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ASSOCIATION

September 8, 2016

Dr. Grant Forsyth
Chair
Citizens Commission for Performance Measurement of Tax Preferences
1300 Quince St. S.E.
Olympia, WA 98504-0910

Dear Mr. Forsyth:

Thank you for the opportunity to provide written testimony regarding the tax preference that exempts flavor-imparting items from sales and use tax. (Sales and Use RCW's 82.08.210 and 82.12.210.)

The Washington Restaurant Association (WRA) represents over 6,000 restaurants in the State of Washington. Our membership includes both full service and quick service restaurants, and 84% of industry are considered small businesses, employing fewer than 20 people. Restaurants in Washington have average sales of just over \$800,000 annually.

In 2013 the WRA approached the Legislature and requested they enact legislation that would make it clear flavor imparting items used in the cooking process were not subject to sales tax, as those items were integral to the final meals provided to customers. Prior to the passage of this legislation, the taxation of flavor imparting items was not clear in statute, and that ambiguity was leading to disagreements between our industry and the Department of Revenue. (DOR) The WRA worked closely with the DOR to draft this legislation to ensure the Legislature clearly expressed legislative intent regarding the taxation of flavor imparting items. Ultimately lawmakers agreed to provide this clarity.

Please see below specific answers to questions posed by the Commission:

Is there evidence that the tax preference achieved its purpose, as noted in the 2016 tax preferences reports?

Indeed the provision of clarity by the Legislature in this matter did forestall all litigation between restaurants and the Department of Revenue.

Many establishments never imagined that flavor imparting items would be taxed, as they considered the use of these items integral to the cooking process – similar to the use of spices. Those restaurants that were aware of the DOR's position at audit were bewildered by a finding these items would be taxed, and that resulted in the disagreements in 2012. The JLARC report refers to the under reporting of data for this preference, which is not surprising given most of our members are small and never appreciated these items may have been taxable in the first place. We are hopeful lawmakers will make permanent this tax treatment, and given the very low fiscal impact, will remove the requirement to file Buyer Addendums.

The WRA's mission is to help our members succeed.

Does the preference provide benefits in addition to those stated in its intended or inferred purpose?

This tax preference has been beneficial to restaurants of all sizes. Restaurants in Washington State have some of the lowest margins in the nation, averaging around 4.5%. As a result our member employ three fewer employees per establishment than peer restaurants in other states. Restaurants -- particularly smaller establishments -- face increasing expense pressures from minimum wage, labor costs, food costs, and energy costs. This tax treatment helps to keep at least one cost down for restaurants that use flavor imparting items.

Do taxes associated with any increased economic activity stimulated by this tax preference exceed the preference's loss of tax revenue?

No research has been done to answer this question definitively. Anecdotally, we have heard from a number of establishments of all sizes -- from steak houses to pizza parlors -- that this clarification by the legislature has helped them to keep costs down for the specialty items they sell. The lower cost basis for these restaurateurs enables them to offer their products at a reasonable and attractive cost to their customers.

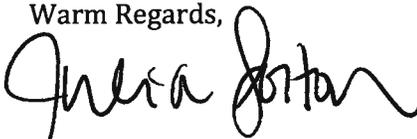
Does this preference have negative consequences? For example, were other industries, workers, or the environment harmed by activities stimulated by this tax preference?

Again, this legislation was sought so the Legislature could provide public policy clarity and avoid costly litigation between WRA members and the State. We know of no negative or untended consequences from this legislation.

Thank you again for the opportunity to provide input to you and to the Commission. We also very much appreciate the process undertaken by the JLARC staff in regard to this tax preference.

Regrettably, our subject matter experts on this matter will not be in town for the hearing on September 8, 2016. If you, your fellow Commission members, or your staff has any questions; please feel free to call me directly at 360-956-7279.

Warm Regards,



Julia Gorton
Senior Manager, State Government Affairs
Washington Restaurant Association

cc. Keenan Konopaski, Legislative Auditor