

SENATE BILL REPORT

EHB 2163

As of Second Reading

Title: An act relating to revenue.

Brief Description: Relating to revenue.

Sponsors: Representative Ormsby.

Brief History: Passed House: 6/30/17, 53-40.

Committee Activity:

Brief Summary of Engrossed Bill

- Repeals the bottled water retail sales tax preference.
- Repeals the state tax preference for self-produced fuels.
- Requires marketplace facilitators, referrers, and their sellers to collect and remit sales or use tax, or comply with notice and reporting requirements.
- Modifies the Streamlined Sales and Use Tax Mitigation Account and payments.
- Expands the economic nexus for Business and Occupation tax.

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Background: 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 taxes apply to the value when used in this state. The state, most cities, and all counties 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 3.9 percent, depending on the location.

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

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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, wholesaling, and extracting; and 1.5 percent for services, and activities not classified elsewhere. Several preferential rates also apply to specific business activities.

In addition, there are other tax preferences, including credits and deductions, that a business may be eligible to utilize 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. In general, the small business credit is \$35 per month multiplied by the number of months in the reporting period.

A business that does not owe other taxes or fees to the Department of Revenue (DOR) and that has annual gross proceeds of sales, gross income, or value of products for all B&O tax classifications less than \$28,000 per year, or \$46,667 if at least 50 percent of their taxable income is from certain activities, does not have to file an annual B&O tax return.

Nexus. Nexus is required before a taxing jurisdiction can impose taxes on an entity. In the case of sales or use taxes, nexus is necessary in determining whether an out-of-state business selling products into a state is liable for the collection of sales or use taxes for that state. A legal analysis of nexus involves the Dormant Commerce Clause and the Due Process Clause in the United States Constitution. If a tax violates either, it will be invalid. The Dormant Commerce Clause analysis focuses on the structural concerns on the national economy, and whether the tax inhibits interstate commerce. The Due Process Clause analysis focuses on the authority of a state to impose the tax on a particular taxpayer.

In 2015 Washington adopted "click through" nexus. Under this nexus standard, certain remote sellers are required to collect and remit Washington sales tax for sales made into the state, and may also have to pay B&O tax on their Washington sales. A remote seller is covered by "click through" nexus if the remote seller: enters into agreements with Washington residents who, for a commission or other consideration, refers potential customers to the remote seller, such as by a link on a website; and generates more than \$10,000 in gross receipts during the prior calendar year under such agreements from sales into this state.

Streamlined Sales and Use Tax Agreement. In 2007 the Legislature fully adopted the Streamlined Sales and Use Tax Agreement (SSUTA). The SSUTA includes provisions for determining where a sale is deemed to occur for local sales and use tax purposes. As part of the legislation, the Streamlined Sales and Use Tax Mitigation Account was created to mitigate the effect of the change in sourcing rules to negatively impacted local jurisdictions. Each July 1, the State Treasurer must transfer an amount determined by the DOR to fully mitigate negatively impacted local jurisdictions. The DOR determines each local jurisdiction's annual losses. Distributions are made quarterly representing one-fourth of a jurisdiction's annual loss less voluntary compliance revenue from the previous quarter.

Summary of Bill: Part I – Eliminating or Narrowing Tax Preferences. The sales tax exemption for bottled water is eliminated; however, there are exceptions for medically prescribed water, or if a person's primary source of drinking water is considered unsafe.

The use tax exemption for self-produced fuel is narrowed to include only biomass fuels. The use tax for refinery fuel gas is 3.852 percent. The value of refinery fuel gas is set to the United States natural gas wellhead price and local sales tax does not apply.

Part II – Remote Sellers, Referrers & Marketplace Facilitators. Beginning January 1, 2018, remote sellers, marketplace facilitators and referrers that meet the statutory criteria must remit sales or use tax, or comply with the notice and reporting requirements in this act. An election by a marketplace facilitator, referrer, or remote seller to collect and remit sales or use tax can only be changed upon written notice to the DOR, will not take effect until January 1 of the calendar year at least 12 months past the date of election to collect and remit, and the written notice must occur at least 30 days prior to the election being changed. The remit or report requirements for certain digital goods and digital codes is delayed until January 1, 2020.

This act applies to marketplace facilitators or remote sellers that have gross receipts sourced to Washington of at least \$10,000. A referrer must comply with this act if during the current or previous calendar year, the gross business income received from its referral services sourced to Washington, whether or not they are subject to sales or use tax, is at least \$267,000.

Notice and Reporting Requirements. A seller that meets the nexus criteria in this act, but not the physical presence nexus, and who does not collect and remit sales or use tax on all taxable retail sales into Washington, must comply with the reporting and notice requirements.

A seller, other than a referrer, must post a conspicuous notice on its website or catalog, as well as on its invoices or sales receipts, that includes a statement for Washington consumers that sales or use tax is due on certain purchases, and that Washington requires the purchaser to file a use tax return. In addition, this seller must also provide an annual report to each Washington purchaser that the seller did not collect sales or use tax on any sales, and must include the details on the purchaser's transactions in the previous year. Finally, a seller, other than a referrer, must file an annual report with the DOR that includes Washington purchasers' information, and an affidavit signed under penalty of perjury from a seller's officer affirming that the seller has made reasonable efforts to comply with consumer notice and reporting requirements. These reporting requirements do not apply to sellers registered with the DOR to collect and remit sales and use tax, and who make a reasonable effort to comply with current requirements.

A referrer must post conspicuous notice on its platform that informs Washington purchasers that sales or use tax is due on certain purchases, and a purchaser may have to file a use tax return with the DOR. Annually, a referrer must send a report to its marketplace sellers to whom the referrer transferred a potential purchaser located in Washington during the previous year. The report to a referrer's seller must state that Washington imposes a sales or use tax on retail sales, and a seller meeting the acts requirements must either collect and remit sales or use tax, or comply with the states notice and reporting requirements for sellers.

The referrer must also send a report to the DOR that includes a list of sellers who received notice, and an affidavit signed under the penalty of perjury from a referrer's officer stating that the referrer has made reasonable efforts to comply with the notice and reporting requirements under this act.

Penalties. A penalty is imposed on a seller, other than a referrer, who fails to provide notice or post a conspicuous notice to consumers at the time of purchase, in the amount of \$20,000. A penalty is imposed on a seller, other than a referrer, who fails to provide a report to each of its purchasers of all sales in the previous calendar year (CY) as follows:

- if the gross receipts of the seller through the seller's marketplace sourced to Washington is less than \$50,000, the penalty is \$5,000;
- if the gross receipts of the seller through the seller's marketplace sourced to Washington is at least \$50,000 but less than \$150,000, the penalty is \$10,000;
- if the gross receipts of the seller through the seller's marketplace sourced to Washington is at least \$150,000 but less than \$300,000, the penalty is \$50,000; and
- if the gross receipts of the seller through the seller's marketplace sourced to Washington is at least \$300,000, the penalty is \$100,000, plus \$20,000 for every \$50,000 in gross receipts over \$300,000.

A penalty is imposed on a referrer that fails to post a notice to consumers on its platform in the amount of \$20,000. A penalty is imposed on a referrer who fails to provide a report to each of its sellers of all potential purchasers referred from Washington in the previous CY as follows:

- if the gross income of the referrer through the referrer's referral services sourced to Washington is at least \$267,000 but less than \$300,000, the penalty is \$50,000; and
- if the gross income of the referrer through the referrer's referral services sourced to Washington is at least \$300,000, the penalty is \$100,000, plus \$20,000 for every \$50,000 in gross receipts over \$300,000.

A penalty of \$25 per failure, but not less than \$20,000, is imposed on any seller who fails to file required reports with the the DOR.

A seller is entitled to a conditional waiver if the seller enters into a written agreement to fully comply with all notice and reporting requirements beginning on a date acceptable to the DOR. The DOR may grant a waiver for one or more violations; however, the DOR may not grant more than one request by a seller for a waiver. A conditional waiver may be granted for reasonable cause. A conditional waiver can be invalidated if the seller fails to comply.

Definitions. A "marketplace facilitator" is a person that contracts with sellers to facilitate, for consideration, regardless of whether its deducted as fees from a transaction, the sale of the seller's products through a catalog, or a physical or electronic marketplace, and engages:

- directly or indirectly, through one or more affiliated persons in: communicating an offer and acceptance between the buyer and seller; owning or operating the infrastructure (electronic or physical) that brings buyers and sellers together; providing virtual currency; or software development or research and development related to the marketplace operated; and
- in any of the following activities with respect to sellers or producers: payment processing services; fulfillment or storage services; listing for sale for consideration;

setting prices; branding sales as those of the marketplace facilitator; order taking; advertising or promotion; or providing customer service and assistance with returns and exchanges.

A "marketplace seller" is a seller that makes retail sales through a physical or electronic marketplace operated by a marketplace facilitator, regardless of whether the seller is required to be registered with the DOR.

A "referrer" is defined as a person who contracts or otherwise agrees with a seller to list or advertise for sale items in any medium, receives a commission, fee, or other consideration from a seller for listing or advertising, transfers a potential purchaser to a seller or an affiliated person to complete the sale, and does not collect receipts from the purchasers for the transaction. A referrer does not include a newspaper or a newspaper publisher nor does it include a person that provides internet advertising services and does not ever provide either the marketplace seller's shipping terms or advertise whether a marketplace seller charges sales tax.

A "remote seller" refers to any seller who does not have a physical presence in this state, and makes sales to purchasers.

Liability for Unpaid Taxes. A marketplace facilitator or referrer is relieved of liability for failure to collect the correct sales or use tax if it can show that the error was due to incorrect information from an unaffiliated seller. The seller would be solely liable for unpaid tax. A marketplace facilitator or referrer is also relieved of liability, if: (1) the sale was made in a marketplace facilitator's marketplace or directly resulting from referral by the referrer; (2) the seller is unaffiliated; and (3) the seller fails to pay the tax, not due to sourcing the sale. The maximum amount of relief is phased in, and represents a percentage of a marketplace facilitator's total tax due, or a percentage of a referrer's taxable retail sales in Washington.

The marketplace seller is relieved of liability for failure to collect and remit the correct sales or use tax if there is documentation that the marketplace facilitator is registered with the DOR, and it will collect all applicable taxes on behalf of the marketplace seller made through the facilitator's marketplace. In addition, a marketplace seller is relieved of liability for all taxes on sales made through a marketplace facilitator if the marketplace seller is also a remote seller, and the marketplace facilitator provides the seller with written confirmation that the facilitator has elected to comply with notice and reporting requirements in lieu of collecting sales or use tax. The relief of liability does not affect the obligation of any purchaser to remit sales or use tax concerning any applicable taxable transaction in which the seller or seller's agent does not collect and remit sales tax.

Class action lawsuits are prohibited against a marketplace facilitator on behalf of buyers arising from overpayment of sales or use tax. In addition, this act is subject to compliance with the Streamlined Sales and Use Tax Agreement and federal law.

Nothing in this act relieves sellers or consumers currently subject to sales or use tax from their responsibilities under chapters 82.08 and 82.12 of the RCW, nor prevents the DOR from administering or enforcing those taxes.

Part III – Economic Nexus for B&O taxes. Economic nexus for B&O taxes is extended to persons engaged in retail sales so long as the person has more than \$267,000 in receipts from Washington or at least 25 percent of the person's total property, payroll or total receipts are in this state during the current or immediately preceding calendar year.

Part IV – Streamlined Sales Tax Mitigation to Local Governments. The streamlined sales tax mitigation payments to local governments are repealed as of October 1, 2019. Adjusted mitigation payments reflect the impact of marketplace fairness on local tax revenues.

Part V – Miscellaneous. This act applies prospectively and includes a savings clause, and a severability clause.

Appropriation: None.

Fiscal Note: Requested on June 30, 2017.

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

Effective Date: The bill contains an emergency clause and takes effect immediately, except for Sections 101-109, relating to tax preferences, which take effect August 1, 2017; Section 213, relating to tax collection, which takes effect August 23, 2017; and Sections 301-304, relating to excise taxes, which take effect July 1, 2017.