TAX EXEMPTION FACT SHEETS

Office of Financial Management

January 2014

Eliminate preferential tax rate for resellers of prescription drugs

Description

This proposal eliminates the preferential business and occupation (B&O) tax rate of 0.138% for resellers of prescription drugs. It instead applies the wholesaling B&O tax rate of 0.484% or the retailing B&O tax rate of 0.471% to these activities.

Current Law

A preferential B&O tax rate of 0.138% is provided in RCW 82.04.272 to persons who warehouse and resell prescription drugs to retailers, hospitals, clinics, health care providers or other providers of health care services.

Original Purpose and Current Analysis

This tax preference was enacted in 1998 to encourage out-of-state prescription drug companies to build warehouses in Washington.

The state was unable to restrict the preferential rate only to companies with in-state warehouses, so it now provides tax relief to out-of-state wholesalers with nexus in Washington. This negates the purpose of the preferential rate.

Citizen Commission Recommendation

The Citizen Commission recommended the Legislature continue this preference, but based on public testimony questioning its necessity, the Commission further commented that the Legislature could consider a review.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013–15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015–17 Biennium
$0	$15.6	$15.6	$16.6	$17.7	$34.3

Notes:

- *Estimates assume a June 1, 2014, effective date, representing 12 months of collections for FY 2015.*
- *Estimates reflect the November 2013 Economic and Revenue Forecast Council revenue forecast.*

Refund state portion of sales tax to nonresidents

Description

This proposal would change the current nonresident sales tax exemption to a refund program for the state portion (6.5%) of the sales tax only. This would require qualified nonresidents (both businesses and individuals) to apply for a refund of state sales tax (not local sales tax) from the Department of Revenue instead of receiving the exemption at the point of sale.

The sales tax exemption at the point of sale would cease. In addition:

- Applications for state sales tax refunds would be made electronically once a year for purchases made in the preceding calendar year;
- Applications would be accepted only for refunds of $25 or more; and
- Sales receipts, addresses of the places of purchase and other documentation as required by the Department of Revenue would need to be submitted.

Current Law

Under RCW 82.08.0273, bona fide residents of a state, U.S. possession or territory, or province of Canada that does not impose a sales tax or similar consumer tax of 3% or more may purchase tangible personal property for use outside this state without paying Washington's sales tax.

The seller is not required to make a tax-free sale to a nonresident, but if the seller does:

- The purchaser must provide proof of exemption to the seller; and
- The seller must retain a record of the proof.

Original Purpose and Current Analysis

To enable Washington sellers, especially along the Oregon border, to compete with merchants in other states that either: (1) do not levy a retail sales tax or (2) levy a sales tax with a low rate.

Citizen Commission Recommendation

The Citizen Commission recommended the Legislature review and clarify this preference because there is no explicitly stated public policy objective.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013–15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015–17 Biennium
$0	$29.0	$29.0	$30.1	$31.2	$61.3

Notes:

- *Estimates assume a June 1, 2014, effective date, representing 12 months of collections for FY 2015.*
- *Estimates reflect the November 2013 Economic and Revenue Forecast Council revenue forecast.*

Repeal the public utility tax deduction for the in-state portion of interstate transportation

Description

This proposal would repeal the state's public utility tax deduction for the in-state portion of interstate transportation of goods and passengers, such as by motor vehicle, rail, pipeline or vessel.

Current Law

Gross income from the operation of transportation services is subject to the public utility tax. At the time that the Revenue Act of 1935 was enacted, the U.S. Supreme Court interpreted the Commerce Clause as barring a direct tax on gross receipts from interstate transportation. As a result, the Tax Commission's rules to implement the Revenue Act recognized explicitly that the state could not tax the income derived from the transportation of goods across the state's boundaries. This exemption has remained in the rules to this day.

However, the Commerce Clause as interpreted by the U.S. Supreme Court no longer bars states from taxing the privilege of engaging in an interstate business as long as the tax:

- Is applied to an activity with a substantial nexus with the taxing state;
- Is fairly apportioned;
- Does not discriminate against interstate commerce; and
- Is fairly related to the services provided by the state.

Original Purpose and Current Analysis

To reflect Commerce Clause decisions when the Revenue Act of 1935 was enacted. Current Commerce Clause decisions do not bar states from taxing the privilege of engaging in an interstate business.

Citizen Commission Recommendation

The Citizen Commission recommended the Legislature review and clarify this preference.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013–15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015–17 Biennium
$0	$33.6	$33.6	$35.0	$36.4	$71.4

Notes:

- *Estimate assumes a June 1, 2014 effective date, representing 12 months of collections for FY 2015.*
- *Estimates reflect the November 2013 Economic and Revenue Forecast Council revenue forecast.*

Repeal sales tax exemption for trade-ins valued over $10,000

Description

This proposal would limit the exclusion of trade-in value from retail sales and use tax to $10,000 for motor vehicles, recreational vehicles, boats and other items.

Current Law

When a consumer purchases tangible personal property, the measure of sales or use tax excludes the value of like-kind property traded in at the time of sale. Consequently, the trade-in value is deducted from the selling price that is subject to sales tax. (RCW 82.08.010(1) and 82.12.010(1))

Original Purpose and Current Analysis

The trade-in exclusion was approved by voter initiative in 1984 to encourage purchases of new items, especially motor vehicles.

Trade-ins of motor vehicles average $7,500, so limiting deductible trade-in values to $10,000 benefits most households. The current unlimited deduction primarily benefits high-income purchasers with the lowest tax burdens in Washington. Setting a limit would reduce the regressivity of the current tax system.

Citizen Commission Recommendation

The Citizen Commission has not reviewed the trade-in exclusion.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013–15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015–17 Biennium
$0	$45.4	$45.4	$47.7	$50.1	$97.8

Notes:

- *Estimates assume a June 1, 2014, effective date, representing 12 months of collections for FY 2015.*
- *Estimates reflect the November 2013 Economic and Revenue Forecast Council revenue forecast.*

Repeal sales tax exemption on bottled water

Description

This proposal would repeal the sales tax exemption on sales of bottled water to consumers. The tax would apply to both portable-sized bottles *and* to bulk bottled water sales (sales of water in large, reusable containers).

Current Law

- Under current law, sales tax does not apply to retail sales of bottled water.
- Until Jan. 1, 2004, sales of bottled water were subject to sales tax. At that time, legislation to conform to the Streamlined Sales and Use Tax Agreement (SSUTA) took effect and sales of bottled water became exempt from sales tax. In 2010, the SSUTA was amended to allow member states to separately tax bottled water sales.
- In 2010, Senate Bill 6143 imposed sales tax on sales of bottled water beginning July 1, 2010, until Dec. 2, 2010, when the sales tax on bottled water was repealed by Initiative 1107.

Original Purpose and Current Analysis

To conform to definitions of SSUTA. However, SSUTA has been amended to allow taxation of bottled water.

Citizen Commission Recommendation

Not reviewed by the Citizen Commission.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013–15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015–17 Biennium
$0	$24.3	$24.3	$24.2	$24.0	$48.2

Notes:

- *Estimates assume a June 1, 2014, effective date, representing 12 months of collections for FY 2015.*
- *Estimates reflect the November 2013 Economic and Revenue Forecast Council revenue forecast.*

Repeal sales tax exemption on janitorial services

Description

This proposal would make the sale of janitorial services to consumers a retail sale. Janitorial businesses would report business and occupation (B&O) tax under the retailing classification and collect retail sales tax from their customers.

Current Law

Under current law, the definition of retail sale specifically excludes janitorial services. Janitorial service is defined as the cleaning and caretaking of buildings and structures, including wall and window washing, floor cleaning and waxing, and the cleaning in place of rugs, drapes and upholstery.

Businesses providing janitorial services currently report their gross income under the service and other activities B&O tax classification.

Original Purpose and Current Analysis

To reflect the fact that janitorial services were considered to be a service instead of a retail sale.

Cleaning services are taxed two different ways. Specialized cleaning services or cleaning of building exteriors are subject to sales tax. Routine janitorial services are taxed as a non-retail service.

Citizen Commission Recommendation

The Citizen Commission recommended the Legislature terminate this tax preference.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013–15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015–17 Biennium
$0	$20.5	$20.5	$20.5	$21.5	$42.0

Notes:

- *Estimates assume a June 1, 2014, effective date, representing 12 months of collections for FY 2015.*
- *Estimates reflect the November 2013 Economic and Revenue Forecast Council revenue forecast.*

Repeal use tax exemption for extracted fuel, except hog fuel

Description

This proposal would limit the use tax exemption for fuel produced by the extractor or manufacturer when the fuel is directly used in the same extracting or manufacturing operation that produced the fuel. Only wood byproducts, also referred to as "hog fuel," would be eligible for the exemption.

Current Law

Fuel consumed by manufacturers or extractors is exempt from use tax when the fuel is used in the process of manufacturing or extracting at the same plant.

- The fuels for which the exemption applies are generally wood byproducts, also referred to as "hog fuel," and refinery fuel.
- Approximately 180 wood product manufacturers and five petroleum products refineries are eligible for the exemption.
- In its preliminary 2011 Tax Preference Review Report, the Joint Legislative Audit and Review Committee notes that while no refineries existed in the state when the exemption was enacted in 1949, refinery fuels account for approximately 98% of the estimated value of the exemption.

Original Purpose and Current Analysis

To support the fuel manufacturing and extracting industry.

However, the biggest beneficiaries of this exemption are oil refineries that did not even exist when this statute was originally enacted. Other industries pay tax when they use materials that they manufacture themselves.

Citizen Commission Recommendation

The Citizen Commission recommended that the Legislature review and clarify this preference because the public policy objective and intended beneficiaries are not clear.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013–15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015–17 Biennium
$0	$31.7	$31.7	$30.1	$29.0	$59.1

Notes:

- *Estimates assume a June 1, 2014, effective date, representing 12 months of collections for FY 2015.*
- *Estimates reflect the November 2013 Economic and Revenue Forecast Council revenue forecast.*