SENATE BILL REPORT

E2SHB 1024

As of April 3, 1995

Title: An act relating to tax exemptions for manufacturing and processing.

Brief Description: Providing tax exemptions for manufacturing and processing.

Sponsors: House Committee on Finance (originally sponsored by Representatives Van Luven, Foreman, B. Thomas, Lisk, Horn, Chandler, Casada, Dyer, Ballasiotes, Silver, Cooke, Brumsickle, Carlson, Sehlin, Sherstad, Dellwo, Benton, Skinner, Kremen, Hargrove, Costa, Delvin, Schoesler, Buck, Johnson, Thompson, Beeksma, Goldsmith, Radcliff, Hickel, Backlund, Crouse, Cairnes, Elliot, Reams, Pennington, Mastin, Mitchell, Conway, Quall, Ogden, Chappell, Regala, G. Fisher, Basich, Grant, Campbell, Smith, Robertson, Honeyford, Pelesky, Hankins, Koster, Lambert, D. Schmidt, Mulliken, Boldt, McMorris, Clements, Fuhrman, Sheldon, L. Thomas, Huff, Mielke, Talcott, McMahan, Stevens, Morris and Hymes).

Brief History:
Committee Activity: Ways & Means: 4/3/95.

SENATE COMMITTEE ON WAYS & MEANS

Staff: Terry Wilson (786-7715)

Background: The sales tax is imposed on each retail sale of most articles of tangible personal property and certain services. Taxable services include construction, repair, telephone, lodging of less than 30 days, physical fitness, and some recreation and amusement services. Materials and labor used to alter or improve real or personal property is subject to the tax. Exempt from tax are purchases for resale and purchases of components and ingredients that become part of another product for sale.

Three sales and use tax deferral programs have been enacted to encourage the location of business in Washington.

The Distressed Area Deferral Program targets areas with unemployment rates 20 percent higher than the state average. Manufacturing, research and development, and computer-related businesses may defer sales and use taxes on buildings, machinery and equipment, and installation labor. The business is required to create at least one job per $750,000 of investment. Expansion of an existing facility is eligible if the cost of the expansion exceeds 25 percent of the existing facility. To be eligible, a cogeneration project must be integral to the manufacturing facility and be at least 50 percent owned by the manufacturer. The deferred taxes are forgiven if the investment project meets the program criteria during the repayment period.

The New Business Deferral Program is available statewide to manufacturing and research and development firms that were not doing business in the state prior to 1985. The sales and use tax on new buildings, equipment and machinery, and installation labor is deferred for a three-year period after completion of the project. The business is required to repay the deferred taxes over a five-year period.

The High Technology Deferral Program is available statewide to businesses involved in "high-tech" research and development and pilot scale manufacturing. The business must be involved in biotechnology, advanced computing, electronic device technology, advanced materials, or environmental technology. These businesses may defer sales and use taxes on buildings, machinery and equipment, and installation labor. The sales and use tax is deferred for a three-year period after completion of the project. The business is required to repay the deferred taxes over a five- or six-year period.

In 1994, the Legislature directed the Department of Revenue to study the impact of the current state tax structure on the manufacturing industry.

Summary of Bill: A statewide sales and use tax exemption is provided and the state's sales and use tax deferral programs are revised as follows.

Sales Tax Exemption. Sales of new and replacement machinery and equipment used directly in the manufacturing process, or in potato-packaging operations, including installation labor and services, and sales of pollution control equipment to be used in a manufacturing facility, including installation labor and services, are exempt from sales and use taxes.

Manufacturing process does not include research and development activities, the production of electricity, or the preparation of food products on the premises of a person selling food at retail.

The state may reimburse local governments for the loss of local sales and use tax revenue due to the statewide tax exemption on manufacturing machinery and equipment. Reimbursements are limited to losses that exceed 5 percent of the local government's sales and use tax revenue.

Distressed Area Tax Deferral. Sales of machinery and equipment, including installation labor and services, used in businesses located in distressed areas are exempt from sales and use taxes whether or not the project continues to meet the program criteria during the repayment period.

The distressed area tax deferral requirement that businesses create one job per $750,000 of investment in buildings, machinery and equipment or cogeneration projects, including labor and services, is repealed. Eligible cogeneration projects are limited to projects that generate power for consumption within the manufacturing site. The job per investment requirement is retained for projects located in community empowerment zones and counties that are contiguous to eligible counties.

An expansion or renovation must increase the floor space or production capacity of an existing structure to qualify rather than costing more than 25 percent of the value of the existing facility.

New Business Tax Deferral. The New Business Tax Deferral Program for buildings and machinery and equipment, including labor, for businesses not involved in manufacturing and research and development activities in the state prior to 1985, is terminated December 31, 1995, instead of December 31, 1998.

High Technology Tax Deferral. The high technology tax deferral is extended to all research and development activities. Taxes deferred under the program need not be repaid. However, if a portion of the facility is used for other than research and development or pilot scale manufacturing during the eight years following completion of the facility, a pro-rated share of the taxes must be repaid with interest. However, no repayment is required on machinery and equipment exempt from sales tax under this act.

An expansion or renovation must increase the floor space or production capacity of an existing structure to qualify rather than costing more than 25 percent of the existing facility.

The Department of Revenue must conduct a study on the effects of the statewide tax exemption program. The results are to be reported to the Governor and Legislature by September 1, 1998.

The Department of Revenue is directed to adopt rules to implement the programs.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill contains an emergency clause and takes effect on July 1, 1995. However, the reimbursement of local sales tax losses is null and void if not funded in the budget.