SENATE BILL REPORT
SB 5673

As Reported By Senate Committee On:
Ways & Means, February 16, 2005

Title: An act relating to the high technology business and occupation tax credit.

Brief Description: Changing provisions relating to the high technology business and occupation tax credit.

Sponsors: Senators Prentice, Zarelli, Shin, Benton and Rasmussen; by request of Department of Revenue.

Brief History:
Committee Activity: Ways & Means: 2/15/05, 2/16/05 [DPS].

SENATE COMMITTEE ON WAYS & MEANS

Majority Report: That Substitute Senate Bill No. 5673 be substituted therefor, and the substitute bill do pass.
Signed by Senators Prentice, Chair; Doumit, Vice Chair; Fraser, Vice Chair; Brandland, Fairley, Hewitt, Kohl-Welles, Parlette, Pflug, Pridemore, Rasmussen, Regala, Roach, Rockefeller, Schoesler and Thibaudeau.

Staff: Terry Wilson (786-7433)

Background: 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. A business may have more than one B&O tax rate, depending on the types of activities conducted. Currently, there are seven different B&O tax rates. The three principal rates are:

Manufacturing/ wholesaling 0.484%
Retailing 0.471%
Services 1.5%

In the 2004 session, the legislature modified and extended the B&O tax credit for high-technology research and development (R&D) expenditures. The credit is equal to the amount of R&D expenditures in excess of 0.92 percent of the business's taxable amount multiplied by 0.484 percent for nonprofit organizations and by the taxpayer's average tax rate for taxpayers other than nonprofit organizations, with a $2.0 million maximum annual credit per business.
Under prior law, the credit was based on a business's entire R&D expenditures if the expenditures exceeded 0.92 percent of the business's taxable amount. In addition, calculation of the credit for for-profit businesses was based on 1.5 percent rather than on the average tax rate of the business.

"Average tax rate" is a business' tax liability divided by the business' taxable income. However, taxable "income" does not include the tax base for manufacturers, which is the "value" of the products manufactured. A manufacturer with no other income would qualify for no credit, but a manufacturer with some other income would qualify for a substantially higher credit.

In the 2004 changes, businesses that take the high-technology B&O tax credit for R&D spending must submit an annual survey. Program participants must provide information on: the amount of B&O tax credit or sales tax exemption; the number of new products, trademarks, patents, and copyrights; the number of jobs and the percent of full-time, part-time and temporary jobs; wages by salary band; and the number of jobs with employer provided health and retirement benefits. The survey is in addition to an annual report that must be submitted that documents the amount of credit claimed, the amount of qualified R&D expenditures made during the year, and the taxable amount during the year. The aggregate information is not subject to disclosure, but the amount of the credit is disclosable. Both the survey and report are due by March 31 of the year following the year the credits were taken. If the survey is not completed by the due date, the business is not eligible to take or assign the credit.

Summary of Substitute Bill: For the purposes of calculating the high-technology B&O tax credit for R&D spending, the average tax rate is based on a business's total annual taxable amount rather than taxable income. The average tax rate may be calculated using estimated information if the business's reporting requirement is more frequent than annually, but the business must make an adjustment in the final reporting period for the year if the actual tax and taxable amounts were different than the estimates. This provision is retroactive to June 10, 2004.

The annual report is incorporated into the annual survey. The department must extend the time for filing for a business that fails to submit a survey as a result of circumstances beyond the control of the business. The amount of the credit is not subject to disclosure.

Beginning January 1, 2006, a business required to submit the survey must do so electronically, unless the tax relief as a result of tax incentives requiring surveys or reports is $1,000 or less.

A business that owes additional tax because of this act is liable for interest, but not penalties, if the additional tax is paid to the department by January 1, 2006.

Substitute Bill Compared to Original Bill: The original bill was not considered.

Appropriation: None.

Fiscal Note: Available.

Committee/Commission/Task Force Created: No.

Effective Date: The bill contains several effective dates. Please refer to the bill.

Testimony For: Manufacturers cannot take the credit or can take too much. Some no longer qualify and others over qualify. Because of the penalty for not filing on time, electronic filing was added to enable the Department of Revenue to contact taxpayers in time. The credit does not create jobs directly but creates favorable conditions for job creation. Most firms taking the credit are small.

Testimony Against: None.

Who Testified: PRO: Julie Sexton, Department of Revenue; Lew McMurran, WA Software Alliance; Tom McBride, Assoc. of WA Business; Nancy Atwood, ACA, Vicki Austin, WBBA; Dan Coyne, Hewlett-Packard Co.