

# HOUSE BILL REPORT

## HB 1382

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As Reported by House Committee On:  
Finance

**Title:** An act relating to the excise taxation of sales of tangible personal property originating from or destined to foreign countries.

**Brief Description:** Regarding excise taxation of sales of tangible personal property originating from or destined to foreign countries.

**Sponsors:** Representatives Ericks, Hunter, Orcutt, McIntire and Condotta; by request of Department of Revenue.

**Brief History:**

**Committee Activity:**

Finance: 1/30/07, 2/13/07 [DP].

**Brief Summary of Bill**

- Codifies the Department of Revenue's tax policies regarding the business and occupation and retail sales taxation of products in import and export commerce.

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### HOUSE COMMITTEE ON FINANCE

**Majority Report:** Do pass. Signed by 9 members: Representatives Hunter, Chair; Hasegawa, Vice Chair; Orcutt, Ranking Minority Member; Condotta, Assistant Ranking Minority Member; Conway, Ericks, McIntire, Roach and Santos.

**Staff:** Jeff Mitchell (786-7139).

**Background:**

The Import-Export Clause (IEC) of the United States Constitution contains an explicit limitation on the taxing powers of the states. The IEC prohibits any imposts or duties from being levied on imports or exports. The IEC applies to goods inbound from, or outbound to, a foreign country. Two issues need to be considered to properly analyze a tax under the IEC: (1) does the tax constitute a duty or impost; and (2) is the tax levied on a product in the process of importation or exportation.

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

In 1976, in *Michelin Tire Corp. v. Wages*, the United States Supreme Court dramatically shifted its analysis of the IEC. Prior to *Michelin*, any tax levied on imports or exports was considered an impost or duty. The bulk of the analysis in pre-*Michelin* cases addressed whether the products were still in transit, and therefore considered products in the process of importation or exportation. The court in *Michelin* identified the three principal concerns of the Constitutional Framers with respect to the IEC: (1) the federal government must speak with one voice when conducting foreign policy, and a state tax could interfere in these efforts; (2) import revenues are to be the major source of revenue for the federal government and should not be diverted to the states; and (3) harmony among the states might be disturbed unless seaboard states, with their crucial ports of entry, are prohibited from imposing taxes on goods transported to inland states. After *Michelin*, if a tax does not offend any of these elements, it is not considered an impost or duty. This analysis limits the scope of the IEC.

The Department of Revenue's (DOR) tax policies regarding goods in import and export commerce are implemented in Rule 193C (WAC 458-20-193C). Rule 193C provides business and occupation (B&O) and retail sales exemptions for goods in the process of being imported or exported from this state. The rule has not been amended in more than 20 years, and has been generally administered in the same manner since at least the 1950s. As described above, the United States Supreme Court in recent decades has narrowed the scope of the IEC. Furthermore, the Washington State Supreme Court decisions have cast doubt on the DOR's ability to implement any rule that expands tax immunity beyond that found in statute.

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### **Summary of Bill:**

The tax policies under Rule 193C are codified in statute. Tangible personal property (TPP) in import or export commerce is exempted from B&O and retail sales taxation.

The TPP is in the process of import commerce if the TPP is moving through this state to a destination outside the state or the TPP is in the process of being delivered to a buyer in this state. The TPP is no longer in the process of import transportation if the property is:

- (1) put to actual use;
- (2) resold after the property has arrived in this state or any other state; or
- (3) processed in any way not related to shipping.

The TPP is in export commerce when the seller delivers the property to:

- (1) the buyer at a destination in a foreign country;
- (2) a carrier for transportation to a foreign country;
- (3) the buyer at shipside or aboard the buyer's vessel, or any other vehicle of transportation, where it is clear that the process of exportation of the property has begun; or
- (4) the buyer in this state if the property is capable of being transported to a foreign destination under its own power, the seller files a shipper's export declaration, and the property is directly transported to a destination in a foreign country.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill takes effect 90 days after adjournment of session in which bill is passed.

**Staff Summary of Public Testimony:**

(In support) This is a status quo bill. It is intended to codify the DOR's current policy regarding the taxation of imports and exports. Currently, import and export sales are exempt from B&O and retail sales tax. There is no specific statute that exempts imports and exports from taxation. The only restriction is the IEC. Over time, the United States Supreme Court has changed its analysis of the IEC. Recent decisions have brought the continued validity of the rule into question. The Washington State Supreme Court has twice cited Rule 193C as a rule that unlawfully creates a tax exemption. Only the Legislature can create an exemption. If Rule 193C were found to be invalid, many businesses would have large tax bills. The DOR estimates that importers alone would owe over \$60 million in taxes. This would have three effects: it would damage the reputation of Washington as a leader in international trade; it would drive business to ports outside the State of Washington; and it would increase cost of goods to Washington consumers.

(In support with concerns) Generally, my clients are in favor of the concept of the bill. We disagree with the DOR regarding the current state of the law. We feel that Rule 193C is still constitutionally mandated. Codifying the rule is a good idea. We have one technical concern. The language in the bill is slightly different than in the administrative rule. On its face, it doesn't appear to be different than the rule. A change in language creates a change in meaning and therefore we would ask for an amendment to create parallel language.

(Opposed) None.

**Persons Testifying:**

(In support) Representative Ericks, prime sponsor; and Gil Brewer, Department of Revenue.

(In support with concerns) Scott Edwards, Perkins Cole.

**Persons Signed In To Testify But Not Testifying:** None.