VETO MESSAGE ON SB 6117

January 22, 1996

To the Honorable President and Members,
The Senate of the State of Washington

Ladies and Gentlemen:

I am returning herewith, without my approval as to Senate Bill No. 6117 entitled:

"AN ACT Relating to reducing business and occupation taxes by reducing the 1993 service rate increases by fifty percent and increasing tax credits in distressed areas;"

At a time of strong demands on our state's financial resources and expectations of significant reductions in federal support for state programs in future years, Senate Bill No. 6117 would reduce state revenues more than any other tax measure currently under consideration by the state legislature « by $132.4 million in the 1995-97 Biennium and $216.6 million in the 1997-99 Biennium. Moreover, as apportioned by this bill, these reductions are not targeted to create family-wage jobs, correct inequities in the state's tax code, or improve our state's overall economy.

It is important to remember that although the state currently anticipates a reserve of $677 million under the biennial budget approved last June, only $118 million of this amount is from surplus revenues projected in the 1995-97 Biennium. The remainder is a one-time surplus carried forward from the previous biennium and does not represent an ongoing flow of excess revenues. We must maintain a prudent reserve for the future.

Sections 1 and 2 of Senate Bill No. 6117 reduce the Business & Occupation (B&O) tax rate for the three classifications of service firms in the state. The B&O tax rate for selected business services– is reduced from 2.5 percent to 2.0 percent. The B&O tax rate for financial services– is reduced from 1.7 percent to 1.6 percent, and the rate for other services– and real estate brokers is reduced from 2.0 percent to 1.75 percent. The reductions represent a 50 percent roll-back of the increase for these categories enacted in 1993. The estimated revenue loss on a cash basis associated with sections 1 and 2 of this bill is $129.2 million in the 1995-97 Biennium and $211.2 million in the next biennium.

While I support extending additional tax incentives to business this year, I believe these measures must be carefully targeted to produce the greatest possible economic return for our state. Targeted tax initiatives, such as tax exemptions on the purchase or repair of machinery and equipment, will do much more to spur further investment in our state's important manufacturing sector and draw new employers to our state than will a simple tax cut for certain service industries. Historically, each new job created in manufacturing generates two additional jobs elsewhere in our economy. Service industries, by contrast, generate less than one additional job for every new job added to that sector « and Senate Bill No. 6117 provides no inducement for those businesses to create the additional family-wage jobs essential to our state's economic development.

I also believe that any tax initiatives that reduce state revenues should be targeted to help those businesses and individuals who need it most. If this bill was meant to help new or small businesses such as barber shops or janitorial services, it misses the mark. More than three-quarters of the tax cut proposed by this measure would go to large companies involved in banking, law, medicine, and engineering.

Sections 3 and 4 of Senate Bill No. 6117 would provide or expand B&O tax credits for certain business activities, with an estimated reduction of $3.2 million in revenues during the 1995-97 Biennium and $5.4 million in the next biennium. Although I support the general intent of these provisions, I have not approved these sections for the reasons stated below.

Section 3 of Senate Bill No. 6117 increases the distressed area B&O tax credit in chapter 82.62 RCW from $1,000 to $2,000 for each qualified employment position created in an eligible business project approved after January 1, 1996. Eligible businesses are those engaged in manufacturing, research and development activities, or computer services. Current law caps the program for all participants at $15 million in tax credits per biennium, and any single employer is limited to a total of $300,000 dollars of credit during the life of the program.

The legislature’s goal through increasing the tax credit allowed for each new employment position created under chapter 82.62 RCW appears to be to expand participation in the program. However, the state’s experience has shown that the primary constraint on business participation is not the size of the tax credit for each new position created, but rather the requirement that an employer increase its existing work force by 15 percent or create a new work force to qualify for the tax credit.

The Department of Revenue estimates that increasing the tax credit from $1,000 to $2,000 for each new position created would result in an additional $900,000 in credits claimed during the current biennium. However, the department also believes that most of those additional credits would be claimed by companies already participating in the program. As a result, those firms would reach the $300,000 cap more quickly, after which there would be no incentive to hire additional employees. Rather than inducing more businesses to participate in the program, the primary effect of section 3 of Senate Bill No. 6117 would be to curtail the incentive for participating businesses to hire additional employees « in direct opposition to the goal of this measure.

Section 4 of Senate Bill No. 6117 establishes a new B&O tax credit for job training provided or sponsored by employers to enhance the performance of their employees. This tax credit would be limited to businesses engaged in manufacturing, research and development activities, or computer services in distressed areas of the state. To qualify for the tax credit, training must be offered to employees without charge and must be approved by the state Employment Security Department. The credit, effective after January 1, 1996, would be limited to 20 percent of the value of the training services, and total credits for a business could not exceed $5,000 per calendar year.

Although this section stipulates that job-training activities must be approved by the Employment Security Department to qualify for the proposed tax credit, it offers no assurance that the training will produce a long-term enhancement of the employee’s skills or abilities. The language is sufficiently broad as to allow on-the-job training which employees currently receive to qualify for the credit. While I strongly support the idea of providing job-training incentives for businesses, I also believe that the state must endeavor to gain the greatest benefit possible out of each dollar of credit.

For these reasons, I have vetoed Senate Bill No. 6117 in its entirety.

Respectfully submitted,
Mike Lowry
Governor