



TO: Elizabeth Pauli, City Manager
FROM: Andy Cherullo, Finance Director
COPY: Government Performance and Finance Committee
PRESENTER: Danielle Larson, Tax & License Division Manager
SUBJECT: Tacoma Municipal Code, Title 6 Amendments – November 5, 2019
DATE: October 22, 2019

PRESENTATION TYPE:

Request for Ordinance

SUMMARY:

Two mandatory changes to cities business and occupation (B&O) tax model ordinance were made by the 2019 State Legislation in Substitute House Bill 1403 and Second Substitute House Bill 1059. These mandatory changes require amendments to Tacoma Municipal Code Title 6A, Business & Occupation Tax with an effective date of January 1, 2020. Staff is recommending the mandatory amendments be forwarded to the full council for consideration.

BACKGROUND:

Legislation adopted in the 2003 session required all cities with local B&O taxes to adopt a city B&O tax model ordinance. (RCW 35.102) The last update occurred in 2012. Over the summer, a workgroup of cities, in consultation with the business community, revised the model ordinance to include the changes to RCW 35.102 and to reflect other changes made to state law since 2012. All cities with local B&O taxes are required to adopt the mandatory changes by the end of the year.

ISSUE:

SHB 1403 – Service & Other Apportioned B&O Tax

In 2017, state legislation directed city and business representatives to create a seven-member task to recommend changes to RCW 35.102.130 that would:

- simplify the two-factor apportionment formula for municipal business and occupation taxes;
- develop a method for assigning gross receipts to a local jurisdiction using a market-based model; and
- focus on methods that rely on information typically available in commercial transactions and captured by common business recordkeeping systems

The taskforce submitted a report to the Legislature on October 31, 2018. As a result, legislators passed SHB 1403 amending RCW 35.102.130.

2SHB 1059 – Change to Annual B&O Tax Filing Date

Independent Contractors receive IRS Form 1099 by January 31 of the year following payment. This does not leave ample time for independent contractors to prepare and file their annual tax return due on January 31. 2SHB 1059 requires cities to change the due date for annual B&O tax filers from January 31 to April 15 beginning in 2021.

ALTERNATIVES:

The mandatory amendments to Title 6 are required to be adopted by the end of 2019.



FISCAL IMPACT:

There is no fiscal impact to the 2019/2020 biennium.

RECOMMENDATION:

The mandatory amendments to Title 6 are required to be adopted by the end of 2019. Staff recommends the amendments to Title 6 be forwarded to the full council for consideration.

6A.10.040 Reporting periods – Due date – Filing Requirements – Threshold provisions – Failure to file returns.

A. The tax imposed by this subtitle shall be due and payable in quarterly installments. At the Director's discretion, businesses may be assigned to a monthly or annual reporting period depending on the tax amount owing or type of tax.

B. Tax payments are due on or before the last day of the next month following the end of the assigned reporting period covered by the return, unless it is a Saturday, Sunday, or City or federal legal holiday, in which case the due date shall be the next succeeding day which is neither a Saturday, Sunday, or City or federal legal holiday. Effective January 1, 2021, for annual filers, tax payments, along with reports and returns on forms prescribed by the department are due on or before April 15th of the year immediately following the end of the period covered by the return as provided in RCW 82.32.045(2).

C. Taxes shall be paid as provided in this subtitle and accompanied by a return on forms as prescribed by the Director. The return shall be signed by the taxpayer personally or by a responsible officer or agent of the taxpayer. The individual signing the return shall swear or affirm that the information in the return is complete and true.

D. Tax returns must be filed and returned by the due date whether or not any tax is owed, except that persons whose gross income is exempt from taxation under 6A.30.90.V are not required to submit a tax return.

E. For purposes of the tax imposed by Chapter 6A.30, any person whose value of products, gross proceeds of sales, or gross income of the business, subject to tax after all allowable deductions, is equal to or less than \$20,000 in the current calendar year shall file a return, declare no tax due on their return, and submit the return to the Director. The gross receipts and deduction amounts shall be entered on the tax return even though no tax may be due, except that persons whose gross income is exempt from taxation under 6A.30.90.V are not required to submit a tax return.

F. A taxpayer that commences to engage in business activity shall file a return and pay the tax for the portion of the reporting period during which the taxpayer is engaged in business activity.

G. If any taxpayer fails, neglects, or refuses to make a return as and when required in this subtitle, the Director is authorized to determine the amount of the tax payable by obtaining facts and information upon which to base the Director's estimate of the tax due. Such assessment shall be deemed prima facie correct and shall be the amount of tax owed to the City by the taxpayer. The Director shall notify the taxpayer of the amount of tax so determined, together with any penalty, interest, and fees due; the total of such amounts shall thereupon become immediately due and payable.

6A.30.077 Allocation and apportionment of income when activities take place in more than one jurisdiction.

For tax reporting periods beginning January 1, 2008, gross income, other than persons subject to the provisions of chapter 82.14A RCW, shall be allocated and apportioned as follows:

A. Gross income derived from all activities other than those taxed as service or royalties under 6A.30.050(A)(9) shall be allocated to the location where the activity takes place.

B. In the case of sales of tangible personal property, the activity takes place where delivery to the buyer occurs.

C. In the case of sales of digital products, the activity takes place where delivery to the buyer occurs. The delivery of digital products will be deemed to occur at:

1. The seller's place of business if the purchaser receives the digital product at the seller's place of business;
2. If not received at the seller's place of business, the location where the purchaser or the purchaser's donee, designated as such by the purchaser, receives the digital product, including the location indicated by instructions for delivery to the purchaser or donee, known to the seller;
3. If the location where the purchaser or the purchaser's donee receives the digital product is not known, the purchaser's address maintained in the ordinary course of the seller's business when use of this address does not constitute bad faith;
4. If no address for the purchaser is maintained in the ordinary course of the seller's business, the purchaser's address obtained during the consummation of the sale, including the address of a purchaser's payment instrument, if no other address is available, when use of this address does not constitute bad faith; and
5. If no address for the purchaser is obtained during the consummation of the sale, the address where the digital good or digital code is first made available for transmission by the seller or the address from which the digital automated service or service described in RCW 82.04.050 (2)(g) or (6)(b) was provided, disregarding for these purposes any location that merely provided the digital transfer of the product sold.

D. If none of the methods in subsection 6A.30.077.C for determining where the delivery of digital products occurs are available after a good faith effort by the taxpayer to apply the methods provided in subsections 6A.30.077.C.1 through 6A.30.077.C.5, then the city and the taxpayer may mutually agree to employ any other method to effectuate an equitable allocation of income from the sale of digital products. The taxpayer will be responsible for petitioning the city to use an alternative method under this subsection 6A.30.077.D. The city may employ an alternative method for allocating the income from the sale of digital products if the methods provided in subsections 6A.30.077.C.1 through 6A.30.077.C.5 are not available and the taxpayer and the city are unable to mutually agree on an alternative method to effectuate an equitable allocation of income from the sale of digital products.

E. For purposes of subsections 6A.30.077.C.1 through 6A.30.077.C.5, the following definitions apply:

1. "Digital automated services," "digital codes," and "digital goods" have the same meaning as in RCW 82.04.192;

2. "Digital products" means digital goods, digital codes, digital automated services, and the services described in RCW 82.04.050(2)(g) and (6)(c); and

3. "Receive" has the same meaning as in RCW 82.32.730.

F. Effective January 1, 2020, Gross income derived from activities taxed as services and other activities taxed under 6A.30.050(A)(9) shall be apportioned to the city by multiplying apportionable income by a fraction, the numerator of which is the payroll factor plus the service-income factor and the denominator of which is two.

~~(1)~~ The payroll factor is a fraction, the numerator of which is the total amount paid in the city during the tax period by the taxpayer for compensation and the denominator of which is the total compensation paid everywhere during the tax period. Compensation is paid in the city if:

- a. The individual is primarily assigned within the city;
- b. The individual is not primarily assigned to any place of business for the tax period and the employee performs 50 percent or more of the individual's service for the tax period in the city; or

c. The individual is not primarily assigned to any place of business for the tax period, the individual does not perform 50 percent or more of the individual's service in any city and the employee resides in the city.

~~(2.)~~ The service income factor is a fraction, the numerator of which is the total service income of the taxpayer in the city during the tax period, and the denominator of which is the total service income of the taxpayer everywhere during the tax period. Service income is in the city if the customer location is in the city.

~~a. The customer location is in the city; or~~

~~b. The income producing activity is performed in more than one location and a greater proportion of the service income producing activity is performed in the city than in any other location, based on costs of performance, and the taxpayer is not taxable at the customer location; or~~

~~c. The service income producing activity is performed within the city, and the taxpayer is not taxable in the customer location.~~

3. Gross income of the business from engaging in an apportionable activity must be excluded from the denominator of the service income factor if, in respect to such activity, at least some of the activity is performed in the city, and the gross income is attributable under (b) of this subsection (6) to a city or unincorporated area of a county within the United States or to a foreign country in which the taxpayer is not taxable. For purposes of this subsection (6)(c), "not taxable" means that the taxpayer is not subject to a business activities tax by that city or county within the United States or by that foreign country, except that a taxpayer is taxable in a city or county within the United States or in a foreign country in which it would be deemed to have a substantial nexus with the city or county within the United States or with the foreign country under the standards in RCW 35.102.050 regardless of whether that city or county within the United States or that foreign country imposes such a tax.

34. If the allocation and apportionment provisions of this subsection do not fairly represent the extent of the taxpayer's business activity in the city~~or cities in which the taxpayer does business,~~ the taxpayer may petition for or the tax administrators may ~~jointly~~ require, in respect to all or any part of the taxpayer's business activity, ~~that one of the following methods be used jointly by the cities to allocate or apportion gross income,~~ if reasonable:

a. Separate accounting;

~~b. The use of a single factor~~The exclusion of any one or more of the factors;

c. The inclusion of one or more additional factors that will fairly represent the taxpayer's business activity in the city; or

d. The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

5. The party petitioning for, or the tax administrator requiring, the use of any method to effectuate an equitable allocation and apportionment of the taxpayer's income pursuant to subsection (4) of this subsection (F) must prove by a preponderance of the evidence:

a. That the allocation and apportionment provisions of this subsection (6) do not fairly represent the extent of the taxpayer's business activity in the city; and

b. That the alternative to such provisions is reasonable.

The same burden of proof shall apply whether the taxpayer is petitioning for, or the tax administrator is requiring, the use of an alternative, reasonable method to effectuate an equitable allocation and apportionment of the taxpayer's income.

6. If the tax administrator requires any method to effectuate an equitable allocation and apportionment of the taxpayer's income, the tax administrator cannot impose any civil or criminal penalty with reference to the tax due that is attributable to the taxpayer's reasonable reliance solely on the allocation and apportionment provisions of this subsection (F).

7. A taxpayer that has received written permission from the tax administrator to use a reasonable method to effectuate an equitable allocation and apportionment of the taxpayer's income shall not have that permission revoked with respect to transactions and activities that have already occurred unless there has been a material change in, or a material misrepresentation of, the facts provided by the taxpayer upon which the tax administrator reasonably relied in approving a reasonable alternative method.

G. The definitions in this subsection apply throughout this section unless otherwise provided for periods prior to January 1, 2020.

"Apportionable income" means the gross income of the business taxable under the service classifications of a city's gross receipts tax, including income received from activities outside the city if the income would be taxable under the service classification if received from activities within the city, less any exemptions or deductions available.

"Business activities tax" means a tax measured by the amount of, or economic results of, business activity conducted in a city or county within the United States or within a foreign country. The term includes taxes measured in whole or in part on net income or gross income or receipts. "Business activities tax" does not include a sales tax, use tax, or a similar transaction tax, imposed on the sale or acquisition of goods or services, whether or not denominated a gross receipts tax or a tax imposed on the privilege of doing business.

"Compensation" means wages, salaries, commissions, and any other form of remuneration paid to individuals for personal services that are or would be included in the individual's gross income under the federal internal revenue code.

"Customer" means a person or entity to whom the taxpayer makes a sale or renders services or from whom the taxpayer otherwise receives gross income of the business.

"Customer location" means the following: city or unincorporated area of a county where the majority of the contacts between the taxpayer and the customer take place.

i. For a customer not engaged in business, if the service requires the customer to be physically present, where the service is performed.

ii. For a customer not engaged in business, if the service does not require the customer to be physically present:

1. The customer's residence; or
2. If the customer's residence is not known, the customer's billing/mailling address.

iii. For a customer engaged in business:

1. Where the services are ordered from;
2. At the customer's billing/mailling address if the location from which the services are ordered is not known; or
3. At the customer's commercial domicile if none of the above are known

"Individual" means any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee of that taxpayer.

~~"Customer location" means the city or unincorporated area of a county where the majority of the contacts between the taxpayer and the customer take place.~~

"Primarily assigned" means the business location of the taxpayer where the individual performs their duties.

"Service-taxable income" or "service income" means gross income of the business subject to tax under either the service or royalty classification.

"Tax period" means the calendar year during which tax liability is accrued. If taxes are reported by a taxpayer on a basis more frequent than once per year, taxpayers shall calculate the factors for the previous calendar year for reporting in the current calendar year and correct the reporting for the previous year when the factors are calculated for that year, but not later than the end of the first quarter of the following year.

~~"Taxable in the customer location" means either that a taxpayer is subject to a gross receipts tax in the customer location for the privilege of doing business, or that the government where the customer is located has the authority to subject the taxpayer to gross receipts tax regardless of whether, in fact, the government does so.~~

~~H. For periods prior to January 1, 2020, the following language is still in effect:~~

~~Sec. 6A.30.077(F)(2) provides "The service income factor is a fraction, the numerator of which is the total service income of the taxpayer in the city during the tax period, and the denominator of which is the total service income of the taxpayer everywhere during the tax period. Service income is in the city if:~~

~~(i) The customer location is in the city; or~~

~~(ii) The income-producing activity is performed in more than one location and a greater proportion of the service-income-producing activity is performed in the city than in any other location, based on costs of performance, and the taxpayer is not taxable at the customer location; or~~

~~(iii) The service-income-producing activity is performed within the city, and the taxpayer is not taxable in the customer location."~~

~~Sec. 6A.30.077(G) provides "Customer location" means the city or unincorporated area of a county where the majority of the contacts between the taxpayer and the customer take place.~~

~~Sec. 6A.30.077(G) provides "Taxable in the customer location" means either that a taxpayer is subject to a gross receipts tax in the customer location for the privilege of doing business, or that the government where the customer is located has the authority to subject the taxpayer to gross receipts tax regardless of whether, in fact, the government does so.~~

~~H~~I. Assignment or apportionment of revenue under this Section shall be made in accordance with and in full compliance with the provisions of the interstate commerce clause of the United States Constitution where applicable.

6A.30.090 Exemptions.

A. Certain fraternal and beneficiary organizations. This chapter shall not apply to fraternal benefit societies or fraternal fire insurance associations as described in Chapter 48 RCW; nor to beneficiary corporations or societies organized under and existing by virtue of Chapter 24 RCW, if such beneficiary corporations or societies provide in their bylaws for the payment of death benefits. This exemption is limited, however, to gross income from premiums, fees, assessments, dues, or other charges directly attributable to the insurance or death benefits provided by such societies, associations, or corporations.

B. Credit unions. This chapter shall not apply to the gross income of credit unions organized under the laws of this state, any other state, or the United States.

C. Nonprofit health care organization fees. This chapter shall not apply to amounts derived from medical, nursing, ambulance, hospital, and other appropriate outpatient care as charges and service fees by nonprofit health care organizations for the benefit of subscribers where none of such fees and charges inure to the benefit of the organization or any of its employees, provided further that if a nonprofit health care organization's annual gross income, minus any allowed deductions or exemptions as provided in this chapter, exceeds \$30,000,000.00 for any calendar year the deduction shall not apply to the amounts derived from health care organization service fees and charges.

D. Public utilities – Gambling. This chapter shall not apply to the business activity of any person to which tax liability is specifically imposed under the provisions of Chapters 6A.40 (Communications Tax), 6A.50 (Electricity Business and Solid Waste Collection), 6A.60 (Gambling), and 6A.90 (Natural or Manufactured Gas Tax).

E. Investments – dividends from subsidiary corporations. This chapter shall not apply to amounts derived by persons other than those engaging in banking, loan, security, or other financial businesses, from investments or the use of money as such, and also amounts derived as dividends by a parent from its subsidiary corporations.

F. International banking facilities. This chapter shall not apply to the gross receipts of an international banking facility. As used in this subsection, an “international banking facility” means a facility represented by a set of asset and liability accounts segregated on the books and records of a commercial bank, the principal office of which is located in this state, and which is incorporated and doing business under the laws of the United States or of this state, a United States branch or agency of a foreign bank, an Edge corporation organized under Section 25(a) of the Federal Reserve Act, 12 United States Code 611-631, or an Agreement corporation having an agreement or undertaking with the Board of Governors of the Federal Reserve System under Section 25 of the Federal Reserve Act, 12 United States Code 601-604(a), that includes only international banking facility time deposits (as defined in subsection (a)(2) of Section 204.8 of Regulation D (12 CFR Part 204), as promulgated by the Board of Governors of the Federal Reserve System), and international banking facility extensions of credit (as defined in subsection (a)(3) of Section 204.8 of Regulation D).

G. Insurance business. This chapter shall not apply to amounts received by any person who is an insurer or their appointed insurance producer upon which a tax based on gross premiums is paid to the state pursuant to RCW 48.14.020; and provided further, that the provisions of this subsection shall not exempt any bonding company from tax with respect to gross income derived from the completion of any contract as to which it is a surety, or as to any liability as successor to the liability of the defaulting contractor.

H. Farmers – agriculture. This chapter shall not apply to any farmer with respect to amounts received from selling fruits, vegetables, berries, butter, eggs, fish, milk, poultry, meats, or any other agricultural product that is raised, caught, produced, or manufactured by such persons.

I. Athletic exhibitions. This chapter shall not apply to any person with respect to the business of conducting boxing contests and sparring or wrestling matches and exhibitions for the conduct of which a license must be secured from the Washington State Boxing Commission.

J. Racing. This chapter shall not apply to any person with respect to the business of conducting race meets for the conduct of which a license must be secured from the Washington State Horse Racing Commission.

K. Ride sharing. This chapter does not apply to any funds received in the course of commuter ride sharing or ride sharing for persons with special transportation needs in accordance with RCW 46.74.010.

L. Employees.

1. This chapter shall not apply to any person with respect to the person's employment in the capacity as an employee or servant as distinguished from that of an independent contractor. For the purposes of this

subsection, the definition of employee shall include those persons that are defined in the Internal Revenue Code, as hereafter amended.

2. A booth renter is an independent contractor for purposes of this chapter.

M. Amounts derived from sale of real estate. This chapter shall not apply to gross proceeds derived from the sale of real estate. This, however, shall not be construed to allow an exemption of amounts received as commissions from the sale of real estate, nor as fees, handling charges, discounts, interest or similar financial charges resulting from or relating to real estate transactions. This chapter shall also not apply to amounts received for the rental of real estate, if the rental income is derived from a contract to rent for a continuous period of 30 days or longer.

N. Mortgage brokers' third-party provider services trust accounts. This chapter shall not apply to amounts received from trust accounts to mortgage brokers for the payment of third-party costs if the accounts are operated in a manner consistent with RCW 19.146.050 and any rules adopted by the director of financial institutions.

O. Amounts derived from manufacturing, selling, or distributing motor vehicle fuel. This chapter shall not apply to the manufacturing, selling, or distributing motor vehicle fuel, as the term "motor vehicle fuel" is defined in RCW ~~82.36.010~~82.38.020 and exempt under RCW ~~82.36.440~~82.38.280, provided that any fuel not subject to the state fuel excise tax or any other applicable deduction or exemption will be taxable under this chapter.

P. Amounts derived from liquor, and the sale or distribution of liquor. This chapter shall not apply to liquor as defined in RCW 66.04.010 and exempt in RCW 66.08.120.

Q. Accommodation sales. This chapter shall not apply to sales for resale by persons regularly engaged in the business of making retail sales of the type of property so sold to other persons similarly engaged in the business of selling such property where (1) the amount paid by the buyer does not exceed the amount paid by the seller to the vendor in the acquisition of the article, and (2) the sale is made as an accommodation to the buyer to enable the buyer to fill a bona fide existing order of a customer or is made within 14 days to reimburse in-kind a previous accommodation sale by the buyer to the seller.

R. Casual and isolated sales. This chapter shall not apply to the gross proceeds derived from casual or isolated sales.

S. Taxes collected as trust funds. This chapter shall not apply to amounts collected by the taxpayer from third parties to satisfy third party obligations to pay taxes such as the retail sales tax, use tax, and admission tax.

T. The gross income received by the United States or any instrumentality thereof and by the state of Washington or any municipal subdivision thereof; provided, however, that the exemption contained in this subsection shall only apply to gross income which the City is prohibited from taxing pursuant to the terms of any federal or state law.

U. Any person with respect to a business activity conducted in an area that, after the date hereof, has become part of the City by annexation; provided, however, that the business premises of such person be located in the said area on the date of annexation; and provided, further, that the exemption provided herein shall cease at the end of the calendar quarter three years after the date of such annexation.

V. Those persons whose gross proceeds of sales or gross income of the business both from within and outside the City for the entire calendar year do not exceed a minimum threshold of \$50,000 through December 31, 1998; \$55,000 from January 1 through December 31, 1999; \$60,000 from January 1, 2000, through December 31, 2000; \$65,000 from January 1, 2001, through December 31, 2001; \$70,000 from January 1, 2002 through December 31, 2008, \$72,500 from January 1, 2009 through December 31, 2009, \$75,000 from January 1, 2010 through December 31, 2010 and \$250,000 from January 1, 2011, and thereafter shall be exempt from the tax imposed under this Subtitle 6A and will not be required to submit

a tax return; provided, however, that said persons shall still be obligated to obtain a registration certificate.

Tax Period Year	Gross Income Threshold
1998 and prior years	\$50,000
1999	\$55,000
2000	\$60,000
2001	\$65,000
2002 through 2008	\$70,000
2009	\$72,500
2010	\$75,000
2011 and beyond	\$250,000

W. Amounts received from the sale of licenses to use grave sites and related finance charges by persons owning or operating cemeteries located within the City; provided, however, that this exemption shall not apply to amounts derived from the sale of licenses to use crypts or cremation niches located in mausoleums.