
SUBSTITUTE HOUSE BILL 2546

State of Washington

58th Legislature

2004 Regular Session

By House Committee on Finance (originally sponsored by Representatives McIntire, Morris, Hunter, Ruderman, Kessler, Lovick, Hunt, Grant, Hatfield, Fromhold, Clibborn and Clements; by request of Governor Locke)

READ FIRST TIME 01/27/04.

1 AN ACT Relating to high technology and research and development tax
2 incentives; amending RCW 82.63.005, 82.04.4452, 82.63.010, 82.63.020,
3 82.63.030, 82.63.045, and 82.63.070; adding new sections to chapter
4 82.04 RCW; providing an effective date; and providing expiration dates.

5 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

6 **Sec. 1.** RCW 82.63.005 and 1994 sp.s. c 5 s 1 are each amended to
7 read as follows:

8 The legislature finds that high-wage, high-skilled jobs are vital
9 to the economic health of the state's citizens, and that targeted tax
10 incentives will encourage the formation of high-wage, high-skilled
11 jobs. The legislature also finds that tax incentives should be subject
12 to the same rigorous requirements for efficiency and accountability as
13 are other expenditure programs, and that tax incentives should
14 therefore be focused to provide the greatest possible return on the
15 state's investment.

16 The legislature also finds that high-technology businesses are a
17 vital and growing source of high-wage, high-skilled jobs in this state,
18 and that the high-technology sector is a key component of the state's
19 effort to encourage economic diversification. However, the legislature

1 finds that many high-technology businesses incur significant costs
2 associated with research and development and pilot scale manufacturing
3 many years before a marketable product can be produced, and that
4 current state tax policy discourages the growth of these companies by
5 taxing them long before they become profitable.

6 The legislature further finds that stimulating growth of high-
7 technology businesses early in their development cycle, when they are
8 turning ideas into marketable products, will build upon the state's
9 established high-technology base, creating additional research and
10 development jobs and subsequent manufacturing facilities.

11 For these reasons, the legislature hereby establishes a program of
12 business and occupation tax credits for qualified research and
13 development expenditures. The legislature also hereby establishes a
14 tax deferral program for high-technology research and development and
15 pilot scale manufacturing facilities. The legislature declares that
16 these limited programs serve the vital public purposes of incenting
17 expenditures in research and development, supporting, and sustaining as
18 they develop new technologies and products, and creating quality
19 employment opportunities in this state. The legislature further
20 declares its intent to create a contract within the meaning of Article
21 I, section 23 of the state Constitution as to those businesses that
22 make capital investments in consideration of the tax deferral program
23 established in this chapter.

24 **Sec. 2.** RCW 82.04.4452 and 2000 c 103 s 7 are each amended to read
25 as follows:

26 (1) In computing the tax imposed under this chapter, a credit is
27 allowed for each person whose research and development spending during
28 the year in which the credit is claimed exceeds 0.92 percent of the
29 person's taxable amount during the same calendar year.

30 (2) The credit (~~is equal to~~) shall be calculated as follows: (a)
31 Determine the greater of the amount of qualified research and
32 development expenditures of a person or eighty percent of amounts
33 received by a person other than a public educational or research
34 institution in compensation for the conduct of qualified research and
35 development(~~(, multiplied)~~); (b) subtract 0.92 percent of the person's
36 taxable amount from the amount determined under (a) of this subsection;
37 (c) multiply the amount determined under (b) of this subsection by the

1 rate provided in RCW 82.04.260(3) in the case of a nonprofit
2 corporation or nonprofit association engaging within this state in
3 research and development, and the rate provided in RCW 82.04.290(2) for
4 every other person.

5 (3) Any person entitled to the credit provided in subsection (2) of
6 this section as a result of qualified research and development
7 conducted under contract may assign all or any portion of the credit to
8 the person contracting for the performance of the qualified research
9 and development.

10 (4) The credit, including any credit assigned to a person under
11 subsection (3) of this section, shall be taken against taxes due for
12 the same calendar year in which the qualified research and development
13 expenditures are incurred. The credit, including any credit assigned
14 to a person under subsection (3) of this section, for each calendar
15 year shall not exceed the lesser of two million dollars or the amount
16 of tax otherwise due under this chapter for the calendar year.

17 (5) Any person taking the credit, including any credit assigned to
18 a person under subsection (3) of this section, whose research and
19 development spending during the calendar year in which the credit is
20 claimed fails to exceed 0.92 percent of the person's taxable amount
21 during the same calendar year shall be liable for payment of the
22 additional taxes represented by the amount of credit taken together
23 with interest, but not penalties. Interest shall be due at the rate
24 provided for delinquent excise taxes retroactively to the date the
25 credit was taken until the taxes are paid. Any credit assigned to a
26 person under subsection (3) of this section that is disallowed as a
27 result of this section may be taken by the person who performed the
28 qualified research and development subject to the limitations set forth
29 in subsection (4) of this section.

30 (6) Any person claiming the credit, and any person assigning a
31 credit as provided in subsection (3) of this section, shall file an
32 ~~((affidavit))~~ annual report in a form prescribed by the department
33 which shall include the amount of the credit claimed, ~~((an estimate~~
34 ~~of))~~ the ~~((anticipated))~~ qualified research and development
35 expenditures during the calendar year for which the credit is claimed,
36 ~~((an estimate of))~~ and the taxable amount during the calendar year for
37 which the credit is claimed, and such additional information as the

1 department may prescribe. The report is due by March 31st following
2 any year a credit is taken.

3 (7)(a) The legislature finds that accountability and effectiveness
4 are important aspects of setting tax policy. In order to make policy
5 choices regarding the best use of limited state resources the
6 legislature needs information on how a tax incentive is used.

7 (b) A person claiming the credit shall agree to ((supply the
8 department with information necessary to measure the results of the tax
9 credit program for qualified research and development expenditures))
10 complete an annual survey. The annual survey is in addition to the
11 annual report due under subsection (6) of this section. The survey is
12 due by March 31st following any year in which a credit is taken.
13 Survey information is not subject to the confidentiality provisions of
14 RCW 82.32.330 and may be disclosed to the public upon request, except
15 that persons taking less than ten thousand dollars of credit during the
16 period covered by the survey may request the department to treat the
17 survey information as confidential under RCW 82.32.330. The survey
18 shall include the amount of the tax credit taken, the number of new
19 products or research projects by general category, and the number of
20 trademarks, patents, and copyrights associated with the research and
21 development activities for which a credit was taken. The survey shall
22 also include the following information for employment positions in
23 Washington:

24 (i) The number of total employment positions;

25 (ii) Full-time, part-time, and temporary employment positions as a
26 percent of total employment;

27 (iii) The number of employment positions according to the following
28 wage bands: Less than thirty thousand dollars; thirty thousand dollars
29 or greater, but less than sixty thousand dollars; and sixty thousand
30 dollars or greater. A wage band containing less than three individuals
31 may be combined with another wage band; and

32 (iv) The number of employment positions that have employer-provided
33 medical, dental, and retirement benefits, by each of the wage bands.

34 (c) The department may request additional information necessary to
35 measure the results of the tax credit program, to be submitted at the
36 same time as the survey. This additional information is deemed
37 taxpayer information under RCW 82.32.330 and is not disclosable.

1 (d) If a person fails to complete the survey required under this
2 subsection by the due date, the person entitled to the credit provided
3 in subsection (2) of this section is not eligible to take or assign the
4 credit provided in subsection (2) of this section in the year the
5 person failed to complete the survey.

6 (8) The department shall use the information (~~(required under)~~)
7 from subsection (7) of this section to (~~(perform three assessments on)~~)
8 study the tax credit program authorized under this section. (~~The~~
9 ~~assessments will take place in 1997, 2000, and 2003. The department~~
10 ~~shall prepare reports on each assessment and deliver their reports by~~
11 ~~September 1, 1997, September 1, 2000, and September 1, 2003. The~~
12 ~~assessments)) The department shall report to the legislature by
13 December 1, 2009. The report shall measure the effect of the program
14 on job creation, the number of jobs created for Washington residents,
15 company growth, the introduction of new products, the diversification
16 of the state's economy, growth in research and development investment,
17 the movement of firms or the consolidation of firms' operations into
18 the state, and such other factors as the department selects.~~

19 (9) For the purpose of this section:

20 (a) "Qualified research and development expenditures" means
21 operating expenses, including wages, compensation of a proprietor or a
22 partner in a partnership as determined under rules adopted by the
23 department, benefits, supplies, and computer expenses, directly
24 incurred in qualified research and development by a person claiming the
25 credit provided in this section. The term does not include amounts
26 paid to a person other than a public educational or research
27 institution to conduct qualified research and development. Nor does
28 the term include capital costs and overhead, such as expenses for land,
29 structures, or depreciable property.

30 (b) "Qualified research and development" shall have the same
31 meaning as in RCW 82.63.010.

32 (c) "Research and development spending" means qualified research
33 and development expenditures plus eighty percent of amounts paid to a
34 person other than a public educational or research institution to
35 conduct qualified research and development.

36 (d) "Taxable amount" means the taxable amount subject to the tax
37 imposed in this chapter required to be reported on the person's

1 combined excise tax returns during the year in which the credit is
2 claimed, less any taxable amount for which a credit is allowed under
3 RCW 82.04.440.

4 (10) This section expires (~~December 31, 2004~~) January 1, 2011.

5 **Sec. 3.** RCW 82.63.010 and 1995 1st sp.s. c 3 s 12 are each amended
6 to read as follows:

7 Unless the context clearly requires otherwise, the definitions in
8 this section apply throughout this chapter.

9 (1) "Advanced computing" means technologies used in the designing
10 and developing of computing hardware and software, including
11 innovations in designing the full spectrum of hardware from hand-held
12 calculators to super computers, and peripheral equipment.

13 (2) "Advanced materials" means materials with engineered properties
14 created through the development of specialized processing and synthesis
15 technology, including ceramics, high value-added metals, electronic
16 materials, composites, polymers, and biomaterials.

17 (3) "Applicant" means a person applying for a tax deferral under
18 this chapter.

19 (4) "Biotechnology" means the application of technologies, such as
20 recombinant DNA techniques, biochemistry, molecular and cellular
21 biology, genetics and genetic engineering, cell fusion techniques, and
22 new bioprocesses, using living organisms, or parts of organisms, to
23 produce or modify products, to improve plants or animals, to develop
24 microorganisms for specific uses, to identify targets for small
25 molecule pharmaceutical development, or to transform biological systems
26 into useful processes and products or to develop microorganisms for
27 specific uses.

28 (5) "Department" means the department of revenue.

29 (6) "Electronic device technology" means technologies involving
30 microelectronics; semiconductors; electronic equipment and
31 instrumentation; radio frequency, microwave, and millimeter
32 electronics; optical and optic-electrical devices; and data and digital
33 communications and imaging devices.

34 (7) "Eligible investment project" means an investment project which
35 either initiates a new operation, or expands or diversifies a current
36 operation by expanding, renovating, or equipping an existing facility.

1 The lessor or owner of the qualified building is not eligible for a
2 deferral unless:

3 (a) The underlying ownership of the buildings, machinery, and
4 equipment vests exclusively in the same person(~~(, or unless)~~); or

5 (b)(i) The lessor by written contract agrees to pass the economic
6 benefit of the deferral to the lessee (~~(in the form of reduced rent~~
7 payments));

8 (ii) The lessee that receives the economic benefit of the deferral
9 agrees in writing with the department to complete the annual survey
10 required under RCW 82.63.020(2); and

11 (iii) The economic benefit of the deferral passed to the lessee is
12 no less than the amount of tax deferred by the lessor and is evidenced
13 by written documentation of any type of payment, credit, or other
14 financial arrangement between the lessor or owner of the qualified
15 building and the lessee.

16 (8) "Environmental technology" means assessment and prevention of
17 threats or damage to human health or the environment, environmental
18 cleanup, and the development of alternative energy sources.

19 (9) "Investment project" means an investment in qualified buildings
20 or qualified machinery and equipment, including labor and services
21 rendered in the planning, installation, and construction or improvement
22 of the project.

23 (10) "Person" has the meaning given in RCW 82.04.030 and includes
24 state universities as defined in RCW 28B.10.016.

25 (11) "Pilot scale manufacturing" means design, construction, and
26 testing of preproduction prototypes and models in the fields of
27 biotechnology, advanced computing, electronic device technology,
28 advanced materials, and environmental technology other than for
29 commercial sale. As used in this subsection, "commercial sale"
30 excludes sales of prototypes or sales for market testing if the total
31 gross receipts from such sales of the product, service, or process do
32 not exceed one million dollars.

33 (12) "Qualified buildings" means construction of new structures,
34 and expansion or renovation of existing structures for the purpose of
35 increasing floor space or production capacity used for pilot scale
36 manufacturing or qualified research and development, including plant
37 offices and other facilities that are an essential or an integral part
38 of a structure used for pilot scale manufacturing or qualified research

1 and development. If a building is used partly for pilot scale
2 manufacturing or qualified research and development, and partly for
3 other purposes, the applicable tax deferral shall be determined by
4 apportionment of the costs of construction under rules adopted by the
5 department.

6 (13) "Qualified machinery and equipment" means fixtures, equipment,
7 and support facilities that are an integral and necessary part of a
8 pilot scale manufacturing or qualified research and development
9 operation. "Qualified machinery and equipment" includes: Computers;
10 software; data processing equipment; laboratory equipment,
11 instrumentation, and other devices used in a process of experimentation
12 to develop a new or improved pilot model, plant process, product,
13 formula, invention, or similar property; manufacturing components such
14 as belts, pulleys, shafts, and moving parts; molds, tools, and dies;
15 vats, tanks, and fermenters; operating structures; and all other
16 equipment used to control, monitor, or operate the machinery. For
17 purposes of this chapter, qualified machinery and equipment must be
18 either new to the taxing jurisdiction of the state or new to the
19 certificate holder, except that used machinery and equipment may be
20 treated as qualified machinery and equipment if the certificate holder
21 either brings the machinery and equipment into Washington or makes a
22 retail purchase of the machinery and equipment in Washington or
23 elsewhere.

24 (14) "Qualified research and development" means research and
25 development performed within this state in the fields of advanced
26 computing, advanced materials, biotechnology, electronic device
27 technology, and environmental technology.

28 (15) "Recipient" means a person receiving a tax deferral under this
29 chapter.

30 (16) "Research and development" means activities performed to
31 discover technological information, and technical and nonroutine
32 activities concerned with translating technological information into
33 new or improved products, processes, techniques, formulas, inventions,
34 or software. The term includes exploration of a new use for an
35 existing drug, device, or biological product if the new use requires
36 separate licensing by the federal food and drug administration under
37 chapter 21, C.F.R., as amended. The term does not include adaptation
38 or duplication of existing products where the products are not

1 substantially improved by application of the technology, nor does the
2 term include surveys and studies, social science and humanities
3 research, market research or testing, quality control, sale promotion
4 and service, computer software developed for internal use, and research
5 in areas such as improved style, taste, and seasonal design.

6 (17)(a) "Initiation of construction" means the date that a building
7 permit is issued under the international building code for:

8 (i) Construction of the qualified building, in the event the
9 underlying ownership of the building vests exclusively with the person
10 receiving the economic benefit of the deferral;

11 (ii) Construction of the qualified building, in the event the
12 economic benefits of the deferral are passed to a lessee as provided in
13 subsection (7) of this section; or

14 (iii) Tenant improvements for a qualified building, in the event
15 the economic benefits of the deferral are passed to a lessee as
16 provided in subsection (7) of this section.

17 (b) "Initiation of construction" does not include soil testing,
18 site clearing and grading, site preparation, or any other related
19 activities that are initiated before the issuance of a building permit
20 for the construction of the foundation of the building.

21 (c) If the investment project is a phased project, "initiation of
22 construction" shall apply separately to each phase.

23 **Sec. 4.** RCW 82.63.020 and 1994 sp.s. c 5 s 4 are each amended to
24 read as follows:

25 (1) Application for deferral of taxes under this chapter must be
26 made before initiation of construction of, or acquisition of equipment
27 or machinery for the investment project. The application shall be made
28 to the department in a form and manner prescribed by the department.
29 The application shall contain information regarding the location of the
30 investment project, the applicant's average employment in the state for
31 the prior year, estimated or actual new employment related to the
32 project, estimated or actual wages of employees related to the project,
33 estimated or actual costs, time schedules for completion and operation,
34 and other information required by the department. The department shall
35 rule on the application within sixty days.

36 (2)(a) The legislature finds that accountability and effectiveness

1 are important aspects of setting tax policy. In order to make policy
2 choices regarding the best use of limited state resources the
3 legislature needs information on how a tax incentive is used.

4 (b) Applicants for deferral of taxes under this chapter shall agree
5 to ((supply the department with nonproprietary information necessary to
6 measure the results of the tax deferral program for high technology
7 research and development and pilot scale manufacturing facilities))
8 complete an annual survey. The survey is due by March 31st of the year
9 following the calendar year in which the investment project is
10 certified by the department as having been operationally complete and
11 the seven succeeding calendar years. Survey information is not subject
12 to the confidentiality provisions of RCW 82.32.330 and may be disclosed
13 to the public upon request. The survey shall include the amount of tax
14 deferred, the number of new products or research projects by general
15 category, and the number of trademarks, patents, and copyrights
16 associated with activities at the investment project. The survey shall
17 also include the following information for employment positions in
18 Washington:

19 (i) The number of total employment positions;

20 (ii) Full-time, part-time, and temporary employment positions as a
21 percent of total employment;

22 (iii) The number of employment positions according to the following
23 wage bands: Less than thirty thousand dollars; thirty thousand dollars
24 or greater, but less than sixty thousand dollars; and sixty thousand
25 dollars or greater. A wage band containing less than three individuals
26 may be combined with another wage band; and

27 (iv) The number of employment positions that have employer-provided
28 medical, dental, and retirement benefits, by each of the wage bands.

29 (c) The department may request additional information necessary to
30 measure the results of the deferral program, to be submitted at the
31 same time as the survey. This additional information is deemed
32 taxpayer information under RCW 82.32.330 and is not disclosable.

33 (3) The department shall use the information to ((perform three
34 assessments on)) study the tax deferral program authorized under this
35 chapter. ((The assessments will take place in 1997, 2000, and 2003.))
36 The department shall ((prepare reports on each assessment and deliver
37 their reports by September 1, 1997, September 1, 2000, and September 1,
38 2003)) report to the legislature by December 1, 2009. The

1 ((assessments)) report shall measure the effect of the program on job
2 creation, the number of jobs created for Washington residents, company
3 growth, the introduction of new products, the diversification of the
4 state's economy, growth in research and development investment, the
5 movement of firms or the consolidation of firms' operations into the
6 state, and such other factors as the department selects.

7 **Sec. 5.** RCW 82.63.030 and 1994 sp.s. c 5 s 5 are each amended to
8 read as follows:

9 (1) Except as provided in subsection (2) of this section, the
10 department shall issue a sales and use tax deferral certificate for
11 state and local sales and use taxes due under chapters 82.08, 82.12,
12 and 82.14 RCW on each eligible investment project.

13 (2) No certificate may be issued for an investment project that has
14 already received a deferral under chapter 82.60 or 82.61 RCW or this
15 chapter, except that an investment project for qualified research and
16 development that has already received a deferral may also receive an
17 additional deferral certificate for adapting the investment project for
18 use in pilot scale manufacturing.

19 (3) This section shall expire July 1, ((2004)) 2010.

20 **Sec. 6.** RCW 82.63.045 and 2000 c 106 s 10 are each amended to read
21 as follows:

22 (1) Except as provided in subsection (2) of this section, taxes
23 deferred under this chapter need not be repaid.

24 (2)(a) If, on the basis of ((a report)) survey under RCW 82.63.020
25 or other information, the department finds that an investment project
26 is used for purposes other than qualified research and development or
27 pilot scale manufacturing at any time during the calendar year in which
28 the investment project is certified by the department as having been
29 operationally completed, or at any time during any of the seven
30 succeeding calendar years, a portion of deferred taxes shall be
31 immediately due according to the following schedule:

32	Year in which use occurs	% of deferred taxes due
33	1	100%
34	2	87.5%

1	3	75%
2	4	62.5%
3	5	50%
4	6	37.5%
5	7	25%
6	8	12.5%

7 (b) If a recipient of the deferral fails to complete the annual
8 survey required under RCW 82.63.020 by the date due, 12.5 percent of
9 the deferred tax shall be immediately due.

10 (c) If an investment project is used for purposes other than
11 qualified research and development or pilot scale manufacturing at any
12 time during the calendar year in which the investment project is
13 certified as having been operationally complete and the recipient of
14 the deferral fails to complete the annual survey due under RCW
15 82.63.020, the portion of deferred taxes immediately due is the amount
16 on the schedule in (a) of this subsection.

17 (3) The department shall assess interest at the rate provided for
18 delinquent taxes, but not penalties, retroactively to the date of
19 deferral. The debt for deferred taxes will not be extinguished by
20 insolvency or other failure of the recipient. Transfer of ownership
21 does not terminate the deferral. The deferral is transferred, subject
22 to the successor meeting the eligibility requirements of this chapter,
23 for the remaining periods of the deferral.

24 ~~((+3))~~ (4) Notwithstanding subsection (2) of this section,
25 deferred taxes on the following need not be repaid:

26 (a) Machinery and equipment, and sales of or charges made for labor
27 and services, which at the time of purchase would have qualified for
28 exemption under RCW 82.08.02565; and

29 (b) Machinery and equipment which at the time of first use would
30 have qualified for exemption under RCW 82.12.02565.

31 **Sec. 7.** RCW 82.63.070 and 1994 sp.s. c 5 s 9 are each amended to
32 read as follows:

33 Applications ~~((and other information))~~ received by the department
34 under this chapter are not confidential and are subject to disclosure.

35 NEW SECTION. **Sec. 8.** A new section is added to chapter 82.04 RCW
36 to read as follows:

1 This chapter does not apply to amounts received by any person for
2 research and development under the federal small business innovation
3 research program (114 Stat. 2763A; 15 U.S.C. Sec. 638 et seq.).

4 NEW SECTION. **Sec. 9.** A new section is added to chapter 82.04 RCW
5 to read as follows:

6 This chapter does not apply to amounts received by any person for
7 research and development under the federal small business technology
8 transfer program (115 Stat. 263; 15 U.S.C. Sec. 638 et seq.).

9 NEW SECTION. **Sec. 10.** Sections 8 and 9 of this act take effect
10 July 1, 2004.

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