

HOUSE BILL REPORT

SB 5725

As Reported by House Committee On:
Finance

Title: An act relating to providing tax incentives to support the semiconductor cluster in Washington state.

Brief Description: Providing tax incentives to support the state's semiconductor cluster.

Sponsors: Senators Zarelli, T. Sheldon, Carlson, Reardon, Benton, Hewitt, Winsley, Hale, Sheahan, Honeyford, Finkbeiner, Johnson and West.

Brief History:

Committee Activity:

Finance: 4/16/03 [DPA].

Brief Summary of Bill
(As Amended by House Committee)

- Lowers business and occupation (B&O) tax rate for manufacturing semiconductor materials from 0.484 percent to 0.138 percent.
- Exempts gases and chemicals used in semiconductor manufacturing from retail sales and use tax.
- Exempts construction of new semiconductor manufacturing buildings from retail sales and use tax.
- Creates a B&O tax job credit of \$3,000 for each employment position in semiconductor manufacturing production.
- Exempts machinery and equipment used in manufacturing semiconductor materials from property taxation.
- Provides for accountability reporting and a review of the rates, credits, and exemptions.

HOUSE COMMITTEE ON FINANCE

Majority Report: Do pass as amended. Signed by 8 members: Representatives Gombosky, Chair; Cairnes, Ranking Minority Member; Orcutt, Assistant Ranking

Minority Member; Ahern, Conway, Morris, Roach and Santos.

Minority Report: Do not pass. Signed by 1 member: Representative McIntire, Vice Chair.

Staff: Rick Peterson (786-7150).

Background:

Sales tax is imposed on retail sales of most items of tangible personal property and some services, including construction and repair services. Sales and use taxes are imposed by the state, counties, and cities. Sales and use tax rates vary between 7 and 8.9 percent, depending on location. There are a number of sales and use tax exemptions including machinery and equipment directly used in manufacturing.

Washington's major business tax is the business and occupation (B&O) tax. The B&O tax is imposed on the gross receipts of business activities conducted within the state, without any deduction for the costs of doing business. The tax is imposed on the gross receipts from all business activities conducted within the state. Revenues are deposited to the state General Fund. A business may have more than one B&O tax rate, depending on the types of activities conducted. Manufacturing activity is generally taxed at a rate of 0.484 percent although food processing is taxed at 0.138 percent.

Property taxes are imposed by state and local governments. All real and personal property in this state is subject to the property tax based on its value, unless a specific exemption is provided by law. There are exemptions for certain properties, including property owned by federal, state and local governments, churches, farm machinery, and business inventory.

The tax bill is determined by multiplying the assessed value by the tax rate for each taxing district in which the property is located. The county assessor determines assessed value for each property. The county assessor also calculates the tax rate necessary to raise the correct amount of property taxes for each taxing district. The assessor calculates the rate so the individual district rate limit, the district revenue limit, and the aggregate rate limits are all satisfied.

The annual increase in district property taxes is restricted by the property tax revenue limit. This limit requires the district's tax rate to be reduced as necessary to limit the total amount of property taxes to the highest property tax amount in the three most recent years, plus 1 percent, plus an amount equal to last year's tax rate multiplied by the value of new construction in the district. The value of new construction does not include any property that is exempt from taxation. This limit acts to reduce district rates below the maximum rate allowed for the district.

Summary of Amended Bill:

The business and occupation (B & O) tax rate for manufacturing of semiconductor materials is reduced from 0.484 percent to 0.138 percent. "Semiconductor materials" means silicon crystals, silicon ingots, raw polished semiconductor wafers, compound semiconductors, integrated circuits, and microchips.

Gases and chemicals used for the manufacture of semiconductor materials are exempt from retail sales and use tax.

The construction of new buildings for the manufacture of semiconductor materials is exempt from sales and use tax. The exemption includes tangible personal property incorporated as an ingredient or component of the building and the labor and services related to the installation of building fixtures.

To qualify for the sales and use tax exemption, the manufacturer must maintain at least 75 percent of full employment at the new building for eight years following the start of commercial production. One-eighth of the exempt sales and use tax must be paid for each year the manufacturer fails to meet this requirement.

An annual B & O tax credit of \$3,000 for up to eight years is available for each employment position in a semiconductor manufacturing facility that is exempt from the sales and use tax under the bill.

Machinery and equipment used at manufacturing buildings exempted from the retail sales and use taxes under this bill are exempt from property taxes. The property tax exemption is limited to machinery and equipment that is eligible for the retail sales and use tax exemption for manufacturing machinery and equipment. In order to qualify for this exemption, the manufacturer must comply with the employment requirements of the retail sales and use tax exemptions.

A manufacturer who uses the preferential B&O tax rate or who uses an exemption under the bill must file an annual report to the Department of Revenue (DOR) detailing the employment, wages, and employer provided health and retirement benefits at the manufacturing site. The contents of the report are not confidential and may be disclosed to the public upon request.

Failure to submit an annual report revokes the preferential rate, exemption, or credit and the amount of taxes exempted or credited for that year must be paid with interest.

By November 1, 2010, and November 1, 2016, the fiscal committees of the House of Representatives and the Senate, in consultation with the DOR, shall report to the Legislature on the effectiveness of these tax exemptions on job retention, net jobs created

for Washington residents, company growth, diversification of the state's economy, cluster dynamics, and other related factors.

All the exemptions start July 1, 2005, and end July 1, 2017, except the property tax exemption applies for taxes levied for collection in 2006 through 2018.

Amended Bill Compared to Original Bill:

The amended bill adds the following to the original bill. Compound semiconductors are added to the list of semiconductor materials eligible for the tax exemptions. The full employment targets used for compliance with qualifications for the sales tax exemption on construction of new semiconductor manufacturing buildings are available for disclosure. Specific employment, wage and benefit information is required in the annual report made by users of the tax exemptions. The amount of taxes repaid by a firm that fails to file an annual report is available for disclosure. The November 1, 2010, report by the fiscal committees is added.

Appropriation: None.

Fiscal Note: Available.

Effective Date of Amended Bill: The bill takes effect July 1, 2005.

Testimony For: Southwest Washington has developed a semiconductor cluster that is critical to the economy. We are now at the point where we either move forward or lose this cluster to Portland or Texas or somewhere out of the country. The bill applies statewide. The industry has over 3,000 jobs paying over \$50,000 per year in wages and benefits. We need to protect these jobs. The manufacturing exemption was responsible for bringing in manufacturing investment to Washington. Other states have caught up. Other states and countries are willing to do a lot to attract these businesses. Are we going to continue to be a leader in the semiconductor industry? We are not giving up anything because this investment will generate more revenue over time. It is worth \$250 million in new revenue to the state.

Testimony Against: None.

Testified: Senator Zarelli, prime sponsor; and Senator Benton, sponsor.