HOUSE BILL REPORT
ESHB 2081

As Passed Legislature

Title: An act relating to funding public schools, including higher education, health care, social services, and other programs and services to benefit Washingtonians by modifying business and occupation tax surcharges, rates, and the advanced computing surcharge cap, clarifying the business and occupation tax deduction for certain investments, and creating a temporary business and occupation tax surcharge on large companies with annual revenues with more than $250,000,000.

Brief Description: Modifying business and occupation tax surcharges, rates, and the advanced computing surcharge cap, clarifying the business and occupation tax deduction for certain investments, and creating a temporary business and occupation tax surcharge on large companies.

Sponsors: House Committee on Finance (originally sponsored by Representatives Fitzgibbon, Peterson, Pollet, Parshley, Scott, Reed, Berry and Macri).

Brief History:

Committee Activity:

Finance: 4/18/25, 4/19/25 [DPS].

Floor Activity:

Passed House: 4/22/25, 50-48.
Passed Senate: 4/26/25, 26-22.
Passed Legislature.

Brief Summary of Engrossed Substitute Bill

- Increases the business and occupation (B&O) tax rate for manufacturing, retailing, and wholesaling to 0.5 percent beginning January 1, 2027.
- Increases the B&O tax rate for multiple rate categories beginning January 1, 2027.
- Increases the B&O tax rate for services and other activities for businesses with gross receipts over $1 million beginning October 1,

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2025.

- Imposes a 0.5 percent B&O tax surcharge on taxpayers with Washington taxable income over $250 million from January 1, 2026, through December 30, 2029.
- Increase the B&O surcharge on financial institutions to 1.5 percent beginning October 1, 2025.
- Increases the B&O advanced computing surcharge to 7.5 percent and increases the annual cap to $75 million beginning January 1, 2026.
- Clarifies the B&O tax deduction for investment income.

HOUSE COMMITTEE ON FINANCE

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 9 members: Representatives Berg, Chair; Street, Vice Chair; Mena, Parshley, Ramel, Santos, Scott, Springer and Wylie.

Minority Report: Do not pass. Signed by 6 members: Representatives Orcutt, Ranking Minority Member; Jacobsen, Assistant Ranking Minority Member; Abell, Chase, Penner and Walen.

Staff: Tracey Taylor (786-7152).

Background:

Business and Occupation Tax.
Washington's major business tax is the business and occupation (B&O) tax. The B&O tax is imposed on the gross receipts of business activities conducted within the state, without any deduction for the costs of doing business. Businesses must pay the B&O tax even though they may not have any profits or may be operating at a loss.

A taxpayer may have more than one B&O tax rate, depending on the types of activities conducted. Major B&O tax rates are 0.471 percent for retailing; 0.484 percent for manufacturing and wholesaling; and 1.5 percent (businesses with taxable income of less than $1 million) or 1.75 percent (businesses with taxable income of $1 million or more) for services and for activities not classified elsewhere. There are many specialized B&O tax rates and preferential rates that apply to specific business activities.

In addition, a taxpayer may be eligible to utilize other tax preferences, including credits and deductions, to reduce their tax liability. For example, a taxpayer engaging in activities subject to different B&O tax rates may be eligible for a Multiple Activities Tax Credit. A taxpayer may also be eligible for a small business credit that will either eliminate or reduce

their B&O tax liability. The credit is $160 per month for taxpayers that report at least 50 percent or greater of their total B&O taxable amount under service and other activities, real estate brokers, and contests of chance and $55 per month for all other businesses, multiplied by the number of months in the reporting period. The amount of the credit available phases out based on the business's gross receipts.

A business does not have to file an annual B&O tax return if the business does not owe other taxes or fees to the Department of Revenue (DOR) and has annual gross proceeds of sales, gross income, or value of products for all B&O tax classifications of less than $125,000 per year.

Additional Business and Occupation Tax on Financial Institutions.
An additional B&O tax is imposed on specified financial institutions. The additional tax is equal to the taxpayer's gross taxable service and other income multiplied by 1.2 percent.

A specified financial institution is a financial institution that is a member of a consolidated financial institution group that reported on its consolidated financial statement for the previous calendar year annual net income of at least $1 billion, not including net income attributable to noncontrolling interests, as the terms "net income" and "noncontrolling interest" are used in the consolidated financial statement. If financial institutions are no longer required to file consolidated financial statements, "specified financial institution" means any person that was subject to the additional tax in at least two of the previous four calendar years.

The DOR may require a taxpayer believed to be a specified financial institution to disclose whether it is a member of a consolidated financial institution group and, if so, to identify all other members of its consolidated financial institution group. A person failing to comply with this requirement is deemed to have intended to evade tax payable under this section and is subject to a penalty on any additional tax due from the taxpayer and any financial institution affiliated with the taxpayer.

Advanced Computing Business and Occupation Tax Surcharge.
In addition to the applicable business and occupation tax rate, advanced computing businesses with a worldwide gross revenue in excess of $25 billion are subject to an additional 1.22 percent advanced computing surcharge (ACS). An advanced computing business is one that designs or develops software or computer hardware, including modifications, or provides cloud computing services, operates an online marketplace, an online search engine, or an online social networking platform. The total ACS an advanced computing business is subject to is capped at $9 million per year. The proceeds from the ACS are deposited into the Workforce Education Investment Account.

Business and Occupation Deduction for Investment Income.
In computing their B&O tax liability, a business may deduct amounts derived from investments, so long as the business is not a banking, lending, or security business.

Tax Preference Performance Statement.
Tax preferences confer reduced tax liability upon a designated class of taxpayers. These include tax exclusions, deductions, exemptions, preferential tax rates, deferrals, and credits. There are over 700 tax preferences. Legislation that establishes or expands a tax preference must include a tax preference performance statement (TPPS) that identifies the public policy objective of the preference, as well as specific metrics that the Joint Legislative Audit and Review Committee (JLARC) can use to evaluate the effectiveness of the preference. All new tax preferences automatically expire after 10 years unless an alternative expiration date is provided.

Summary of Engrossed Substitute Bill:

Part I—Business and Occupation Tax Rate changes.
Beginning October 1, 2025, the B&O tax rate for services and other activities for businesses with a gross income of over $5 million is increased to 2.1 percent.

Beginning January 1, 2027, the rate for the following categories is increased to 0.5 percent:

- standard manufacturing, extracting, and wholesaling;
- standard retailing;
- radioactive waste cleanup;
- retail or wholesale sales of digital goods, digital codes, and digital automated services;
- research and development by non-profits;
- insurance agents;
- childcare;
- treatment of chemical dependency;
- salmon canners;
- manufacturing, wholesaling, and retailing of commercial airplanes or components of such airplanes;
- manufacturing and retailing of tooling, specifically for use in manufacturing of commercial airplanes or components of such airplanes;
- printing materials, other than newspapers, and of publishing periodicals and magazines;
- highway contractors and government contractors;
- cold storage warehousing; and
- radio and television broadcasting.

In addition, the B&O tax rate for contests of chance is increased to 1.8 percent.

Part II—Business and Occupation Surcharges on High Grossing Businesses and Financial Institutions.
Beginning January 1, 2026, an additional B&O tax is imposed on businesses in Washington with at least $250 million in Washington taxable income. The tax is 0.5 percent of the

business's annual Washington taxable income in excess of $250 million and is in addition to the other B&O taxes imposed on the income. This surcharge expires December 31, 2029.

The following income is exempt from the additional tax:

- income related to manufacturing activities, which includes the income from the wholesale or retail sale of products manufactured by a person subject to the manufacturing tax rates;
- income related to the sale of food, food stamp purchases, and prescription drugs;
- income attributable to the wholesale or retail sale of petroleum products by a person who is located in another state and the owner of such materials processed for it in Washington by an affiliated processor for hire;
- income from the retail and wholesale transactions of fuel; and
- income subject preferential rates for timber and timber products, including manufacturing, processing for hire, extracting, and wholesaling activities.

In addition, persons primarily engaged as a farmer or eligible apiarist as well as financial institutions are exempt from the additional B&O tax. Taxpayers who pay the ACS are also exempt from this additional B&O tax.

Beginning October 1, 2025, the additional B&O tax on certain financial institutions is increased to 1.5 percent.

Part III—Advanced Computing Surcharge.
The B&O ACS rate is increased to 7.5 percent, and the annual cap is increased to $75 million beginning January 1, 2026.

Beginning in fiscal year 2028, and each year thereafter, the number of enrollments at computer science and engineering degree programs at four-year state universities must be automatically added and funded when the number of qualified Washington state applicants exceed the available enrollments at these programs by 100 applicants.

Part IV—Investment Deduction.
The criteria for utilizing the B&O tax deduction for the proceeds from investments is clarified.

The B&O tax deduction is for amounts derived from investment that are incidental to the main purpose of the business. Investments are considered incidental to the main purpose of a business if less than 5 percent of the business's total worldwide gross income is derived from such investments annually. "Investments" include securities, trading account assets, federal funds, options, futures contracts, forward contracts, notional principal contracts, equities, foreign currency transactions, fixed income instruments, derivative instruments, and commodities.

If the business is a nonprofit organization, the business may continue to deduct proceeds

from investments. In addition, retirement accounts and certain family investment vehicles, as well as the recipients of distributions from these accounts, may continue to deduct the proceeds from these investments.

A collective investment vehicle (CIV) may also continue to deduct the proceeds from investments. A CIV means a taxpayer who meets the following criteria:

- The taxpayer's total gross income derived from its investments is at least 90 percent of the taxpayer's worldwide gross income of the business annually.
- The taxpayer holds title to passive investment assets for the benefit of the taxpayer's investors, and the investment decisions are made by another person who serves as the CIV's manager or advisor.
- The taxpayer accepts unrelated persons as its investors.

A CIV may be a mutual fund, collective fund, or similar investment vehicle. A CIV may be structured in various ways including as a limited or general partnership, limited liability company, corporation, or trust.

A CIV may not deduct the following amounts:

- amounts derived from investments that are invested in the CIV but are not themselves a CIV;
- amounts received by persons as compensation for services rendered to a CIV, the CIV investors, or both;
- amounts derived from sources other than investments by a CIV; or
- amounts derived from factoring.

Part V—Other Provisions.
This act is exempt from the requirements of the TPPS, JLARC review, and automatic 10-year expiration.

The DOR is required to engage its business advisory council as well as a group of taxpayers to recommend statutory and administrative changes to simplify tax compliance for taxpayers.

Appropriation: None.

Fiscal Note: Preliminary fiscal note available.

Effective Date: The bill contains multiple effective dates. Please see the bill.

Staff Summary of Public Testimony:

(In support) This state is facing a budget shortfall that is threatening our social safety net. It is important to continue investing in the important programs, including food banks, nursing homes, kindergarten through twelfth grade education, higher education, and other vital

public services.

Moreover, Washington needs a more progressive tax code. It is necessary and fair to require the large businesses to pay their fair share. These businesses have benefited from the investments in our communities and schools in achieving their success, and now everyone must contribute to avoid devastating budget cuts

Nonprofit organizations were concerned about the impact of the *Antio, LLC v. DOR* decision and their ability to deduct investment income. This legislation provides much needed guidance for a large number of taxpayers, although some clarity about previous tax reporting periods would be appreciated.

(Opposed) The B&O surcharge provides an exemption for the sale of food; however, it should also include the wholesaling of food to help protect the small, independent grocers. The B&O surcharge exemption for manufacturing is important, but unfortunately does not apply to refineries. The imposition of the B&O surcharge will increase the cost of gas for everyone and hurt families.

In 2019 the Legislature imposed the B&O surcharge on banks that it is now seeking to increase. This will increase the cost of lending and negatively impact housing.

Spending has outpaced revenues, and, as a result, taxpayers are being asked to pay more in taxes instead of Washington living within its means.

The B&O tax rate increase for retailing is a significantly larger increase than the other rates. Retailers work on low margins and imposing a higher rate increase will hurt Washington retailers and consumers. Moreover, the lower retailing B&O tax rate recognized that retailers collected and remitted sales tax revenues to the state without any cost reimbursement.

The B&O rate increase will negatively impact healthcare providers and their patients. The providers have no ability to set prices, and the industry is facing increased costs and consolidation.

Persons Testifying: (In support) Representative Joe Fitzgibbon, prime sponsor; Bernadette Jungblut, Faculty Legislative Representative for Central Washington University; Becky Bogard, Inspire Washington; Nancy Sapiro, Jewish Federation of Greater Seattle; Adan Espino Jr, Nonprofit Association of WA; Krystal Johnson; Claire Lane, Anti-Hunger and Nutrition Coalition; Molly Gallagher, Statewide Poverty Action Network; Lilly Deerwater, WA Physicians for Social Responsibility; Michael Cook; Julianna Dauble; Mike Braak; Treasure Mackley; and Erin Haick, SEIU 925.

(Opposed) Sean Graham, Washington State Medical Association; Tim Eyman, Initiative Activist; Greg Hanon, Western States Petroleum Assoc.; Van Collins, American Council of

Engineering Companies of Washington (ACEC); Amber Carter, WA Retail Association; Glen Simecek, Washington Bankers Association; Katie Beeson, Washington Food Industry Association (WFIA); Brandon Houskeeper, NW Grocery Retail Association; Julia Gorton, Washington Hospitality Association; Diana Carlen, Washington Oil Marketers Association; Sven Akerman Jr, Outlook Insight LLC; and Dakota Manley, Washington State Young Republicans.

Persons Signed In To Testify But Not Testifying: More than 20 persons signed in. Please contact the House Public Records Office at https://leg.wa.gov/public-records-requests/ or call (360) 786-0926.