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**Finance Committee**

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**HB 3222**

**Brief Description:** Modifying excise tax exemptions for the handling and processing of livestock manure.

**Sponsors:** Representatives Pettigrew, Haler, Chandler, Kretz, Hinkle, Kristiansen, Holmquist and Linville.

**Brief Summary of Bill**

- Changes the existing retail sales and use tax exemptions for dairy nutrient management facilities and anaerobic digesters to a remittance program in which only the state portion of the tax is exempt.
- Expands the coverage of the exemptions for dairy nutrient management facilities and anaerobic digesters to include certain other livestock operations.

**Hearing Date:** 2/1/06

**Staff:** Mark Matteson (786-7145).

**Background:**

*Retail sales and use tax.* The retail sales tax applies to the selling price of tangible personal property and of certain services purchased at retail. The use tax applies if retail sales tax has not been collected. Both the state and local governments impose sales and use taxes; the state rate is 6.5 percent and the average local rate is 2 percent statewide. Sales taxes are collected by the seller from the buyer at the time of sale. Use tax is remitted directly to the Department of Revenue (Department). State revenues are deposited to the state general fund.

*Water pollution control and animal feeding operations.* The Federal Clean Water Act (CWA) provides that the discharge of pollutants from point sources to surface waters is unlawful except in accordance with a National Pollutant Discharge Elimination System (NPDES) permit. The State Water Pollution Control Act requires any person who conducts a commercial or industrial operation which results in the disposal of liquid or solid waste material into waters of the state to obtain a permit. Waters of the state include both surface and ground waters.

Animal feeding operations (AFOs) are agricultural enterprises where animals are kept and raised in confined situations. AFOs congregate animals, feed, manure and urine, dead animals, and production operations on a small land area. feed is brought to the animals rather than the animals grazing or otherwise seeking feed in pastures, fields, or on rangeland. There are approximately

450,000 AFOs in the United States. Concentrated animal feeding operations (CAFOs) are a relatively small number of AFOs that are regulated by the U.S. Environmental Protection Agency (EPA).

*Dairy nutrient management and anaerobic digesters.* In 1998, the Legislature enacted the Dairy Nutrient Management Act (Act) to address water quality concerns associated with dairy farm nutrients. The legislation required that each dairy farm in the state develop and implement a nutrient management plan (NMP) that met standard specifications by December 31, 2003. Plans included both physical and management elements. Physical elements included items such as pumps, pipes, spray guns, lagoons, concrete pads and structures, gutters and downspouts.

In 2001, the Legislature approved a retail sales and use tax exemption to help dairy farmers comply with the Act. Once a dairy nutrient management plan has been certified as fully implemented, the purchase of services, replacement equipment and parts necessary to maintain the plan are exempted from the retail sales and use tax. The same 2001 legislation also provided an exemption for the acquisition of anaerobic digesters for the primary purpose of treating dairy manure. Anaerobic digesters are facilities that use bacteria to process manure into biogas and dried manure in the absence of oxygen.

*Recent regulatory activity.* Since 2003, there have been statutory and rule changes at the state and federal levels that broaden dairy nutrient management requirements to also encompass certain livestock operations. In February 2003, the EPA adopted rules affecting how AFOs and CAFOs would be regulated for the purposes of controlling water pollution. These rules expanded the type and number of CAFOs required to obtain NPDES permits.

In February 2005, the Federal 2nd Circuit Court (Court) of Appeals issued a ruling that overturned aspects of the 2003 EPA rule. The Court vacated rule provisions that allow permitting authorities to issue permits to CAFOs without including the terms of the CAFO's NMP in the permit and without the NMP being reviewed by the permitting agency and available to the public. The Court also invalidated the provision that requires all CAFOs to apply for an NPDES permit unless they can demonstrate that they have no potential to discharge. The Court found that the "duty to apply" provision, which the Agency had based on a presumption that all CAFOs have at least a potential to discharge, was invalid, because the CWA subjects only actual discharges to regulation rather than potential discharges.

In response to the EPA rule change and the court ruling, the Department of Ecology (DOE) is developing a general CAFO NPDES permit to become effective in early 2006. The general permit will require large and certain medium CAFOs to develop and implement nutrient management plans by December 31, 2006.

### **Summary of Bill:**

The sales and use tax exemptions concerning dairy nutrient management equipment and anaerobic digesters are repealed and replaced with an exemption-remittance program that is broader in its applicability but which exempts only the state portion of the retail sales and use tax.

Under the program, eligible persons must first pay retail sales or use tax on qualifying project equipment or services and then apply to the Department for a remittance of the state portion of the tax. The Department must remit exempted amounts on a quarterly basis to eligible persons who have applied.

Eligible persons are:

- licensed dairies with certified dairy nutrient management plan;
- animal feeding operations with a state waste discharge permit;
- persons establishing or operating anaerobic digesters to treat livestock manure; and
- large or medium CAFOs with nutrient management plans verified by a conservation district as meeting natural resource conservation service practice standards.

The Conservation Commission is required to provide a list of eligible persons that are large or medium CAFOs with NMPs that have been verified by a conservation district as meeting natural resource conservation service practice standards. The Department of Agriculture must provide a list of eligible persons in the other categories to the Department of Revenue.

Qualifying projects are:

- livestock nutrient management equipment and facilities, including services rendered in respect to operating, repairing, cleaning, altering or improving the facilities; and
- anaerobic digesters, including services rendered in respect to installing, constructing, repairing, cleaning, altering, or improving the facilities.

Livestock nutrient management equipment and facilities qualify for exemption only if used exclusively for the purpose of a NMP. An exemption on such equipment or facilities is available only after the NMP is certified under state law, approved as part of a state water pollution control permit, or verified by a conservation district as meeting natural resource conservation service practice standards. Anaerobic digesters qualify for exemption only if they are used primarily to treat livestock manure.

The buyer is required to submit an information sheet to the Department on a quarterly basis specifying the amount of exempted tax claimed and the qualifying project for which the exemption is claimed. The buyer is required to maintain records to allow the Department to verify eligibility.

The amount of remittances that may be claimed in any fiscal year by large or medium CAFOs with NMPs that have been verified by a conservation district may not exceed \$200,000. If a remittance is disallowed because the cap is exceeded, the disallowed portion may be carried over.

**Appropriation:** None.

**Fiscal Note:** Requested on January 27, 2006.

**Effective Date:** The bill takes effect on July 1, 2006 .