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Overview

Process for Commission Action on 2011 Tax Preference Reviews

October 11, 2011

Reviews are placed into one of seven groups based on the JLARC recommendation. Each group will be addressed using the steps noted below.

Group A: Continue – endorse without comment

First, the Commission will consider 12 reviews that have no proposed comments.

- Commissioners will be asked if they would like to adopt individual comments for any preferences from Group A.
- If there are any, those preferences will be moved to Group B (see below).
- The Commission will then entertain a motion to act on those remaining in the Group A list.
- Any Commissioner can ask to add a minority report reflecting their individual comments. (See Citizen Commission Citizen Commission for Performance Measurement of Tax Preferences Bylaws, Article VII: Minority Reports on back of this page)

Groups B Through E

The Commission will then consider adopting additional comments for preferences in Groups B through E, in order.

- Action on the remaining specific preference reviews will be considered in order of the following groups. For each of these the Commission will determine whether to endorse or not endorse, and adopt any additional comments. These groups are organized based on the JLARC recommendation:
 - **GROUP B:** Continue – endorse or not endorse; consider whether to provide a comment
 - **GROUP C:** Re-examine or Clarify Intent – endorse without comment
 - **GROUP D:** Re-examine or Clarify Intent – endorse and consider whether to provide a comment
 - **GROUP E:** Allow to Expire – endorse without comment
 - **GROUP F:** Allow to Expire – do not endorse and consider whether to provide a comment
 - **GROUP G:** Terminate – endorse without comment
- Each preference and any associated Commission comments will be discussed individually.
- The Commission will then entertain a motion to act on each individual preference.
- Any Commissioner can ask to add a minority report reflecting their individual comments.

Citizen Commission for Performance Measurement of Tax Preferences

Bylaws

Article VII: Minority Reports

Section 1: Minority Report(s): Any Commission member may request a minority report for any motion that has been approved by a vote of the Commission. Requests must be made to the Chair at the meeting, following the approval of the motion. The Chair shall ensure that minority reports requested by members are registered in the record of business for the Commission meeting.

Group A
Continue – endorse without comment

1. *There are 13 tax preference reviews with no proposed Commission comments.*

Tax Preference		Comment
1.	Boat sales to nonresidents & foreign residents (p. 29)	No Proposed Commission Comment
2.	Church camps (p. 43)	
3.	Display items for trade shows (p. 51)	
4.	Interest from state/municipal obligations (p. 77)	
5.	Interstate bridges (p. 95)	
6.	Investment of businesses in related entities (p. 103)	
7.	Laundry for nonprofit health care facilities (p. 111)	
8.	Nonprofit blood and tissue banks (p. 149)	
9.	Nonprofit day care centers (p. 157)	
10.	Open space compensating tax (p. 173)	
11.	Real estate excise tax exemptions (p. 181)	
12.	Sales or use tax paid in another state (p. 231)	
13.	State Chartered Credit Unions (p. 249)	

2. *If a Commissioner would like to have individual comments adopted on any of these preferences, we will defer discussion of those preferences to Group B. Do any Commissioners have comments on individual preferences they would like to discuss later with Group B?*

3. *Is there a motion for the Commission to take action on the remaining reviews in Group A?*

4. *Potential motion language:*

“The Commission acknowledges receipt of the 2011 JLARC Tax Preference Reviews of [preferences being discussed]. The Commission has provided a forum for discussion and public comment on these recommendations. The Commission endorses the JLARC recommendations for these preferences. The Commission does not have additional comments to append to the 2011 JLARC reports related to these preferences.”

Group B

Continue – endorse or not endorse; consider whether to provide a comment

1. There is **one** tax preference reviews in Group B with proposed Commission comments:

Tax Preference	Comment
<p>1. Sales of goods to certain nonresidents for use out-of-state (p. 217)</p>	<p><u>Audit staff recommendation:</u> Because the preference is meeting its public policy objective of removing a disincentive for nonresidents from no or lower tax locations to purchase goods in Washington, the sales tax exemption for certain nonresidents should be continued.</p> <p>William Longbrake:</p> <p><u>Possible comment:</u> The Commission does not endorse the recommendation because <u>there is ambiguity about it is not clear that</u> the Legislature’s public policy objective <u>and the economic benefits and costs is to remove a disincentive for nonresidents from no or lower tax locations to purchase goods in Washington</u>; the Legislature should review and clarify the public policy objective and evaluate the economic impacts of this preference.</p> <p><u>Rationale for comment:</u> The Legislature has not stated an explicit public policy objective for this preference. However, based on various commentaries and patterns of practice, JLARC staff determined that the “implied” public policy objective is to remove a disincentive for nonresidents to purchase goods in Washington. The beneficiaries are businesses that have greater sales than otherwise might be the case, thus benefiting the state’s economy. However, it is possible that many of the purchases of goods benefiting from this preference would have occurred in the absence of this preference. To the extent that this has occurred, the state is sacrificing revenue without realizing any offsetting economic benefits. <u>For example, it is possible suggested</u> that purchase of high value items <u>would</u> decline in the absence of this preference while the impact on purchase of low value items might be limited. While it would be difficult and expensive to conduct a thorough analysis of costs and benefits of this preference, it would be useful for the Legislature <u>to</u> consider the benefits and consequences that might stem from limiting the items and geographies covered by this preference.</p>

2. We will now take action on each of the preferences in Group B.

3. Is there any discussion on each of the above preferences?

4. Is there a motion for the Commission to take action on these reviews?

5. *Potential motion language:*

“The Commission acknowledges receipt of the 2011 JLARC Tax Preference Review of [preferences being discussed]. The Commission has provided a forum for discussion and public comment on these reviews. The Commission (endorses) OR (does not endorse) the JLARC recommendation(s) for this review, (subject to the following additional comments.) OR (without appending additional comments.)”

GROUP C
Re-examine or Clarify Intent – endorse without comment

1. *There are two tax preference review in Group C with no proposed Commission comments:*

Tax Preference		Comment
1.	Municipal sewer charges (p. 143)	No Proposed Commission Comment
2.	Extracted fuel (p. 57)	

2. *We will now take action on each of the preferences in Group C.*

3. *Is there any discussion on the above preference?*

4. *Is there a motion for the Commission to take action on this review?*

5. *Potential motion language:*

“The Commission acknowledges receipt of the 2011 JLARC Tax Preference Review of [preferences being discussed]. The Commission has provided a forum for discussion and public comment on these reviews. The Commission (endorses) OR (does not endorse) the JLARC recommendation(s) for this review, (subject to the following additional comments.) OR (without appending additional comments.)”

GROUP D

Re-examine or Clarify Intent – endorse and consider whether to provide a comment

1. There are six tax preference reviews in Group D with proposed Commission comments:

	Tax Preference	Comment
1.	Aircraft fuel, exports & commercial use (p. 17)	<p><u>Audit Staff recommendation:</u> Because parties that are exempt from paying the aircraft fuel tax now benefit from the expenditures of fuel tax receipts, the Legislature should review and clarify the preferences to determine whether more of the parties that benefit from the expenditures should pay the tax.</p> <p>William Longbrake:</p> <p><u>Possible comment:</u> The Commission endorses the recommendation and encourages the Legislature to state the public policy objectives of the preference and narrow the scope of the preference commensurate with the stated public policy objectives.</p> <p><u>Rationale for comment:</u> The JLARC staff study indicates that there are two implied public policy objectives for this preference. The first is that parties benefiting from the expenditure of aircraft fuel tax receipts were the ones that paid the tax. This implied public policy objective is not being met. The second implied public policy objective was to comply with U.S. Constitutional prohibitions on taxing goods in interstate commerce. However, in many instances the tax could be levied and comply with the U.S. Constitution provided that credit was provided for taxes paid in other states.</p>
2.	Interest on real estate loans (p. 83)	<p><u>Audit Staff recommendation:</u> Because it is unclear whether the original public policy objective applies, given changes in the lending industry and the rise in the secondary mortgage market, the Legislature should clarify the public policy objective of the first mortgage interest deduction.</p> <p>William Longbrake:</p> <p><u>Possible comment:</u> The Commission endorses the recommendation that the Legislature should review and clarify the public policy objective of the preference and should consider whether the preference is essential to maintaining competitive residential lending capability for state-domiciled residential real estate lenders.</p> <p><u>Rationale for comment:</u> The Legislature did not specify a public purpose for this preference. JLARC staff inferred from the record that the implied public policy purpose was to encourage Washingtonians to buy homes by making loans more available and less expensive. However, if the deduction were to</p>

		<p>be removed, the holder of the residential mortgage loan would bear the full burden rather than the borrower, unless the elimination of the deduction applied only to loans originated or purchased after the effective date of the repeal of the deduction. On a prospective basis the portfolio lender could attempt to recoup the cost of the B&O tax by charging a higher interest rate to the borrower; however, the mortgage market is national in scope, which virtually makes it impossible to charge interest-rate differentials on a geographic basis.</p> <p>As is often the case when the B&O gross receipts tax is involved in a preference, another unstated public policy purpose may be to assure competitive balance with similarity situated business firms in other states subject to other types of tax regimes. The Commission received testimony that removal of the deduction would place a burden on state-domiciled residential mortgage lenders that retain the loans they originate in their portfolios.</p>
3.	<p>Limited income property tax deferral (p. 117)</p>	<p><u>Audit Staff recommendation:</u> Because the intended beneficiaries of this preference are not clear in light of recent economic recession, the Legislature should clarify the preference to define “families in economic crisis” and identify measurable evaluation criteria.</p> <p><i>William Longbrake:</i></p> <p><u>Possible comment:</u> The Commission endorses the recommendation that the Legislature should clarify the preference to define “families in economic crisis” and, if the Legislature determines to continue the preference, identify measurable evaluation criteria; however, the Commission notes that costs to administer the program are considerable relative to the participation rate and, as such, it might be appropriate to terminate the preference unless the preference can be restructured in a way that assures cost effective achievement of the public policy objectives.</p> <p><u>Rationale for comment:</u> To date only 181 out of an estimated 425,000 potential participants have taken advantage of the preference. Participant benefits in the 2009-11 biennium were \$270,891 while costs to administer the preference \$350,184 for fiscal years 2009, 2010, and 2011. JLARC staff recommends that the Legislature clarify the definition of “families in economic crisis”. While this might result increasing the participation rate, it is possible that the low participation rate also results from the eligibility criteria and the design of the program. Furthermore, it is not clear that the preference, as designed, is serving a critical public policy purpose of helping families in economic crisis. If the Legislature determines that is the case, the Commission believes it would be better to terminate the preference and save the state costs of administering the program.</p>

4.	Meat processors (p. 131)	<p><u>Audit Staff recommendation:</u> Because it is unclear what the public purpose is for providing differential tax treatment of meat processors compared to other food processors, the Legislature should clarify the public policy purpose for this preference.</p> <p><i>William Longbrake:</i></p> <p><u>Possible comment:</u> The Commission endorses the recommendation that the Legislature should review and clarify the public policy purpose of the preference and further recommends that the Legislature determine whether the tax differential provides approximate competitive parity with state tax rates and geography-based differences in other business costs for meat processors domiciled in other states.</p> <p><u>Rationale for comment:</u> Meat processing is a highly competitive, low margin business. This means that small differentials in state tax rates and other costs of business, such as transportation expenses, can have significant impacts on profitability and impact locational decisions. Public testimony provided to the Commission argued that the preferential tax rate for meat processors is comparable to the maximum corporate tax rate in other western states.</p>
5.	Nonprofit sheltered workshops (p. 165)	<p><u>Audit Staff recommendation:</u> Because public policy related to employment of the disabled has changed from the time the tax preference was enacted, the Legislature should clarify the public policy objective of the property tax exemption for sheltered workshops.</p> <p><i>William Longbrake:</i></p> <p><u>Possible comment:</u> The Commission endorses the recommendation that the Legislature should review and clarify the public policy objective of the preference and further recommends that the Legislature evaluate whether the preference is necessary any longer to encourage employment of persons with disabilities.</p> <p><u>Rationale for comment:</u> Although the statute does not state a public policy purpose, the implied purpose was to encourage employment of persons with disabilities in sheltered workshops. Since the enactment of this preference in 1970 the Federal government enacted the Americans with Disabilities Act in 1990. In response, over time employers have made efforts to employ persons with disabilities, frequently with beneficial economic results. In addition, the state has taken initiatives, beginning in 1992, to encourage employment of persons with disabilities. Thus, the need for sheltered workshops to employ persons with disabilities has diminished since enactment of the preference. While the preference clearly benefits established sheltered workshops, it is no longer clear that this preference is necessary to assure employment of persons with disabilities.</p>
6.	Shared real estate	<p><u>Audit Staff recommendation:</u> Because it is not clear why the Legislature granted a tax preference to</p>

<p>commissions (p. 239)</p>	<p>real estate brokers and agents and not to other businesses with similar broker-agent and cooperating broker relationships, the Legislature should clarify the B&O tax preference for shared real estate commissions.</p> <p>William Longbrake:</p> <p><u>Possible comment:</u> The Commission endorses the recommendation that the Legislature should clarify the B&O tax preference for shared real estate commissions and further recommends that the Legislature align B&O tax treatment of real estate brokers and agents to brokers and agents in other industries unless there is a compelling reason for differential treatment.</p> <p><u>Rationale for comment:</u> The standard approach to applying the B&O tax to commissions received by brokers and agents is that the broker is taxed on the full amount of the commission and the agent, if any, who receives a portion of the broker's commission, must pay an additional B&O tax on the amount he/she receives. This approach is the standard for all but real estate brokers and agents in which case real estate agents are exempted from paying B&O tax. The Legislature did not specify a public policy objective for differential treatment between real estate agents and agents in other industries, such as insurance and investment services. The Washington Realtors, in a letter to the Commission, presented information which may be pertinent to the Legislature's consideration of this preference; however, this information also appears to be pertinent to brokers and agents in other industries and, as such, does not address the issue of differential treatment.</p>
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2. *We will now take action on each of the preferences in Group D.*

3. *Is there any discussion on each of the above preferences: [proceed with the first item above]?*

4. *Is there a motion for the Commission to take action on these reviews?*

5. *Potential motion language:*

“The Commission acknowledges receipt of the 2011 JLARC Tax Preference Review of [preferences being discussed]. The Commission has provided a forum for discussion and public comment on these reviews. The Commission (endorses) OR (does not endorse) the JLARC recommendation(s) for this review, (subject to the following additional comments.) OR (without appending additional comments.)”

GROUP E
Allow to Expire – endorse without comment

1. *There is one tax preference reviews in Group E with proposed Commission comments:*

Tax Preference	Comment
1. Renewable energy machinery (p. 195)	No Proposed Commission Comment

2. *We will now take action on the preference in Group E.*

3. *Is there any discussion on each of the above preferences: [proceed with the first item above]?*

4. *Is there a motion for the Commission to take action on these reviews?*

5. *Potential motion language:*

“The Commission acknowledges receipt of the 2011 JLARC Tax Preference Review of [preferences being discussed]. The Commission has provided a forum for discussion and public comment on these reviews. The Commission (endorses) OR (does not endorse) the JLARC recommendation(s) for this review, (subject to the following additional comments.) OR (without appending additional comments.)”

GROUP F

Allow to Expire – do not endorse and consider whether to provide a comment

5. There is one tax preference reviews in Group F with proposed Commission comments:

	Tax Preference	Comment
1.	Hog fuel to produce energy (p. 69)	<p><u>Audit Staff recommendation:</u> Because the Legislature intended the exemptions to be temporary and did not provide performance goals to guide any other assessment of performance, the Legislature should allow the sales and use tax exemptions for hog fuel to expire.</p> <p>William Longbrake:</p> <p><u>Possible comment:</u> The Commission does not endorse the recommendation that the Legislature should allow the sales and use tax exemptions for hog fuel to expire because it is unclear that the Legislature intended the exemptions in this preference to be temporary. The Commission recommends that the Legislature review available evidence before determining whether to let the preference expire. Further, if the Legislature determines to extend the preference, the Commission recommends that performance goals (public policy objectives) be specified and reporting be required to enable subsequent assessment of the benefits and costs of the preference.</p> <p><u>Rationale for comment:</u> Although the Legislature did not specify a public policy objective for this preference, public testimony provided to the Commission argued that the public purpose was summarized in testimony on SB 5442, which was a precursor to SB 6170, which included the hog fuel tax preference: <i>“The forestry industry is facing an economic crisis, and this bill will help preserve jobs, promote healthy forest, and ensure CO2-neutral energy by encouraging the use of woody biomass. The forestry industry in eastern and western Washington is distressed, which is stressing rural local governments and social programs. This bill will help preserve the forestry industry and thereby rural economies.”</i></p> <p>As the JLARC study points out part of the rationale for the hog fuel tax preference may have been because hog fuel was less competitive during a time of declining oil prices. Because the price of oil since enactment has risen, presumably the economic disadvantage no longer exists. However, public testimony provided to the Commission asserted that the more relevant alternative fuel price is natural gas rather than oil and, further, because of significant structural changes in the market for natural gas the price of natural gas has declined significantly since the hog fuel preference was enacted. Public testimony also pointed out that since hog fuel must be transported, diesel fuel costs, which are subject to tax, have risen along with oil prices, and this has exacerbated hog fuel’s price competitiveness relative to natural gas.</p>

		Public testimony suggested that the Legislature extend the hog fuel tax preference for two years subject to collection of sufficient data to evaluate the public policy merits of this preference.
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6. *We will now take action on the preference in Group F.*

7. *Is there any discussion on each of the above preferences: [proceed with the first item above]?*

8. *Is there a motion for the Commission to take action on these reviews?*

6. *Potential motion language:*

“The Commission acknowledges receipt of the 2011 JLARC Tax Preference Review of [preferences being discussed]. The Commission has provided a forum for discussion and public comment on these reviews. The Commission (endorses) OR (does not endorse) the JLARC recommendation(s) for this review, (subject to the following additional comments.) OR (without appending additional comments.)”

GROUP G
Terminate – endorse without comment

9. *There is one tax preference reviews in Group G with no proposed Commission comments:*

Tax Preference	Comment
1. Repaired goods delivered out-of-state (p. 209)	No Proposed Commission Comment

10. *We will now take action on the preference in Group G.*

11. *Is there any discussion on each of the above preferences: [proceed with the first item above]?*

12. *Is there a motion for the Commission to take action on these reviews?*

7. *Potential motion language:*

“The Commission acknowledges receipt of the 2011 JLARC Tax Preference Review of [preferences being discussed]. The Commission has provided a forum for discussion and public comment on these reviews. The Commission (endorses) OR (does not endorse) the JLARC recommendation(s) for this review, (subject to the following additional comments.) OR (without appending additional comments.)”

William Longbrake:

Possible general comment pertaining to use of the term “expiration” in legislation:

The Legislature frequently specifies an expiration date when it enacts a tax preference statute. JLARC staff and the Citizens Commission for Performance Measurement of Tax Preferences (Commission) have had difficulty in discerning the Legislature’s intent for some preferences. An expiration date could simply mean that the Legislature intends to review experience with the preference before determining whether to extend it. Or, the Legislature can intend the preference to be temporary in response to short-term economic or industry conditions with the expectation that the preference will not be extended. Absence of explicit legislative guidance on the intended meaning of “expiration date” lead JLARC staff to conclude that the Hog Fuel to Produce Energy preference should be allowed to expire because the Legislature intended the exemptions to be temporary. This interpretation was disputed in public testimony provided to the Commission. Accordingly, the Commission recommends that the Legislature either clarify directly in a tax preference statute the intent of an expiration date or provide commentary in the legislative record that clarifies the intent of an expiration date.