

Cite as Det. No. 00-075, 20 WTD 362 (2001)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Correction of)	<u>D E T E R M I N A T I O N</u>
Assessment of)	
)	No. 00-075
...)	Registration No. . . .
)	FY. . . /Audit No. . . .

RCW 82.63.005, RCW 82.63.010: B&O TAX--TAX DEFERRAL FOR QUALIFIED HIGH-TECHNOLOGY RESEARCH AND DEVELOPMENT FACILITIES -- The growing, monitoring, and assessment of genetically altered plants are research and development activities that qualify the costs of the facility for the high technology business tax deferral.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

NATURE OF ACTION:

Taxpayer protests the denial of a high technology tax deferral.¹

FACTS:

Lewis, A.L.J. – Taxpayer is a port authority. Taxpayer manages an airport and encourages business growth. Consistent with fostering business growth, Taxpayer constructed a building to lease to . . . (“Tenant”) for use as a biological plant product development and testing laboratory. The building is located on port property next to a . . . research and development farm. Taxpayer applied for and was issued a tax deferral under the provisions of RCW 82.63 (“Tax Deferrals For High Technology Businesses”) to construct a building.²

The Department of Revenue (“Department”) audited Taxpayer’s purchases made under the tax deferral for the period October 1, 1997 through September 30, 1998.³ On January 29, 1999, the Department issued a \$. . . assessment. The tax assessment resulted from the Audit Division’s assessment of use tax on purchases made under the tax deferral. The Audit Division disallowed the deferral reasoning that Tenant’s primary activity at the . . . research and development facility was testing, a nonqualified activity.

¹ Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

² Under the provisions RCW 82.63, no repayment of the deferred taxes is required if the building is used for qualified research.

³ Tax Deferral No. . . .

Taxpayer's disagreed and filed a petition for correction of the assessment on February 22, 1999. Taxpayer's maintained in both its petition and during a teleconference that the tax deferral was disallowed in error because Tenant performed qualified activities.

Taxpayer explained the its Tenant is a major multinational corporation involved deeply in chemical, biological, and genetic research. Tenant has a substantial commitment to developing genetically altered plants that will allow for less expensive growing and increased yield. Examples provided included genetically altered plants. Examples of such genetically altered plants would include a herbicide resistant plant that would allow the grower to spray a field with a herbicide to kill weeds and grass, but not harm the crop and a genetically altered cotton or corn plant that would be poisonous to the insects that feed on them.⁴

During the teleconference, Tenant explained that production of such genetically engineered plants is a multi-step process.

Step 1. The first step is to examine an existing plant, analyze its characteristics and determine what characteristics would be added or altered.

Step 2. The second step is for the scientists to map the genetic make up of the plant.

Step 3. The third step is to determine what part of the plant's genetic structure needs to be added or altered produce the desired result.

Step 4. The fourth step is to make that alteration to the seed.

Step 5. The fifth step is to grow and monitor the seed's growth to mature plant to determine how the genetic alteration has changed the plant's characteristics.

Step 6. The sixth step, may be and frequently is, to make another alteration to the seed in an attempt to achieve the result that was not produced by the first alteration.

⁴ An article in The Seattle Times (April 6, 2000, Page A6) entitled "Better oversight of gene-modified crops suggested" stated in part:

The long awaited, 260-page report, which focused on crops engineered to protect themselves from pests or herbicides, was immediately seized upon by both advocates and opponents of engineered crops to support their position that either the crops are safe and benefit the environment or that they are potentially unsafe And may pose a hazard.

Scientists have begun splicing a variety of genes into crops, including genes that enable crops to produce their own pesticides. The engineered crops have become increasingly popular among U.S. farmers because they reduce the need to use chemicals.

But the crops have also become increasingly controversial, especially in Europe. Opponents fear that crops that produce their own pesticides might cause insects to become more resistant, causing the need for more or stronger chemicals in the future. One recent study also suggested such crops could kill Monarch butterflies.

Step 7. The seventh step, once a “prototype” plant has been grown that contains the desired characteristics, to have a farmer grow a “limited” amount of the seed to determine how consistent the altered seed grows in a large plot.

Step 8. The eighth step, following the growing of a successful “test” crop, is to produce the seed for sale to the public.

Tenant’s facility in . . . is staffed by two (2) scientists with Ph.Ds whose job it is to determine what changes in a plant must be made; what genes to alter; and then monitor the altered seeds growth to determine how successful the alteration of the seed has been in producing a plant with changed characteristics. Thus, Tenant performs many of the above enumerated steps at the . . . research facility.

ISSUE:

Whether the growing, monitoring, and assessment of genetically altered plants is an activity qualifying for the high technology business deferral?^[5]

DISCUSSION:

The legislature, in an effort to encourage high technology business location in Washington, provided a tax deferral program for qualified high-technology research and development facilities. RCW 82.63.005. The benefits of the deferral program are only available to those that meet the requirements of the program.

RCW 82.63.010(14) defines “Qualified research and development” to mean:

. . . research and development performed within this state in the fields of advanced computing, advanced materials, biotechnology, electronic device technology, and environmental technology.

RCW 82.63.010(4) defines “Biotechnology” to mean:

. . . the application of technologies, such as recombinant DNA techniques, biochemistry, molecular and cellular biology, genetics and genetic engineering, cell fusion techniques, and new bioprocesses, using living organisms, or parts of organisms, to produce or modify products, to improve plants or animals, to develop microorganisms for specific uses, to identify targets for small molecule pharmaceutical development, or to transform biological systems into useful processes and products or to develop microorganisms for specific uses.

⁵ [The facts presented at this hearing by the Department and the Taxpayer and the analysis of this determination relate only to a facility for the development of genetically altered plants. Other activities which do not qualify for the R&D credit, if undertaken by a taxpayer at the same facility, would affect both the analysis and the result.]

The Audit Division denied the tax deferral maintaining that the activity conducted at the [facility] was “primarily testing products for market.” “Market research or testing” is specifically excluded from the definition of “Research and development” contained in RCW 82.63.010(16), which states:

“Research and Development” does . . . not include adaptation or duplication of existing products where the products are not substantially improved by application of the technology, nor does the term include surveys and studies, social science and humanities research, market research or testing, quality control, sale promotion and service, computer software developed for internal use, and research in areas such as improved style, taste, and seasonal design.

(Emphasis added.)

Webster’s Third International Dictionary 1383 (1993) defines “marketing research” as “the gathering of factual information as to consumer preferences for goods and services.” Neither the Audit Division nor Taxpayer have presented any information that indicates that Tenant’s activities at the . . . research facility have even the remotest connection to gathering information about consumer preferences. Rather, Tenant’s activities relate to the development of new products, i.e., genetically engineered plants.

The complexities of genetic engineering, whether plant or animal, are at best difficult for the lay person to comprehend. However, we find that Taxpayer’s step-by-step explanation of the activities necessary to bring a genetically-altered seed to market very helpful, as well as, an analogy with animal genetic engineering to be helpful in understanding the activities Taxpayer’s tenant performs.

If Taxpayer were altering the genes of a small animal, such as a rabbit or a dog, arguably we would not have the confusion presented by an outside growing plot. Tenant genetically alters seeds and grows them outdoors, just as a genetically altered animal would be raised in cages inside a laboratory facility. Accordingly, we should not be confused that the growing field is anything more than an outside laboratory.

If the scientist were attempting to develop a larger rabbit or flea resistant dog, the animal would be bred and its growth monitored. The animal would be tested to determine whether the genetic alteration had been successful. If less than full success was obtained, the experiment would be repeated using a different combination of altered genes. Once the desired result was achieved in the laboratory, more animals would be bred to verify the consistency of the results. Finally, after the scientists were satisfied that they had produced a successful genetic alteration and that the desired results were consistent on replication the product would be brought to market.

From the facts presented, we are satisfied that the activities performed at the . . . location by Taxpayer's tenant are research and development activities that qualify for the tax deferral allowed high technology businesses.⁶ Accordingly, we grant the Taxpayer's request for relief.

DECISION AND DISPOSITION:

The Taxpayer's petition is granted. The matter will be remanded to the Audit Division for an adjustment consistent with this decision.

Dated this 28th day of April, 2000.

⁶ In coming to this conclusion we take special note that some of the activities Tenant performs are appropriately called testing. Testing that is an integral part of a scientific inquiry process. However, none of the testing is in any way related to marketing and determining consumer preferences and needs.