development, and computer-related services are given a deferral on their sales and use taxes on buildings, machinery and equipment, and construction or installation labor.

To be eligible for the tax deferral, the business must create at least one job per $750,000 of investment. The tax deferral also applies to: (1) expansion of an existing eligible facility where the costs of the improvement exceeds 25 percent of the value of the facility prior to improvement; and (2) cogeneration projects that are integral to the manufacturing facility and be at least 50 percent owned by the manufacturer. The deferred taxes are forgiven if the project meets the program requirements during the 5-year repayment period.

New Business Tax Deferral

The new business tax deferral program was created in 1986 to encourage the location of new businesses state-wide. The program is targeted to businesses not located in the state prior to 1985 and involved in manufacturing and research and development. The sales and use taxes on new buildings, equipment and machinery, and installation labor is deferred for a 3-year period after completion of the project. The deferred taxes are repayed over a 5-year period. The new business tax deferral program is scheduled to terminate July 1, 1998

High Technology Tax Deferral

The high technology tax deferral was created in 1994 to encourage the location, expansion, and development of "high-tech" research and development and pilot scale manufacturing businesses state-wide. The business must be involved in biotechnology, advanced computing, electronic device technology, advanced materials, or environmental technology. The sales and use taxes on new or expanded structures, machinery and equipment, and installation or construction labor and services are deferred for a 3-year period after completion of the project. The deferred taxes are repayed over a 5- or 6-year period.

In 1994, the Legislature directed the Department of Revenue to study the impact of the state’s sales and use tax structure on manufacturers. The department, through its advisory committee, reviewed the existing tax structure and the economic and other effects of tax relief.

Summary of Bill: A state-wide sales and use tax exemption on machinery and equipment used by manufacturers is provided and the state's existing sales and use tax relief programs are revised.

State-Wide Tax Exemption

A state-wide sales and use tax exemption program is created. Sales of new and replacement machinery and equipment used directly in the manufacturing operation, including installation labor and services, and sales of pollution control equipment to be used in the manufacturing facility, including installation labor and services, are exempt from sales and use taxes.

The term "manufacturing operation" does not include research and development, cogeneration or the production of electricity, or the preparation of food products on the premises of a person selling food at retail.

Distressed Area Tax Deferral

The distressed area tax deferral program is revised. All machinery and equipment, including installation labor and services, that is eligible for the state-wide exemption is exempt from sales and use taxes regardless if the project continues to meet the program criteria during the 5-year repayment period.

The requirement that the business create at least one job per $750,000 of investment in buildings or machinery and equipment is eliminated except for projects in community empowerment zones and counties that are contiguous to eligible counties.

The tax deferral eligibility requirements are revised to require: (1) eligible cogeneration projects to generate power that is totally consumed within the manufacturing site; and (2) expansion or renovation of a facility to increase the floor space or production capacity to qualify rather than cost more than 25 percent of the value of the existing facility.

Businesses currently in the program do not have to repay deferred taxes, that have not been repaid, on machinery and equipment for lumber and wood products industries, including installation labor and services, of the type that qualifies for that state-wide sales and use tax exemption.

New Business Tax Deferral

The new business tax deferral program for buildings and machinery and equipment, including installation labor and services, for businesses not involved in manufacturing and research and development activities in the state prior to 1985, is terminated December 31, 1995.

High-Technology Tax Deferral

All taxes deferred under the high-technology tax deferral program need not be repaid. If a portion of the facility is used for other than qualified research and development, or pilot scale manufacturing during the 8-year period following completion of the facility, a pro-rated share of the deferred taxes must be repaid with interest. All machinery and equipment, including installation labor and services, that is eligible for the state-wide exemption is exempt from sales and use taxes regardless if the project continues to meet the high-tech program requirements.

Projects involving an expansion or renovation must increase the floor space or production capacity of an existing structure to qualify for a tax deferral. The requirement that the expansion or renovation cost of an existing structure be greater than 25 percent of the value of the existing facility is removed.

The legislative fiscal committees are required to analyze the economic impacts of the manufacturers' tax exemptions and report the findings to the Legislature by December 1, 1999

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill contains an emergency clause and takes effect July 1, 1995.

Testimony For: Washington has to take an aggressive role to retain and attract manufacturing. These are the jobs that pay the highest wages. This bill levels the playing field with surrounding states that do not charge taxes on these type of investments. The committee needs to include the House language that creates an account or fund to reimburse local governments for loss revenue as a result of the sales and use tax exemption.

Testimony Against: None.

Testified: (Pro) Senator Al Bauer, Sponsor; Senator Emilio Cantu, Sponsor; Robert Osmun, Kyocera; Bob Levin and Robert Schaefer, Columbia River Economic Development Council; John Osjrowski, city of Vancouver; Mike Loggins, SEH-America; Mel Gordon, Clark County Commissioner; Lanny Cawley, Port of Kalama;

Joseph Pinzone, Sharp Micro Electronics; Tom Dooley, Association of Washington Business; and (Pro w/ concerns) Stan Finkelstein, Association of Washington Cities.