

HOUSE BILL REPORT

HB 2267

As Reported by House Committee On:

Finance

Title: An act relating to revenue for dedicated accounts.

Brief Description: Providing revenue for the student achievement fund and the health services account.

Sponsors: Representatives Gombosky, Sommers, Moeller, Cody, Conway, Fromhold and McIntire.

Brief History:

Committee Activity:

Finance: 4/26/03 [DPS].

Brief Summary of Substitute Bill

- Eliminates tax credits for insurance guaranty funds.
- Increases liquor store taxes.
- Reduces the holding period for certain types of unclaimed property under the Uniform Unclaimed Property Act from five to three years.
- Increases penalties for underpayments of state excise taxes.
- Imposes an additional tax on cigarettes of 50 cents per pack.
- Eliminates the sales and use tax exemptions for candy and gum.
- Deposits revenue from all these tax changes in the Student Achievement Fund and the Health Services Account.

HOUSE COMMITTEE ON FINANCE

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 5 members: Representatives Gombosky, Chair; McIntire, Vice Chair; Conway, Morris and Santos.

Minority Report: Do not pass. Signed by 4 members: Representatives Cairnes, Ranking Minority Member; Orcutt, Assistant Ranking Minority Member; Ahern and

Roach.

Staff: Bob Longman (786-7139).

Background:

Insurance guaranty associations are organizations created by statute for the purpose of reimbursing policy holders and beneficiaries for losses resulting from the financial impairment or insolvency of insurance companies. Members of these associations are the individual companies authorized to write particular types of insurance within a state. Washington has two insurance guaranty associations. The Washington Insurance Guaranty Association protects property and casualty policyholders. The Washington Life and Disability Insurance Guaranty Association protects life and disability insurance policyholders.

When an insolvency or liquidation occurs, the member insurance companies of the affected guaranty association are assessed based on their percentage of Washington premiums; the assessment is limited to 2 percent of a member company's Washington premiums.

Insurance companies are exempt from the state's business and occupation tax. Instead insurance companies pay a 2 percent insurance premium tax. Insurance companies are allowed to take amounts paid as assessments to the guaranty associations as credits against their insurance premium tax obligations. The tax credit is taken over a five-year period.

The Uniform Unclaimed Property Act governs the disposition of intangible property that is unclaimed by its owner. A business that holds unclaimed intangible property must transfer it to the Department of Revenue (DOR) after a holding period set by statute. The holding period varies by type of property, but for most unclaimed property the holding period is five years. After the holding period has passed, the business in possession of the property transfers the property to the DOR.

Abandoned property is turned over from many sources including banks, credit unions, corporations, utilities, insurance companies, governmental entities and retailers throughout the United States. The types of abandoned property that are subject to the DOR program include bank accounts; uncashed checks such as payroll, insurance payments or travelers checks; utility and/or phone company deposits; safe deposit box contents; insurance proceeds; and stocks, bonds, and mutual funds.

Under the program, the DOR's duty is to find the rightful owner of the property, if possible. The DOR sends notices to the last known addresses of owners, places advertisements with names of owners in newspapers, sends press releases to television and radio stations, and undertakes other efforts to find owners. The DOR is not required

to publish or mail notices when the property value is less than \$75. With some exceptions, the DOR will sell property that is still unclaimed five years after it is received. The sale proceeds are deposited in the state general fund. However, the owner of unclaimed property may still come forward and obtain reimbursement from the state general fund at any time.

The retail sales tax applies to the selling price of tangible personal property and of certain services purchased at retail. The use tax is imposed on value of an item used in this state when the acquisition of the item has not been subject to sales tax. Retail sales and use taxes are imposed at the same rate. The state imposes retail sales and use taxes at a rate of 6.5 percent. Cities and counties may impose local taxes with rates up to 3.1 percent. The combined rate of state and local sales and use taxes ranges from 7.0 to 8.9 percent, depending on location. Food products are exempt from retail sales and use taxes. Candy and gum are included within the definition of food products.

Sales taxes and volume taxes apply to spirits (hard liquor). Spirits are subject to a volume tax of \$2.4408 per liter. A sales tax rate of 20.5 percent applies to spirits sold to consumers in the original package. The regular retail sales tax is not imposed on these sales. A sales tax rate of 13.7 percent applies to spirits sold to establishments that sell the spirits on their premises. The regular sales tax applies to retail sales of beverages by these establishments.

A tax is imposed on cigarettes at the rate of 142.5 cents per pack of 20 cigarettes. Revenue from the first 23 cents of the cigarette tax goes to the General Fund. The next eight cents are dedicated to Water Quality Improvement Programs through June 30, 2021, and to the General Fund thereafter. The next 101 cents goes to the Health Services Account. The remaining 10.5 cents are dedicated to youth violence prevention and drug enforcement.

The state's major excise taxes, such as the retail sales and the business and occupation tax, are reported to the DOR on a combined excise tax return. Taxpayers report monthly, quarterly, or annually, depending on the size of the business. Monthly taxpayers are required to pay taxes by the 25th of each month for activity in the previous month. Quarterly and annual taxpayers are required to pay taxes by the end of the month following the end of the reporting period. Penalties are imposed if a tax return is not filed or if the return is filed late. If the return is filed on time, without any tax, the penalty is imposed. If the return is filed on time, with only part of the tax, no penalty is imposed unless the underpayment appears to be intentional. The penalties are 5 percent if paid within the first month after the due date; 10 percent within the second month, and 20 percent after that. In addition, a penalty of 10 percent is imposed if the taxpayer disregards specific written instructions from the DOR on how to report tax liabilities. The total of these penalties cannot exceed 35 percent of the tax due. An additional penalty of 50 percent applies to underpayments resulting from an intent to evade taxes.

Summary of Substitute Bill:

Credits for both property and casualty and life and disability insurance companies on assessments paid to guaranty associations may no longer be taken against their insurance premium tax obligations.

The holding period for abandoned property under the Uniform Unclaimed Property Act is shortened from five to three years for the following types of property: bank accounts; certain uncashed checks such as payroll and cashier's checks; gift certificates and credit memos; and stocks, bonds and mutual funds.

Candy and gum are no longer exempt from retail sales and use taxes.

An additional tax of \$0.46 per liter is imposed on spirits. An additional sales tax rate of 3.9 percent is imposed on spirits sold to consumers in the original package. An additional sales tax rate of 2.6 percent is imposed on spirits sold to establishments that sell the spirits on their premises.

An additional tax on cigarettes is imposed at the rate of 50 cents per pack.

Penalties for failure to pay excise taxes on time are increased. The penalty for being more than one month late is increased from 10 percent to 15 percent. The penalty for being more than two months late is increase from 20 to 25 percent. The penalty for disregarding written instructions is increased from 10 percent to 15 percent. A new penalty of 25 percent is imposed on collecting but not remitting retail sales tax. A new penalty of 15 percent is imposed on substantial underpayments of tax. This when a taxpayer pays less than 90 percent of the tax owed. The cap on total penalties, other than the penalty for evasion, is increased from 35 percent to 40 percent.

Revenue from the changes related to insurance guaranty credits, liquor, unclaimed property, and excise tax penalties is deposited in the Student Achievement Fund. Revenue from the changes related to cigarette taxes, candy, and gum are deposited in the health services accounts. For those changes where it is not practical to determine precisely the revenue derived from the change, a portion of state sales tax revenue is dedicated in lieu thereof.

Substitute Bill Compared to Original Bill:

The original bill included a sales tax increase, repeal of deductions for cash discount, and limitations on deductions for membership fees, which are not in the substitute. The substitute adds provisions related to insurance guaranty and unclaimed property. The substitute modifies provisions related to liquor taxes and penalties compared to the original bill.

Appropriation: None.

Fiscal Note: Requested on April 18, 2003.

Effective Date of Substitute Bill: The bill contains an emergency clause and takes effect on July 1, 2003, except sections 4 through 9 related to unclaimed property and sections 11 and 13 conforming the definition of taxable food to the streamlined sales tax agreement take effect January 1, 2004.

Testimony For: This bill provides revenue for programs to help the biggest losers in the current economic downturn. Lives depend on the safety nets funded by this bill. Candy is not food. It should not be exempt from sales tax like food is. Candy, cigarettes, and liquor are completely discretionary purchases and it is appropriate to increase taxes on these items. If taxes can be raised for asphalt, taxes can be raised for children.

Testimony Against: We are opposed to tax increases. The state should live within its means. Small businesses are losing money during the economic downturn, but still must pay taxes. Increasing the penalties for late payments just adds insult to injury. Another tax increase just makes the economic situation worse. Adding sales tax to candy and gum is a tax on the citizens. It is impossible to meet the July 1, 2003, effective date for candy and gum. Retailers need at least 90 days to sort through inventory and work with candy manufacturers to determine which items are taxable. Retailers are uncompensated for collecting sales tax. To add this additional burden, and then not give enough time to do is very unfair. Alcohol taxes are already the highest in the nation. This bill increases alcohol taxes on top of these already high rates. Cigarette taxes are among the most regressive. We are only 10 months into the last major cigarette tax increase. Cigarette taxes are so high that sales are declining and the revenue estimates for increased taxes are too optimistic. Stores in Washington are losing sales to smoke shops, internet vendors, and Idaho stores who do not collect Washington tax. The re-enactment of insurance guaranty tax credits in 1997 passed by a big margin. These credits represent appropriate public policy. Reimbursement of policy holders of an insolvent insurer is a public benefit; the cost should be borne by the public through tax credits. It would be better to expand gambling opportunities to raise revenue.

Testified: (In support) Representative Gombosky, prime sponsor; and Nick Federici, American Lung Association of Washington.

(Opposed) Mark Johnson, National Federation of Independent Business; Gary Smith, Independent Business Association; Gary Chandler, Association of Washington Business; Jan Gee, Retail Association; Stan Bowman, Washington Restaurant Association; Steve Gano, Kraft Foods; Mel Sorensen, National Association of Independent Insurers and Allstate Insurance; Mike Kapphahn, Farmers Insurance; Mark Triplett, Triplett and Associates; Gary Strannigan, Safeco Insurance; T.K. Bentler, Washington Association of

Neighborhood Stores and Washington State Hotel and Lodging Association; Dave Ducharme, Distilled Spirits Council of the United States; and Joe Daniels, Phillip Morris, Inc.

(Comments) Julie Sexton, Department of Revenue.