

# SALT Breakfast Series

Washington Tax Incentives  
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# Agenda

- Overview of Incentives in Washington
- Available Tax Incentives by Industry
- Eligibility and Application Procedures
- Annual Survey Requirements
- Opportunities for Refunds
- State & Local Tax Update
- Questions & Answers

# Overview

- What is a tax incentive?
  - Feature of a balanced tax system
  - Inducement to investment
- Discretionary v. statutory incentives
- Changing legislative environment
  - Accountability
  - New terminology
    - “Loopholes”
    - “Tax Preferences”
  - ESSB 5882

# Tax Incentives by Industry

- Manufacturing
- High Technology
- Aerospace
- Farming
- Green/Environmental
- Rural/High Unemployment Areas
- Miscellaneous

# Manufacturing

- Sales and Use Tax
- Exemption for Machinery and Equipment (M&E) purchases (no expiration date)
- Includes installing, repairing, cleaning, altering, or improving the M&E
- What qualifies?
- What doesn't qualify?
- Relevant case 23WTD190 (2004)

# High Technology B&O Tax Credit

- How to qualify?
  - Engaging in R&D in WA in one of the 5 areas of high technology
  - R&D spending must exceed .92% of taxable income in the calendar year
  - Must have qualified R&D spending
    - What is qualified R&D spending?
    - What is not qualified R&D spending?

# High Technology B&O Tax Credit

- Calculating the credit
- Determine the greater of:
  - The qualified R&D expenditures *or*
  - 80% of amounts received by a person other than a public educational or research institution as compensation for conducting qualified R&D
- Then subtract .92% of the taxable income amount
- Then multiply the result by 1.5%
  - For the period Jan – Dec 2009, use the greater of the average tax rate or 1.25%

# High Technology Sales/Use Tax Deferral

- How to qualify?
  - Engaging in qualified R&D or pilot scale manufacturing in WA
  - In one of the 5 high technology areas
- What is eligible for the deferral?
  - Construction, expansion or renovation of qualified structures
  - Machinery & equipment - fixtures, equipment and support facilities
    - Must be integral and necessary
    - Must be “new” to the certificate holder



# High Technology Sales/Use Tax Deferral

- When do I apply for the Deferral Certificate?
  - Before the initiation of construction (the date that a building permit is issued)
  - Before the acquisition of equipment or machinery
- Submit copy of Deferral Certificate to vendors to receive sales tax exemption
- The application or certificate may be amended if necessary
  - Written request required

# High Technology Sales/Use Tax Deferral

- The project is operationally complete, now what?
  - Inform the DOR in writing that it is operationally complete
  - DOR will send a field auditor to audit the deferral
- What will the auditor do?
  - Tour the facility
  - Review the purchase invoices
  - Determine if use tax is due on nonqualifying purchases

# High Technology Sales/Use Tax Deferral

- What can you do?
  - Document qualifying expenditures as such in your records
  - Keep track of any purchase invoices with sales or use tax paid (tax should be refunded to you if a qualifying purchase)
  - Be able to explain how the purchase is integral and necessary to the R&D or pilot scale mfg. operation
  - Show that the item or constructed area is still in existence during the auditor's visit
  - Don't be alarmed at the auditor's "tax deferred schedule"

# High Technology Sales/Use Tax Deferral

- When is repayment of the deferred taxes required?
- Repayment schedule
- When is repayment not required?

# Aerospace B&O Tax

## – Reduced Rates

- Aerospace manufacturers/processors for hire reduced rate of .2904%
- Must be mfg. of commercial airplanes or component parts of commercial airplanes
- Aerospace nonmanufacturers in the business of aerospace product development – reduced rate of .9%
  - Includes research, design and engineering activities

# Aerospace B&O Tax – Credits

- Credit equal to 1.5% of qualified aerospace product development expenditures
  - What expenses qualify?
  - What expenses do not qualify?
- Credit equal to property tax or leasehold excise taxes paid on buildings constructed after June 30, 2008
  - What qualifies?

# Aerospace Sales/Use Tax Exemption

- Exemption allowed on purchases of computer hardware, software, and peripherals used primarily in the development, design & engineering of aerospace products or providing aerospace service
- Credit effective July 1, 2008; expires July 1, 2024
- Exemption includes installation and shipping charges
- Provide vendor with a completed Buyers Retail Sales Tax Exemption Certificate to receive exemption form to receive exemption
- Do not need annual survey/annual report to qualify

# Green Incentives

- Sales and Use Tax exemption – machinery & equipment used to generate electricity using a variety of different green sources that convert lost energy from exhaust or landfill gas
- Sales and Use Tax exemption – Clean Alternative Fuel Vehicles for any person
- Renewal Energy Cost Recovery Incentive Payment Program
- Reduces B&O rate – manufacturers/processors for hire of solar energy systems and specified components of solar energy systems



# Farming & Agriculture – Sales/Use Tax

- Replacement parts for qualifying farm machinery & equipment
- Anaerobic Digesters
- Livestock Nutrient Management Equipment and Facilities

# Rural/High Unemployment Incentives

- Rural County/Community Empowerment Zone
  - Sales & Use Tax Exemption – data centers
  - B&O Credit – new employees
  - Sales & Use Tax Deferral – corporate HQ
- High Unemployment County
  - Sales & Use Tax Deferral – manufacturing facilities

# Miscellaneous Incentives

- Commute Trip Reduction Program – B&O and PUT credit
  - Available to all employees and property managers who provide commute trip reduction incentives to or on behalf of their own or other employees
  - Expiration date extended to July 1, 2014
- Motion picture and video production companies
  - Sales/Use tax exemption on rental of production equipment and purchase of production services
  - No expiration date

# Miscellaneous Incentives

- B&O exemptions for food manufacturing industry
- Reduced B&O rates for timber extracting/mfg.
- B&O and sales/use tax exemptions for the biofuel industry
- Reduced B&O rates & sales/use tax exemptions for the semiconductor industry and aluminum smelting industry
- Sales/Use tax deferral for processing plants and cold storage warehouses
- Reduced B&O rate for newspaper publishers

# Eligibility and Applicable Procedures

- DOR rules and laws determine who or what qualifies for the incentive
- Certain incentives require prior DOR approval before receiving the benefit
- Other incentives are only reviewed if the business is under audit
- Credits/exemptions are narrowly construed

# Eligibility and Applicable Procedures

- Buyer's Retail Sales Tax Exemption Certificate
- Sales and Use Tax Deferral Application – DOR issues certificate
- Farm M&E application for exemption certificate – DOR issues certificate
- Manufacturers Sales Tax Exemption for M&E

# Annual Survey/Annual Report Requirements

- Required to be filed annually to receive certain incentives
- Due on April 30<sup>th</sup> of the following year
- First time filers to include specified information for the two preceding calendar years
- Must be filed electronically (unless permission is granted by DOR)

# Annual Survey/Annual Report Requirements

- Failure to timely file annual survey or annual report will result in disallowance of incentive for the year
- 30 day extension allowed for circumstances beyond the control of taxpayer
- 90 day one time only extension allowed



# Annual Survey/Annual Report Requirements

- ESSB 5882 – part XVII and part VIII
  - Every new or amended tax preference must sunset after 10 years unless otherwise provided
  - DOR required to prepare tax preference performance statements
  - DOR to update and improve annual surveys and reports
  - Taxpayer disclosure requirements

# Refund Opportunities

- May be able to claim the benefit of missed incentives for prior tax periods
  - Period for refunds is open back to December 31, 2013
  - For incentives requiring an annual survey or report, refunds available for any year for which a survey or report is filed. If no survey or report, only refunds for current year (2013)

# Refund Opportunities

- Sales/Use Tax paid on items purchased for:
  - Manufacturing machinery and equipment
  - High technology deferral (assuming application received prior to purchase)
  - Computer hardware/software/peripherals purchased by aerospace industry
  - Component or ingredient consumed
- What you need:
  - The purchase invoice showing sales tax paid
  - Proof of use tax paid on the purchase (if applicable)
  - Buyer's declaration for refund of sales taxes paid

# Refund Opportunities

- B&O credits (high tech and aerospace)
- Were all qualified expenses included in calculation?
  - Officer salaries related to qualifying activity
  - Random expenses directly incurred
  - Are additional activities qualifying, but the related expenses were not included
- B&O Preferences
  - Reclassifying revenue to a preferential rate

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# Washington Tax Update

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# Recent Developments

- 2013 Tax Legislation
- Administrative and Judicial Decisions
- DOR Rulemaking Activities
- DOR Stakeholder Projects
- Emerging City B&O Tax Issues

# 2013 Legislation – Tax Preferences

ESSB 5882 (C 13. L 2013) – Effective Dates Vary  
(most effective October 1, 2013)

- Reinforces concept of “tax preferences” developed during budget dialogue from recent years
- Imposes mandatory 10 year sunset on all new or expanded tax preferences
- DOR and taxpayer reporting responsibilities
- Common Paymasters – No Additional B&O tax liability
- Notable new preferences: food flavoring, dancing, fundraiser winners



# 2013 Legislation – Miscellaneous

- SB 5715 (7/28/13)
  - Provides various civil and criminal sanctions related to sales suppression devices (known as “Zappers”)
- SSB 5444 (7/28/13)
  - Elimination of the Leasehold Excise Tax Credit
- ESSB 5024 (5/20/13)
  - Extends the Commute Trip Reduction Credit to 7/1/14 - caps credit at \$1.5 million

# Administrative Changes & Decisions

- Decreased B&O Rates Effective July 1, 2013
- Published Appeal Decisions
  - Sales Tax: escrow services, dinner theater, resale of digital automated services, skydiving, nightclub cover charges, mobile arcade charges, and rental of crane with operator
  - Audits/recordkeeping: use of estimation methods by auditor allowed, taxpayer must retain proof of exemption
  - Deductions/Credits/Exemptions: prototypes, rental of real estate, dialysis equipment, bona fide dues, bad debt sales tax credit, CPAP machines, drug delivery devices, utility hook-up charges
  - Classification: roadside assistance/damage waiver taxable as service

# Judicial Decisions

- *State of Washington, Department of Revenue, v. Bi-Mor, Inc.* 286 P3d 417 (2012)
- *Cashmere Valley Bank v. State of Washington, Department of Revenue* 42514-9-II (2013)
- *Sprint Spectrum, LP v. State of Washington Department of Revenue* 302 P3d 1280 (2013)
- *Charles H. Morse v. State of Washington Department of Revenue* 12-044 (2013)

# Rule Development

- Requirement to separately state sales tax – amend existing Rule 107 to recognize *Bi-Mor* court decision
- Apportionment – adopt new rule 19405 to provide current substantial nexus thresholds per RCW 82.04.067
- Radio & TV broadcasting – amend existing rule 241 to be consistent with statutory requirements
- Nexus & place of sale – amend rule 193 to update for legislative changes and clarify drop shipments
- Warranties & maintenance agreements – amend rule 257 to recognize sale of extended warranties is retailing

# Rule Adoptions/Amendments

- 458-20-162 – Stockbroker and security houses
- 458-20-155 – Computer hardware, software, and digital products
- 458-20-15501 – Taxation of computer systems and hardware
- 458-20-15502 – Taxation of computer software
- 458-20-15503 – Digital products
- 458-20-179, 17901, & 180 – Public utility tax
- 458-20-270 – Telephone excise taxes

# Excise Tax Advisories (ETAs)

- 3173.2013 – Distributor Discounts/Allowances to Grocery Stores
- 3174.2013 – B&O Tax and Out-of-State Printers
- 3175.2013 – Purchases made with Funds Provided by the Federal Government
- 3176.2013 – Digital Products-General Implementation
- 3177.2013 – Digital Products-General Analysis of Tax Liability
- 3178.2013 – Domestic International Sales Corporations
- 3179.2013 – Washington State Estate Tax Treatment of Same-Sex Spouses

# Draft ETA Topics

- 3180.2013 – Warehousing/Reselling Prescription Drug B&O Tax Preference
  - Adopted, but not yet issued
- Alarm Monitoring and the Primary Human Effort Exclusion
- Professional Employer Organizations

# Special Notices of 2013

- Livestock Nutrient Management Equipment Sales Tax Exemption Reinstated
- Opportunity to Dance
- Charcoal Briquettes/Wood Chips
- Clay Targets
- Commute Trip Reduction Tax Credit Extended
- Automotive Adaptive Equipment to Disabled Veterans
- Telephone Program Excise Tax Rates for FY 2014
- Telephone Tax Changes Effective Aug 1, 2013
- Personal Chefs



# Special Notices of 2013, cont.

- B&O credit for Harvesters extended
- Hog Fuel Sales/Use Tax Exemption extended
- Beekeepers
- Fresh Fruit/Vegetable, Seafood, and Dairy Product Mfg. B&O Exemptions Extended
- Leasehold Excise Tax Credit Eliminated
- Oil Spill Response Tax Suspended April 1, 2013
- Industrial Development District Levies for Port Districts
- Transit Authorities Providing Paratransit Services
- Foreign Diplomats Motor Vehicle Tax Exemption

# Current Stakeholder Projects

- Affiliated Entity Transactions
- Derived from the Getty Images decision
- DOR to provide additional guidance
- DOR has been working with stakeholders since January 2013 on the issues

# Emerging City Tax Issues

- Kent

- Adopted a B&O tax effective January 1, 2013
  - Rates - .046% / .152%
- Mandatory online filing of returns effective October 1, 2013
- Square footage tax (Warehouses < 4K sq. ft. exempt, others 12k sq. ft.)
  - 3¢ / 1¢ per sq. ft. per quarter

- Bellevue

- Changes made to the Square Footage Tax form effective January 1, 2013
- B&O tax guide issued on January 1, 2013

# City B&O Tax Model Ordinance

- Cities must adopt 2012 revisions with effective date of January 1, 2013
- 2012 revised model ordinance reflects 6 changes
  - Digital goods definitions and apportionment
  - Board of director licensing and tax
  - “Super Nexus”
  - Insurance business preemption
  - First mortgage deduction
  - Confidentiality