SENATE BILL REPORT

SB 5168

As Reported By Senate Committee On:
Agriculture & Rural Economic Development, February 22, 1999

Title: An act relating to distressed area programs.

Brief Description: Encouraging economic development in distressed areas.

Sponsors: Senators T. Sheldon, Rasmussen, Swecker, Franklin, Hargrove, Honeyford, Patterson, Morton, Haugen, Benton, Goings, Snyder, Zarelli and McCaslin.

Brief History:

Committee Activity: Agriculture & Rural Economic Development: 2/22/99 [DPS-WM]
Ways & Means: 3/1/99.

SENATE COMMITTEE ON AGRICULTURE & RURAL ECONOMIC DEVELOPMENT

Majority Report: That Substitute Senate Bill No. 5168 be substituted therefor, and the substitute bill do pass and be referred to Committee on Ways & Means.
Signed by Senators Rasmussen, Chair; T. Sheldon, Vice Chair; Gardner, Honeyford, Morton, Prentice, Snyder and Swecker.

Staff: David Schumacher (786-7474)

SENATE COMMITTEE ON WAYS & MEANS

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Background: The retail sales tax is imposed on the sale of most items of tangible personal property and some services purchased at retail. The state's retail sales and use tax is based on 6.5 percent of the selling price. Local governments may also impose additional taxes; therefore the combined state and local retail sales and use tax rate currently ranges from 7.0 percent to 8.6 percent

<u>Distressed Area Tax Incentives</u>. Washington has developed various incentives that are designed to assist in job creation or retention in economically distressed areas. To be eligible, a business must be in either the manufacturing, research and development or computer-related service industry. There are currently seven (often overlapping) categories of eligibility for distressed area sales and/or business and occupation tax relief.

Category 1 - Businesses in counties with average unemployment 20 percent higher than the state average for the previous three years receive both the sales and the B&O tax incentives.

Category 2 - Businesses in counties in a metropolitan statistical area (MSA) with unemployment 20 percent higher than the state average for the previous year receive both the sales and the B&O tax incentives.

Category 3 - Businesses in counties designated by the Governor as eligible due to a sudden and severe increases in unemployment resulting from a natural disaster, military base closure or mass layoff of a major employer receive both the sales and the B&O tax incentives.

Category 4 - Businesses in counties with median household income less than 75 percent of the state average for the previous three years receive only the sales tax incentive.

Category 5 - Businesses in counties that are contiguous to counties that are eligible under Category 1 or 4 are eligible for only the sales tax incentive if they fill 75 percent of new jobs with residents from the contiguous county.

Category 6 - Businesses in counties that contain community empowerment zones (CEZs) are eligible under Category 1 or 4 for the sales tax incentive only if they fill 75 percent of new jobs with residents from within the CEZ.

Category 7 - Businesses in towns with populations less than 1,200 persons located in a timber impact area.

Revenue Source for Distressed Counties. In 1997, the Legislature passed 2SSB 5740 which allowed distressed counties to levy a 0.04 percent sales tax which was credited against the state. Revenues from this tax may be used for public facilities.

In 1998, the voters passed Referendum 49 which distributes a portion of the motor vehicle excise tax (MVET) to distressed counties in proportion to the 0.04 percent sales tax credit. These revenues may be broadly used for criminal justice and other purposes.–

Warehouses. In 1996, SHB 2708 directed the Department of Revenue to undertake a comprehensive warehouse and distribution study. In 1997, 2SSB 5174 provided sales tax incentives to large warehouse operations. These include wholesalers, third-party warehousers, grain elevator operators and retailers who own or operate a distribution center.

Eligible warehouse operations may receive tax incentives on material handling and racking equipment; labor and services rendered in installing, repairing, cleaning, altering, or improving the equipment; and construction including materials, service and labor costs.

Warehouses over 200,000 square feet are exempt on 50 percent of machinery and equipment purchases and 100 percent of construction costs. Grain elevators larger than two million bushels receive a 50 percent sales and use tax exemption on machinery and equipment and 100 percent on construction. (Grain elevators with capacities between one million and two million bushels receive a 50 percent sales and use tax exemption on machinery, equipment and construction.)

Utility Revolving Fund. Public- and privately-owned utilities are subject to the public utility tax instead of the business and occupation (B&O) tax. Like the B&O tax, the public utility tax is applied to the gross receipts of the business.

Competitive Generating Facilities. In 1995, the Legislature passed 2ESSB 5201 which included a sales tax exemption for new machinery and equipment (M&E) used directly in the manufacturing process. Currently, the production of electrify is not considered to be "manufacturing."

Summary of Substitute Bill: Distressed Area Tax Incentives. The eligibility requirements are significantly changed for distressed area sales and/or business and occupation tax relief. The current seven categories are converted into a single category based on a definition of rural– population density. Businesses in counties with populations per square mile of 100 or less are allowed both the sales tax and B&O exemption.

Eligibility based on the contiguous county– definition (Category 5 above) and the CEZ– definition (Category 6) is no longer allowed.

Revenue Source for Distressed Counties. The current 0.04 percent sales tax credit for distressed counties is increased to 0.08 percent. The additional revenue may only be used for financing public facilities that are part of a county's economic development plan.

Help Desks. B&O tax credits are provided to businesses in rural counties engaged in the business of providing information technology "help desk" services to third parties. The credit is equal to 100 percent of B&O taxes due for the first seven years and 68 percent every year thereafter. In addition, a retail sales tax exemption is provided for construction, machinery and equipment.

Software Companies. A $1,000 per job B&O tax credit is provided for new software manufacturing or software programing jobs created in rural counties. The credit may last up to six years if the position is maintained.

Utility Revolving Fund. A 50 percent public utility tax credit is offered for light and power businesses that contribute to an "electric utility rural economic development revolving fund." These funds may only be used for qualifying "non electrical infrastructure" projects in rural areas. The tax credits expire in 2005. To qualify for the credit, the business must establish a local board to determine the criteria and conditions for the expenditure of the funds.

Warehouses. Tax incentives are provided to smaller warehouses (those with square footage between 100,000 and 200,000 square feet) or "controlled atmosphere" warehouses over 40,000 square feet, if they locate in a rural county. The tax exemption is equal to 100 percent of the construction costs and 50 percent of the costs for material handling and racking equipment.

Competitive Generating Facilities. Certain electrical generating facilities in rural counties are included within the definition of manufacturing for purpose of the sales tax exemption for machinery and equipment.

Substitute Bill Compared to Original Bill: The substitute bill added the provisions for help desk companies, software companies, warehouses, the utility revolving fund, and the competitive generating facilities.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill takes effect on August 1, 1999.

Testimony For: It is a good idea to simplify the tax programs by basing them on a definition of "rural" based on population density. The increased sales tax credit is just what local governments need to make local decisions to invest in needed infrastructure projects.

Testimony Against: None.

Testified: PRO: Mary Hunt, Douglas County Commissioner; Bill Vogler, Association of Counties; Bill Lotto, Lewis Co EDC; Don White, Association of Economic Development Councils; Scott Taylor, WA Public Port Assn.; Tom Dooley, AWB; Ron Rosenbloom, AWC; Corey Balkan, Cowlitz, EDC; Lynn Micheau, Grays Harbor, EDC.