

SENATE BILL REPORT

SB 6057

As of June 26, 2015

Title: An act relating to revenue.

Brief Description: Relating to revenue.

Sponsors: Senator Hill.

Brief History:

Committee Activity: Ways & Means: 6/26/15.

SENATE COMMITTEE ON WAYS & MEANS

Staff: Juliana Roe (786-7438)

Background: Part I - Reinstating Tax Preferences for High-technology research and Development: In 1994 the Legislature created a program of business and occupation (B&O) tax credits for qualified research and development (R&D) expenditures, and a sales and use tax deferral program for high-technology R&D and pilot-scale manufacturing facilities. The R&D tax preferences expired January 1, 2015.

Business and Occupation 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. Revenues are deposited in the state general fund. A business may have more than one B&O tax rate, depending on the types of activities conducted. Major B&O tax rates include 0.471 percent for retailing; 0.484 percent for manufacturing, wholesaling, and extracting; and 1.5 percent for professional and personal services, and activities not classified elsewhere.

Business and Occupation Tax Credit for High Technology Research and Development. Under the program that expired January 1, 2015, qualified research and development meant R&D performed within this state in the fields of advanced computing, advanced materials, biotechnology, electronic device technology, and environmental technology. In 2014 the B&O tax credit available was 1.5 percent of the greater of (1) qualified R&D expenditures that exceed 0.92 percent of the person's taxable income; or (2) 80 percent of the compensation received for conducting qualified R&D under contract. Person was broadly defined to include, among other categories, individuals, companies, political subdivisions, nonprofits, and federal agencies. No person could take more than \$2 million per year in credit. Qualified R&D expenditures that were claimable included those directly incurred as

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operating expenses, partner or owner compensation, benefits, supplies, and computer expenses. Excluded as claimable expenses were amounts paid to a person other than a public educational or R&D institution to conduct R&D, and capital costs and overhead, including expenses for land and structures. Any credit over claimed or claimed by an ineligible person must be repaid, with interest but not penalties.

Sales and Use Tax Deferral for Certain Construction-Related Expenses. Until January 1, 2015, application for deferral of sales and use taxes could be made before initiation of, construction of, or acquisition of, equipment or machinery for an investment project. The Department of Revenue (DOR) was required to issue a sales and use tax deferral certificate for taxes due on each eligible investment project.

- Investment project was defined as an investment in qualified buildings or qualified machinery and equipment, including labor and services rendered in the planning, installation, and construction or improvement of the project.
- Eligible investment project was defined as an investment project that either initiates a new operation or expands or diversifies a current operation by expanding, renovating, or equipping an existing facility. In the case of an investment project involving multiple qualified buildings, applications must be made for, and before the initiation of construction of, each qualified building.
- Qualified building was defined as construction of new structures and expansion or renovation of existing structures for the purpose of increasing floor space or production capacity used for pilot-scale manufacturing or qualified R&D.
- Qualified research and development was defined as R&D performed within this state in the fields of advanced computing, advanced materials, biotechnology, electronic device technology, and environmental technology.
- Qualified machinery and equipment was defined as fixtures, equipment, and support facilities integral and necessary to a pilot-scale manufacturing or qualified R&D development operation.

The lessor or owner of a qualified building may be eligible for the deferral, only if the lessor by written contract agrees to pass the economic benefit, in an amount no less than the tax deferred, to the lessee, and the lessee agrees in writing with DOR to complete the required annual survey.

Annual Survey. Taxpayers claiming tax preferences aimed at creating jobs or increasing industry competitiveness were required to file an annual survey with DOR. The annual survey included a report of the tax preference amounts claimed each calendar year and information related to employment positions and wages in Washington. In addition if the annual survey or other information caused DOR to find that an investment project, within seven years of being certified as operationally complete, was used for a purpose other than qualified R&D or pilot-scale manufacturing, a percentage of the deferred taxes were immediately due. The sales tax deferral became a waiver of the tax if the business maintained qualified activities for eight years once the facility was operationally complete.

Part II - Extending the Expiration date of Tax Preferences for Food Processing: Manufacturers of fresh fruit or vegetables, seafood products, and dairy products are eligible for exemptions from the B&O tax.

The B&O tax exemptions provide an exemption from the manufacturing B&O tax on the value of products sold by fresh fruit or vegetable, seafood product, or dairy product manufacturers; and, generally, an exemption from retailing and wholesaling B&O tax for those products manufactured and sold by the manufacturer to a customer who transports the product outside this state in the normal course of business.

These exemptions expire June 30, 2015. When they expire, the income is no longer exempt from B&O tax but will become subject to a reduced B&O tax rate of 0.138 percent for the manufacturing, retailing, and wholesaling activities. All businesses claiming the exemptions are required to electronically file an Annual Tax Incentive Survey by April 30 of the year following the year the exemption was claimed. The Annual Survey provides employment and wage information regarding firms claiming the exemptions and also provides the tax savings to individual firms from claiming the exemptions.

Part III - Providing a Sales and Use Tax Exemption for Eligible Server Equipment Installed in Certain Data Centers: Sales and Use Tax. Retail sales taxes are imposed on retail sales of most articles of tangible personal property, digital products, and some services. A retail sale is a sale to the final consumer or end user of the property, digital product, or service. If retail sales taxes were not collected when the user acquired the property, digital products, or services, then use taxes apply to the value of property, digital products, or services when used in this state. The state, most cities, and all counties levy retail sales and use taxes. The state sales and use tax rate is 6.5 percent. Local sales and use tax rates vary from 0.5 percent to 3 percent, depending on the location.

Sales and Use Tax Exemption for Eligible Server Equipment. In 2010 the Legislature enacted Chapter 1, 2010 Laws 1st sp. s (ESB 6789) which provided a sales and use tax exemption for server equipment and power infrastructure for computer data centers. The exemption was to expire on April 1, 2018. In order to qualify, a data center must be located in a rural county, have at least 20,000 square feet dedicated to housing servers, and have commenced construction between April 1, 2010, and before July 1, 2011. Additionally, within six years of construction, a qualifying business must have created 35 family wage employment positions or three family wage employment positions per 20,000 square feet of space. Construction of a data center includes the expansion, renovation, or other improvements made to existing facilities, including leased or rented space. A family wage employment position is a new full-time position at the qualifying data center requiring 40 hours of weekly work, or their equivalent, on a weekly basis and the wage must be greater than 150 percent of the county's per-capita income of the county where the qualified data center is located.

The exemption applied to the original server equipment installed after April 1, 2010, and replacement server equipment which replaces servers originally exempt from tax and installed prior to April 1, 2018.

In 2012 Legislation was enacted that extended the time for eligible data centers and qualifying tenants of data centers to qualify for the sales and use tax exemption on server equipment and power infrastructure to those that commenced construction between April 1, 2012, and July 1, 2015. The exemption time is extended for eligible replacement server equipment placed in new data centers and for qualifying tenants until April 1, 2020.

Part IV - Creating a Pilot Program that Provides Incentives for Investments in Washington State Job Creation and Economic Development: Economic development policies are designed to improve the economic wellbeing of a community through efforts that include job creation, job retention, infrastructure improvements, workforce training, tax base enhancements, and improvements to quality of life. State and local governments may utilize a variety of tools to attract economic investment in their communities. In Washington there are a variety of tax polices including preferential tax rates, credits, exemptions, deductions, and deferrals that are designed to enhance economic activity, create or retain jobs, and attract business investments. For example the High Unemployment County Sales & Use Tax Deferral/Waiver for Manufacturing Facilities, established in 2010, encourages job creation in areas with high unemployment by offering certain businesses a sales and use tax deferral on construction of new buildings or purchases of qualifying machinery and equipment. Businesses that maintain a qualified activity for seven years after completion of the project are no longer required to repay deferred sales and use taxes.

Part V - Continuing Tax Preferences for Aluminum Smelters: In 2004 the Legislature passed a package of tax preferences for the aluminum industry that were scheduled to expire on January 1, 2007. The tax preferences for the aluminum industry include the following:

- a reduced B&O rate from 0.484 percent to 0.2904 percent for manufacturers of aluminum;
- a B&O tax credit for the amount of property taxes paid on an aluminum smelter;
- a sales and use tax credit against the state portion of the tax for personal property, construction materials, and labor and services performed on buildings and property at an aluminum smelter; and
- an exemption from the brokered natural gas use tax on gas delivered through a pipeline.

In 2006 the Legislature extended the tax preferences to 2012, and again in 2010 the Legislature extended the tax preferences to 2017.

The Citizen Commission for Performance Measurement of Tax Preferences (Commission) was established by the Legislature in 2006. The Commission develops a schedule to review nearly all tax preferences at least once every ten years. The Commission also schedules tax preferences with expiration dates to be reviewed two years before the tax preference expires.

Tax preference reviews are conducted by the Joint Legislative Audit and Review Committee (JLARC) according to the schedule established by the Commission. The aluminum tax incentives were reviewed in 2009. JLARC recommended that the Legislature extend the expiration date for these tax preferences – which it did – because the public policy goal of preserving family wage jobs is being maintained, and because the high energy prices that brought about the tax preferences were higher and more volatile than when the tax preferences were originally enacted.

The Commission endorsed the recommendation to extend the expiration dates and further recommended that the Legislature consider establishing a final expiration date.

JLARC is scheduled to review the aluminum industry tax preferences in 2015.

Part VI - Concerning the Definition of Newspaper: In 2008 and again in 2012, the Legislature temporarily revised the definition of newspaper to include electronic versions of newspapers. The effect of this is that both the online version of a newspaper and the physical version of a newspaper are taxed at the B&O rate of 0.35 percent until July 1, 2015, and 0.2904 percent thereafter. The definition is set to expire July 1, 2015.

If the electronic version of a newspaper is not included in the definition of a newspaper, the B&O tax will apply to the electronic version based on the revenue-generating activity. For advertising revenues the rate of 1.5 percent would apply, and for subscription sales the rate of .471 percent would apply.

Part VII - Providing a Reduced Public Utility Tax for Log Transportation Businesses: B&O Tax. Washington's major business tax is the 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. Revenues are deposited in the state general fund. A business may have more than one B&O tax rate, depending on the types of activities conducted. There are a number of different rates. The main rates are 0.471 percent for retailing; 0.484 percent for manufacturing, wholesaling, and extracting; and 1.5 percent for professional and personal services, and activities not classified elsewhere.

Public Utility Tax (PUT). Income from utility operations is taxed under the PUT and is in lieu of the B&O tax; other income of the utility firm, e.g. retail sales of tangible personal property, is subject to the B&O tax. Unlike the B&O tax which pyramids, the PUT applies only on sales to consumers. Five different rates apply, depending upon the specific utility activity. The current rates, including permanent surtaxes, are as follows:

- distribution of water, 5.029 percent;
- generation or distribution of electrical power, 3.873 percent;
- telegraph companies, distribution of natural gas, and collection of sewerage, 3.852 percent;
- urban transportation and watercraft vessels under 65 feet in length, 0.642 percent; and
- railroads, railroad car companies, motor transportation, and all other public service businesses, 1.926 percent.

In 2009 the Legislature passed ESSB 6170, which reduced the usual PUT rate on log hauling from 1.926 percent to 1.3696 percent of gross income. That reduced rate expired in June 2013.

Part VIII - Concerning Nonresident Vessel Permits and Taxation: Retail sales taxes are imposed on retail sales of most articles of tangible personal property, digital products, and some services. A retail sale is a sale to the final consumer or end user of the property, digital product, or service. If retail sales taxes were not collected when the property, digital products, or services were acquired by the user, then use taxes apply to the value of most tangible personal property, digital products, and some services when used in this state.

Nonresident individuals purchasing a vessel in Washington or piloting a vessel into Washington waters may be eligible for a special use permit that exempts the purchase or use of the vessel from sales and use taxation. A use permit also satisfies vessel registration

requirements administered by the state Department of Licensing (DOL). A use permit may be obtained by a nonresident individual purchasing or using a vessel in Washington if the vessel is at least 30 feet in length. A use permit is not renewable and costs \$500 for vessels 30 to 50 feet and \$800 for vessels greater than 50 feet in length. A use permit is valid for 12 consecutive months from the date of purchase. A nonresident business entity, e.g. corporation, limited liability company, partnership, etc., is not eligible to receive a use permit.

Generally, a nonresident individual or business entity bringing a vessel into Washington waters does not need to obtain a permit from DOL for up to 60 days if the vessel is currently registered in another state or the vessel has a current U.S. Coast Guard Documentation Paper. If a vessel owner is a nonresident individual and will be operating a vessel on Washington waters for more than 60 days, the owner may apply for a vessel permit on or before the sixtieth day of the visit to remain in the state for an additional 60 days. The person may renew the vessel permit once for an additional 60 days. When the renewed permit expires, the vessel owner must either register the boat in Washington or remove the boat from Washington waters. A nonresident business entity owning a vessel is not eligible to receive a vessel permit.

Part IX - Concerning Distribution and use of Aircraft Excise Taxes: Current law requires the collection of an annual aircraft excise tax. The amount of the tax varies by the type of aircraft and generally ranges from \$20 for a home-built aircraft up to \$125 for a turbojet multi-engine fixed wing plane. Of the taxes collected, 90 percent is deposited into the general fund and 10 percent is retained in the aeronautics account to cover administrative expenses. This distribution has been the same since 1987, prior to that 100 percent of the aircraft excise tax was deposited into the general fund.

The Aviation Division of the Washington State Department of Transportation (WSDOT) annually awards grants to public use airports in the state for pavement, safety, planning, and security. Awards are funded from the aeronautics account. Aeronautics account state funds are typically used to leverage additional federal funds beyond those already received by WSDOT.

A fuel tax administration bill (SHB 1883) passed in the 2013 legislative session, and which becomes effective July 1, 2015, erroneously eliminated the aeronautics account.

Part X - Providing a Business and Occupation Tax Credit for Businesses That Hire Veterans: Washington's major business tax is the B&O tax. The B&O tax is imposed on the gross receipts of all business activities conducted within the state, without any deduction for the costs of doing business. Revenues are deposited in the state general fund. There are several rate categories, and a business may be subject to more than one B&O tax rate, depending on the types of activities conducted.

The B&O tax code contains many exemptions and deductions for specific types of business activities and revenue. Tax credits, which provide a dollar-for-dollar offset against tax liability, are also authorized in certain circumstances. Some existing B&O tax credits were enacted for the specific purpose of encouraging employment growth. For example, a credit

against the B&O tax is provided for firms that create employment positions in rural counties or community empowerment areas.

The public utility tax (PUT) applies to the gross income derived from the operation of public and privately owned utilities. The tax is in lieu of the B&O tax and applies to the general categories of transportation and the supply of energy and water.

The federal government recently had a program that provided a tax credit for hiring various groups, including qualified veterans, known as the Work Opportunity Tax Credit. It expired December 31, 2013.

Part XI - Defining Honey Bee Products and Services as an Agricultural Product: A B&O tax on the gross receipts of all in-state business activities, except utility activities, is imposed on every person who has a substantial nexus to the state for the act or privilege of doing business. The B&O tax does not apply to farmers (persons producing agricultural products for sale) selling agricultural products at wholesale or growing agricultural products owned by others, such as custom feed operations.

In 2008 and 2013 the Legislature enacted temporary tax exemptions related to apiarists and honey bee products. Honey bee products are defined as queen honey bees, packaged honey bees, honey, pollen, beeswax, propolis, or other substances obtained from honey bees. Honey bee products do not include manufactured substances or articles. The following is a list of tax exemptions set to expire on July 1, 2017:

- wholesale sales of honey bee products that do not otherwise qualify for the general agricultural product exemption (B&O);
- bee pollination services to a farmer using a bee colony owned or kept by the person providing the pollination services (B&O);
- sales of honey bees to eligible apiarists (retail);
- sales of feed to eligible apiarists to raise a bee colony to make honey bee products (retail);
- use of honey bees by eligible apiarists (use); and
- use of feed by eligible apiarists in raising a bee colony to make honey bee products (use).

Part XII - Providing Sales and Use Tax Exemptions to Encourage Coal-Fired Electric Generation Plants or biomass Energy Facilities to Convert to Natural Gas-Fired Plants: Emission Performance Standards (EPS) were adopted for electric generation plants to meet greenhouse gas emission standards adopted in Washington in 2008. In 2009 the Governor issued an executive order directing the Department of Ecology (Ecology) to work with the existing coal-fired plant within Washington to establish an agreed order to apply the EPS to the facility by no later than December 31, 2025. The agreed order must include a schedule of major decision making and resource investment milestones. In 2011 the Legislature established a schedule for applying the EPS to the Centralia coal-fired electric generation facility.

State and local sales and use taxes are levied on the sale of tangible personal property and certain services. Exemptions from sales and use taxes have been established to create jobs and encourage investments in Washington, including, for example, the exemptions for

manufacturing machinery and equipment and investments in aerospace manufacturing facilities.

Part XIII - Providing Use Tax Relief for Individuals Who Support Charitable Activities:

Retail sales taxes are imposed on retail sales of most articles of tangible personal property, digital products, and some services. A retail sale is a sale to the final consumer or end user of the property, digital product, or service. If retail sales taxes were not collected when the user acquired the property, digital products, or services, then use taxes apply to the value of property, digital product, or service when used in this state.

Washington's major business tax is the 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.

Amounts received from fundraising activities by nonprofit organizations and libraries are exempt from the B&O tax. Similarly, sales made by nonprofit organizations or libraries are exempt from the sales tax. However, those who purchase or receive as a prize an article of personal property from a nonprofit organization or library for a fundraising activity owe use tax to the state if the article of personal property is worth \$10,000 or more. This exemption is set to expire July 1, 2017.

Part XIV - Revising a Property Tax Exemption for Veterans with total Disability Ratings and Their Surviving Spouses or Domestic Partners:

All real and personal property is subject to property tax each year based on its value, unless a specific exemption is provided by law. Some senior citizens and persons retired due to disability are entitled to a property tax exemption for their principal residences. To qualify a person must be age 61 in the year of application; retired from employment because of a disability or 100 percent disabled due to military service; own the person's principal residence; and have a disposable income of less than \$35,000 per year. Persons meeting this criteria are entitled to partial property tax exemptions and a property valuation freeze. A surviving spouse or domestic partner of a person receiving the exemption may retain the exemption if the survivor is at least age 57 and otherwise meets the eligibility requirements.

Disposable income is defined as adjusted gross income, in addition to the following: capital gains; pension and annuity receipts; military pay and benefits other than attendant-care and medical-aid payments; veterans' benefits, other than attendant-care and medical-aid payments, disability compensation, and dependency and indemnity compensation; federal Social Security Act and railroad retirement benefits; dividend receipts; and interest received on state and municipal bonds, less amounts deducted for loss and depreciation.

Combined disposable income is defined as the disposable income of the person claiming the exemption, plus the disposable income of the person's spouse or domestic partner, and the disposable income of each cotenant occupying the residence, less amounts paid by the person claiming the exemption or the person's spouse or domestic partner during the assessment year for the following:

- prescription drugs;
- the treatment or care of either person in the home or a facility; and
- health care insurance premiums for Medicare.

Partial exemptions for senior citizens and persons retired due to disability are provided if the person's disposable annual income is as follows:

- \$30,001 to \$35,000 – the person is exempt from all excess property tax levies, but not regular levies;
- \$25,001 to \$30,000 – the person is exempt from all regular property tax levies on the greater of \$50,000 or 35 percent of assessed valuation, \$70,000 maximum, and all excess levies; and
- \$25,000 or less – the person is exempt from all regular property tax levies on the greater of \$60,000 or 60 percent of assessed valuation, and all excess levies.

Part XV - Concerning Property Tax Exemptions for Service-Connected Disabled Veterans and Senior Citizens: All real and personal property is subject to property tax each year based on its value, unless a specific exemption is provided by law. Some senior citizens and persons retired due to disability are entitled to a property tax exemption for their principal residences. To qualify a person must be age 61 in the year of application; retired from employment because of a disability or 100 percent disabled due to military service; own the person's principal residence; and have a disposable income of less than \$35,000 per year. Persons meeting this criteria are entitled to partial property tax exemptions and a property valuation freeze.

Disposable income is defined as adjusted gross income, plus: capital gains; pension and annuity receipts; military pay and benefits other than attendant-care and medical-aid payments; veterans' benefits, other than attendant-care and medical-aid payments, disability compensation, and dependency and indemnity compensation; federal Social Security Act and railroad retirement benefits; dividend receipts; and interest received on state and municipal bonds, less amounts deducted for loss and depreciation.

Combined disposable income is defined as the disposable income of the person claiming the exemption, plus the disposable income of the person's spouse or domestic partner, and the disposable income of each cotenant occupying the residence, less amounts paid by the person claiming the exemption or the person's spouse or domestic partner during the assessment year for the following:

- prescription drugs;
- the treatment or care of either person received in the home or a facility; and
- health care insurance premiums for Medicare.

Part XVI - Reducing the Frequency of Local Sales and Use Tax Changes: Sales and Use Tax. Retail sales taxes are imposed on retail sales of most articles of tangible personal property, digital products, and some services. A retail sale is a sale to the final consumer or end user of the property, digital product, or service. If retail sales taxes were not collected when the user acquired the property, digital products, or services, then use taxes apply to the value of property, digital product, or service when used in this state. The state, most cities, and all counties levy retail sales and use taxes. The state sales and use tax rate is 6.5 percent; local sales and use tax rates vary from 0.5 percent to 3.0 percent, depending on the location.

Local Sales Tax Changes. In general, local sales and use tax changes can take effect no sooner than 75 days after the DOR receives notice of the change and only on the first day of January, April, July, or October.

A local sales and use tax that is a credit against the state tax can take effect no sooner than 30 days after DOR receives notice and only on the first day of a month.

Part XVII - Providing Reasonable Tools for the Effective Administration of the Public utility District Privilege Tax: Public utility district (PUD) privilege tax is an in-lieu-of property tax. It applies to electricity generating facilities for the privilege of operating in this state. The tax rate has several components including gross income derived from the sale of electricity, the number of kilowatt hours of self-generated energy which is either distributed to consumers or resold to other utilities, and the wholesale value of energy produced in thermal generating facilities.

The PUDs report the facts pertinent to the calculation of the privilege tax to the DOR once per year. The DOR calculates the tax owed and collects the taxes paid by the PUDs.

The following distribution requirements apply to the PUD privilege tax collected on electricity generating or distribution facilities – other than the nuclear power plant on the Hanford reservation. The State Treasurer deposits 4 percent of the proceeds from the basic tax rate to the state general fund. The remaining 96 percent is distributed as follows: 37.6 percent to the state general fund for public schools; and 62.4 percent to the counties to be redistributed.

A county must distribute funds to each taxing district in the county, except school districts, in a manner the county deems most equitable. However, a city within the county must receive an amount at least equal to 0.75 percent of the gross revenues obtained from the sale of electricity within the city.

Part XVIII - Concerning a Hazardous Substance Tax Exemption for Certain Hazardous Substances that Are Used as Agricultural Crop Protection Products and Warehoused but not Otherwise Used, Manufactured, Packaged, or Sold in this State: The tax imposed on hazardous substances was initiated in the late 1980s, first by the Legislature and then by Initiative 97.

The tax base of the hazardous substance tax created by the Model Toxics Control Act (MCTA) is the wholesale value of substances defined as hazardous. It is a privilege tax imposed on the first possession in Washington State of petroleum products under the federal Comprehensive Environmental Response, Compensation, and Liability Act; pesticides registered under the Federal Insecticide, Fungicide, and Rodenticide Act; and substances designated by rule by the Washington State Department of Ecology to present a threat to human health or the environment.

The tax rate is 0.7 percent. The proceeds, up to \$140 million since July 1, 2013, are deposited into two accounts: 56 percent to the state toxics control account; and 44 percent to the local toxics control account. Any amount over \$140 million is deposited into the environmental legacy stewardship account. The purpose of MCTA is to raise sufficient funds

to clean up all hazardous waste sites and to prevent the creation of future hazards due to improper disposal of toxic wastes into the state's land and waters. The 2014 proceeds of \$195,010,885 are \$3,452,782 less than those of 2013.

There are exemptions from the hazardous substance tax, one of which includes persons and activities that the state is prohibited from taxing under the United States Constitution. This prohibition applies to materials in interstate commerce under article 1, section 8, clause 3, of the Constitution. This clause empowers Congress "to regulate commerce with foreign nations, and among several states, and with the indian tribes."

Agricultural crop protection products that meet the definition of pesticides under MCTA are sometimes manufactured at an out-of-state location and then are shipped to Washington warehouses. Sometimes the product is shipped from the Washington warehouse to a Washington retailer for sale to the Washington farmer or certified pesticide applicator. These products are subject to the hazardous substance tax because they are not items in interstate commerce.

A question has arisen when the product is shipped out of Washington from the warehouse. The DOR rules allow the exemption if the product in the warehouse is already owned by the out-of-state recipient when the product is received at the warehouse. Under any other shipping scenario, DOR levies the tax on the product even though it is ultimately sold out of state.

Part XIX - Concerning the Taxation of Certain Rented Property Owned by Nonprofit Fair Associations: Property Tax. All real and personal property in this state is subject to the property tax each year based on its value, unless a specific exemption is provided by law. 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 treasurer mails a notice of tax due to taxpayers and collects the tax.

Property Tax Exemption For Nonprofit Fair Associations. Generally, the real and personal property of a nonprofit fair association that sponsors or conducts a fair or fairs eligible to receive support from the fair fund and allocated by the director of the Department of Agriculture is exempt from property taxation. The property must be used exclusively for fair purposes.

Property Tax Exception. Property that would not otherwise qualify may be exempt from taxation if the nonprofit fair association had purchased or acquired the majority of such property between 1995 and 1998. This exception cannot be claimed after 2018.

Leasehold Interest. Leasehold interest means an interest in publicly owned real or personal property which exists by virtue of any lease, permit, license, or any other agreement, written or verbal, between the public owner of the property and a person who would not be exempt from property taxes if that person owned the property in fee, granting possession and use, to a degree less than fee-simple ownership.

Leasehold Excise Tax. A leasehold excise tax is levied on the act or privilege of occupying or using publicly owned real or personal property or real or personal property of a

community center through a leasehold interest on and after January 1, 1976, at a rate of 12 percent of taxable rent. A tax credit is available against the county tax for the full amount of any city tax imposed on the same taxable event.

Part XX - Improving the Administration of Unclaimed Property: The Uniform Unclaimed Property Act (Act) governs the disposition of property that is unclaimed by its owner. A business that holds unclaimed property (holder) must report and transfer the property to the DOR after a holding period set by statute. The holding period varies by the type of property, but for most unclaimed property, such as abandoned bank accounts, stocks, and bonds, the holding period is three years. After the holding period has passed, the holder in possession of the property transfers the property to DOR. A holder who willfully fails to file a report, or deliver property, as required under the Act is subject to a \$100 per-day penalty plus an additional 100 percent penalty based on the value of the property that should have been reported.

DOR's duty is to find the rightful owner of the property, if possible. Most property reported is intangible property and holders remit the cash value to DOR. With some exceptions, DOR will sell tangible property that is still unclaimed within five years after it is received. State law requires DOR to hold stocks, bonds, and other securities for a period of time – usually three years – before being sold. When the unclaimed property is sold, the sale proceeds are deposited in the state general fund.

The owner of unclaimed property may come forward at any time to claim the property. If the property has already been sold by DOR, the owner is generally entitled to the proceeds of the sale, plus any interest accruing as part of the security, less administrative costs. However, if abandoned stock or other securities are sold before the expiration of the three-year holding period by DOR, the owner is entitled to the greater of the market value of the security at the time the claim is made or the proceeds of the sale, less any administrative costs.

Summary of Bill: The bill as referred to committee not considered.

Summary of Bill (Proposed Substitute): Part I - Reinstating Tax Preferences for High-technology Research and Development: The high technology B&O tax credit and sales and use tax deferral, with certain modifications, are reinstated. The new tax preferences go into effect July 1, 2015, and expire January 1, 2025.

Business and Occupation Tax Credit for High Technology Research and Development. The total B&O tax credit that may be claimed by a person is reduced from the original \$2 million cap to the lesser of \$500,000 or the total amount of B&O tax due for the calendar year.

Sales and Use Tax Deferral for Certain Construction-Related Expenses. DOR must issue a sales and use tax deferral certificate upon receipt of an application from a person for an eligible investment project, if the application indicates that meaningful construction will occur within five years of the application date.

Sales and Use Tax Deferral. The total amount of sales and use tax deferred is limited to \$1 million per eligible project, per person, and only one eligible project per person may qualify for a deferral under this chapter per calendar year. Applicants may be a person or company,

broadly defined to include entities such as municipal corporations, a state university, or an affiliate of any such entity. Projects for which an application for deferral was denied prior to January 1, 2015, are not allowed to re-apply for deferral. The sales and use taxes deferred for qualified machinery and equipment integral and necessary to the development of pilot-scale manufacturing or qualified R&D operations, and sale of or charges made for labor and services, need not be repaid.

Meaningful Construction. A new term is defined. Meaningful construction means an active construction site, where excavation of a building site, laying of a building foundation, or other tangible signs of construction are taking place and that clearly shows a progression in the construction process, at the location designated by the taxpayer in the application for deferral. Planning, permitting, or land clearing before excavation of the building site, without more, does not constitute meaningful construction. If meaningful construction of a project does not begin within five years of the application date, or a project is not operationally complete within ten years of the application date, the full amount of deferred tax is immediately due.

Qualified Buildings and Partial Use for Other Purposes. The definition for qualified buildings is modified in that it excludes areas for amusement and recreational activities, physical fitness activities, parking, the selling or furnishing of meals or other food and beverages, or similar commercial and noncommercial activities as not essential or integral to pilot-scale manufacturing or qualified R&D. If a building or buildings are used partly for pilot-scale manufacturing or qualified R&D, and partly for other purposes, the applicable tax deferral will be determined by apportionment of the costs of construction under rules adopted by DOR.

Tax Preference Performance Statement. The Legislature states that the tax preferences are intended to improve industry competitiveness and create or retain jobs. The tax preference should be extended beyond the 2025 expiration date if a review finds that, as compared to the effective date of the act, (1) the number of businesses participating in the tax preference programs increased; and (2) the overall number of jobs for businesses participating in the tax preference programs increased.

Part II - Extending the Expiration Date of Tax Preferences for Food Processing: The B&O tax exemptions for food processors are extended from July 1, 2015, to July 1, 2025.

A tax preference performance statement is included. The stated public policy objectives of the act are to create and retain jobs in the food processing industry and to provide tax relief.

Part III - Providing a Sales and Use Tax Exemption for Eligible Server Equipment Installed in Certain Data Centers: A sales and use tax exemption is provided for eligible server equipment and eligible power infrastructure located in data centers in which construction commences between July 1, 2015, and July 1, 2025. Eligible server equipment affected by this act is equipment installed in a data center built after July 1, 2015, and includes original server equipment and replacement server equipment. The exemption for replacement server equipment continues for twelve years. Substations do not qualify as eligible power infrastructure.

Data centers built between 2012 and July 1, 2025, can receive a sales tax exemption for replacement servers for twelve years instead of eight.

Qualifying data centers are limited to eight from July 1, 2015, to July 1, 2019, and no more than 12 until July 1, 2025, on a first-come, first-served basis.

Buildings that are constructed on or after July 1, 2015, must be a fully enclosed structure with concrete, masonry, or weather-resistant exterior walls and must meet state building code.

Part IV - Creating a Pilot Program that Provides Incentives for Investments in Washington State Job Creation and Economic Development: The Invest in Washington pilot program is established to evaluate the effectiveness of providing a tax incentive for businesses that invest in manufacturing facilities and equipment and reinvest those tax savings in employee training programs. The pilot program consists of up to five qualified industrial facilities, of which at least two must be located in eastern Washington. An eligible investment project includes up to \$10 million in sales and use tax on construction costs or purchases of qualified machinery and equipment. Amounts paid for the construction of qualified buildings, machinery, and equipment are eligible for a sales and use tax deferral. To qualify for the deferral, the person must apply to the DOR before beginning construction of the investment or acquisition of the equipment or machinery. The DOR must award deferrals to qualifying applicants on a first-in-time basis. The recipient of the deferral must begin repaying the deferred taxes five years after the date that the project is complete. There is no interest charged on deferred taxes, and the taxes may be repaid over a ten-year period in equal annual payments.

Deferred taxes, when repaid, are deposited in the newly created Invest in Washington Account. The Invest in Washington Account, administered by the State Board for Community and Technical Colleges, must be used to support customized job training programs, job skills programs, job readiness training, workforce professional development, and to assist employers with state-approved apprenticeship programs for manufacturing and production occupations. The DOR must notify the State Treasurer by June 1, 2016, and annually thereafter, the amount of repaid deferred taxes contributed to the Invest in Washington Account.

The JLARC must measure the effectiveness of the credit for creating or retaining jobs and providing funding for job training.

Part V - Continuing Tax Preferences for Aluminum Smelters: The aluminum industry tax preferences that are set to expire in 2017 are extended for ten years to 2027.

A tax preference statement is included that directs JLARC to measure the effectiveness of the exemption in preserving employment positions within the industry by evaluating the change in the number of aluminum industry employment positions in Washington State.

Part VI - Concerning the Definition of Newspaper: Both the electronic version of a newspaper and the newspaper will be subject to the B&O tax at the rate of 0.35 percent. If the subscription revenue for the electronic version of a newspaper exceeds that of the

traditional revenue, the newspaper will be taxed at the rate of .471 percent for subscriptions and 1.5 percent for advertising.

Part VII - Providing a Reduced Public Utility Tax for Log Transportation Businesses: The PUT rate is permanently reduced from 1.926 percent to 1.3696 percent on the hauling of logs over public highways.

The hauling of logs over private roads is subject to the B&O tax under the service and other activities classification. The taxation of the transportation of logs that occur exclusively over private roads is not affected.

Part VIII - Concerning Nonresident Vessel Permits and Taxation: The availability of use permits for purposes of vessel sales and use taxation is extended to nonresident business entities, e.g. corporations, limited liability companies, partnerships, etc. There is a limit of 20 permits available in a calendar year given out on a first-come, first-served basis. Vessel dealers may not issue a use permit to a nonresident who is not an individual. In addition, acceptable documentation requirements for a nonresident business entity to qualify for the use permit are established.

A nonresident business entity owning a vessel may obtain a vessel permit allowing the vessel to remain in Washington for up to six months. Only 20 nonresident vessel permits may be given in a calendar year.

Part IX - Concerning Distribution and Use of Aircraft Excise Taxes: All of the annual aircraft excise tax is deposited into the aeronautics account to be used for state grants to airports and to cover administrative expenses associated with grant execution and collection of the aircraft excise tax.

The aeronautics account is restored.

Part X - Providing a Business and Occupation Tax Credit for Businesses That Hire Veterans: PUT or B&O tax credits are provided to businesses that provide positions to qualified employees. A qualified employee is an unemployed veteran who is employed in a permanent full-time position for at least two consecutive full calendar quarters. Full time is a normal work week of at least 35 hours per week. A veteran is a person who has received a general discharge under honorable conditions, including a discharge for medical reasons with an honorable record, or is currently serving honorably; and who has served as a member in any branch of the armed forces, including the National Guard and armed forces reserves. Unemployed means that the veteran was unemployed for at least 30 days immediately preceding the date on which the veteran was hired by the person claiming the credit. The credit is equal to 20 percent of wages and benefits paid up to a maximum of \$1,500 for each qualified employment position filled by an unemployed veteran. The credits are available on a first-in-time basis not to exceed \$500,000 in any fiscal year. Credits disallowed in one year can be carried over to the next fiscal year. Priority is given to credits carried over from a previous fiscal year.

Credits may be earned for tax reporting periods through June 30, 2021, and no credits may be claimed after June 30, 2022.

Tax preference credits are intended to induce employers to hire and create jobs for unemployed veterans. The JLARC must review the new credits by December 31, 2021. If, in its review, it finds that the number of unemployed veterans has decreased by 30 percent, then the Legislature intends to extend the expiration date of the credits.

Part XI - Defining Honey Bee Products and Services as an Agricultural Product: The definitions of agricultural product and farmer are amended to include apiarists and honey bee products. Therefore, the tax exemptions provided to agricultural products and farmers are extended to apiarists and honey bee products and are intended to be permanent. By modifying these definitions, the temporary, industry-specific, honey bee tax exemptions become redundant. This act repeals those redundant tax exemptions. The coinciding evaluation by the JLARC is also repealed.

Part XII - Providing Sales and Use Tax Exemptions to Encourage Coal-fired Electric Generation Plants or Biomass Energy Facilities to Convert to Natural Gas-fired Plants: The construction of new structures or renovation of existing structures for the purpose of converting a coal-fired electric generation facility into a natural gas-fired electric generation facility or biomass energy facility is exempt from sales and use tax. The exemption includes the labor and services to construct the facility and the machinery and equipment that is required for the conversion. The tax exemptions are in the form of a remittance and no remittance may be paid until the conversion of the facility is operationally complete, but not earlier than April 1, 2019.

A tax preference performance statement is provided and the exemption expires July 1, 2025.

Part XIII - Providing Use Tax Relief for Individuals Who Support Charitable Activities: Those who purchase or receive as a prize an article of personal property from a nonprofit organization or library for a fundraising activity do not owe use tax, regardless of the value of the property. This tax exemption is permanent.

Part XIV - Revising a Property Tax Exemption for Veterans with Total Disability Ratings and Their Surviving Spouses or Domestic Partners: A veteran receiving Veterans Administration compensation at a total disability rating for a service-connected disability qualifies for an exemption from all regular and excess property tax levies on their principal residence, without any income requirements, on taxes levied for collection in 2016 and thereafter. The surviving spouse or surviving domestic partner of a veteran receiving the exemption, may retain the total exemption if the surviving spouse or surviving domestic partner is at least 57 years of age.

A tax preference statement is included and states that the policy objective is to provide more extensive property tax relief to veterans with total disability ratings and their surviving spouses or domestic partners to properly recognize their sacrifice on behalf of the nation and to enable them to remain in their residences, thus reducing homelessness and demand for services in state veterans' homes. The JLARC must report to the Legislature by December 1, 2020, assessing the impact of the tax preference in reducing homelessness and demand for services in state veterans' homes among veterans with total disability ratings and their

surviving spouses or domestic partners. This tax exemption is permanent and, therefore, not subject to the ten-year expiration date for new or expanded tax preferences.

Part XV - Concerning Property Tax Exemptions for Service-Connected Disabled Veterans and Senior Citizens: The combined disposable incomes, for senior citizens and persons retired due to disability, used to determine their qualifications for a property tax exemption are increased by \$5,000. They must have as follows:

- a combined disposable income of \$40,000 or less to be exempt from excess property taxes; and
- a combined disposable income between \$30,001 and \$35,000 to be exempt from all regular property taxes on the greater of \$50,000 or 35 percent of the valuation of the person's residence, not to exceed \$70,000 of the valuation of the person's residence; or
- a combined disposable income of \$30,000 or less is exempt from all regular property taxes on the greater of \$60,000 or 60 percent of the valuation of the person's residence.

The combined disposable income for a person entitled to defer property taxes is increased by \$5,000. The person's combined disposable income must be \$45,000 or less, and the person must be at least 60-years old or retired from regular employment because of physical disability.

The increases are exempt from the ten-year tax preference expiration date.

Part XVI - Reducing the Frequency of Local Sales and Use Tax Changes: Local sales and use tax changes can only be made on the first day of January, April, or July. DOR must still receive notice 75 days prior to the change.

Part XVII - Providing Reasonable Tools for the Effective Administration of the Public Utility District Privilege Tax: Beginning January 1, 2016, PUDs must file all reports and remit all PUD privilege tax payments electronically. These requirements may be waived for good cause. Good cause is defined as circumstances or conditions that prevent the district from electronically submitting reports or remitting payments, or if the DOR determines relief from electronic filing supports the efficient or effective administration of the tax. If a district fails to remit payments electronically, the DOR must assess a 5 percent penalty.

An administrative mechanism is provided for obtaining refunds of overpaid taxes and applying interest to refund amounts. The PUD privilege tax distributions by the state to counties, cities, fire protection districts, and library districts must be reduced to account for taxes previously distributed to these jurisdictions and subsequently refunded to a PUD. Refunds or credits of taxes, penalties, or interest paid are limited to the DOR to three years after June 1 of the year the PUD privilege tax report is due. The DOR must provide an informal review of assessments and refund claims.

Assessments of additional taxes, penalties, and interest due are limited to three years after June 1 of the year the PUD privilege tax report is due.

Any taxpayer liable for the PUD privilege tax must maintain suitable records that are necessary to calculate tax liability for a period of five years. The records must be available for audit by the DOR.

The DOR may waive or cancel delinquent penalties and interest under certain circumstances.

Tax refund lawsuits may be brought to the Thurston County Superior Court. The DOR may enter into settlement agreements without the need to resort to litigation.

Part XVIII - Concerning a Hazardous Substance Tax Exemption for Certain Hazardous Substances that Are Used as Agricultural Crop Protection Products and Warehoused but not Otherwise Used, Manufactured, Packaged, or Sold in this State:

An exemption from the hazardous substance tax imposed under MCTA is created. It applies to the possession of an agricultural crop protection product when that possession is solely for use by a farmer or certified pesticide applicator and the product is warehoused in Washington or transported to or from Washington. To qualify for this exemption, the person possessing the product may not use, repackage, manufacture, or sell the product in Washington.

Part XIX - Concerning the Taxation of Certain Rented Property Owned by Nonprofit Fair Associations: Property Tax Exception.

The exception for property purchased or acquired by the nonprofit fair association from a county or a city between 1995 and 1998 does not expire after 2018. If any portion of the property is knowingly rented for more than 50 days, the exemption still applies but the rental income is subject to leasehold excise tax.

Leasehold Interest. Leasehold interest also includes portions of property owned by a nonprofit fair association exempt from property tax but rented for periods of 50 days or more.

Leasehold Excise Tax. The leasehold excise tax applies to the rental income of nonprofit fair association-owned land rented for 50 or more days. Taxable rental income or rent means contract rent. The rents or donations received for the use of the rented property must be reasonable and may not exceed the maintenance and operation expenses of the property.

Part XX - Improving the Administration of Unclaimed Property: The penalty provisions of the Act are restructured. The current 100 percent penalty for willful failure to file a report or provide notice to apparent property owners is replaced with the following penalties:

- 10 percent for failure to file a report or pay or deliver property under a report; and
- 10 percent assessment penalty with an additional 5 percent penalty if the assessment is not paid by the due date.

Gift certificates presumed abandoned and compliant with the gift certificate laws do not need to be reported as unclaimed property.

DOR may publish notice to apparent owners of unclaimed property on the online version of a printed newspaper of general circulation.

Enforcement action on assessments is subject to a three-year statute of limitation.

Holders must file reports of lost property and remit funds to DOR electronically beginning July 1, 2016. DOR may waive this requirement for good cause, which is defined as a

circumstance or condition that prevents the holder from electronically filing reports or remitting payments, or a DOR determination that relief from the electronic filing requirement supports the efficient or effective administration of the Act.

A refund process is established allowing holders to reacquire erroneously reported and delivered property, subject to a six-year limitation period. A review and appeal process is established, including appeal rights to Thurston County Superior Court, for assessments or denials for a refund or the return of property. DOR may waive or cancel delinquent penalties and interest under certain circumstances.

All unclaimed amounts and property identified in any assessment issued by DOR must be paid or delivered within 30 days of issuance. If a petition for review of an assessment is filed and received in writing by DOR before the due date of the assessment, only the uncontested amounts and property must be paid or delivered to the department within 30 days of issuance.

DOR's authority to enter into settlement agreements with holders is clarified.

Information obtained during examinations is confidential, except as necessary for the administration of the Act.

Appropriation: None.

Fiscal Note: Not requested.

Committee/Commission/Task Force Created: No.

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