
SENATE BILL 5544

State of Washington

62nd Legislature

2011 Regular Session

By Senators Fraser and Zarelli; by request of Department of Revenue

Read first time 01/28/11. Referred to Committee on Ways & Means.

1 AN ACT Relating to sales and use tax exemptions for certain
2 property and services used in manufacturing, research and development,
3 or testing operations, not including changes to RCW 82.08.02565 and
4 82.12.02565 that reduce state revenue; amending RCW 82.08.02565,
5 82.04.120, and 82.32.585; adding a new section to chapter 82.08 RCW;
6 adding a new section to chapter 82.12 RCW; creating new sections; and
7 declaring an emergency.

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

9 NEW SECTION. **Sec. 1.** (1) In 1995, the legislature enacted a sales
10 and use tax exemption for manufacturing machinery and equipment,
11 commonly referred to as the "M&E exemption." The legislature finds
12 that the purposes of this exemption were to encourage the growth and
13 development of the state's private sector manufacturing industry and
14 improve this state's ability to compete with other states for
15 manufacturing investment. The legislature further finds that it was
16 not the purpose of the M&E exemption to provide tax breaks to state
17 agencies and institutions, nor to public utilities and other businesses
18 with respect to machinery and equipment primarily used for activities

1 that are taxable under the state public utility tax or are otherwise
2 not considered to be manufacturing for business and occupation tax
3 purposes.

4 (2) The legislature further finds that despite previous attempts at
5 clarifying the M&E exemption, significant ambiguity persists,
6 particularly with respect to the scope of the exemption. Such
7 ambiguity results in costly appeals and litigation and may result in
8 significant unanticipated revenue losses for the state and local
9 governments.

10 (3) Therefore, the legislature finds it necessary to reaffirm its
11 original intent in establishing the M&E exemption. The legislature
12 declares that the amendments to the existing M&E exemption and to RCW
13 82.04.120 in this act are clarifying and, as such, apply retroactively
14 as well as prospectively.

15 (4) The legislature finds that Washington is home to premier public
16 research institutions. The legislature recognizes that the state's
17 public universities provide cutting-edge research and development,
18 which helps stimulate growth in the private sector and is vital to the
19 economic well-being of our state. University research leads directly
20 to new products, companies, production methods, and ways of organizing
21 work. The legislature further recognizes that our public universities
22 will play an important role in shaping the next generation of
23 Washington industries, including biofuels and other renewable energy,
24 global health, and advanced manufacturing. Therefore, because the
25 amendments to the existing M&E exemption in this act clarify that state
26 agencies and institutions are not eligible for the M&E exemption, this
27 act provides a new, stand-alone sales and use tax exemption for
28 machinery and equipment used primarily in technological research and
29 development operations by the state's four-year institutions of higher
30 education.

31 **Sec. 2.** RCW 82.08.02565 and 2009 c 535 s 510 are each amended to
32 read as follows:

33 (1)(a) The tax levied by RCW 82.08.020 does not apply to sales to
34 a manufacturer or processor for hire of machinery and equipment used
35 directly in a manufacturing operation or research and development
36 operation, to sales to a person engaged in testing for a manufacturer
37 or processor for hire of machinery and equipment used directly in a

1 testing operation, or to sales of or charges made for labor and
2 services rendered in respect to installing, repairing, cleaning,
3 altering, or improving the machinery and equipment(~~(, but only when the~~
4 ~~purchaser provides the seller with)~~).

5 (b) Sellers making tax-exempt sales under this section must obtain
6 from the purchaser an exemption certificate in a form and manner
7 prescribed by the department by rule. The seller must retain a copy of
8 the certificate for the seller's files.

9 (2) For purposes of this section and RCW 82.12.02565:

10 (a) "Machinery and equipment" means industrial fixtures, devices,
11 and support facilities, and tangible personal property that becomes an
12 ingredient or component thereof, including repair parts and replacement
13 parts. "Machinery and equipment" includes pollution control equipment
14 installed and used in a manufacturing operation, testing operation, or
15 research and development operation to prevent air pollution, water
16 pollution, or contamination that might otherwise result from the
17 manufacturing operation, testing operation, or research and development
18 operation. "Machinery and equipment" also includes digital goods.

19 (b) "Machinery and equipment" does not include:

20 (i) Hand-powered tools;

21 (ii) Property with a useful life of less than one year;

22 (iii) Buildings, other than machinery and equipment that is
23 permanently affixed to or becomes a physical part of a building; and

24 (iv) Building fixtures that are not integral to the manufacturing
25 operation, testing operation, or research and development operation
26 that are permanently affixed to and become a physical part of a
27 building, such as utility systems for heating, ventilation, air
28 conditioning, communications, plumbing, or electrical.

29 (c) Machinery and equipment is "used directly" in a manufacturing
30 operation, testing operation, or research and development operation if
31 the machinery and equipment:

32 (i) Acts upon or interacts with an item of tangible personal
33 property;

34 (ii) Conveys, transports, handles, or temporarily stores an item of
35 tangible personal property at the manufacturing site or testing site;

36 (iii) Controls, guides, measures, verifies, aligns, regulates, or
37 tests tangible personal property at the site or away from the site;

1 (iv) Provides physical support for or access to tangible personal
2 property;

3 (v) Produces power for, or lubricates machinery and equipment;

4 (vi) Produces another item of tangible personal property for use in
5 the manufacturing operation, testing operation, or research and
6 development operation;

7 (vii) Places tangible personal property in the container, package,
8 or wrapping in which the tangible personal property is normally sold or
9 transported; or

10 (viii) Is integral to research and development as defined in RCW
11 82.63.010.

12 (d) "Manufacturer" means a person that qualifies as a manufacturer
13 under RCW 82.04.110. "Manufacturer" also includes a person that prints
14 newspapers or other materials.

15 (e) "Manufacturing" means only those activities that come within
16 the definition of "to manufacture" in RCW 82.04.120 and are taxed as
17 manufacturing or processing for hire under chapter 82.04 RCW, or would
18 be taxed as such if such activity were conducted in this state or if
19 not for an exemption or deduction. "Manufacturing" also includes
20 printing newspapers or other materials. An activity is not taxed as
21 manufacturing or processing for hire under chapter 82.04 RCW if the
22 activity is within the purview of chapter 82.16 RCW.

23 (f) "Manufacturing operation" means the manufacturing of articles,
24 substances, or commodities for sale as tangible personal property. A
25 manufacturing operation begins at the point where the raw materials
26 enter the manufacturing site and ends at the point where the processed
27 material leaves the manufacturing site. With respect to the production
28 of class A or exceptional quality biosolids by a wastewater treatment
29 facility, the manufacturing operation begins at the point where class
30 B biosolids undergo additional processing to achieve class A or
31 exceptional quality standards. Notwithstanding anything to the
32 contrary in this section, the term also includes that portion of a
33 cogeneration project that is used to generate power for consumption
34 within the manufacturing site of which the cogeneration project is an
35 integral part. The term does not include (~~the production of~~
36 electricity by a light and power business as defined in RCW 82.16.010
37 or)) the preparation of food products on the premises of a person
38 selling food products at retail.

1 ((+e)) (g) "Cogeneration" means the simultaneous generation of
2 electrical energy and low-grade heat from the same fuel.

3 ((+f)) (h) "Research and development operation" means engaging in
4 research and development as defined in RCW 82.63.010 by a manufacturer
5 or processor for hire.

6 ((+g)) (i) "Testing" means activities performed to establish or
7 determine the properties, qualities, and limitations of tangible
8 personal property.

9 ((+h)) (j) "Testing operation" means the testing of tangible
10 personal property for a manufacturer or processor for hire. A testing
11 operation begins at the point where the tangible personal property
12 enters the testing site and ends at the point where the tangible
13 personal property leaves the testing site. The term also includes the
14 testing of tangible personal property for use in that portion of a
15 cogeneration project that is used to generate power for consumption
16 within the manufacturing site of which the cogeneration project is an
17 integral part. The term does not include the testing of tangible
18 personal property for use in the production of electricity by a light
19 and power business as defined in RCW 82.16.010 or the preparation of
20 food products on the premises of a person selling food products at
21 retail.

22 **Sec. 3.** RCW 82.04.120 and 2009 c 535 s 406 are each amended to
23 read as follows:

24 (1) "To manufacture" embraces all activities of a commercial or
25 industrial nature wherein labor or skill is applied, by hand or
26 machinery, to materials so that as a result thereof a new, different or
27 useful substance or article of tangible personal property is produced
28 for sale or commercial or industrial use, and ~~((shall))~~ includes:

29 ((+1)) (a) The production or fabrication of special made or custom
30 made articles;

31 ((+2)) (b) The production or fabrication of dental appliances,
32 devices, restorations, substitutes, or other dental laboratory products
33 by a dental laboratory or dental technician;

34 ((+3)) (c) Cutting, delimiting, and measuring of felled, cut, or
35 taken trees; and

36 ((+4)) (d) Crushing and/or blending of rock, sand, stone, gravel,
37 or ore.

1 (2) "To manufacture" (~~shall~~) does not include:

2 (a) Conditioning of seed for use in planting; cubing hay or
3 alfalfa;

4 (b) Activities which consist of cutting, grading, or ice glazing
5 seafood which has been cooked, frozen, or canned outside this state;

6 (c) The growing, harvesting, or producing of agricultural products;

7 (d) Packing of agricultural products, including sorting, washing,
8 rinsing, grading, waxing, treating with fungicide, packaging, chilling,
9 or placing in controlled atmospheric storage;

10 (e) The production of digital goods; (~~or~~)

11 (f) The production of computer software if the computer software is
12 delivered from the seller to the purchaser by means other than tangible
13 storage media, including the delivery by use of a tangible storage
14 media where the tangible storage media is not physically transferred to
15 the purchaser; and

16 (g) Any activity that is integral to any public service business as
17 defined in RCW 82.16.010 and with respect to which the gross income
18 associated with such activity: (i) Is subject to tax under chapter
19 82.16 RCW; or (ii) would be subject to tax under chapter 82.16 RCW if
20 such activity were conducted in this state or if not for an exemption
21 or deduction.

22 (3) With respect to wastewater treatment facilities:

23 (a) "To manufacture" does not include the treatment of wastewater,
24 the production of reclaimed water, and the production of class B
25 biosolids; and

26 (b) "To manufacture" does include the production of class A or
27 exceptional quality biosolids, but only with respect to the processing
28 activities that occur after the biosolids have reached class B
29 standards.

30 NEW SECTION. Sec. 4. A new section is added to chapter 82.08 RCW
31 to read as follows:

32 (1)(a) The tax levied by RCW 82.08.020 does not apply to sales to
33 a public research institution of machinery and equipment used primarily
34 in a research and development operation, or to sales of or charges made
35 for labor and services rendered in respect to installing, repairing,
36 cleaning, altering, or improving the machinery and equipment.

1 (b) Sellers making tax-exempt sales under this section must obtain
2 from the purchaser an exemption certificate in a form and manner
3 prescribed by the department. The seller must retain a copy of the
4 certificate for the seller's files.

5 (2) A public research institution claiming the exemption provided
6 in this section must file a complete annual survey with the department
7 under RCW 82.32.585.

8 (3) For purposes of this section, the following definitions apply:

9 (a) "Machinery and equipment" means those fixtures, pieces of
10 equipment, digital goods, and support facilities that are an integral
11 and necessary part of a research and development operation, and
12 tangible personal property that becomes an ingredient or component of
13 such fixtures, equipment, and support facilities, including repair
14 parts and replacement parts. "Machinery and equipment" may include,
15 but is not limited to: Computers; software; data processing equipment;
16 laboratory equipment, instrumentation, and other devices used in a
17 process of experimentation to develop a new or improved pilot model,
18 plant process, product, formula, or invention; vats, tanks, and
19 fermenters; operating structures; and all equipment used to control,
20 monitor, or operate the machinery and equipment.

21 (b) "Machinery and equipment" does not include:

22 (i) Hand-powered tools;

23 (ii) Property with a useful life of less than one year;

24 (iii) Buildings; and

25 (iv) Those building fixtures that are not an integral and necessary
26 part of a research and development operation and that are permanently
27 affixed to and become a physical part of a building, such as utility
28 systems for heating, ventilation, air conditioning, communications,
29 plumbing, or electrical.

30 (c) "Primarily" means greater than fifty percent as measured by
31 time. If machinery and equipment is used simultaneously in a research
32 and development operation and also for other purposes, the use for
33 other purposes must be disregarded during the period of simultaneous
34 use for purposes of determining whether the machinery and equipment is
35 used primarily in a research and development operation.

36 (d) "Public research institution" means any college or university
37 included within the definitions of state universities, regional
38 universities, or state college in RCW 28B.10.016.

1 (e) "Research and development operation" means engaging in research
2 and development as defined in RCW 82.63.010.

3 NEW SECTION. **Sec. 5.** A new section is added to chapter 82.12 RCW
4 to read as follows:

5 (1) The provisions of this chapter do not apply in respect to the
6 use by a public research institution of machinery and equipment used
7 primarily in a research and development operation, or to the use of
8 labor and services rendered in respect to installing, repairing,
9 cleaning, altering, or improving the machinery and equipment.

10 (2) The definitions in section 4 of this act apply to this section.

11 (3) A public research institution receiving the benefit of the
12 exemption provided in this section must file a complete annual survey
13 with the department under RCW 82.32.585.

14 **Sec. 6.** RCW 82.32.585 and 2010 c 114 s 102 are each amended to
15 read as follows:

16 (1)(a) Every person claiming a tax preference that requires a
17 survey under this section must file a complete annual survey with the
18 department.

19 (i) Except as provided in (a)(ii) of this subsection, the survey is
20 due by April 30th of the year following any calendar year in which a
21 person becomes eligible to claim the tax preference that requires a
22 survey under this section.

23 (ii) If the tax preference is a deferral of tax, the first survey
24 must be filed by April 30th of the calendar year following the calendar
25 year in which the investment project is certified by the department as
26 operationally complete, and a survey must be filed by April 30th of
27 each of the seven succeeding calendar years.

28 (b) The department may extend the due date for timely filing of
29 annual surveys under this section as provided in RCW 82.32.590.

30 (2)(a) The survey must include the amount of the tax preference
31 claimed for the calendar year covered by the survey. For a person that
32 claimed an exemption provided in section 4 or 5 of this act, the survey
33 must include the amount of tax exempted under those sections in the
34 prior calendar year for each general area or category of research and
35 development for which exempt machinery and equipment and labor and
36 services were acquired in the prior calendar year.

1 (b) The survey must also include the following information for
2 employment positions in Washington, not to include names of employees,
3 for the year that the tax preference was claimed:

4 (i) The number of total employment positions;

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

7 (iii) The number of employment positions according to the following
8 wage bands: Less than thirty thousand dollars; thirty thousand dollars
9 or greater, but less than sixty thousand dollars; and sixty thousand
10 dollars or greater. A wage band containing fewer than three
11 individuals may be combined with another wage band; and

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

14 (c) For persons claiming the tax preference provided under chapter
15 82.60 or 82.63 RCW, the survey must also include the number of new
16 products or research projects by general classification, and the number
17 of trademarks, patents, and copyrights associated with activities at
18 the investment project.

19 (d) For persons claiming the credit provided under RCW 82.04.4452,
20 the survey must also include the qualified research and development
21 expenditures during the calendar year for which the credit was claimed,
22 the taxable amount during the calendar year for which the credit was
23 claimed, the number of new products or research projects by general
24 classification, the number of trademarks, patents, and copyrights
25 associated with the research and development activities for which the
26 credit was claimed, and whether the tax preference has been assigned,
27 and who assigned the credit. The definitions in RCW 82.04.4452 apply
28 to this subsection (2)(d).

29 (e) For persons claiming the tax exemption in section 4 or 5 of
30 this act, the survey must also include the general areas or categories
31 of research and development for which machinery and equipment and labor
32 and services were acquired, exempt from tax under section 4 or 5 of
33 this act, in the prior calendar year.

34 (f) If the person filing a survey under this section did not file
35 a survey with the department in the previous calendar year, the survey
36 filed under this section must also include the employment, wage, and
37 benefit information required under (b)(i) through (iv) of this

1 subsection for the calendar year immediately preceding the calendar
2 year for which a tax preference was claimed.

3 (3) As part of the annual survey, the department may request
4 additional information necessary to measure the results of, or
5 determine eligibility for, the tax preference.

6 (4) All information collected under this section, except the
7 (~~amount of the tax preference claimed~~) information required in
8 subsection (2)(a) of this section, is deemed taxpayer information under
9 RCW 82.32.330. Information (~~on the amount of tax preference claimed~~)
10 required in subsection (2)(a) of this section is not subject to the
11 confidentiality provisions of RCW 82.32.330 and may be disclosed to the
12 public upon request, except as provided in subsection (5) of this
13 section. If the amount of the tax preference claimed as reported on
14 the survey is different than the amount actually claimed or otherwise
15 allowed by the department based on the taxpayer's excise tax returns or
16 other information known to the department, the amount actually claimed
17 or allowed may be disclosed.

18 (5) Persons for whom the actual amount of the tax reduced or saved
19 is less than ten thousand dollars during the period covered by the
20 survey may request the department to treat the amount of the tax
21 reduction or savings as confidential under RCW 82.32.330.

22 (6)(a) Except as otherwise provided by law, if a person claims a
23 tax preference that requires an annual survey under this section but
24 fails to submit a complete annual survey by the due date of the survey
25 or any extension under RCW 82.32.590, the department must declare the
26 amount of the tax preference claimed for the previous calendar year to
27 be immediately due. If the tax preference is a deferral of tax, twelve
28 and one-half percent of the deferred tax is immediately due. If the
29 economic benefits of the deferral are passed to a lessee, the lessee is
30 responsible for payment to the extent the lessee has received the
31 economic benefit.

32 (b) The department must assess interest, but not penalties, on the
33 amounts due under this subsection. The interest must be assessed at
34 the rate provided for delinquent taxes under this chapter,
35 retroactively to the date the tax preference was claimed, and accrues
36 until the taxes for which the tax preference was claimed are repaid.
37 Amounts due under this subsection are not subject to the

1 confidentiality provisions of RCW 82.32.330 and may be disclosed to the
2 public upon request.

3 (7) The department must use the information from this section to
4 prepare summary descriptive statistics by category. No fewer than
5 three taxpayers may be included in any category. The department must
6 report these statistics to the legislature each year by October 1st.

7 (8) For the purposes of this section:

8 (a) "Person" has the meaning provided in RCW 82.04.030 and also
9 includes the state and its departments and institutions.

10 (b) "Tax preference" has the meaning provided in RCW 43.136.021 and
11 includes only the tax preferences requiring a survey under this
12 section.

13 NEW SECTION. **Sec. 7.** The legislature declares that the only
14 reason why the phrase "the production of electricity by a light and
15 power business as defined in RCW 82.16.010" was deleted from the
16 definition of "manufacturing operation" in RCW 82.08.02565(2)(f) in
17 section 2 of this act is because that language is superfluous.

18 NEW SECTION. **Sec. 8.** This act is necessary for the immediate
19 preservation of the public peace, health, or safety, or support of the
20 state government and its existing public institutions, and takes effect
21 immediately.

22 NEW SECTION. **Sec. 9.** Sections 2 and 3 of this act apply both
23 prospectively and retroactively to any tax period open for assessment
24 or refund of taxes.

25 NEW SECTION. **Sec. 10.** If any provision of this act or its
26 application to any person or circumstance is held invalid, the
27 remainder of the act or the application of the provision to other
28 persons or circumstances is not affected.

29 NEW SECTION. **Sec. 11.** Nothing in this act may be construed as a
30 repudiation of any provision of WAC 458-20-13601.

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