SENATE BILL REPORT
ESSB 5814

As Amended by House, April 23, 2025

Title: An act relating to funding public schools, health care, social services, and other programs and services to benefit Washingtonians by modifying the application and administration of certain excise taxes.

Brief Description: Modifying the application and administration of certain excise taxes.

Sponsors: Senate Committee on Ways & Means (originally sponsored by Senators Frame, Trudeau, Alvarado, Nobles, Pedersen, Valdez and Wilson, C.).

Brief History:

Committee Activity: Ways & Means: 4/16/25, 4/18/25 [DPS, DNP, w/oRec].

Floor Activity: Passed Senate: 4/19/25, 27-22.
Passed House: 4/23/25, 50-47.

Brief Summary of Engrossed First Substitute Bill

- Extends retail sales and use tax to certain specified services.
- Makes certain products containing nicotine subject to the other tobacco products tax.
- Imposes an additional tax on cigarettes.
- Imposes a one-time prepayment of retail sales tax collections for businesses with $3 million or more in taxable retail sales during calendar year 2026.

SENATE COMMITTEE ON WAYS & MEANS

Majority Report: That Substitute Senate Bill No. 5814 be substituted therefor, and the substitute bill do pass.

Signed by Senators Robinson, Chair; Stanford, Vice Chair, Operating; Trudeau, Vice

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

Chair, Capital; Frame, Vice Chair, Finance; Cleveland, Conway, Dhingra, Hansen, Hasegawa, Pedersen, Riccelli, Saldaña, Wellman and Wilson, C..

Minority Report: Do not pass.
Signed by Senators Gildon, Ranking Member, Operating; Torres, Assistant Ranking Member, Operating; Schoesler, Ranking Member, Capital; Dozier, Assistant Ranking Member, Capital; Boehnke, Braun, Muzzall, Wagoner and Warnick.

Minority Report: That it be referred without recommendation.
Signed by Senator Kauffman.

Staff: Alia Kennedy (786-7405)

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. Revenues are deposited in the state general fund. There are several rate categories, and a business may be subject to more than one B&O tax rate, depending on the types of activities conducted. The general B&O tax rates are 0.471 percent for retailing; 0.484 percent for manufacturing, wholesaling, and extracting; and 1.5 or 1.75 percent for services and for activities not classified elsewhere—depending on taxable income. Current law authorizes multiple exemptions, deductions, and credits to reduce the B&O tax liability for specific taxpayers and business industries.

Retail Sales and Use Tax. Retail sales taxes are imposed on retail sales of most articles of tangible personal property, digital products, and some services. A retail sale is a sale to the final consumer or end user of the property, digital product, or service. If retail sales taxes were not collected when the user acquired the property, digital products, or services, then use tax applies to the value of property, digital product, or service when used in this state. The state, all counties, and all cities levy retail sales and use taxes. The state sales and use tax rate is 6.5 percent. Local sales and use tax rates vary from 0.5 percent to 4.1 percent, depending on the location.

Retail Services. Businesses that sell intangible products to customers are generally subject to B&O tax under the services and other classification. Customer do not pay retail sales and use tax on most services. A select number of services are subject to retail sales and use tax, such as construction services, personal training at athletic and fitness facilities, extended warranties and maintenance agreements, alarm monitoring services, and vehicle towing, to name a few. If the service is taxable as a retail sale, then the business activity is subject to retailing B&O tax.

Information technology products and services sold as a non-itemized package are generally subject to retail sales and use tax. When the products and services are separately stated on a sales invoice or contract, charges for computer hardware and prewritten computer software are subject to retail sales or use tax. Separately stated charges for custom software and

customization of prewritten software are not subject to retail sales or use tax.

Digital Products. Retail sales or use taxes apply to all digital products, regardless of how they are accessed. Digital products are digital goods and digital automated services (DAS). A DAS is any service transferred electronically that uses one or more software applications. A digital good is a sound, image, data, fact, or information, or any combination thereof, transferred or accessed electronically.

Some DAS exclusions exist that exempt specific DAS from the definition of retail sales. A few of those exclusions include, but are not limited to:

- any service that primarily involves the seller's application of human effort;
- live presentations, such as lectures, seminars, workshops, or courses, where participants are connected to other participants via the internet or telecommunications equipment that allows audience members and the presenter or instructor to give, receive, and discuss information with each other in real time;
- advertising services; and
- data processing services.

"Advertising services" is defined as services directly related to the creation, preparation, production, or the dissemination of advertisements, including layout, art direction, graphic design, mechanical preparation, production supervision, placement, and rendering advice to a client concerning the best methods of advertising that client's products or services. Advertising services also include online referrals, search engine marketing and lead generation optimization, web campaign planning, the acquisition of advertising space in the internet media, and the monitoring and evaluation of website traffic for purposes of determining the effectiveness of an advertising campaign. Advertising services do not include web hosting services and domain name registration.

"Data processing service" is defined as a primarily automated service provided to a business or other organization where the primary object of the service is the systematic performance of operations by the service provider on data supplied in whole or in part by the customer to extract the required information in an appropriate form or to convert the data to usable information. Data processing services include check processing, image processing, form processing, survey processing, payroll processing, claim processing, and similar activities.

The above exclusions are exempt from retail sales and use tax and retailing B&O tax and are instead subject to the service and other activities B&O tax.

Digital goods concurrently available for use inside and outside Washington are not subject to retail sales or use taxes if the goods or services are not for personal use.

Cigarette Tax. Two separate state taxes are imposed on the sale, use, consumption, handling, possession, or distribution of all cigarettes. One is at the rate of $0.12125 per cigarette. The other tax is $0.03 per cigarette, and the revenues from which are deposited

into the state general fund. This creates a total tax rate of $0.15125 per cigarette, or $3.025 per pack. This is in addition to retail sales and use, B&O, and litter taxes that may apply.

Other Tobacco Products Tax. Taxes are imposed on the sale, handling, or distribution of all tobacco products at the following rates:

- for cigars except little cigars, 95 percent of the taxable sales price of cigars, not to exceed $0.65 per cigar;
- for little cigars, $0.15125 per stick;
- for moist snuff:
    1. cans that weigh 1.2 ounces or less, $2.526 per can; or
    2. cans that weigh more than 1.2 ounces, $2.105 per ounce; and
- for all other tobacco products, 95 percent of the taxable sales price.

The other tobacco products (OTP) tax is deposited into the state general fund. The OTP tax is in addition to retail sales and use, B&O, and litter taxes that may apply.

The definition of tobacco products is made up of a list of forms of tobacco prepared for human consumption, and specifically excludes cigarettes.

Filing Frequency and Due Dates. Taxpayers are required to electronically file and pay excise taxes on a monthly basis. The Department of Revenue (DOR) may provide a quarterly or annual tax filing frequency to taxpayers below a certain annual estimated tax liability. Businesses that collect retail sales and use tax generally file a combined excise tax return that includes both the B&O tax and any sales and use taxes collected by the business. The combined excise tax return for monthly filers is due on the 25th of the following month. The filing due date for combined excise tax returns creates a delay between when retailers receive the sales tax from their customers and when they remit those funds to the state.

Summary of Engrossed First Substitute Bill: Retail Services. The following select services are classified as retail services and subject to retail sales and use tax and retailing B&O tax:

- information technology technical consulting services;
- information technology training services and technical support;
- custom website development services;
- custom software and customization of prewritten computer software;
- investigation, security services, security monitoring services, and armored car services;
- temporary staffing services; and
- advertising services.

The following DAS are classified as retail services and subject to retail sales and use tax and retailing B&O tax:

- any service that primarily involves the application of human effort by the seller;

- live presentations;
- advertising services; and
- digital processing services.

The following services are excluded from retail sales and use tax and retailing B&O tax:

- temporary staffing services used by hospitals;
- telehealth and telemedicine services; and
- the following services when the sale of such service is between members of an affiliated group:
    1. information technology consulting training, and support services;
    2. custom web design services;
    3. investigation, security, security monitoring, and armored car services;
    4. advertising services;
    5. any digital automated service that primarily involves the application of human effort by the seller;
    6. live presentations in which participants are connected via the internet or telecommunications equipment; and
    7. data processing services.

Additional Cigarette Tax. An additional tax on the sale, use, consumption, handling, possession, or distribution of cigarettes is imposed at a rate of $0.10 per cigarette, or $2.00 per pack, for a total tax rate of $5.025 per pack. This is in addition to retail sales and use, B&O, and litter taxes that may apply.

Taxation of Nicotine Products. The definition of tobacco products is expanded to include products that contain nicotine, whether derived from tobacco or created synthetically. The definition of moist snuff is expanded to include similar products containing nicotine. Such products are subject to the OTP tax.

Pre-payment of Sales Tax. Taxpayers who file a monthly combined excise tax return and had $3 million or more taxable retail sales during calendar year 2026 must make a one-time prepayment of state sales tax collected in June 2027. The prepayment of state sales tax is due on June 25, 2027, and must be equal to 80 percent of the state sales tax collected and remitted for the June 2026 reporting period. The remaining tax liability is due on or before July 26, 2027. The taxpayer must correct the collection amounts on the regularly filed excise tax return due on or before July 26, 2027.

A one-time penalty equal to 10 percent of the amount of tax due and payable is assessed on any taxpayer who fails to submit a prepayment or submits a prepayment that is less than 80 percent of the June 2026 state sales tax. DOR may waive the penalty if the taxpayer demonstrates that the June 2027 taxable retail sales were less than 80 percent of the June 2026 taxable retail sales.

Appropriation: None.

Fiscal Note: Requested on April 15, 2025.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: The bill contains several effective dates. Please refer to the bill.

Staff Summary of Public Testimony on Original Bill: *The committee recommended a different version of the bill than what was heard.* PRO: More revenue is needed to fund essential state programs.

CON: The tax on services will ultimately increase costs for consumers. The tax on alternative nicotine products is not equitable and discourages the use of tobacco cessation products.

OTHER: Industries, such as the health care industry, already pay a large amount in tax and this bill will significantly increase the cost of doing business. The sales tax pre-payment requirements will be administratively burdensome for businesses.

Persons Testifying: PRO: Molly Gallagher, Washington Statewide Poverty Action Network.

CON: Jeff Pack, Washington Citizens Against Unfair Taxes; Dr. Pritika Kumar, Philip Morris International; John Morgan; Katie Beeson, Washington Food Industry Association (WFIA); Tim eyman, Initiative activist; Mark Holmes, Council On State Taxation (COST); Amber Carter, WA Retail Association; Julia Gorton, Washington Hospitality Association; Lisa Thatcher, Washington State Hospital Association; Chelene Whiteaker, Washington State Hospital Association; Carolyn Logue, ABC Inland, South Sound Chambers, WA ACCA, NWHPBA; Katherine Mahoney, LeadingAge WA; Max Martin, Association of Washington Business; Catherine Morrison, Allegis Group, Redwood Holdings, Maxim Healthcare, and Amergis; Glen Simecek, Washington Bankers Association; Natalie K McNair, TrueBlue, Inc.; Tony Sermonti, Motion Picture Association ; Enrique Rico Rico , Washington State Young Republicans.

OTHER: Audrey Miller Garcia , American Cancer Society Cancer Action Network ; Rowland Thompson, Allied Daily Newspapers and WSABroadcasters.

Persons Signed In To Testify But Not Testifying: No one.

EFFECT OF HOUSE AMENDMENT(S):

- Removes information technology technical consulting services from the defintion of "retail sale" and effectively making such services exempt from retail sales and use tax and the business and occupation services and other activities tax classification.
- Adds signage to exempt forms of advertising services.
- Defines the following terms excluded from advertising services: printing, publishing, and radio and television broadcasting.

- Limits the exclusion for radio and television advertising services to include only those services rendered in respect to radio or television broadcasting stations licensed, regulated, and issued a call sign by the Federal Communications Commission.
- Removes the additional tax on cigarettes.
- Removes the requirement that certain businesses make a one-time prepayment of retail sales tax collections.