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Not just a corporate tax "break"

A bill exempting machinery and equipment used in manufacturing from the sales and use tax cleared the House Finance Committee February 21, moving a step closer to becoming law. The current version of the measure (Second Substitute House Bill 1024) differs from the bill which passed the House Trade and Economic Development Committee in several respects: the requirement that businesses invest $750,000 per job to receive the distressed area tax deferral is retained for community empowerment zones; the exemption applies to the local sales tax, with the state reimbursing local governments when the revenue loss is greater than 5 percent of local sales tax collections; and potato packing operations are added to the list of projects eligible for the exemption.

Some critics call the exemption a tax break for big business. More accurately, it's an attempt to level the playing field for Washington manufacturers by removing a competitive disadvantage. The exemption would have tangible benefits for the state, ultimately resulting in more jobs, more revenue for state and local government, and increased activity throughout the economy.

We've mentioned before that state government would break even within four to nine years; that is, by then the increased investment resulting from the exemption will generate enough new tax dollars to replace the revenue loss (currently estimated to be about $146 million in the coming biennium). According to AUS Consultants' analysis of a more expansive exemption program, local governments enjoy a positive return in about the same time frame.

Because of concerns expressed by several local governments, the bill passed out of Trade and Economic Development would have exempted only the state's portion of the retail sales and use tax on new and replacement machinery and equipment, and the labor and services involved in installation. After negotiation with local officials, bill proponents agreed to the compromise which provides for state reimbursement if losses exceed 5 percent of local revenues. Relatively few governments are likely to be affected, and the projected cost of the reimbursement is about $2 million, which would be appropriated directly.

All sectors of the state economy are expected to benefit dramatically from the exemption. AUS projects additional gross sales of $28.3 billion in the non-manufacturing sectors of the economy between 1996 and 2005, with the primary gains coming in business services, wholesale and retail trade, finance, real estate and insurance. Of the 81,000 new jobs AUS estimates will be created by 2005, almost 60 percent would be in non-manufacturing firms.

While expected to pass the House, the measure may face obstacles in the Senate. Predictably, some members question whether the state can afford to cut taxes. Others prefer to back different tax relief proposals (property tax reductions or B&O rollbacks are most frequently cited).

With the 601 limit, a $500 million reserve and conservative spending, affordability should not be a problem. The exemption pays for itself, and the state cannot afford to remain uncompetitive in pursuit of manufacturing investments. Property tax relief is politically popular, but the proposals advanced so far do little for homeowners. Our property tax burden is below the national average. While there are too many instances of dramatic assessment increases and inequities, general relief measures are expensive, provide negligible economic stimulus, and fail to address imbalances within the state. Finally, B&O tax relief should not be pitted against the machinery and equipment exemption. With expenditure restraint, both can be granted without damaging essential state programs.