September 19, 2014

William A. Longbrake, Chairman
Washington State Citizen Commission for Performance Measurement of Tax Preferences
1300 Quince Street SE
P.O. Box 40910
Olympia, WA 98504-0910

Dear Chairman Longbrake,

This letter is submitted in support of the B&O Tax preferential rate for International Investment Management Services (IIMS).

As requested by the Commissioners, the comments below will focus on the four questions you have asked all stakeholders to address when presenting written or oral testimony.

The questions and responses are as follows:

Question 1: Is there evidence that the tax preference achieved its purpose, as noted in the 2014 tax preference reports? *Please provide any relevant evidence.*

Response: JLARC staff inferred two public policy objectives for the tax preference as follows:

I. To reduce a perceived competitive disadvantage for IIMS business located in Washington,
II. To attract new international trade and finance business to the state, and
III. To retain international trade and finance businesses in the state.

In their report, JLARC quotes the prime sponsor of the original legislation (who stated that the intent was to "...retain the people in this state..." to also infer a public policy objective of retaining jobs in Washington state.

We believe the tax preference has achieved each of the objectives above and is still necessary to maintain these objectives. We will first address the perceived competitive disadvantage issue and then address the impacts on existing businesses and attraction of new businesses.

I. *Competitive Disadvantage*

JLARC staff have stated in their report that adoption of an economic nexus and apportionment standard has reduced the competitive disadvantage for IIMS businesses located in-state compared to out-of-state. We believe this is incorrect for the following 3 reasons:

- ***Issue A: Most states are moving to an economic nexus standard and revised apportionment standards.*** Over 30 states have adopted economic nexus and 20 states have moved to single sales apportionment. Washington's adoption of economic nexus and an apportionment standard is in line with other states and does not reduce the competitive disadvantage of the B&O tax.

- ***Issue B: JLARC improperly assumes that an in-state IIMS business pays the same amount of B&O tax as an out-of-state business.*** This assumption is not correct as B&O tax is not only imposed on sales to third parties (clients) but also on intercompany service transactions.
- If a company operates through multiple subsidiaries (which is often the case in the highly-regulated financial services sector), and these subsidiaries are all located in Washington, an in-state company will pay a significant amount of B&O tax on these intercompany service transactions.
- Therefore, in-state and out-of-state IIMS businesses could generate the same amount of revenue from Washington clients, but the in-state IIMS business could pay significantly higher B&O tax based on the level of its intercompany service transactions.

- ***Issue C: JLARC did not compare the actual amount of B&O tax burden for a Washington-headquartered company vs. what the company would pay if headquartered somewhere else.*** Many states with a tax on net income are moving to a single sales apportionment. This fact, combined with a business model that often has high revenue and low margins, often results in a significantly lower tax burden for a company headquartered in one of those states compared to the B&O tax the same company would pay if headquartered in Washington, even with the lower IIMS rate.

II. *Retention of Existing International Trade and Finance Businesses in Washington*

We believe this preference has achieved its policy objective of retaining jobs in Washington state. A prime example that this public policy is being met is the preservation and expansion of quality jobs at Russell Investments, who was stated as a primary target by the Legislature in policy discussions in 2005. Russell's Washington headcount during this time period has increased by approximately 20% as shown by the chart below.

	12/31/1995	8/12/2014	% Increase
Russell's Washington Employees	796	952	19.60%

III. *Attraction of New International Trade and Finance Businesses to Washington*

Finally, we believe the growth in the number of firms claiming the preference is direct evidence that the policy objective of attracting new international trade and finance business to the state has been met. JLARC staff states in its report that the number of businesses claiming the preference increased from six firms in 1995 to 97 firms in 2012. The graph at Exhibit 75, a copy of which is attached, then attempts to dismiss the majority of the growth as being attributable to out of state businesses who may now be reporting in Washington due to the new economic nexus standard. JLARC staff have inserted a line on January 1, 2009 which is a full 1 year and 5 months prior to the June 1, 2010 date that out of state businesses were subject to tax under the new economic nexus standard. Therefore, any increase between January 1, 2009 and June 1, 2010 cannot be attributable to out of state businesses. If the line is inserted on June 1, 2010 (the effective date of the economic nexus legislation), one can see that the majority of the growth occurred prior to this date. For your reference, we have added a revised chart with the line properly reflected on the June 1, 2010 effective date.

JLARC also dismisses the growth as being partially attributable to businesses erroneously filing under the preferential rate. The Department of Revenue has stated there were approximately 70 taxpayers that were either under audit or being held for audit for this issue. Even if 100% of these taxpayers were found to be erroneously filing, the number of firms properly claiming the preferential rate has grown from 1995. This is direct evidence that the policy objective of attracting new international trade and finance business to the state has been met.

Question 2: Does the preference provide benefits in addition to those stated in its intended or implied purpose?

Response: The IIMS tax preference has been a strong component in the recent work to build a thriving cluster of financial companies in Washington State. In cooperation with many civic and economic development organizations, universities, and various Washington state agencies, the Financial Services Cluster Initiative aims to seek and recruit financial firms who view Washington as a place to domicile their financial businesses.

The current financial services cluster of companies includes banks, insurance, asset management, private equity, venture capital, public sector finance agencies, and other financial-in-nature companies. This cluster provides an enormous contribution to the Washington State economy. The Washington Financial Services Cluster is composed of 8,500 firms that provided 116,000 jobs and generated $28 billion in revenues in 2009-10. Cluster activity supported nearly 360,000 jobs and created $62 billion in revenues throughout the state economy.

The financial services cluster also supports direct investment in Washington's innovation economy. Strategic global funding partners, robust middle-market financing enterprises and a burgeoning venture capital community serve as the investment infrastructure that supports all stages of growth in leading industry clusters such as software, aerospace, and global health. And the impacts of Washington's financial services cluster span the globe: local asset management firms managed over $380 billion in national and international assets in 2010

Washington State has a unique set of attractive components that would make many financial companies take notice and consider this state as a potential new home, including:

1) A highly educated work force of financial professionals who have years of strong experience.
2) A strong state regulator that balances financial safety and soundness with a desire for growth and economic development.
3) Educational partners at the university level who will work to develop curriculum to support the industry and prepare students for the workplace.
4) Geographical location in the northwest that positions us closer to the fast-growing Asian markets.
5) Tax support. The International Investment Management preference is a key support mechanism to incentivize growth in this sector.

The Financial Services Cluster Initiative is an effort that has been established over the last several years to ensure the continued success of this sector and fully realize the potential of this emerging industry cluster for our region. The Greater Seattle Financial Services Collaborative is a partnership between the leading financial services firms in the Seattle Metropolitan region with the goal of growing the industry. It is a program that is also supported by the Economic Development Commission of Seattle and King County in partnership with the Metropolitan Seattle Chamber of Commerce and others.

***Question 3*:** Does the economic activity stimulated by this tax preference exceed the loss of revenue to the state?

Response: We believe that this question was not fully addressed or considered within the JLARC analysis. While Russell is not able to specifically examine the sector's overall economic activity that is spurred by this tax preference, we are able to consider the impact that Russell Investments has on the state's economy, which includes nearly 1,000 employees in Seattle, over $150 million in total payroll, and more than $2 million in philanthropic giving. Furthermore, the Economic & Revenue Forecast Council estimates that, for every dollar that Russell spends, three dollars are created in local economic activity. Russell Investments is a significant contributor to Washington's economy and stimulates valuable economic activities within the state.

Question 4: Does this preference have negative consequences? For example, were other industries, workers, or the environment harmed by activities stimulated by this tax preference?

Response: This preference does not have any negative consequences. Other industries, workers, and the environment were not harmed by activities stimulated by this tax preference. Furthermore, as we have mentioned this preference attempts to balance the inherent inequities in Washington's B&O tax structure, which taxes businesses on their gross receipts. Variations in rates are a necessary component of a gross receipts tax system in order for Washington to be competitive with other states.

In closing, we sincerely appreciate and respect the time that this committee's audit staff have given to review the performance of the complicated tax preferences in Washington's tax code. With that in mind, we urge the Commission to consider all of the data and information available when making tax policy recommendations which will have a significant impact on the competitiveness of Washington's businesses. We thank you for your consideration of our concerns.

Sincerely,

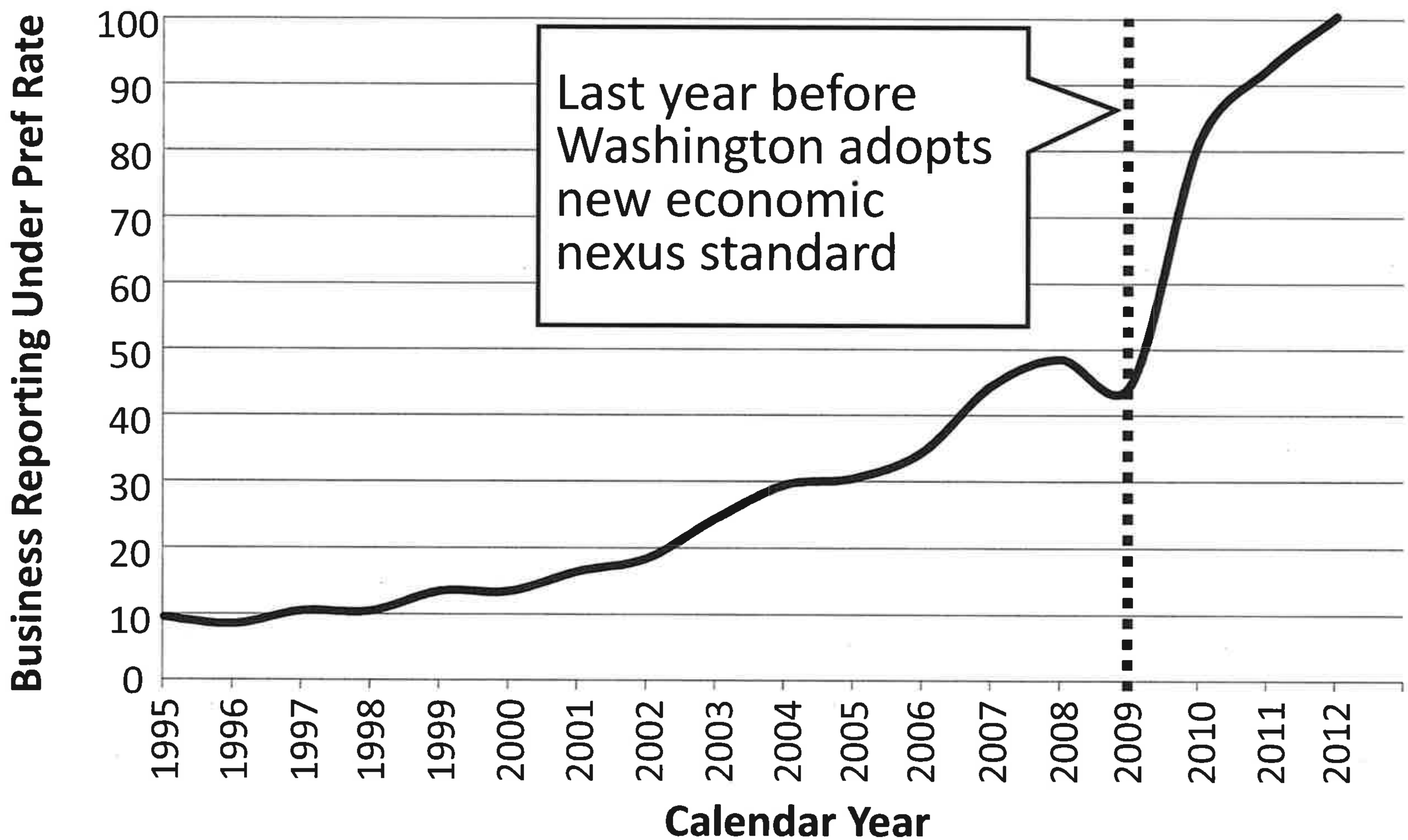
Leanne Webber

Global Tax Director, Russell Investments

Cc Members of the Washington State Citizen Commission for Performance Measurement of Tax Preferences
Mr. Keenan Konopaski; Legislative Auditor, Joint Legislative Audit & Review Committee

Increased Firms Using Preference Include Out-of-State and Non-Qualifying Firms

International Investment Mgmt Services



Source: Department of Revenue detailed tax data by industry and tax line classification, calendar years 1995-2012.

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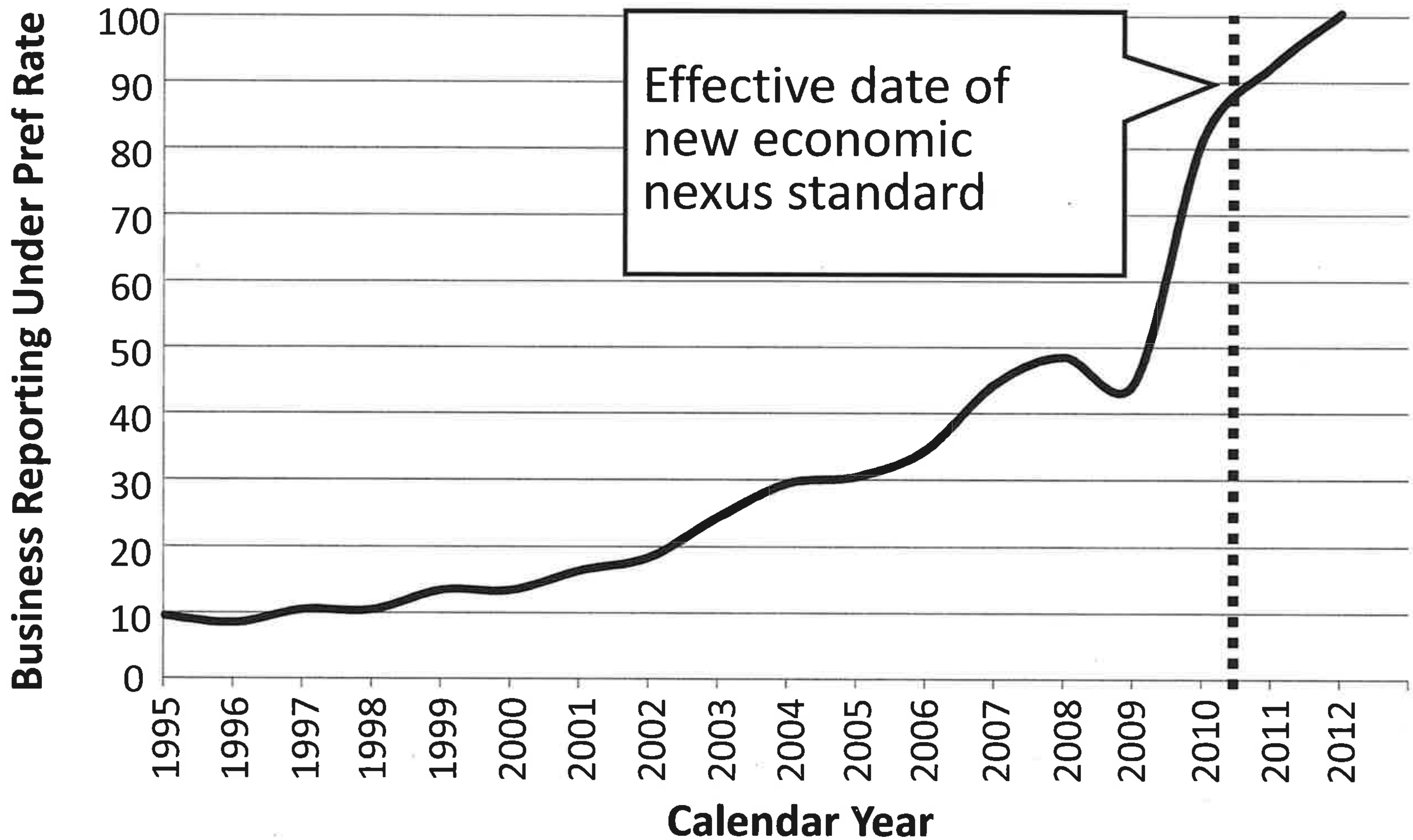

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