
**Community & Economic
Development & Trade Committee**

HB 1171

Brief Description: Providing a business and occupation tax exemption for qualifying small businesses.

Sponsors: Representatives Eickmeyer, Newhouse, Grant, Priest, Chase, Kretz, Hunt, Hasegawa, Kenney, Hurst, Orcutt, Hudgins, Simpson, Sump, Appleton, Ormsby, McDonald, P. Sullivan, Condotta, Kristiansen, Linville, Ross, Haler, Wallace, Springer, Kelley, VanDeWege, Rolfes, Ericks, Haigh and Green.

Brief Summary of Bill

- Exempts qualifying small businesses from the Business and Occupations tax.

Hearing Date: 1/24/07

Staff: Tracey Taylor (786-7196).

Background:

All businesses must register with the Department of Revenue (DOR) if the business is required to collect sales tax or the business is required to pay any other taxes or fees to the DOR. However, if the business has a gross income of less than \$12,000 per year under both the business and occupation (B&O) tax and the public utilities tax and the business is not otherwise required to collect or pay any tax to the DOR, the business is not required to register with the DOR. In addition, businesses that have products, gross proceeds of sales or gross business income of less than \$28,000 are not required to file a return with the DOR.

Washington's B&O tax is the second largest tax source for the state. In Fiscal Year 2006, B&O tax collection totaled \$2.477 billion in gross receipts. Almost all businesses located or doing business in the state of Washington are subject to the state B&O tax, including corporations, partnerships, sole proprietors and nonprofit organizations.

Washington's B&O tax is calculated on gross income from business activities in the state.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

There are no deductions from the B&O tax for labor, materials, taxes or other costs of doing business. However, some businesses may qualify for certain exemptions, deductions or credits. An exempted activity is not subject to the B&O tax and is not reported on the Combined Excise Tax Return (CETR). Exempted activities include raising and selling plantation Christmas trees at wholesale; sales for fund-raising of certain nonprofit organizations; international banking facilities; and growing, raising or producing agricultural products.

Unlike exemptions, deductions must first be reported on a business' CETR as part of the business' gross income, then taken as a deduction. Allowable deductions include bad debts; freight and delivery costs incurred by a Washington manufacturer for out-of-state shipments; and sales made in Washington by an out-of-state seller without activities in Washington that establish, maintain, or facilitate a market for its products or services.

Credits are amounts that have been paid to the DOR which are either not due or are granted by the Legislature for a specific purpose. Credits are subtracted from the B&O tax due on the CETR and include the multiple activities tax credit; the high technology B&O tax credit and the small business B&O tax credit.

Business and occupation tax rates and classifications vary according to the type of business activity. The major B&O tax classifications are retailing, wholesaling, manufacturing and service and other activities.

Summary of Bill:

Qualifying small businesses are exempt from the B&O tax. If a business has products valued, gross proceeds of sales or a gross income of less than \$200,000 during a base period, the business is exempt from paying B&O tax. Also exempt from the B&O tax is a business whose B&O taxes due and paid exceed the net income reported on the business's federal income tax return for the base period. In this case, a sole proprietor may subtract the amount of self-employment tax shown on schedule 1040 SE from the net income reported on schedule C of the federal income tax return. A business that purchases or otherwise acquires, directly or indirectly, and not in the ordinary course of business the bulk of the tangible and intangible assets of another taxpayer or is the surviving corporation of a statutory merger is not eligible for this B&O tax exemption.

The business selects the base period which is a 12-month period covered by a single federal income tax return during which the business operated during the entire 12-month period.

The exemption may be taken based on how the business files its tax returns: if the business is a monthly tax filer, the exemption may be taken on 12 monthly tax returns, or if a business is a quarterly tax filer, the exemption may be taken on four quarterly returns. However, once the business claims the exemption on a tax return, it may not later change the claim to a different tax return.

If a business is a monthly or quarterly filer, the base period must end no earlier than six months before the period covered by the first return on which the business qualifies for this exemption. A monthly or quarterly filer may not claim the exemption for any tax period starting more than 24 months after the base period. Annual filers must claim the exemption on one of the two annual tax returns due following the last month of the base period.

A business claiming an exemption it is not entitled to is engaging in fraud or the misrepresentation of a material fact and is subject to interest and penalties as prescribed the law.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill takes effect 90 days after adjournment of session in which bill is passed.