

# HB 1342

## Bill Analysis

February 18, 1997

**Brief Description:** Revising interest and penalty administration of the department of revenue.

**Bill Sponsors:** Representatives B. Thomas, Dunshee and Wensman.

**Staff:** Linda Brooks (786-7153)

**Background:** The Department of Revenue (DOR) administers a variety of tax programs. Each program provides for the application of interest and penalties when a taxpayer does not satisfy his or her reporting or tax obligations in a timely manner, or when a taxpayer overpays the amount of tax due. The interest rates and penalties applied are not uniform across all tax programs. There are general administrative rules that apply in the absence of specific provisions for a particular tax.

### *Interest Computation - Tax Liabilities - Generally*

Interest is computed on a tax liability from the last day of the year in which a deficiency is incurred until the date of payment.

### *Interest Rate - Tax Liabilities - Generally*

A taxpayer who does not pay the entire amount of a tax obligation on the due date must pay interest on the amount of the remaining tax liability. If the liability arose prior to January 1, 1992, interest is charged at an annual rate of 9 percent. If the tax liability is incurred on or after

January 1, 1992, the interest rate equals an annualized average of the federal short-term rate plus two percentage points. This rate is calculated by taking an arithmetical average of the federal short-term rate, compounded annually, for the months of January, April, July, and October of the preceding calendar year. The federal short-term rate plus two percentage points currently equals 8 percent.

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While most outstanding tax balances are for tax obligations incurred since 1992, there are still some taxpayers who owe back taxes for periods prior to 1992. Therefore, some tax accounts are assessed at the older 9 percent tax rate.

*Interest Rate - Tax Refunds - Generally*

A taxpayer who pays taxes, penalties, or interest in excess of the amount due is entitled to a refund of the overpayment and interest on the amount of the overpayment. The annual interest rate, applicable to refunds on amounts overpaid before January 1, 1992, is 3 percent. The interest rate, applicable to refunds on amounts overpaid on or after January 1, 1992, equals an annualized average of the federal short-term rate plus one percentage point. The federal short-term rate plus one percentage point currently equals 7 percent.

Normally, refunds may only be claimed for amounts overpaid in the preceding four years. However, in some cases, such as a court judgment in a taxpayer's favor, refunds may be owed for periods prior to 1992. For these older cases, the Department of Revenue is obligated to use the lower 3 percent interest rate in computing tax refunds.

*Interest Computation & Rate - Tax Warrants*

Interest is computed on the amount of a warrant. A warrant amount includes taxes owed *plus* penalties and interest already assessed. The Department of Revenue computes interest on warrants every 30 days at a rate of 1 percent on the outstanding balance of the warrant amount.

*Interest Rate - Real Estate Excise Taxes*

Real estate excise tax must be paid within one month of the sale of the property. If payment is not made within 30 days of the sale, then interest is assessed. The interest is charged at a rate of 1 percent per month.

*Penalties - Estate Taxes*

The person responsible for filing a federal estate tax return must also file a Washington estate tax return. The deadline for filing the Washington return is the same as the federal deadline. If a person fails to file a Washington estate tax return on time, the Department of Revenue assesses a penalty. The penalty equals 5 percent of the tax due for each month intervening between the date that the tax was first due and the date that the return is actually filed.

## **Summary of Bill:**

### *Interest Computation - Tax Liabilities - Generally*

The time period for computing interest changes from the last day of the year in which a tax liability is incurred to the last day of the month following the month a tax is first due. For example, if a taxpayer files annually on December 31, then interest on tax not paid is computed starting on January 31. Similarly, if a taxpayer fails to pay tax due on April 30, then interest on the tax liability begins on May 31. This change in interest computation practices particularly affects taxpayers who file monthly or quarterly, as opposed to annual, tax returns.

### *Interest Rate - Tax Liabilities - Generally*

Starting January 1, 1999, all taxpayer accounts will be assessed interest at the same variable rate. The age of the account will not affect the interest rate used. Specifically, interest on a tax liability arising before 1992 will be treated no differently than interest on a tax liability arising during or after 1992. The variable rate equals an annualized average of the federal short-term rate plus two percentage points. The current variable rate equals 8 percent.

### *Interest Rate - Tax Refunds - Generally*

Starting January 1, 1999, all taxpayer refunds will be assessed interest at the same variable rate. The tax period, when taxes were overpaid, will no longer affect the interest rate used. Specifically, interest owed on taxes overpaid prior to 1992 will be computed the same as interest owed on taxes overpaid during or after 1992. The variable rate for refunds equals an annualized average of the federal short-term rate plus one percentage point. The current variable rate equals 7 percent.

### *Interest Computation & Rate - Tax Warrants*

Starting January 1, 1999, interest is only assessed on the portion of the warrant amount representing taxes due. Additional interest is not assessed on penalties and interest included within the total warrant amount.

The Department of Revenue will also start assessing interest on tax warrant amounts using a variable rate on January 1, 1999. The variable rate equals an annualized average of the federal short-term rate plus two percentage points. The current rate equals 8 percent.

*Interest Rate - Real Estate Excise Taxes*

Starting January 1, 1999, interest on delinquent real estate excise taxes will be assessed using a variable rate. The variable rate equals an annualized average of the federal short-term rate plus two percentage points. The current variable rate equals 8 percent.

The Department of Revenue is responsible for notifying county treasurers of the variable rate to be used for each calendar year.

*Penalties - Estate Taxes*

The practice of automatically assessing estate tax penalties when a return is not filed on time is eliminated. The Department of Revenue may waive or cancel estate tax penalties, if the late filing of a return is due to circumstances beyond the control of the person responsible for filing it.

**Fiscal Note:** Available.

**Effective Date:** If enacted, 90 days after adjournment of session.

**Interest and Penalty Administration of the Department of Revenue**

Interest Computation: Tax Liabilities - Generally	Interest calculation starts at the end of year when a tax liability is incurred	Interest calculation starts at the end of the month following the month when a tax liability is incurred. Taxpayers most affected by this change are monthly and quarterly taxpayers.
Interest Rate: Tax Liabilities - Generally	Interest is charged at 9% on tax liabilities incurred prior to 1992.  Interest is charged at variable rate (presently 8%) on tax liabilities incurred during or after 1992.	Starting on January 1, 1999, interest on <i>all</i> tax liabilities is charged at the same variable rate (currently 8%).
Interest Rate: Tax Refunds - Generally	Interest is assessed on refunds at 3% for tax amounts overpaid prior to 1992.  Interest is assessed on refunds at a variable rate (presently 7%) for tax amounts overpaid during or after 1992.	Starting on January 1, 1999, interest is assessed on <i>all</i> refunds at the same variable rate (currently 7%).
Interest Computation & Rate: Tax Warrants	Interest is computed on the full warrant amount. A warrant amount includes not only taxes due but also penalties and interest already assessed on the taxes due.  The interest rate is 1% per month.	Interest is computed on only the portion of the warrant amount representing taxes due.  Starting on January 1, 1999, interest is assessed using a variable rate (currently 8% per year).
Interest Rate: Real Estate Excise Taxes	Interest is assessed on delinquent real estate taxes at a rate of 1% per month.	Starting on January 1, 1999, interest is assessed on delinquent real estate taxes using a variable rate (currently 8% per year).
Penalty Provision: Estate Taxes	Department of Revenue must assess a penalty on any estate tax return not filed on time.	Department of Revenue has the discretion to cancel or waive penalties on estate tax returns not filed on time, if the late filing of a return is due to circumstances beyond the control of the person filing the return.