# HOUSE BILL REPORT
# E2SHB 1024

**As Passed House:**
March 8, 1995

**Title:** An act relating to providing tax exemptions for manufacturing and processing.

**Brief Description:** Providing tax exemptions for manufacturing and processing.

**Sponsors:** By House Committee on Finance (originally sponsored by Representatives Van Luven, Foreman, B. Thomas, Lisk, Horn, Chandler, Casada, Dyer, Ballasiotes, Silver, Cooke, Brumsickle, Carlson, Sehlin, Sherstad, Dellwo, Benton, Skinner, Kremen, Hargrove, Costa, Delvin, Schoesler, Buck, Johnson, Thompson, Beeksma, Goldsmith, Radcliff, Hickel, Backlund, Crouse, Cairnes, Elliot, Reams, Pennington, Mastin, Mitchell, Conway, Quall, Ogden, Chappell, Regala, G. Fisher, Basich, Grant, Campbell, Smith, Robertson, Honeyford, Pelesky, Hankins, Koster, Lambert, D. Schmidt, Mulliken, Boldt, McMorris, Clements, Fuhrman, Sheldon, L. Thomas, Huff, Mielke, Talcott, McMahan, Stevens, Morris and Hymes).

**Brief History:**

**Committee Activity:**

Trade & Economic Development: 1/10/95, 1/11/95, 1/12/95 [DPS];
Finance: 1/19/95, 1/25/95, 2/21/95 [DP2S(w/o sub TED)].

**Floor Activity:**

Passed House: 3/8/95, 91-6.

## HOUSE COMMITTEE ON TRADE & ECONOMIC DEVELOPMENT

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 13 members: Representatives Van Luven, Chair; Radcliff, Vice Chair; D. Schmidt, Vice Chair; Sheldon, Ranking Minority Member; Veloria, Assistant Ranking Minority Member; Backlund; Ballasiotes; Hatfield; Hickel; Mason; Sherstad; Skinner and Valle.

**Staff:** Kenny Pittman (786-7392).

## HOUSE COMMITTEE ON FINANCE

**Majority Report:** The second substitute bill be substituted therefor and the second substitute bill do pass and do not pass the substitute bill by Committee on Trade & Economic Development. Signed by 10 members: Representatives B. Thomas, Chairman; Boldt, Vice Chairman; Carrell, Vice Chairman; Morris, Ranking Minority Member; Hymes; Mulliken; Pennington; Schoesler; Sheldon and Van Luven.

**Minority Report:** Do not pass. Signed by 2 members: Representatives Dickerson and Mason.

**Staff:** Bob Longman (786-7139).

**Background:** The state of Washington's tax structure includes a retail sales and use tax on materials and labor used to construct or renovate a manufacturing facility and to the purchase of new and replacement manufacturing or research and development equipment and machinery. The state imposes a tax that is based on 6.5 percent of the price of the taxable event. Local governments may impose an additional tax up to 1.7 percent of the price of the taxable event.

The state has developed several sales and use tax relief programs for business. These programs are designed to encourage manufacturing and research and development firms to either locate or expand their operations in Washington.

Distressed Area Tax Deferral

The program is targeted to areas with unemployment rates 20 percent higher than the state average. Manufacturing, research and development, and computer related businesses are given a deferral of their sales and use tax on buildings, machinery and equipment, and installation labor. The businesses must create one job per $750,000 of investment. The sales tax is forgiven on new buildings, new equipment, and modernization of existing buildings.

New Business Tax Deferral

The program is available state-wide to manufacturing and research and development businesses not doing business in the state before 1985. The sales and use tax on new buildings and equipment is deferred until 3 years after the project is completed. The business is required to repay the deferred taxes over a 5 year period.

High Technology Tax Deferral

The program is available state-wide to research and development and pilot-scale manufacturing businesses. The business must be involved in biotechnology, advanced computing, electronic device technology, advanced materials, environmental technology. The sales and use tax on new or expanded facilities and machinery and equipment is deferred until 3 years after the project is completed. The business is required to repay the deferred taxes over a 5 or 6 year period.

In an effort to encourage the development of high-wage jobs, the 1994 Legislature directed the Department of Revenue to study the current sales tax structure as it applies to manufacturers. The department, through its advisory committee, studied the existing tax structure and the economic and other effects of tax relief.

**Summary of Bill:** The state's sales and use tax relief programs are revised as follows. The bill: (1) creates a state-wide tax exemption program for equipment and machinery used by manufacturing and research and development firms; (2) revises the distressed area and high technology deferral programs; and (3) repeals the new business tax deferral program.

State-Wide Tax Exemption

A state-wide sales and use tax exemption program is created. Manufacturing, research and development, and potato packing firms are exempt from sales and use taxes on all new and replacement machinery used directly in their process or equipment purchases and the labor and services to install the machinery and equipment. The exemption also applies to the purchase and installation of pollution control equipment used to prevent pollution or contamination as a result of the operation of the facility.

The term manufacturing does not include the production of electricity or the preparation of food products on the premise of a person selling food at retail.

The state may reimburse local governments for the loss of local sales and use tax revenue due to the state-wide tax exemption on manufacturing machinery and equipment. Reimbursements are limited to losses that exceed 5 percent of the local government's sales and use tax revenue.

Distressed Area Tax Deferral

The distressed area tax deferral requirement that businesses create one job per $750,000 of investment in buildings, machinery and equipment or cogeneration projects, including labor and services, is repealed. Eligible cogeneration projects are limited to projects that generate power for consumption within the manufacturing site. The job per investment requirement is retained for projects located in community empowerment zones and counties that are contiguous to eligible counties. The renovation of an existing facility must increase the floor space or production capacity of the facility to qualify for the tax deferral.

New Business Tax Deferral

The tax deferral on new buildings and equipment, including labor and services, for manufacturing and research and development businesses not doing business in the state before 1985 is terminated. The termination date of the program is changed from December 31, 1998, to December 31, 1995.

High Technology Tax Deferral

The high technology tax deferral is extended to the construction of new structures and expansion or renovation of existing structures used for pilot scale manufacturing or qualified research and development. The expansion or renovation costs of the structure must increase the floor space or production capacity of the facility. The requirement that additional purchases of machinery and equipment used in research and development activities exceed the true and fair value of the facility, prior to improvement, by 25 percent is repealed.

A high technology firm is eligible for a total exemption of deferred taxes if specific program requirements are met for a eight-year period after completion of the project. Any firm found in non-compliance, during the eight-year period, will be required to repay a pro-rated share of deferred taxes. The repayment is based on the number of years the project was in compliance plus interest, but not penalties.

The Department of Revenue must conduct a study on the effects of the state-wide tax exemption program. The results are to be reported to the Governor and Legislature by September 1, 1998.

The Department of Revenue is directed to adopt rules to implement the programs.

**Appropriation:** None.

**Fiscal Note:** Available on first substitute bill. New fiscal note requested on February 23, 1995.

**Effective Date of Bill:** The bill contains an emergency clause and takes effect on July 1, 1995. However, the reimbursement of local sales tax losses is null and void if not funded in the budget.

**Testimony For:** (Trade & Economic Development) (Original Bill) The present state tax system is a disincentive to business investment. The sales and use tax is a liability that must be paid even before the product is made or sold. The goal is to provide an incentive to businesses to invest in machinery and equipment and expand their operations in Washington. Business expansion creates high wage manufacturing jobs in the state. The tax exemption would put Washington on a level playing field with surrounding states that do not charge a tax on machinery and equipment.

(Finance) Same as in Trade and Economic Development Committee.

**Testimony Against:** (Trade & Economic Development) (Original Bill) The loss of revenue hurts local governments at a time when demand for services are increasing. Local governments with a large manufacturing base would be hurt the most. Local governments need the revenue to respond to the impacts of growth on the infrastructure, the criminal justice system, and the social service system.

(Finance) Manufacturers should be required to pay adequate family wages.

**Testified:** (Trade & Economic Development) Representative Steve Van Luven, Bill Sponsor (Pro); Len McComb, Department of Revenue (Pro); Larry Culver, CellPro (Pro); Joe Holden, HCI Steel Products (Pro); Roy Wiseman, U.S. Oil (Pro); Tom Dooley, Association of Washington Business (Pro); Randy Lewis, city of Tacoma (Pro); Ron Yamamoto, Boeing (Pro); Krista Fichler, Seattle Chamber of Commerce (Pro); Dennis Matson, Thurston County Economic Development Council (Pro); John Lindsay, TRIDEC (Pro); Melinda Kile, Tree Top (Pro); Pat Dunn, Member of Advisory Committee for the Manufacturing Tax Study (Pro); Larry Young, PACCAR (Pro); Nick Muelln, Weyerhauser (Pro); Stan Finkelstein, Association of Washington Cities (Con); and Rosemarie Ives, Mayor of Redmond (Con).

(Finance) (Pro) Representative Steve Van Luven, Prime Sponsor; Joe Pinzone, Sharp Micro Electronics Technology; John Fratt, Port of Kalama; Tom Ranken, Washington Biotechnology; Len McComb, Department of Revenue; Nick Mullen, Weyerhauser (member of the department's Manufacturing Tax Study); Pat Dunn, Hellen Erhman (member of the department's Manufacturing Tax Study); Tom Dooley, Association of Washington Business; Krista Eichler, Seattle Chamber of Commerce; Jim Boldt, TRIDEC (Tri-Cities Economic Development Council). (with concerns) Rosemarie Ives, Mayor of Redmond; Stan Finkelstein, Association of Washington Cities; and Linda Crawford, City of Redmond. (Con) Robby Stern, Washington State Labor Council.