

HOUSE BILL REPORT

HB 1641

As Reported by House Committee On:
Finance

Title: An act relating to restoring the business and occupation and public utility tax exemption for custom farming and hauling farm products.

Brief Description: Restoring the business and occupation and public utility tax exemption for custom farming and hauling farm products.

Sponsors: Representatives Hoff, Springer, Corry, Dufault, Graham, Sutherland, Rule, Griffey and Young.

Brief History:

Committee Activity:

Finance: 1/17/22, 1/24/22 [DP].

Brief Summary of Bill

- Reinstates the business and occupation tax exemption for custom farming.
- Reinstates the public utilities tax exemption for the hauling of farm products.

HOUSE COMMITTEE ON FINANCE

Majority Report: Do pass. Signed by 16 members: Representatives Frame, Chair; Berg, Vice Chair; Walen, Vice Chair; Orcutt, Ranking Minority Member; Dufault, Assistant Ranking Minority Member; Chase, Chopp, Harris-Talley, Orwall, Ramel, Springer, Stokesbary, Thai, Vick, Wylie and Young.

Staff: Tracey Taylor (786-7152).

Background:

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not part of the legislation nor does it constitute a statement of legislative intent.

Business & Occupation Tax.

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. Businesses must pay the B&O tax even though they may not have any profits or may be operating at a loss.

A taxpayer may have more than one B&O tax rate, depending on the types of activities conducted. Major B&O tax rates are 0.471 percent for retailing; 0.484 percent for manufacturing, wholesaling, and extracting; and 1.5 percent (businesses with taxable income of less than \$1 million) or 1.75 percent (businesses with taxable income of \$1 million or more) for services and for activities not classified elsewhere. Several preferential rates also apply to specific business activities.

In addition, a taxpayer may be eligible to utilize other tax preferences, including credits and deductions, to reduce their tax liability. For example, a taxpayer engaging in activities subject to different B&O tax rates may be eligible for a Multiple Activities Tax Credit. A taxpayer may also be eligible for a small business credit that will either eliminate or reduce their B&O tax liability. In general, the credit is \$70 per month for service businesses and \$35 per month for all other businesses, multiplied by the number of months in the reporting period. The amount of the credit available phases out based on the business's gross receipts.

A business does not have to file an annual B&O tax return if the business does not owe other taxes or fees to the Department of Revenue (DOR) and has annual gross proceeds of sales, gross income, or value of products for all B&O tax classifications of less than \$28,000 per year, or less than \$46,667 if at least 50 percent of its taxable income is from services or activities not classified elsewhere.

Public Utilities Tax.

The gross income derived from the operation of publicly and privately owned utilities is subject to the public utility tax (PUT), unless otherwise exempt. The tax is imposed in lieu of the B&O tax and is applied only on sales to consumers. Other income of the utility, such as retail sale of tangible personal property, is subject to the B&O tax. There are six different PUT rates, depending on the specific utility activity. The rates are:

- 3.852 percent on telegraph companies, distribution of natural gas, and the collection of sewage;
- 3.8734 percent on the generation or distribution of electrical power;
- 0.642 percent on urban transportation and watercraft vessels under 65 feet in length;
- 1.926 percent on motor transportation, railroads, railroad car companies, and all other public service businesses;
- 5.029 percent on the distribution of water; and
- 1.3696 percent on log transportation.

A taxpayer who engages in one or more businesses subject to the PUT is fully exempt from the tax if their total gross income is \$2,000 or less per month. Any taxpayer that has a total

gross income greater than \$2,000 per month does not receive an exemption or deduction under this provision.

A business does not have to file an excise tax return for PUT if the business does not owe other taxes or fees to the DOR and has annual gross receipts of less than \$24,000.

Tax Preferences.

State law provides for a range of tax preferences that confer reduced tax liability upon a designated class of taxpayer. Tax preferences include tax exclusions, deductions, exemptions, preferential tax rates, deferrals, and credits. Currently, Washington has over 650 tax preferences, including a variety of sales and use tax exemptions. Legislation that establishes or expands a tax preference must include a Tax Preference Performance Statement (TPPS) that identifies the public policy objective of the preference, as well as specific metrics that the Joint Legislative Audit and Review Committee (JLARC) can use to evaluate the effectiveness of the preference. All new tax preferences automatically expire after 10 years unless an alternative expiration date is provided.

Custom Farming and Hauling Farm Products Tax Preferences.

In 2007 the Legislature enacted two tax preferences for farms: a B&O tax exemption for farmers who provide custom farming services to other farmers; and a PUT exemption for those who haul farm machinery, equipment, or agricultural products for a related farmer or person performing customer farming services. Both preferences expired December 31, 2020.

In 2018 JLARC performed a Tax Preference Performance Review on these two exemptions. The Legislative Auditor's (Auditor) conclusion was that the tax preference for custom farming was providing tax relief to eligible farmers. However, the Auditor found lack of data to determine if farmers were using the PUT exemption for hauling farm products and equipment. The Auditor's recommendation, endorsed without comment by the Citizens Commission for Performance Measurement of Tax Preferences, was that the Legislature should continue and clarify the two preferences to add performance statements, specify public policy objectives, and eliminate the expiration dates.

Summary of Bill:

The B&O tax exemption for custom farming services and the PUT exemption for agricultural hauling are reinstated and made permanent.

The bill contains a TPPS that categorizes the tax preference as one to reduce structural inefficiencies in the tax structure. It further states that the legislative public policy objective is to provide tax relief to farmers, including those who changed their farm structure in response to federal regulations regarding irrigated water.

The preference is exempt from the automatic 10-year expiration and the requirement that the TPPS must specify clear, relevant, and ascertainable metrics and data requirements that allow JLARC and the Legislature to measure the effectiveness of the new tax preference in achieving its purpose.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill takes effect on July 1, 2022.

Staff Summary of Public Testimony:

(In support) This bill extends a limited tax exemption that assists family farmers and their employees. It reflects the reality of operating farming businesses under a common ownership structure by exempting payments between the commonly owned farms from B&O and public utility taxes. For example, a family farm may hire employees that work among the different farm operations and locations. Without this bill, the family farm would have to pay the worker in several different checks from the different farming operations in order to avoid paying the B&O tax on the transfer of funds between the farming operations. An employee may use a check-cashing service to access the wages, paying a fee for each check-cashing transaction. This bill will save family farms and their employees money by allowing for a single check to be issued for work on farming operations with a common ownership. This legislation helps farmers during these difficult times. Moreover, it lowers barriers for new farmers by allowing for the use of expensive equipment.

(Opposed) None.

Persons Testifying: Representative Larry Hoff, prime sponsor; Kriss Zerr, Domex Superfresh Growers; and Flor Maldonado, Maldonado Orchards.

Persons Signed In To Testify But Not Testifying: None.