

HOUSE BILL REPORT

SHB 2640

As Passed Legislature

Title: An act relating to biotechnology product and medical device manufacturing tax incentives.

Brief Description: Providing biotechnology product and medical device manufacturing tax incentives.

Sponsors: By House Committee on Finance (originally sponsored by Representatives B. Sullivan, McCoy, O'Brien, Haler, Sells, Morris, Ericks, Strow and Dunn).

Brief History:

Committee Activity:

Technology, Energy & Communications: 1/24/06, 1/31/06 [DP];

Finance: 2/6/06 [DPS].

Floor Activity:

Passed House: 2/10/06, 93-5.

Passed Senate: 3/8/06, 43-3.

Passed Legislature.

Brief Summary of Substitute Bill

- Exempts manufacturing facilities used to produce biotechnology products and medical devices from sales and use tax.

HOUSE COMMITTEE ON TECHNOLOGY, ENERGY & COMMUNICATIONS

Majority Report: Do pass. Signed by 11 members: Representatives Morris, Chair; Kilmer, Vice Chair; Crouse, Ranking Minority Member; Haler, Assistant Ranking Minority Member; Ericks, Hudgins, Nixon, P. Sullivan, Sump, Takko and Wallace.

Staff: Scott Richards (786-7156).

HOUSE COMMITTEE ON FINANCE

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 11 members: Representatives McIntire, Chair; Hunter, Vice Chair; Orcutt, Ranking Minority Member; Roach, Assistant Ranking Minority Member; Ahern, Condotta, Conway, Ericks, Hasegawa, Santos and Shabro.

Staff: Rick Peterson (786-7150).

Background:

According to the Department of Community, Trade and Economic Development (DCTED), Washington has 190 companies dedicated to biotechnology, of which:

- 37 percent pursue the research and development of therapeutic products;
- 27 percent focus on diagnostics;
- 21 percent engage in contract manufacturing and genetic testing;
- 9 percent undertake plant, agriculture and animal research; and
- 4 percent concentrate on natural resources.

Since 1995, local biotechnology companies have attracted more than \$400 million in venture capital investment and produced more than \$500 million in research partnerships with biotech and pharmaceutical companies. The biotech industry generates an estimated \$1.8 billion in revenues and nearly \$500 million in exports. The DCTED estimates that biotechnology and medical technology companies in Washington, in 2005, directly employed more than 23,000 people with indirect employment exceeding 69,000.

Rural County Sales Tax Deferral

To encourage manufacturing and research and development (R&D) activities, and related job creation in rural areas, a deferral of state and local retail sales and use tax is available for new or remodeled buildings and/or equipment used in manufacturing or R&D in certain areas. To qualify, the project must be located in a county with an average population density of no more than 100 persons per square mile or in a targeted community empowerment zone.

High Technology Deferral

To stimulate the creation of high wage jobs in high technology industries and ultimately to encourage the expansion of manufacturing in Washington, a deferral of state and local retail sales/use tax is allowed for the construction of buildings and acquisition of machinery and equipment for projects involving research and development or pilot scale manufacturing. To qualify, the firm must be engaged in one of five areas related to high technology: advanced computing, advanced materials, biotechnology, electronic device technology, or environmental technology.

Credit for Job Training Services

To encourage firms in rural counties to employ local residents who may need training, 20 percent of the amount spent on job training by firms that are eligible for the rural county sales tax deferral/exemption program may be taken as a credit against business and occupation tax. The training must be designed to enhance job performance in a state-approved program which is sponsored or provided by the employer.

Summary of Substitute Bill:

A biotechnology product means any virus, therapeutic serum, antibody, protein, toxin, antitoxin, vaccine, blood, blood component or derivative, allergenic product, or analogous product produced through the application of biotechnology that is used in the prevention, treatment, or cure of diseases or injuries to humans.

Medical device means an instrument, apparatus, implement, machine, contrivance, implant, in vitro reagent, or other similar or related article, including any component, part, or accessory, that is designed or developed. It is required that medical devices be:

- recognized in the national formulary, or the United States pharmacopeia, or any supplement to them;
- intended for use in the diagnosis of disease, or in the cure, mitigation, treatment, or prevention of disease or other conditions in human beings or other animals; or
- intended to affect the structure or any function of the body of man or other animals, and which does not achieve any of its primary intended purposes through chemical action within or on the body of man or other animals and which is not dependent upon being metabolized for the achievement of any of its principal intended purposes.

Sales and Use Tax Deferral for Building Construction and Machinery and Equipment

The Department of Revenue (Department) may issue a sales and use tax deferral certificate for state and local sales and use tax for construction of the investment project and acquisition of equipment or machinery for qualified biotechnology products and medical devices. The Department will not issue a tax deferral certificate if an eligible project qualifies for a tax deferral under the Rural County Sales and Use Tax Deferral Program or High Technology Businesses Sales and Use Tax Deferral Program.

Compliance and Enforcement

For investment projects used for purposes other than qualified biotechnology product manufacturing and medical devices at any time during the calendar year or at any time during any of the seven succeeding calendar years, a portion of deferred taxes shall be immediately due. The portion due ranges from 100 percent for the first year to 12.5 percent the eighth and final year applicable. If the deferral recipient meets eligibility criteria over eight years, repayment of the sales and use tax is not required.

To qualify as for the construction-related sales and use tax deferral, a qualified building must mean construction of new structures, and expansion or renovation of existing structures for the purpose of increasing floor space or production capacity used for biotechnology product manufacturing or medical device manufacturing activities, including plant offices, commercial laboratories for process development, quality assurance and quality control, and warehouses or other facilities for the storage of raw material or finished goods if the facilities are an essential or an integral part of a factory, plant, or laboratory used for biotechnology product manufacturing or medical device manufacturing. If a building is used partly for biotechnology product manufacturing or medical device manufacturing and partly for other purposes, the applicable tax deferral shall be determined by apportionment of the costs of construction under rules adopted by the Department.

To qualify as for the machinery and equipment-related sales and use tax deferral, qualified machinery and equipment must mean all new industrial and research fixtures, equipment, and support facilities that are an integral and necessary part of a biotechnology product manufacturing or medical device manufacturing operation. Qualified machinery and equipment may include: computers; software; data processing equipment; laboratory equipment; manufacturing components such as belts, pulleys, shafts, and moving parts;

molds, tools, and dies; operating structures; and all equipment used to control or operate the machinery.

Preferential Business and Occupation Tax Rate for Biotechnology

A preferential tax rate of 0.138 is provided for persons manufacturing and/or making wholesale or retail sales of biotechnology products and medical devices.

Business and Occupation Tax Credit for Job Training Services

To encourage biotechnology and medical devices manufacturing, 20 percent of the amount spent on job training by firms that are eligible may be taken as a credit against business and occupation tax. The training must be designed to enhance job performance in a state-approved program which is sponsored or provided by the employer.

Accountability and Reporting

Persons who receive the benefit of a biotechnology product and medical device business tax incentive shall provide an annual survey to the Department. The survey must consist of the amount of the tax incentives claimed or used for the reporting year; the number of employees (full-time, part-time and temporary) as a percent of total employment; the number of employment positions according to their wage bands; and positions that have employer-provided medical, dental and retirement benefits. The Department will use these statistics to prepare summaries and to report to the Legislature.

Appropriation: None.

Fiscal Note: Requested on February 7, 2006.

Effective Date: The bill takes effect on July 1, 2006.

Testimony For: (Technology, Energy & Communications) In order for Washington to compete in a global market, we must think outside of the box and look for ways to provide opportunities for the sector. A few years back, Washington took bold action to save the aerospace industry in the state and that same bold action is needed for the biotechnology and bioscience community. As the industry matures, the sector will shift from upstream research to more downstream activities like clinical development, manufacturing, sales and marketing. This will present us with an opportunity for more jobs. Washington has been a premiere center for biotechnology and medical devices, but growth has slowed in recent years. There is lagging investment and employment while competition is heating up in other states. Washington has no comprehensive strategy to assist in the growth of the sector, no tax incentives targeted for the sector, no facilities financing and no support for early stage firms. We need a better understanding of the weaknesses of the sector and apply the appropriate policy measures to ensure growth. This bill will bring tax incentives in line with other states. Current manufacturers in the state are evaluating Washington and other locations throughout the country and the world for site locations. It's difficult for Washington to compete against other locations around the world.

Testimony For: (Finance) Washington has been a center for biotechnology and medical devices, but growth has slowed in recent years. Competition from other states is heating up.

Expansion has been based on the intellectual horsepower already here in Washington but we won't be able to leverage intellectual horsepower any longer. There are no tax incentives to growth the full cycle of the industry. The life sciences cluster is important. We need to make Washington more competitive on cost. It's difficult for Washington to compete against other locations.

Testimony Against: (Technology, Energy & Communications) None.

Testimony Against: (Finance) None.

Persons Testifying: (Technology, Energy & Communications) Representative Brian Sullivan, prime sponsor; Dave Carlson, Berlex; Deborah Knutson, Snohomish County Economic Development Council; Steve Collins, University of Washington Bothell; Tom Clements, Pathway; Aaron Reardon, Snohomish County Executive; and Patti McKinnell Davis, Washington Biotechnology and Biomedical Association.

Persons Testifying: (Finance) Deborah Knutson, Snohomish County Economic Development Council; Tom Clements, Pathway; Dave Carlson, Berlex; Angela Kerwin, PSRC; and Patti McKinnell Davis, Washington Biotechnology and Biomedical Association.

Persons Signed In To Testify But Not Testifying: (Technology, Energy & Communications) None.

Persons Signed In To Testify But Not Testifying: (Finance) None.