

WSR 16-02-057
EXPEDITED RULES
DEPARTMENT OF REVENUE

[Filed January 4, 2016, 8:58 a.m.]

Title of Rule and Other Identifying Information:

- WAC 458-20-169 (Rule 169) Nonprofit organizations, reviews how the B&O tax, retail sales tax, and use tax apply to activities often performed by nonprofit organizations.
- WAC 458-20-272 (Rule 272) Tire fee—Core deposits or credits, describes the tire fee and the B&O, sales, and use tax consequences related to battery core charges and core deposits or credits.

NOTICE

THIS RULE IS BEING PROPOSED UNDER AN EXPEDITED RULE-MAKING PROCESS THAT WILL ELIMINATE THE NEED FOR THE AGENCY TO HOLD PUBLIC HEARINGS, PREPARE A SMALL BUSINESS ECONOMIC IMPACT STATEMENT, OR PROVIDE RESPONSES TO THE CRITERIA FOR A SIGNIFICANT LEGISLATIVE RULE. IF YOU OBJECT TO THIS USE OF THE EXPEDITED RULE-MAKING PROCESS, YOU MUST EXPRESS YOUR OBJECTIONS IN WRITING AND THEY MUST BE SENT TO Gayle Carlson, Department of Revenue, P.O. Box 47453, Olympia, WA 98504-7453, e-mail GayleC@dor.wa.gov, AND RECEIVED BY March 7, 2016.

Purpose of the Proposal and Its Anticipated Effects, Including Any Changes in Existing Rules: The department is proposing revisions to:

- Rule 169 to:
 - o Reflect the use tax exemption increase for tangible personal property for values of less than \$10,000 to values of less than \$12,000 provided by RCW 82.12.225;
 - o Add B&O tax exemption (RCW 82.04.755) for grants received to fund certain education programs as provided by RCW 70.93.180 (1)(b)(ii); and
 - o Delete reference to resale certificates, as resale certificates were replaced by reseller permits effective January 1, 2010.
- Rule 272 to:
 - o Add information on the new studded tire fee of \$5.00, passed during the 2015 3rd sp. sess. (chapter 44 (2ESSB 5987)); and
 - o Revise the title of the rule to Tire fee—Studded tire fee—Core deposits or credits.

Copies of draft rules are available for viewing and printing on our web site at Rules Agenda.

Reasons Supporting Proposal: Chapter 32, Laws of 2015 3rd sp. sess. (ESB 6013), chapter 15, Laws of 2015 (ESHB 1060); and chapter 44, Laws of 2015 3rd sp. sess. (2ESSB 5987).

Statutory Authority for Adoption: RCW 82.32.300 and 82.01.060(2).

Statute Being Implemented: RCW 46.37.427 and 82.04.-755.

Rule is not necessitated by federal law, federal or state court decision.

Name of Proponent: Department of revenue, governmental.

Name of Agency Personnel Responsible for Drafting: Gayle Carlson, 1025 Union Avenue S.E., Suite #544, Olympia, WA, (360) 534-1576; Implementation and Enforcement: Marcus Glasper, 1025 Union Avenue S.E., Suite #500, Olympia, WA, (360) 534-1615.

January 4, 2016
 Kevin Dixon
 Rules Coordinator

AMENDATORY SECTION (Amending WSR 14-13-105, filed 6/17/14, effective 7/18/14)

WAC 458-20-169 Nonprofit organizations. (1) **Introduction.** Unlike ~~the tax systems of~~ most states~~((¹))~~ and the federal ~~((tax systems))~~ government, Washington's tax system, ~~((specifically))~~ including its primary business tax, applies to the activities of nonprofit organizations. Washington's business and occupation (B&O) tax is imposed ~~((upon))~~ on all entities that generate gross receipts or proceeds, unless there is a specific statutory exemption or deduction. This rule ~~((reviews))~~ explains how the ~~((business and occupation ⁽⁻⁾B&O(⁺))~~ retail sales, and use taxes apply to activities often performed by nonprofit organizations. Although some nonprofit organizations may be subject to other taxes (e.g., public utility or insurance premium taxes on income from utility or insurance activities), these taxes are not discussed in this rule. The rule describes the most common ~~((exemptions and deductions for the))~~ B&O, retail sales, and use ~~((taxes))~~ tax exemptions and deductions that are specifically provided to nonprofit organizations by state law. Other exemptions ~~((and/or))~~ or deductions not specific to nonprofit organizations may also apply.

(a) Examples. This rule contains examples that identify a number of facts and then state a conclusion. These examples should be used only as a general guide. The tax results of other situations must be determined after a review of all facts and circumstances.

(b) Other rules that may be relevant ~~((to specific activities of))~~. Rules in the following list may contain additional relevant information for nonprofit organizations ~~((include the following))~~:

~~((^(a)))~~ (i) WAC 458-20-167~~((⁽⁻⁾))~~ Educational institutions, school districts, student organizations, and private schools;

~~((^(b)))~~ (ii) WAC 458-20-168~~((⁽⁻⁾))~~ Hospitals, nursing homes, assisted living facilities, adult family homes and similar health care facilities;

~~((^(c)))~~ (iii) WAC 458-20-183~~((⁽⁻⁾))~~ Amusement, recreation, and physical fitness services;

~~((^(d)))~~ (iv) WAC 458-20-249~~((⁽⁻⁾))~~ Artistic or cultural organizations; and

~~((^(e)))~~ (v) WAC 458-20-256~~((⁽⁻⁾))~~ Trade shows, conventions and seminars.

(2) **Registration requirements.** Nonprofit organizations with \$12,000 or more per year in gross receipts from sales, and/or gross income from services subject to the B&O tax, or that are required to collect or pay to the department of reve-

nue (department) retail sales tax or any other tax or fee which the department administers (regardless of the level of annual gross receipts) must register with the department. Nonprofit organizations with less than twelve thousand dollars per year in gross receipts and that are not required to collect retail sales tax or any other tax or fee administered by the department are not required to register with the department. ~~((Refer to)) For more information on whether registration with the department is required see WAC 458-20-101 ((Tax registration and tax reporting) for more information on registration requirements)).~~

(3) **Filing excise tax returns.** Nonprofit organizations making retail sales that require the collection of ~~((the))~~ retail sales tax must file ~~((a))~~ an excise tax return, regardless of the annual level of gross receipts or gross income and whether or not any B&O tax is due. ~~((See also)) For information on when a taxpayer may qualify for a small business B&O tax credit, see WAC 458-20-104((Small business tax relief based on income of business)).~~ The excise tax return with payment is generally filed on a monthly basis. ~~((However,))~~ Under certain conditions the department may authorize taxpayers to file and remit payment on either a quarterly or an annual basis. ~~((Refer to)) For information on how reporting frequencies are assigned to taxpayers see WAC 458-20-22801 ((Tax reporting frequency) for more information regarding how reporting frequencies are assigned)).~~

Nonprofit organizations that do not have retail sales tax to remit, but are required to register, do not have to file ~~((a))~~ an excise tax return if they meet certain statutory requirements (e.g., annual gross income of less than \$28,000) and are placed on an "active nonreporting" status by the department. ~~((Refer to)) For additional information on whether an organization qualifies for the "active nonreporting" status see WAC 458-20-101 ((for more information regarding the "active nonreporting" status)).~~

(4) **General tax reporting responsibilities.** While Washington state law provides some tax exemptions and deductions specifically ~~((targeted toward))~~ for nonprofit organizations, these organizations otherwise have the same tax-reporting responsibilities as ~~((those of))~~ for-profit organizations.

(a) **Business and occupation tax.** Chapter 82.04 RCW imposes a B&O tax on every person with substantial nexus in Washington (see RCW 82.04.067) engaged in business activities within this state, unless the income is specifically exempt or deductible under state law. The B&O tax applies to the value of products, gross proceeds of sales, or gross income of the business, as the case may be. RCW 82.04.220.

(i) **Common B&O tax classifications.** Chapter 82.04 RCW provides a number of classifications that apply to specific activities. The most common B&O tax classifications applying to income received by nonprofit organizations are the retailing, wholesaling, and service~~(s)~~ and other activities classifications. RCW 82.04.250, 82.04.270, and 82.04.290. If an organization engages in more than one kind of business activity, it must report the gross income from each activity ~~((must be reported))~~ under the appropriate tax classification. RCW 82.04.440(1).

(ii) **Measure of tax.** The most common measures of the B&O tax are "gross proceeds of sales" and "gross income of

the business." RCW 82.04.070 and 82.04.080, respectively. These measures include the value proceeding or accruing from the sale of tangible personal property or services rendered without any deduction for the cost of property sold, cost of materials used, labor costs, discounts paid, delivery costs, taxes, losses, or any other expenses.

(b) **Retail sales tax.** A nonprofit organization must collect and remit retail sales tax on all retail sales, unless the sale is specifically exempt by statute. Examples of retail sales tax exemptions that may apply to nonprofit organizations are those for sales of certain food products (see WAC 458-20-244, Food and food ingredients), construction materials purchased by a health or social welfare organization for new construction of alternative housing ~~((for youth in crisis,))~~ to be licensed as a family foster home for youth in crisis (see RCW 82.08.02915), and fund-raising activities (see subsection (5)(g) of this rule). New construction includes renovating an existing structure to provide new housing for youth in crisis.

A nonprofit organization must pay retail sales tax when it purchases goods or retail services for its own use as a consumer, unless the purchase is specifically exempt by statute. Items purchased for resale without intervening use are purchases at wholesale and are not subject to the retail sales tax if the seller takes from the buyer a copy of the buyer's reseller permit. The reseller permit documents the wholesale nature of any sale. Reseller permits replaced resale certificates effective January 1, 2010. For additional information on reseller permits see WAC 458-20-102 ((Reseller permits) for more information on reseller permits and their proper use. Even though resale certificates are no longer used after December 31, 2009, they must be kept on file by the seller for five years from the date of last use or December 31, 2014)).

(c) **Use tax.** The use tax is imposed on every person, including nonprofit organizations, using tangible personal property within this state as a consumer, unless such use is specifically exempt by statute. The use tax applies only if retail sales tax has not previously been paid on the item. The rate of tax is the same as the sales tax rate that applies at the location where the property is first used.

A common application of the use tax occurs when items are purchased from an out-of-state seller who has no presence in Washington. ~~((Because))~~ When the out-of-state seller ~~((is under no obligation to))~~ does not collect Washington's retail sales or use tax, the buyer is statutorily required to remit use tax directly to the department. ~~((See))~~ For more information on use tax and the use of tangible personal property see WAC 458-20-178 ((for more information regarding the use tax)).

Except for fund-raising, use tax exemptions generally correspond to retail sales tax exemptions. For example, the use tax exemption for construction materials acquired by a health or social welfare organization for new construction of alternative housing for youth in crisis, to be licensed as a family foster home (RCW 82.12.02915) corresponds with the retail sales tax exemption described in subsection (4)(b) of this rule for purchasing these construction materials.

(i) **Use tax exemption for donated items.** RCW 82.12-02595 provides a use tax exemption for personal property donated to a nonprofit charitable organization. This exemption is available for the nonprofit charitable organization and

the donor, if the donor did not previously use the personal property as a consumer. It also applies to the use of property by a donor who is incorporating the property into a nonprofit organization's real or personal property for no charge.

The exemption also applies to another person using property originally donated to a charitable nonprofit organization that is subsequently donated or bailed to that person by the charitable nonprofit organization, provided that person uses the property in furtherance of the charitable purpose for which the property was originally donated to the charitable nonprofit organization. For example, a hardware store donates an industrial pressure washer to a nonprofit community center for neighborhood cleanup, the community center bails this washer to people enrolled in its neighborhood improvement group for neighborhood clean-up projects. No use tax is due from any of the participants in these transactions. An example of a gift that would not qualify is when a car is donated to a church for its staff and the church gives that car to its pastor. The pastor must pay use tax on the car because it serves multiple purposes. It serves the church's charitable purpose, but it also acts as compensation to the pastor and is available for the pastor's personal use. The subsequent donation of property from the charity to another person must be solely for a charitable purpose. If the property is donated or bailed to the third party for a charitable purpose in line with the nonprofit organization's charitable activities, generally, no additional proof is required that this was the charitable purpose for which the property was originally donated.

(ii) **Use tax implications with respect to fund-raising activities.** Subsection (5)(g) of this rule explains that a retail sales tax exemption is available for certain fund-raising sales. However, there is usually no comparable use tax exemption provided to the buyer/user of property purchased at these fund-raising sales. While the nonprofit organization is not obligated to collect use tax from the buyer, the organization is encouraged to inform the buyer of the buyer's possible use tax obligation.

(iii) ~~(Effective)~~ From October 1, 2013, through October 8, 2015, RCW 82.12.225 ((provides)) provided a use tax exemption for the use of any article of personal property, valued at less than ten thousand dollars, purchased or received as a prize in a contest of chance, as defined in RCW 82.04.285, from a nonprofit organization or a library. Effective October 9, 2015, chapter 32, Laws of 2015 3rd Sp. Sess. (ESB 6013), the exemption applies to qualifying personal property valued at less than twelve thousand dollars. This exemption only applies if the gross income from the sale by the nonprofit organization or library is exempt under RCW 82.04.3651. This exemption is scheduled to expire July 1, ~~((2017))~~ 2020.

(5) **Exemptions.** The following sources of income are specifically exempt from tax. As such, they should not be included or reported as gross income if the organization is required to file an excise tax return.

(a) **Adult family homes.** RCW 82.04.327 exempts from B&O tax amounts received by licensed adult family homes or adult family homes that are exempt from licensing under rules of the department of social and health services.

(b) **Nonprofit assisted living facilities.** RCW 82.04.-4262 exempts from B&O tax amounts received by a non-

profit assisted living facility licensed under chapter 18.20 RCW for providing room and domiciliary care to residents of the assisted living facility. Nonprofit assisted living facilities were formerly known as "nonprofit boarding homes" in the statute.

(c) **Camp or conference centers.** RCW 82.04.363 and 82.08.830 respectively exempt from B&O tax and retail sales tax amounts received by a nonprofit organization from the sale or furnishing of certain items or services at a camp or conference center conducted on property exempt from the property tax under RCW 84.36.030 (1), (2), or (3). ~~((See))~~ For information about property tax exemptions that may apply see: WAC 458-16-210 (Nonprofit organizations or associations organized and conducted for nonsectarian purposes)~~((;))~~; WAC 458-16-220 (Church camps)~~((;))~~; and WAC 458-16-230 (Character building organizations) ~~((for more information about property tax exemptions that may apply)).~~

Amounts received from the sale of the following items and services are exempt:

(i) Lodging, conference and meeting rooms, camping facilities, parking, and similar licenses to use real property;

(ii) Food and meals;

(iii) Books, tapes, and other products ~~((that are)),~~ including electronically transferred items, available exclusively to the participants at the camp, conference, or meeting and ~~((are))~~ not available to the public at large. ~~((Effective July 26, 2009, electronically transferred items are included in the exemption.))~~

(d) **Child care resource and referral services.** RCW 82.04.3395 exempts from B&O tax amounts received by nonprofit organizations for providing child care resource and referral services. Child care resource and referral services do not include child care services provided directly to children.

(e) **Credit and debt services.** RCW 82.04.368 exempts from B&O tax amounts received by nonprofit organizations for providing specialized credit and debt services. These services include:

(i) Presenting individual and community credit education programs including credit and debt counseling;

(ii) Obtaining creditor cooperation allowing a debtor to repay debt in an orderly manner;

(iii) Establishing and administering negotiated repayment programs for debtors; and

(iv) Providing advice or assistance to a debtor with regard to (i), (ii), or (iii) of this subsection.

(f) **Day care provided by churches.** RCW 82.04.339 exempts from B&O ~~tax~~ amounts received by a church for the care of children of any age for periods of less than twenty-four hours, provided the church is exempt from property tax under RCW 84.36.020.

(g) **Fund-raising.** RCW 82.04.3651 and 82.08.02573 ~~((respectfully)),~~ respectively, exempt from B&O tax and retail sales tax amounts received from certain fund-raising activities.

These exemptions apply only to the fund-raising income received by the nonprofit organization. For example, commission income received by a nonprofit organization selling books owned by a for-profit entity on a consignment basis is exempt ~~((of))~~ from tax only if the statutory requirements are

satisfied. The nonprofit organization is generally responsible for collecting and remitting retail sales tax (~~(upon)~~) on the gross proceeds of sales when selling items for another person. (See) For additional information on the taxability of sales by agents, auctioneers and other similar types of sellers see WAC 458-20-159 ((Consignees, bailees, factors, agents and auctioneers) for more information regarding such sales)).

(i) **What nonprofit organizations qualify?** Nonprofit organizations that qualify for this exemption are those that are:

(A) A tax-exempt nonprofit organization described by section 501 (c)(3) (educational and charitable), 501 (c)(4) (social welfare), or 501 (c)(10) (fraternal societies operating as lodges) of the Internal Revenue Code; or

(B) A nonprofit organization that would qualify for tax exemption under section 501 (c)(3), (4), or (10) except that it is not organized as a nonprofit corporation; or

(C) A nonprofit organization that does not pay its members, stockholders, officers, directors, or trustees any amounts from its gross income, except as payment for services rendered, does not pay more than reasonable compensation to any person for services rendered, and does not engage in a substantial amount of political activity. Political activity includes, but is not limited to, influencing legislation and participating in any campaign on behalf of any candidate for political office.

(ii) **Qualifying fund-raising activities.** For the purpose of this exemption, "fund-raising activity" means soliciting or accepting contributions of money or other property, or activities involving the anticipated exchange of goods or services for money between the soliciting organization and the organization or person solicited, for ~~((the purpose of))~~ furthering the goals of the nonprofit organization.

(A) Money raised by a nonprofit charitable group from its annual telephone fund drive to fund its homeless shelters where nothing is promised in return for a donor's pledge is exempt as fund-raising contributions of money to further the goals of the nonprofit organization.

(B) A nonprofit group organized as a community playhouse has an annual telephone fund drive. The group gives the caller a mug, jacket, dinner, or vacation trip depending on the amount of pledge made over the phone. The community playhouse does not sell or exchange the mugs, jackets, dinners, or trips for cash or property, except during this pledge drive. The money is used to produce the next season's plays. The money earned from the pledges is exempt from both B&O tax and retail sales tax to the extent these amounts represent an exchange of goods and services for money to further the goals of the nonprofit group. The money earned from the pledges above the value of the goods and services exchanged is exempt as a fund-raising contribution of money to further the goals of the nonprofit organization.

(C) A nonprofit group sells ice cream bars at booths leased during the two-week runs of three county fairs, for a total of six weeks during the year, to fund youth camps maintained by the nonprofit group. The money earned from the booths is exempt from both B&O tax and retail sales tax as a fund-raising exchange of goods for money to further the goals of the nonprofit group.

(iii) **Contributions of money or other property.** The term contributions includes grants, donations, endowments, scholarships, gifts, awards, and any other transfer of money or other property by a donor, provided the donor receives no significant goods, services, or benefits in return for making the gift. For example, an amount received by a nonprofit educational broadcaster from a group that conditions receipt ~~((upon))~~ on the nonprofit broadcaster airing its seminars is not a contribution regardless of how the amount paid is titled by the two organizations.

It is not unusual for the person making a gift to require some accountability for how the gift is used as a condition for receiving the gift or future gifts. Such gifts remain exempt, provided the "accountability" required does not result in a direct benefit to the donor (examples of direct benefits to a donor are: Money given for a report on the soil contamination levels of land owned by the donor, medical services provided to the donor or the donor's family, or market research benefiting the donor directly). This "accountability" can take the form of conditions or restrictions on the use of the gift for specific charitable purposes or can take the form of written reports accounting for the use of the gift. Public acknowledgment of a donor for the gift is not a significant service or benefit.

(iv) **Nonqualifying activities.** Fund-raising activity does not include the operation of a regular place of business in which services are provided or sales are made during regular hours such as a bookstore, thrift shop, restaurant, legal or health clinic, or similar business. It also does not include the operation of a regular place of business from which services are provided or performed during regular hours such as the provision of retail, personal, or professional services. A regular place of business and the regular hours of that business depend on the type of business being conducted.

(A) In the example demonstrating that an amount received by a nonprofit broadcaster was not a contribution because services were given in return for the funds, this activity must also be examined to see whether the exchange was for services as part of a fund-raising activity. The broadcaster is in the business of broadcasting programs. It has a regular site for broadcasting programs and ~~((runs))~~ broadcasts ~~((for))~~ twenty-four hours every day. Broadcasting is a part of its business activity performed from a regular place of business during regular hours. The money received from the group with the requirement that its seminars be broadcast would not qualify as money received from a fund-raising activity even though the parties viewed the money as a "donation."

(B) A nonprofit organization that makes catalog sales throughout the year with a twenty-four hour telephone line for taking orders has a regular place of business at the location where the sales orders are processed and regular hours of twenty-four hours a day. Catalog sales are not exempt as fund-raising amounts even though the funds are raised for a nonprofit purpose.

(C) A nonprofit group organized as a community playhouse has three plays during the year at a leased theatre. The plays run for a total of six weeks and the group provides concessions at each of the performances. The playhouse has a regular place of business with regular hours for that type of business. The concessions are done at that regular place of

business during regular hours. The concessions are not exempt as fund-raising activities even though amounts raised from the concessions may be used to further the nonprofit purpose of that group.

(D) A nonprofit student group, that raises money for scholarships and other educational needs, sets up an espresso stand that is open for two hours every morning during the school year. The espresso stand is a regular place of business with regular hours for that type of business. The money earned from the espresso stand is not exempt, even though the amounts are raised to further the student group's nonprofit purpose.

(v) **Fund-raising sales by libraries.** RCW 82.04.3651 (~~(specifically)~~) provides that the sale of used books, used videos, used sound recording, or similar used information products in a library is not the operation of a regular place of business, if the proceeds are used solely to support the library. The library must be a free public library supported in whole or in part with money derived from taxes. RCW 27.12.010. (~~Effective July 1, 2010~~) In addition to the B&O tax exemption under RCW 82.04.3651, RCW 82.08.02573 provides a comparable retail sales tax exemption for the same sales (~~as mentioned above~~), made by a library. (~~See RCW 82.04.3651~~.)

(h) **Group training homes.** RCW 82.04.385 exempts from B&O tax amounts received from the department of social and health services for operating a nonprofit group training home. The amounts excluded from gross income must be used for the cost of care, maintenance, support, and training of developmentally disabled individuals. As defined in RCW 71A.22.020, a nonprofit group training home is an approved (~~nonsectarian~~) facility equipped, supervised, managed, and operated on a full-time nonprofit basis for the full-time care, treatment, training, and maintenance of individuals with developmental disabilities. (~~RCW 71A.22.020~~.)

(i) **Sheltered workshops.** RCW 82.04.385 also exempts from B&O tax amounts received by a nonprofit organization for operating a sheltered workshop.

(i) **What is a sheltered workshop?** A sheltered workshop is that part of the nonprofit organization engaged in business activities that are performed primarily to provide evaluation and work adjusted services for a handicapped person or to provide gainful employment or rehabilitation services to a handicapped person. The sheltered workshop can be maintained on or off the premises of the nonprofit organization.

(ii) **What is meant by "gainful employment or rehabilitation services to a handicapped person"?** Gainful employment or rehabilitation services must be an interim step in the rehabilitation process (~~(which)~~) that is provided because the person cannot be readily absorbed into the competitive labor market or because employment opportunities for the person do not exist during that time in the competitive labor market.

"Handicapped," for the purposes of this exemption, means a physical or mental disability that restricts normal achievement, including medically recognized addictions and learning disabilities. However, this term does not include social or economic disadvantages that restrict normal

achievement (e.g., prior criminal history or low-income status).

(j) **Student loan services.** RCW 82.04.367 exempts from B&O tax amounts received by nonprofit organizations that are exempt from federal income tax under section 501 (c)(3) of the Internal Revenue Code that:

(i) Are guarantee agencies under the federal guaranteed student loan program or that issue debt to provide or acquire student loans; or

(ii) Provide guarantees for student loans made through programs other than the federal guaranteed student loan program.

(k) Grants received to fund education programs pertaining to litter control, waste reduction, recycling, and composting. Effective July 24, 2015, RCW 82.04.755 provides a B&O tax exemption for grants received by a nonprofit organization from the matching fund competitive grant program established in RCW 70.93.180 (1)(b)(ii). This program provides funding for local or statewide education programs designed to help the public with litter control, waste reduction, recycling, and composting of primarily products upon which litter tax is imposed. For information on the state litter tax program, see chapter 82.19 RCW. The requirements for the grants are listed in RCW 70.93.180 (1)(b)(ii). Chapter 15, Laws of 2015 (ESHB 1060).

(6) B&O tax deduction of payments made to health or social welfare organizations.

(a) **Compensation from public entities.** RCW 82.04.-4297 provides a B&O tax deduction to health or social welfare organizations for amounts received from the United States, any instrumentality of the United States, the state of Washington, or any municipal corporation or political subdivision of the state of Washington as compensation for or to support health or social welfare services, rendered by a health or social welfare organization, as defined in RCW 82.04.431, or by a municipal corporation or political subdivision. These deductible amounts should be included in the gross income reported on the excise tax return, entered on the deduction page, and then deducted on the return when determining the amount of the organization's taxable income. A deduction is not allowed, however, for amounts that are received under an employee benefit plan.

(b) **Mental health services.** (~~Effective August 1, 2011~~.) RCW 82.04.4277 provides a B&O tax deduction for health or social welfare organizations (also qualify for a deduction) for amounts received as compensation for providing mental health services under a government-funded program. Regional support networks, which are renamed behavioral health organizations effective April 1, 2016, may also deduct from the measure of tax amounts received from the state of Washington for distribution to health or social welfare organizations eligible to deduct the distribution under RCW 82.04.4277. Persons claiming deductions under RCW 82.04.4277 must file an annual report with the department. See RCW 82.32.534. These deductions are scheduled to expire August 1, 2016.

(c) **Child welfare services.** (~~Also effective August 1, 2011~~.) RCW 82.04.4275 provides a B&O tax deduction for health or social welfare organizations (qualify for a deduction) for amounts received as compensation for providing

child welfare services under a government-funded program. Persons may also deduct from the measure of tax amounts received from the state of Washington for distribution to health or social welfare organizations eligible to deduct the distribution under RCW 82.04.4275(1).

(d) **What is a health or social welfare organization?** A health or social welfare organization is an organization, including any community action council, providing health or social welfare services as defined in subsection (6)(e) of this rule. To be exempt under RCW 82.04.4297, a corporation must satisfy all of the following conditions:

(i) Be a corporation sole under chapter 24.12 RCW or a domestic or foreign not-for-profit corporation under chapter 24.03 RCW. ~~((It does not include))~~ A corporation providing professional services as authorized under chapter 18.100 RCW does not qualify as a health or social welfare organization;

(ii) Be governed by a board of not less than eight individuals who are not paid corporate employees when the organization is a not-for-profit corporation;

(iii) Not pay any part of its corporate income directly or indirectly to its members, stockholders, officers, directors, or trustees except as executive or officer compensation or as services rendered by the corporation in accordance with its purposes and bylaws to a member, stockholder, officer, or director or as an individual;

(iv) Only pay compensation to corporate officers and executives for actual services rendered. This compensation must be at a level comparable to like public service positions within Washington;

(v) Have irrevocably dedicated its corporate assets to health or social welfare activities. Upon corporate liquidation, dissolution, or abandonment, any distribution or transfer of corporate assets may not inure directly or indirectly to the benefit of any member or individual, except for another health or social welfare organization;

(vi) Be duly licensed or certified as required by law or regulation;

(vii) Use government payments to provide health or social welfare services;

(viii) Make its services available regardless of race, color, national origin, or ancestry; and

(ix) Provide access to the corporation's books and records to the department's authorized agents upon request.

(e) **Qualifying health or welfare services.** The term "health or social welfare services" includes and is limited to:

(i) Mental health, drug, or alcoholism counseling or treatment;

(ii) Family counseling;

(iii) Health care services;

(iv) Therapeutic, diagnostic, rehabilitative, or restorative services for the care of the sick, aged, physically-disabled, developmentally-disabled, or emotionally-disabled individuals;

(v) Activities, including recreational activities, intended to prevent or ameliorate juvenile delinquency or child abuse;

(vi) Care of orphans or foster children;

(vii) Day care of children;

(viii) Employment development, training, and placement;

(ix) Legal services to the indigent;

(x) Weatherization assistance or minor home repairs for low-income homeowners or renters;

(xi) Assistance to low-income homeowners and renters to offset the cost of home heating energy, through direct benefits to eligible households or to fuel vendors on behalf of eligible households; and

(xii) Community services to low-income individuals, families and groups that are designed to have a measurable and potentially major impact on causes of poverty in communities of the state of Washington; and

(xiii) Temporary medical housing, as defined in RCW 82.08.997, if the housing is provided only:

(A) While the patient is receiving medical treatment at a hospital required to be licensed under RCW 70.41.090 or at an outpatient clinic associated with such hospital, including any period of recuperation or observation immediately following such medical treatment; and

(B) By a person that does not furnish lodging or related services to the general public.

AMENDATORY SECTION (Amending WSR 09-19-136, filed 9/22/09, effective 10/23/09)

WAC 458-20-272 Tire fee—~~Studded tire fee~~—Core deposits or credits. (1) **Introduction.** This ~~((section))~~ rule describes the tire fee imposed under RCW 70.95.510 and the studded tire fee imposed under RCW 46.37.427 for collection beginning July 1, 2016. See chapter 44, Laws of 2015 (2ESSB 5987). This rule also describes how business and occupation (B&O), sales, and use ~~((tax consequences related to))~~ taxes apply to tire fees. battery core charges and core deposits or credits, including the exemptions described in RCW 82.08.036 and 82.12.038.

(a) Other rules that may be relevant. Readers may want to refer to other rules for additional information, including those in the following list:

(i) WAC 458-20-228 Returns, payments, penalties, extensions, interest, stay of collection.

(ii) WAC 458-20-278 Returned goods, defective goods—Motor vehicle lemon law.

(b) Examples. This rule contains examples that identify a number of facts and then state a conclusion. These examples should be used only as a general guide. The tax results of other situations must be determined after a review of all of the facts and circumstances.

(2) **Tire fee.**

(a) What is the tire fee? The tire fee is a one-dollar fee collected by the seller from the buyer on every retail sale of each new replacement vehicle tire. If new tires are leased, the fee must be collected once at the beginning of the lease.

(b) How do I report the tire fee? A seller must report on the excise tax return the number of new replacement vehicle tires sold. Tire sellers may retain ten percent of the fee and must remit the remainder to the department of revenue (department). As a result, the amount that must be reported and paid to the department is the number of new replacement vehicle tires sold during the tax reporting period multiplied by ninety cents.

(c) **What if the seller fails to collect the fee or does not pay the fee on time?** The seller is personally liable for payment of the fee, whether or not the fee is collected from the buyer. Any seller who appropriates or converts the fee collected to his or her own use or to any use other than the payment of the fee by the due date, minus the ten percent retained, is guilty of a gross misdemeanor. Interest and penalties apply to late payments. ~~((Refer to WAC 458-20-228 (Returns, payments, penalties, extensions, interest, stay of collection) for more information.))~~

(d) **What happens if a buyer fails to pay the fee?** The tire fee, until paid by the buyer to the seller or the department, is considered a debt from the buyer to the seller. Any buyer who refuses to pay the fee is guilty of a misdemeanor.

(e) **Is sales tax imposed on the tire fee?** No. The measure of the sales tax does not include the tire fee. See RCW 82.08.036.

(f) **Is the ten percent amount retained by the seller ~~(taxed)~~ subject to B&O tax?** Yes. The seller must report the retained amount as gross income under the service and other activities tax classification on the excise tax return.

(g) **What tires are subject to the tire fee?** All new replacement vehicle tires are subject to the tire fee. Refer to RCW 70.95.030 for the definition of "vehicle."

(i) Examples of vehicles for which new replacement tires are subject to the fee include:

- (A) Automobiles;
- (B) Trucks;
- (C) Recreational vehicles;
- (D) Trailers;
- (E) All-terrain vehicles (ATVs);
- (F) Agricultural vehicles, such as tractors or combines;
- (G) Industrial vehicles, such as forklifts;
- (H) Construction vehicles, such as loaders or graders;

and

(I) Golf carts.

(ii) Bicycles, wheelbarrows, and hand trucks are examples of devices to which the new replacement tire fee does not apply.

(iii) The tire fee does not apply to the sale of retreaded vehicle tires. Nor does it apply to tires provided free of charge under the terms of a recall or warranty.

(h) **May I refund the fee if a tire is returned?** If a customer returns the purchased new tire and the entire selling price is refunded to the customer, the one-dollar tire fee is likewise refundable. The refunded amount may be claimed on the excise tax return in the same manner as refunded sales tax. If the seller does not refund the full sales price to the customer, the one-dollar fee is not refundable. ~~((Refer to WAC 458-20-108 (Returned goods, allowances, cash discounts) for more information.))~~

(i) **Does the tire fee apply on sales to the federal government or Indians and Indian tribes?** The tire fee is not imposed on sales to the federal government and need not be collected by the seller. The tire fee does not apply to sales of tires delivered to enrolled members or tribes in "Indian country." ~~((Refer to))~~ For information on sales to the federal government, see WAC 458-20-190, and for sales to Indians and Indian tribes, see WAC 458-20-192 ((for more information)).

(j) **If the sale is exempt from sales tax, is the tire fee due?** Statutory exemptions from sales tax do not apply to the tire fee. The tire fee is due on every retail sale of a new replacement tire whether or not sales tax is due.

(3) **Studded tire fee.**

(a) **What is the studded tire fee?** The studded tire fee is a five dollar fee imposed on the retail sale of each new tire sold, on or after July 1, 2016, that contains studs. The seller will collect the fee from the buyer. For the purpose of this subsection, "new tire sold that contains studs" means a tire that is manufactured for vehicle purposes and contains metal studs, and does not include bicycle tires or retreaded vehicle tires.

(b) **Who remits the studded tire fee to the department?** The seller collects the five dollar fee from the buyer and holds it in trust until paid to the department; however, the seller may retain ten percent of the fee collected.

(c) **What if the seller fails to collect the fee or does not pay the fee on time?** Interest and penalties, as described in subsection (2)(c) of this rule also apply to the studded tire fee.

(d) **What happens if a buyer fails to pay the fee?** As with the tire fee, a buyer who refuses to pay the fee is guilty of a misdemeanor. See subsection (2)(d) of this rule.

(e) **Is sales tax imposed on the tire fee?** No. The seller is collecting the fee as an agent for the state and thus the measure of sales tax does not include the studded tire fee. For additional information on taxpayers acting as collecting agents, see WAC 458-20-195.

(f) **Is the ten percent amount retained by the seller subject to B&O tax?** Yes. As with the tire fee, the seller must report the retained amount as gross income under the service and other activities tax classification on the excise tax return.

(g) **Is the studded tire fee refundable if the tire is returned?** If a new studded tire is returned, the studded tire fee is handled the same as the tire fee as described in subsection (2)(h) of this rule.

(h) **Does the studded tire fee apply to tires sold to the federal government or Indians and Indian tribes?** With respect to these sales, the studded tire fee is handled the same as the tire fee described in subsection (2)(i) of this rule.

(i) **If the sale is exempt from sales tax, is the studded tire fee due?** As with the tire fee described in subsection (2)(j) of this rule, statutory exemptions from sales tax do not apply to the studded tire fee.

(4) **Core deposits or credits - Battery core charges.**

(a) **Definitions.** For purposes of this ~~((section))~~ rule, the following definitions apply:

(i) **Core deposits or credits.** "Core deposits or credits" means the amount representing the value of returnable products such as batteries, starters, brakes, and other products with returnable value added for purposes of recycling or remanufacturing.

(ii) **Battery core charge.** "Battery core charge" refers to a core deposit, not less than five dollars, ~~((which must))~~ that a seller by law ((be retained by the seller)) must retain when a retail purchaser has no used battery to exchange or trade in. A buyer may return within thirty days of the purchase with a used battery of equivalent size and claim the core charge amount. See RCW 70.95.630 and 70.95.640.

(b) **How is tax calculated when the buyer receives a core deposit or credit?** Retail sales and use taxes do not apply to consideration received in the form of core deposits or credits when a purchaser exchanges or trades in a core for recycling or remanufacturing. Therefore, the measure of the sales or use tax may be reduced by the amount of the core deposit or credit. See RCW 82.08.036 and 82.12.038. The core deposit and credit exemptions apply only to the retail sales and use taxes. There is no equivalent exemption or deduction for B&O tax purposes. Therefore, the amount reported under the appropriate B&O tax classification must include the value of core deposits or credits.

(c) **Examples.** ~~((This subsection provides examples that identify a number of facts and then state a conclusion. These examples should be used only as a general guide. The tax results of other situations must be determined after a review of all of the facts and circumstances.))~~

(i) **Example 1.** A customer purchases at retail a new replacement battery and reconditioned starter, providing the seller with a battery core and a starter core in exchange. The selling price of the new battery, including the battery core charge, is \$60.00. The customer is allowed a \$5.00 credit because a battery core is exchanged, meaning the cost of the battery to the customer, excluding sales tax, is \$55.00. The selling price of the starter is \$50.00. The seller allows a \$3.00 credit for the starter core, meaning the cost to the customer, excluding sales tax, is \$47.00. Retailing B&O tax is due upon the total value of cash plus core value, in this case \$110.00, or \$60.00 plus \$50.00. However, the \$8.00 of core deposits or credits may be deducted from the measure of the retail sales tax under RCW 82.08.036. Thus, retail sales tax is due on \$102.00, or \$55.00 plus \$47.00.

(ii) **Example 2.** The seller delivers the starter and battery cores accepted in the exchange to wholesalers. A starter wholesaler issues a refund and a battery wholesaler issues a credit memorandum to be applied against future wholesale battery purchases. The return of the used products by the auto parts store for recycling or remanufacturing and subsequent receipt of a refund or credit for the core deposit or credit is not considered taxable consideration for purposes of the B&O tax.

WSR 16-02-058

EXPEDITED RULES

DEPARTMENT OF REVENUE

[Filed January 4, 2016, 9:17 a.m.]

Title of Rule and Other Identifying Information: WAC 458-20-13601 (Rule 13601) Manufacturers and processors for hire—Sales and use tax exemption for machinery and equipment, explains the retail sales and use tax exemptions for machinery and equipment (M&E) used directly in a manufacturing operation or research and development operation by manufacturers or processors for hire.

NOTICE

THIS RULE IS BEING PROPOSED UNDER AN EXPEDITED RULE-MAKING PROCESS THAT WILL

ELIMINATE THE NEED FOR THE AGENCY TO HOLD PUBLIC HEARINGS, PREPARE A SMALL BUSINESS ECONOMIC IMPACT STATEMENT, OR PROVIDE RESPONSES TO THE CRITERIA FOR A SIGNIFICANT LEGISLATIVE RULE. IF YOU OBJECT TO THIS USE OF THE EXPEDITED RULE-MAKING PROCESS, YOU MUST EXPRESS YOUR OBJECTIONS IN WRITING AND THEY MUST BE SENT TO Gayle Carlson, Department of Revenue, P.O. Box 47453, Olympia, WA 98504-7453, e-mail GayleC@dor.wa.gov, AND RECEIVED BY March 7, 2016.

Purpose of the Proposal and Its Anticipated Effects, Including Any Changes in Existing Rules: The department is considering revisions to Rule 13601 to include 2015 legislation. The legislation added:

- To the definition of "manufacturer" a person that is engaged in the development of prewritten computer software that is not transferred to purchasers by means of tangible storage media; and
- The definitions of an affiliated group and an ineligible person. Exemptions provided by RCW 82.08.02565 and 82.12.02565 do not apply to an ineligible person, which includes an affiliated group, effective August 1, 2015, unless the M&E was first used by the taxpayer in Washington before August 1, 2015.

Copies of draft rules are available for viewing and printing on our web site at Rules Agenda.

Reasons Supporting Proposal: Chapter 5, Laws of 2015 3rd sp. sess. (ESSB 6138).

Statutory Authority for Adoption: RCW 82.32.300 and 82.01.060(2).

Statute Being Implemented: RCW 82.08.02565 and 82.12.02565.

Rule is not necessitated by federal law, federal or state court decision.

Name of Proponent: Department of revenue, governmental.

Name of Agency Personnel Responsible for Drafting: Gayle Carlson, 1025 Union Avenue S.E., Suite #544, Olympia, WA, (360) 534-1576; Implementation and Enforcement: Marcus Glasper, 1025 Union Avenue S.E., Suite #500, Olympia, WA, (360) 534-1615.

January 4, 2016

Kevin Dixon

Rules Coordinator

AMENDATORY SECTION (Amending WSR 15-01-005, filed 12/4/14, effective 1/4/15)

WAC 458-20-13601 Manufacturers and processors for hire—Sales and use tax exemptions for machinery and equipment. (1) Introduction.

(a) This rule explains the retail sales and use tax exemptions provided by RCW 82.08.02565 and 82.12.02565 for sales to or use by manufacturers or processors for hire of machinery and equipment (M&E) used directly in a manufacturing operation or research and development operation. This rule explains the requirements that must be met to substantiate a claim of exemption. For information regarding the sales

and use tax deferral for manufacturing and research/development activities in high unemployment counties, refer to WAC 458-20-24001 and chapter 82.60 RCW. For the high technology business sales and use tax deferral refer to chapter 82.63 RCW.

(b) Effective June 12, 2014, the retail sales and use tax exemptions provided by RCW 82.08.02565 and 82.12.02565 do not apply to:

(i) Sales of machinery and equipment used directly in the manufacturing, research and development, or testing of marijuana; ~~((e))~~ and

(ii) Sales of or charges made for labor and services rendered in respect to installing, repairing, cleaning, altering, or improving such machinery and equipment.

(c) Effective August 1, 2015, an ineligible person, as defined in subsection (2)(e) of this rule, does not qualify for the retail sales and use tax exemptions provided by RCW 82.08.02565 and 82.12.02565, unless the taxpayer first used the qualifying machinery and equipment in this state prior to August 1, 2015.

(2) **Definitions.** For purposes of the manufacturing machinery and equipment tax exemptions, the following definitions ~~((will))~~ apply~~((-))~~:

(a) **Affiliated group.** "Affiliated group" means a group of two or more entities that are either:

(i) Affiliated as defined in RCW 82.32.655; or

(ii) Permitted to file a consolidated return for federal income tax purposes.

(b) **Cogeneration.** "Cogeneration" means the simultaneous generation of electrical energy and low-grade heat from the same fuel. See RCW 82.08.02565.

~~((b))~~ (c) **Device.** "Device" means an item that is not attached to the building or site. Examples of devices are: Forklifts, chainsaws, air compressors, clamps, free standing shelving, software, ladders, wheelbarrows, and pulleys.

~~((e))~~ (d) **Industrial fixture.** "Industrial fixture" means an item attached to a building or to land. Fixtures become part of the real estate to which they are attached and ~~((upon))~~ at the time of attachment are classified as real property, not personal property. Examples of "industrial fixtures" are fuel oil lines, boilers, craneways, and certain concrete slabs.

~~((d))~~ (e) **Ineligible person.** "Ineligible person" means all members of an affiliated group if all of the following apply:

(i) At least one member of the affiliated group was registered with the department of revenue (department) to do business in Washington state on or before July 1, 1981;

(ii) As of August 1, 2015, the combined employment in this state of the affiliated group exceeds forty thousand full-time and part-time employees, based on data reported to the employment security department by the affiliated group; and

(iii) The business activities of the affiliated group primarily include development, sales, and licensing of computer software and services.

(f) **Machinery and equipment (M&E).** "Machinery and equipment" means industrial fixtures, devices, and support facilities, and tangible personal property that becomes an ingredient or component thereof, including repair parts and replacement parts. ~~((("Machinery and equipment")))~~ M&E includes pollution control equipment installed and used in a

qualifying operation to prevent air pollution, water pollution, or contamination that might otherwise result from the operation. ~~((("M&E" means "machinery and equipment."))~~

~~((e))~~ (g) **Manufacturer.** "Manufacturer" has the same meaning as provided in chapter 82.04 RCW. Manufacturer also includes a person that prints newspapers or other materials; and effective August 1, 2015, a person engaged in the development of prewritten computer software that is not transferred to purchasers by means of tangible storage media. RCW 82.08.02565, chapter 5, Laws of 2015 3rd sp. sess. (ESSB 6138).

~~((f))~~ (h) **Manufacturing.** "Manufacturing" has the same meaning as "to manufacture" in chapter 82.04 RCW.

~~((g))~~ (i) **Manufacturing operation.** "Manufacturing operation" means the manufacturing of articles, substances, or commodities for sale as tangible personal property. A manufacturing operation begins at the point where the raw materials enter the manufacturing site and ends at the point where the processed material leaves the manufacturing site. The operation includes storage of raw materials at the site, the storage of in-process materials at the site, and the storage of the processed material at the site. The manufacturing operation is defined in terms of a process occurring at a location. To be eligible as a qualifying use of M&E, the use must take place within the manufacturing operation, unless specifically exempted by law. Storage of raw material or other tangible personal property, packaging of tangible personal property, and other activities that potentially qualify under the "used directly" ~~((criteria))~~ criterion, and that do not constitute manufacturing in and of themselves, are not within the scope of the exemption unless they take place at a manufacturing site. The statute specifically allows testing to occur away from the site.

The term "manufacturing operation" also includes that portion of a cogeneration project that is used to generate power for consumption within the manufacturing site of which the cogeneration project is an integral part. The term does not include the production of electricity by a light and power business as defined in RCW 82.16.010 or the preparation of food products on the premises of a person selling food products at retail.

(i) Neither duration or temporary nature of the manufacturing activity nor mobility of the equipment determine whether a manufacturing operation exists. For example, operations using portable saw mills or rock crushing equipment are considered "manufacturing operations" if the activity in which the person is engaged is manufacturing. Rock crushing equipment that deposits material onto a roadway is not used in a manufacturing operation because this is a part of the constructing activity, not a manufacturing activity. Likewise, a concrete mixer used at a construction site is not used in a manufacturing operation because the activity is constructing, not manufacturing. Other portable equipment used in non-manufacturing activities, such as continuous gutter trucks or trucks designed to deliver and combine aggregate, or specialized carpentry tools, do not qualify for the same reasons.

(ii) Manufacturing tangible personal property for sale can occur in stages, taking place at more than one manufacturing site. For example, if a taxpayer processes pulp from wood at one site, and transfers the resulting pulp to another

site that further manufactures the product into paper, two separate manufacturing operations exist. The end product of the manufacturing activity must result in an article, substance, or commodity for sale.

~~((h))~~ **(j) Marijuana.** "Marijuana" is any product with a THC concentration greater than .03 percent.

~~((h))~~ **(k) Processor for hire.** "Processor for hire" has the same meaning as used in chapter 82.04 RCW and as explained in WAC 458-20-136 Manufacturing, processing for hire, fabricating.

~~((h))~~ **(l) Qualifying operation.** "Qualifying operation" means a manufacturing operation, a research and development operation, or a testing operation.

~~((h))~~ **(m) Research and development operation.** "Research and development operation" means engaging in research and development as defined in RCW 82.63.010 by a manufacturer or processor for hire. RCW 82.63.010 defines "research and development" to mean: Activities performed to discover technological information, and technical and non-routine activities concerned with translating technological information into new or improved products, processes, techniques, formulas, inventions, or software. The term includes exploration of a new use for an existing drug, device, or biological product if the new use requires separate licensing by the Federal Food and Drug Administration under chapter 21, C.F.R., as amended. The term does not include adaptation or duplication of existing products where the products are not substantially improved by application of the technology, nor does the term include surveys and studies, social science and humanities research, market research or testing, quality control, sale promotion and service, computer software developed for internal use, and research in areas such as improved style, taste, and seasonal design.

~~((h))~~ **(n) Sale.** "Sale" has the same meaning as "sale" in chapter 82.08 RCW, which includes by reference RCW 82.04.040. RCW 82.04.040 includes by reference the definition of "retail sale" in RCW 82.04.050. "Sale" includes renting or leasing, conditional sale contracts, leases with option to purchase, and any contract under which possession of the property is given to the purchaser but title is retained by the vendor as security for the payment of the purchase price.

~~((m))~~ **(o) Site.** "Site" means the location at which the manufacturing or testing takes place.

~~((h))~~ **(p) Support facility.** "Support facility" means a part of a building, or a structure or improvement, used to contain or steady an industrial fixture or device. A support facility must be specially designed and necessary for the proper functioning of the industrial fixture or device and must perform a function beyond being a building or a structure or an improvement. It must have a function relative to an industrial fixture or a device. To determine if some portion of a building is a support facility, the parts of the building are examined. For example, a highly specialized structure, like a vibration reduction slab under a microchip clean room, is a support facility. Without the slab, the delicate instruments in the clean room would not function properly. The ceiling and walls of the clean room are not support facilities if they only serve to define the space and do not have a function relative to an industrial fixture or a device.

~~((h))~~ **(q) Tangible personal property.** "Tangible personal property" has its ordinary meaning.

~~((h))~~ **(r) Testing.** "Testing" means activities performed to establish or determine the properties, qualities, and limitations of tangible personal property.

~~((h))~~ **(s) Testing operation.** "Testing operation" means the testing of tangible personal property for a manufacturer or processor for hire. A testing operation begins at the point where the tangible personal property enters the testing site and ends at the point where the tangible personal property leaves the testing site. The term also includes that portion of a cogeneration project that is used to generate power for consumption within the site of which the cogeneration project is an integral part. The term does not include the production of electricity by a light and power business as defined in RCW 82.16.010 or the preparation of food products on the premises of a person selling food products at retail. The testing operation is defined in terms of a process occurring at a location. To be eligible as a qualifying use of M&E, the use must take place within the testing operation, unless specifically excepted by law.

(3) Retail sales and use tax exemptions. The M&E exemptions provide retail sales and use tax exemptions for machinery and equipment used directly in a manufacturing operation or research and development operation, ~~((with the exception of))~~ except for such sales or use relating to marijuana effective June 12, 2014. Sales of or charges made for labor and services rendered in respect to installing, repairing, cleaning, altering, or improving qualifying machinery and equipment are also exempt from sales tax, ~~((with the exception of))~~ except for such sales or charges relating to marijuana effective June 12, 2014. However, because the exemption is limited to items with a useful life of one year or more, some charges for repair, labor, services, and replacement parts may not be eligible for the exemption. In the case of labor and service charges that cover both qualifying and nonqualifying repair and replacement parts, the labor and services charges are presumed to be exempt. If all of the parts are nonqualifying, the labor and service charge is not exempt, unless the parts are incidental to the service being performed, such as cleaning, calibrating, and adjusting qualifying machinery and equipment.

The exemption may be taken for qualifying machinery and equipment used directly in a testing operation by a person engaged in testing for a manufacturer or processor for hire, with the exception of such testing relating to marijuana effective June 12, 2014.

Sellers remain subject to the retailing B&O tax on all sales of machinery and equipment to consumers if delivery is made within the state of Washington, notwithstanding that the sale may qualify for an exemption from the retail sales tax.

(a) Sales tax. The purchaser must provide the seller with an exemption certificate. The exemption certificate must be completed in its entirety. The seller must retain a copy of the certificate as a part of its records. This certificate may be issued for each purchase or in blanket form certifying all future purchases as being exempt from sales tax. Blanket certificates are valid for as long as the buyer and seller have a recurring business relationship. A "recurring business rela-

tionship" means at least one sale transaction within a period of twelve consecutive months. RCW 82.08.050 (7)(c).

The form must contain the following information:

- (i) Name, address, and registration number of the buyer;
- (ii) Name of the seller;
- (iii) Name and title of the authorized agent of the buyer/user;
- (iv) Authorized signature;
- (v) Date; and
- (vi) Whether the form is a single use or blanket-use form.

A copy of the ~~(a)~~ an M&E certificate form may be obtained from the ~~((department of revenue (department) on the internet))~~ department's web site at ~~((www-))~~ dor.wa.gov, or by contacting the department's taxpayer services division at:

Taxpayer Services
Department of Revenue
~~((Taxpayer Services))~~
P.O. Box 47478
Olympia, WA 98504-7478
1-800-647-7706

(b) **Use tax.** The use tax complements the retail sales tax by imposing a tax of like amount ~~((upon))~~ on the use within this state as a consumer of any tangible personal property purchased at retail, where the user has not paid retail sales tax with respect to the purchase of the property used. ~~((See also))~~ For additional information on use tax see chapter 82.12 RCW and WAC 458-20-178 ((Use tax)). ~~((?))~~ If the seller fails to collect the appropriate retail sales tax, the purchaser is required to pay the retail sales tax (commonly referred to as "deferred sales tax") or the use tax directly to the department unless the purchase and/or use is exempt from the retail sales and/or use taxes. A qualifying person using eligible machinery and equipment in Washington in a qualifying manner is exempt from the use tax. If an item of machinery and equipment that was eligible for use tax or sales tax exemption fails to overcome the majority use threshold or is ~~((totally))~~ entirely put to use in a nonqualifying manner, use tax is due on the fair market value at the time the item was put to nonqualifying use. See subsection (9) of this rule for an explanation of the majority use threshold.

(4) **Who may take the exemption((?)?)** The exemption may be taken by a manufacturer or processor for hire who manufactures articles, substances, or commodities for sale as tangible personal property (excluding marijuana), and who, for the item in question, meets the used directly test and overcomes the majority use threshold. (See subsection (8) of this rule for a discussion of the "used directly" ~~((criteria))~~ critere-
rion and see subsection (9) of this rule for an explanation of the majority use threshold.) However, for research and development operations, there is no requirement that the operation produce tangible personal property for sale. A processor for hire who does not sell tangible personal property is eligible for the exemption if the processor for hire manufactures articles, substances, or commodities that will be sold by the manufacturer. For example, a person who is a processor for hire but who is manufacturing with regard to tangible personal property that will be used by the manufacturer, rather than sold by the manufacturer, is not eligible. For additional infor-

mation on manufacturing, processing for hire, or fabricating, see WAC 458-20-136 and RCW 82.04.110 ((for more infor-
mation)). Persons who engage in testing for manufacturers or processors for hire are eligible for the exemption. To be eligible for the exemption, the taxpayer need not be a manufacturer or processor for hire in the state of Washington, but must meet the ~~((Washington))~~ definition of manufacturer provided in subsection (2)(g) of this rule.

(5) **What is eligible for the exemption((?)?)** Machinery and equipment used directly in a qualifying operation by a qualifying person is eligible for the exemption, subject to overcoming the majority use threshold.

There are three classes of eligible machinery and equipment: Industrial fixtures, devices, and support facilities. Also eligible is tangible personal property that becomes an ingredient or component of the machinery and equipment, including repair parts and replacement parts. "Machinery and equipment" also includes pollution control equipment installed and used in a qualifying operation to prevent air pollution, water pollution, or contamination that might otherwise result from the operation.

(6) **What is not eligible for the exemption((?)?)** In addition to items that are not eligible because they do not meet the used directly test or fail to overcome the majority use threshold, ~~((there are))~~ the following four categories of ~~((items that))~~ property are statutorily excluded from eligibility~~((The following property is not eligible for the M&E exemption))~~:

(a) **Hand-powered tools.** Screw drivers, hammers, clamps, tape measures, and wrenches are examples of hand-powered tools. Electric powered, including cordless tools, are not hand-powered tools, nor are calipers, plugs used in measuring, or calculators.

(b) **Property with a useful life of less than one year.** All eligible machinery and equipment must satisfy the useful life ~~((criteria))~~ critere-
rion, including repair parts and replacement parts. For example, items such as blades and bits are generally not eligible for the exemption because, while they may become component parts of eligible machinery and equipment, they generally have a useful life of less than one year. Blades generally having a useful life of one year or more, such as certain sawmill blades, are eligible. See subsection (7) of this rule for thresholds to determine useful life.

(c) **Buildings.** Buildings, other than machinery and equipment that is permanently affixed to or becomes a physical part of a building. Buildings provide work space for people or shelter machinery and equipment or tangible personal property. The building itself is not eligible, however some of its components might be eligible for the exemption. The industrial fixtures and support facilities that become affixed to or part of the building might be eligible. The subsequent real property status of industrial fixtures and support facilities does not affect eligibility for the exemption.

(d) **Building fixtures.** Building fixtures that are not integral to the manufacturing operation, testing operation, or research and development operation that are permanently affixed to and become a physical part of a building, such as utility systems for heating, ventilation, air conditioning, communications, plumbing, or electrical. Examples of nonqualifying fixtures are: Fire sprinklers, building electrical systems, or washroom fixtures. Fixtures that are integral to the manu-

facturing operation might be eligible, depending on whether the item meets the other requirements for eligibility, such as the used directly test.

(7) **The "useful life" threshold.** RCW 82.08.02565 has a per se exception for "property with a useful life of less than one year." Property that meets this description is not eligible for the M&E exemption. The useful life threshold identifies items that do not qualify for the exemption, such as supplies, consumables, and other classes of items that are not expected or intended to last a year or more. For example, tangible personal property that is acquired for a one-time use and is discarded ~~((upon))~~ after use, such as a mold or a form, has a useful life of less than one year and is not eligible. If it is clear from taxpayer records or practice that an item is used for at least one year, the item is eligible, regardless of the answers to the four threshold questions. A taxpayer may work directly with the department to establish recordkeeping methods that are tailored to the specific circumstances of the taxpayer. The following steps should be used ~~((in making a determination))~~ to determine whether an item meets the "useful life" threshold. The series of questions progress from simple documentation to complex documentation. ~~((In order))~~ To substantiate qualification under any step, a taxpayer must maintain adequate records or be able to establish by demonstrating through practice or routine that the threshold is overcome. Catastrophic loss, damage, or destruction of an item does not affect eligibility of machinery and equipment that otherwise qualifies. Assuming the machinery and equipment meets all of the other M&E requirements and does not have a single one-time use or is not discarded during the first year, useful life ~~((can))~~ should be determined by answering the following questions for an individual piece of machinery and equipment:

(a) Is the machinery and equipment capitalized for either federal tax purposes or accounting purposes?

- If the answer is "yes," it qualifies for the exemption.
- If the answer is "no,"

(b) Is the machinery and equipment warranted by the manufacturer to last at least one year?

- If the answer is "yes," it qualifies for the exemption.
- If the answer is "no,"

(c) Is the machinery and equipment normally replaced at intervals of one year or more, as established by industry or business practice? (This is commonly based on the actual experience of the person claiming the exemption.)

- If the answer is "yes," it qualifies for the exemption.
- If the answer is "no,"

(d) Is the machinery and equipment expected at the time of purchase to last at least one year, as established by industry or business practice? (This is commonly based on the actual experience of the person claiming the exemption.)

- If the answer is "yes," it qualifies for the exemption.
- If the answer is "no," it does not qualify for the exemption.

(8) **The "used directly" criteria.** Items that are not "used directly" in a qualifying operation are not eligible for the exemption. The statute provides eight descriptions of the phrase "used directly." The manner in which a person uses an item of machinery and equipment must match one of these descriptions. ~~((If M&E is not "used directly" it is not eligible~~

~~for the exemption.))~~ Examples of items that are not used directly in a qualifying operation are cafeteria furniture, safety equipment not part of qualifying M&E, packaging materials, shipping materials, or administrative equipment. Machinery and equipment is "used directly" in a manufacturing operation, testing operation, or research and development operation, if the machinery and equipment meets any one of the following criteria:

(a) **Acts on or interacts with.** It acts ~~((upon))~~ on or interacts with an item of tangible personal property. Examples ~~((of this are))~~ include drill presses, concrete mixers (agitators), ready-mix concrete trucks, hot steel rolling machines, rock crushers, and band saws. Also included is machinery and equipment used to repair, maintain, or install tangible personal property. Computers qualify under this ~~((criteria))~~ criterion if:

(i) They direct or control machinery or equipment that acts ~~((upon))~~ on or interacts with tangible personal property; or

(ii) If they act ~~((upon))~~ on or interact with an item of tangible personal property.

(b) **Conveys, transports, handles, or temporarily stores.** It conveys, transports, handles, or temporarily stores an item of tangible personal property at the manufacturing site or the testing site. Examples ~~((of this are))~~ include wheelbarrows, handcarts, storage racks, forklifts, tanks, vats, robotic arms, piping, and concrete storage pads. Floor space in buildings does not qualify under this ~~((criteria. Not))~~ criterion. Also not eligible under this ~~((criteria))~~ criterion are items that are used to ship the product or in which the product is packaged, as well as materials used to brace or support an item during transport.

(c) **Controls, guides, measures, verifies, aligns, regulates or tests.** It controls, guides, measures, verifies, aligns, regulates, or tests tangible personal property at the site or away from the site. Examples of "away from the site" are road testing of trucks, air testing of planes, or water testing of boats, with the machinery and equipment used off site in the testing eligible under this ~~((criteria))~~ criterion. Machinery and equipment used to take readings or measurements is eligible under this ~~((criteria))~~ criterion.

(d) **Provides physical support.** It provides physical support for or access to tangible personal property. Examples ~~((of this are))~~ include catwalks adjacent to production equipment, scaffolding around tanks, braces under vats, and ladders near controls. Machinery and equipment used for access to the building or to provide a work space for people or a space for tangible personal property or machinery and equipment, such as stairways or doors, is not eligible under this ~~((criteria))~~ criterion.

(e) **Produces power or lubricates.** It produces power for or lubricates machinery and equipment. A generator providing power to a sander is an example of machinery and equipment that produces such power ~~((for machinery and equipment))~~. An electrical generating plant that provides power for a building is not eligible under this ~~((criteria))~~ criterion. Lubricating devices, such as hoses, oil guns, pumps, and meters, whether or not attached to machinery and equipment, are eligible under this ~~((criteria))~~ criterion.

(f) **Produces another item.** It produces another item of tangible personal property for use in the manufacturing operation, testing operation, or research and development operation. Examples include machinery and equipment that make((s)) dies, jigs, or molds, and printers that produce camera-ready images ((are examples of this)).

(g) **Packs.** It places tangible personal property in the container, package, or wrapping in which the tangible personal property is normally sold or transported.

(h) **Is integral to research and development.** It is integral to "research and development" as it is defined in RCW 82.63.010.

(9) **The majority use threshold.**

(a) **M&E used both in a qualifying and nonqualifying manner.** Machinery and equipment (~~((both))~~) used both directly in a qualifying operation and (~~((used))~~) also in a nonqualifying manner is eligible for the exemption only if the qualifying use satisfies the majority use requirement. Examples of situations in which an item of machinery and equipment is used for qualifying and nonqualifying purposes include: The use of machinery and equipment in manufacturing and repair activities, such as using a power saw to make cabinets in a shop versus using it to make cabinets at a customer location; the use of machinery and equipment in manufacturing and constructing activities, such as using a forklift to move finished sheet rock at the manufacturing site versus using it to unload sheet rock at a customer location; and the use of machinery and equipment in manufacturing and transportation activities, such as using a mixer truck to make concrete at a manufacturing site versus using it to deliver concrete to a customer. Majority use can be expressed as a percentage, with the minimum required amount of qualifying use being greater than fifty percent compared to overall use. To determine whether the majority use requirement has been satisfied, the person claiming the exemption must retain records documenting the measurement used to substantiate a claim for exemption or, if time, value, or volume is not the basis for measurement, be able to establish by demonstrating through practice or routine that the requirement is satisfied. Majority use is measured by looking at the use of an item during a calendar year using any of the following:

(i) **Time.** Time is measured using hours, days, or other unit of time, with qualifying use of the M&E the numerator, and total time used the denominator. Suitable records for time measurement include employee time sheets or equipment time use logs.

(ii) **Value.** Value means the value to the person, measured by revenue if both the qualifying and nonqualifying uses (~~((both))~~) produce revenue. Value is measured using gross revenue, with revenue from qualifying use of the M&E the numerator, and total revenue from use of the M&E the denominator. If there is no revenue associated with the use of the M&E, such as in-house accounting use of a computer system, the value basis may not be used. Suitable records for value measurement include taxpayer sales journals, ledgers, account books, invoices, and other summary records.

(iii) **Volume.** Volume is measured using amount of product, with volume from qualifying use of the M&E the numerator and total volume from use of the M&E the denom-

inator. Suitable records for volume measurement include production numbers, tonnage, and dimensions.

(iv) **Other comparable measurement for comparison.** The department may agree to allow a taxpayer to use another measure for comparison, provided that the method results in a comparison between qualifying and nonqualifying uses. For example, if work patterns or routines demonstrate typical behavior, the taxpayer with the department's approval can satisfy the majority use test using work site surveys as proof.

(b) **Bundling similar M&E into classes.** Each piece of M&E does not require a separate record if the taxpayer can establish that it is reasonable to bundle M&E into classes. Classes may be created only from similar pieces of machinery and equipment and only if the uses of the pieces are the same. For example, forklifts of various sizes and models can be bundled together if the forklifts are doing the same work, as in moving wrapped product from the assembly line to a storage area. An example of when not to bundle classes of M&E for purposes of the majority use threshold is the use of a computer that controls a machine through numerical control versus use of a computer that creates a camera ready page for printing.

(c) **Industry-wide standards.** Typically, whether the majority use threshold is met is decided on a case-by-case basis, looking at the specific manufacturing operation in which the item is being used. However, for purposes of applying the majority use threshold, the department may develop industry-wide standards. For instance, the aggregate industry uses concrete mixer trucks in a consistent manner across the industry. Based on a comparison of selling prices of the processed product picked up by the customer at the manufacturing site and delivery prices to a customer location, and taking into consideration the qualifying activity (interacting with tangible personal property) of the machinery and equipment compared to the nonqualifying activity (delivering the product) of the machinery and equipment, the department has determined that concrete trucks qualify under the majority use threshold. Only in those limited instances where it is apparent that the use of the concrete truck is atypical for the industry would the taxpayer be required to provide recordkeeping on the use of the truck (~~((in order))~~) to support the exemption.