Multiple Agency Fiscal Note Summary

Bill Number: 2030 E HB	**Title:** Municipal b & o tax

Estimated Cash Receipts

Agency Name	2003-05		2005-07		2007-09	
	GF- State	Total	GF- State	Total	GF- State	Total
Total $						

Local Gov. Courts *						
Local Gov. Other **		(1,210,431)		(4,841,722)		(49,798,143)
Local Gov. Total		(1,210,431)		(4,841,722)		(49,798,143)

Estimated Expenditures

Agency Name	2003-05			2005-07			2007-09		
	FTEs	GF-State	Total	FTEs	GF-State	Total	FTEs	GF-State	Total
Department of Revenue	.6	103,500	103,500	.0	0	0	.0	0	0
Municipal Research Council	.0	0	0	.0	0	0	.0	0	0
Total	0.6	$103,500	$103,500	0.0	$0	$0	0.0	$0	$0

Local Gov. Courts *									
Local Gov. Other **			420,000			112,000			112,000
Local Gov. Total			420,000			112,000			112,000

Prepared by: Doug Jenkins, OFM	**Phone:** 360-902-0563	**Date Published:** Revised 4/16/2003

* See Office of the Administrator for the Courts judicial fiscal note

** See local government fiscal note

Department of Revenue Fiscal Note

Bill Number: 2030 E HB	Title: Municipal b & o tax	Agency: 140-Department of Revenue

Part I: Estimates

☐ **No Fiscal Impact**

Estimated Cash Receipts to:

FUND					
Total $					

Estimated Expenditures from:

	FY 2004	**FY 2005**	**2003-05**	**2005-07**	**2007-09**
FTE Staff Years	1.3		0.6		
Fund					
GF-STATE-State 001-1	103,500		103,500		
Total $	103,500		103,500		

The cash receipts and expenditure estimates on this page represent the most likely fiscal impact. Factors impacting the precision of these estimates, and alternate ranges (if appropriate), are explained in Part II.

Check applicable boxes and follow corresponding instructions:

☒ If fiscal impact is greater than $50,000 per fiscal year in the current biennium or in subsequent biennia, complete entire fiscal note form Parts I-V.

☐ If fiscal impact is less than $50,000 per fiscal year in the current biennium or in subsequent biennia, complete this page only (Part I).

☐ Capital budget impact, complete Part IV.

☐ Requires new rule making, complete Part V.

Legislative Contact:	Phone:	Date: 03/20/2003
Agency Preparation: Don Gutmann	Phone: 360-570-6073	Date: 03/26/2003
Agency Approval: Don Taylor	Phone: 360-570-6083	Date: 03/26/2003
OFM Review: Doug Jenkins	Phone: 360-902-0563	Date: 03/26/2003

Part II: Narrative Explanation

II. A - Brief Description Of What The Measure Does That Has Fiscal Impact

Briefly describe, by section number, the significant provisions of the bill, and any related workload or policy assumptions, that have revenue or expenditure impact on the responding agency.

Section 1: This legislation intends to provide for a more uniform system of city business and occupation taxes that eliminates multiple taxation, while allowing for some continued local control and flexibility to cities.

Section 2: Specifically states that this proposal does not apply to service that historically or traditionally has been taxed as a utility business.

Section 3 contains definitions for a "business", a "city", and a "business and occupation tax".

Section 4: Requires the Association of Washington Cities to adopt a model ordinance on municipal business and occupation tax. Requires the Association of Washington Cities to seek input on the Model Ordinance from statewide business associations and local chambers of commerce in cities that levy a gross receipts business and occupation tax.

Requires the Municipal Research Council and any city that imposes a business and occupation tax to make copies of its ordinance available upon request. Requires the Department of Revenue and the Department of Licensing to post copies or links to the model ordinance on their internet web sites.

Restricts the cities to amending the definitions and tax classifications in the Model Ordinance no more than once every four years. However the model ordinance may be amended at any time to comply with changes in state law. Any amendment to a mandatory provision of the model ordinance must be adopted with the same effective date by all cities.

Requires the Association of Washington Cities to use the definitions in Chapter 82.04 RCW as the baseline for all definitions in the Model Ordinance. Any deviation in the Model Ordinance from these definitions must be described by a comment in the model ordinance.

Allows any city to adopt its own provisions for tax exemptions, tax credits, and tax deductions, except for the system of credits developed to address multiple taxation.

Any city that adopts an ordinance that deviates from the non-mandatory provisions of the model ordinance shall make a description of such differences available to the public, in written and electronic form.

Section 5 states that a city may not impose a business and occupation tax on a person unless that person has nexus with the city. Nexus is defined as "business activities conducted by a person sufficient to subject that person to the taxing jurisdiction of a city under the standards established for interstate commerce under the commerce clause of the United State Constitution."

Section 6: Requires the adoption of a system of credits to prevent the multiple taxation of the same income.

Section 7: Allows cities to determine the frequency of reporting and payment of tax (monthly, quarterly, or annual). However, the due dates must coincide with the state's reporting schedule.

Sections 8-11: Requires interest on assessments and refunds/credits and the imposition of penalties to mirror administrative provisions for state excise taxes.

Section 12: Includes mandatory definitions that must be included in the model ordinance and adopted by cities. Software development is not included in the definition of manufacturing.

Section 13 establishes specific guidelines for apportioning income between cities for various types of activities such as retail, wholesale, services and royalty income.

Section 14 requires that all cities imposing business and occupation taxes must comply with all requirements of sections 2 through 12 of this act by December 31, 2004.

Section 15 requires the Department of Revenue to conduct a study of the net fiscal impacts of this act with an emphasis on the revenue impacts of the apportionment and allocation method contained in this proposal. The Department shall report the final results of the study to the Governor and the fiscal committees of the Legislature by November 30, 2005. Progress reports are due on November 30, 2003 and November 30, 2004.

Section 16 requires the Department of Revenue to report by December 31, 2004 to the Governor and the fiscal committees of the Legislature on the definitions used in the proposed model ordinance. The report shall detail the status of the definitions noting any deviations from the definitions in chapter 82.04 RCW and the reason for such deviation. The report shall also estimate the fiscal impact on taxpayers of any deviations from the definitions under Chapter 82.04 RCW.

Section 19 states that Section 13 of this act takes effect January 1, 2008.

II. B - Cash receipts Impact

Briefly describe and quantify the cash receipts impact of the legislation on the responding agency, identifying the cash receipts provisions by section number and when appropriate the detail of the revenue sources. Briefly describe the factual basis of the assumptions and the method by which the cash receipts impact is derived. Explain how workload assumptions translate into estimates. Distinguish between one time and ongoing functions.

ASSUMPTIONS/DATA SOURCES

N/A

AUDIT ASSESSMENTS (Impact resulting from recent audit activity)

N/A

CURRENTLY REPORTING TAXPAYERS (Impact for taxpayers who are known or estimated to be currently paying the tax in question)

This proposal will have no impact on state revenues.

Changing local B&O tax definitions to conform to state definitions and the apportionment guidelines could adversely impact municipal revenues for some cities. The decrease in revenues could be significant.

TAXPAYERS NOT CURRENTLY REPORTING (Although some taxpayers may not now be paying the tax in question, some of them will become aware of their liability in the future, as a result of normal enforcement activities or education programs by the Department. The impact for such taxpayers is based on the Department's studies of average tax compliance)

N/A

TOTAL REVENUE IMPACT:

State Government (cash basis, $000): None.

Local Government, if applicable (cash basis, $000): See text.

II. C - Expenditures

Briefly describe the agency expenditures necessary to implement this legislation (or savings resulting from this legislation), identifying by section number the provisions of the legislation that result in the expenditures (or savings). Briefly describe the factual basis of the assumptions and the method by which the expenditure impact is derived. Explain how workload assumptions translate into cost estimates. Distinguish between one time and ongoing functions.

(Contact: Gil Brewer, 570-6133)

Section 15 of the bill requires the Department to conduct a study of the net fiscal impacts of this act with an emphasis on the revenue impacts of the apportionment and allocation method contained in this proposal. The Research Division will require 1.0 FTE to perform this study.

Section 16 of the bill requires the Department to report on the definitions used in the model ordinance developed under the bill. This will require 0.01 FTE in the Legislation and Policy Division to determine the status of definitions in the model ordinance. The Research Division will require 0.25 FTE to obtain the necessary data and develop the estimate of the fiscal impact due to deviations from the state definitions. This figure is approximate and may vary according to the difficulties in obtaining satisfactory data.

Without an appropriation to cover the expenditure impact, the Department may not be able to fully implement the legislation.

Part III: Expenditure Detail

III. A - Expenditures by Object Or Purpose

	FY 2004	FY 2005	2003-05	2005-07	2007-09
FTE Staff Years	1.3		0.6		
A-	67,900		67,900		
B-	17,700		17,700		
E-	7,800		7,800		
J-	10,100		10,100		
Total $	$103,500		$103,500		

III. B - Detail: *List FTEs by classification and corresponding annual compensation. Totals need to agree with total FTEs in Part I and Part IIIA*

Job Classification	**Salary**	FY 2004	FY 2005	2003-05	2005-07	2007-09
Tax Policy Specialist 1	42,588	0.3		0.1		
Tax Policy Specialist 3	57,252	1.0		0.5		
Total FTE's		1.3		0.6		

Part IV: Capital Budget Impact

None.

Part V: New Rule Making Required

Identify provisions of the measure that require the agency to adopt new administrative rules or repeal/revise existing rules.

None.

Individual State Agency Fiscal Note

Bill Number: 2030 E HB	Title: Municipal b & o tax	Agency: 144-Municipal Research Council

Part I: Estimates

☒ **No Fiscal Impact**

The cash receipts and expenditure estimates on this page represent the most likely fiscal impact. Factors impacting the precision of these estimates, and alternate ranges (if appropriate), are explained in Part II.

Check applicable boxes and follow corresponding instructions:

☐ If fiscal impact is greater than $50,000 per fiscal year in the current biennium or in subsequent biennia, complete entire fiscal note form Parts I-V.

☐ If fiscal impact is less than $50,000 per fiscal year in the current biennium or in subsequent biennia, complete this page only (Part I).

☐ Capital budget impact, complete Part IV.

☐ Requires new rule making, complete Part V.

Legislative Contact:		Phone:	Date: 03/20/2003
Agency Preparation:	Stephen Buxbaum	Phone: 360.725-3005	Date: 03/24/2003
Agency Approval:	Stephen Buxbaum	Phone: 360.725-3005	Date: 03/25/2003
OFM Review:	Robin Campbell	Phone: 360-902-0575	Date: 03/27/2003

Part II: Narrative Explanation

II. A - Brief Description Of What The Measure Does That Has Fiscal Impact

Briefly describe, by section number, the significant provisions of the bill, and any related workload or policy assumptions, that have revenue or expenditure impact on the responding agency.

Sec. 4b: Requires the Municipal Research Council (MRC) to post a model municipal Business and Occupation (B&O) tax ordinance on an Internet web site and make paper copies available for inspection upon request.

ENGROSSED HOUSE BILL 2030 CHANGES:

None relating to sections of the bill that involve the MRC.

II. B - Cash receipts Impact

Briefly describe and quantify the cash receipts impact of the legislation on the responding agency, identifying the cash receipts provisions by section number and when appropriate the detail of the revenue sources. Briefly describe the factual basis of the assumptions and the method by which the cash receipts impact is derived. Explain how workload assumptions translate into estimates. Distinguish between one time and ongoing functions.

II. C - Expenditures

Briefly describe the agency expenditures necessary to implement this legislation (or savings resulting from this legislation), identifying by section number the provisions of the legislation that result in the expenditures (or savings). Briefly describe the factual basis of the assumptions and the method by which the expenditure impact is derived. Explain how workload assumptions translate into cost estimates. Distinguish between one time and ongoing functions.

Sec. 4b would have no fiscal impact on the MRC, because posting a model municipal B&O tax ordinance could be accomplished as part of its existing contract with the Muncipal Research Service Center (MRSC).

ASSUMPTIONS:

The intent of the legislation is for the MRC to post the model ordinance but not write it.

Part III: Expenditure Detail

Part IV: Capital Budget Impact

Part V: New Rule Making Required

Identify provisions of the measure that require the agency to adopt new administrative rules or repeal/revise existing rules.

LOCAL GOVERNMENT FISCAL NOTE

Revised

Department of Community, Trade and Economic Development

Bill Number: 2030 E HB	**Title:** Municipal b & o tax

Part I: Jurisdiction-Location, type or status of political subdivision defines range of fiscal impacts.

Legislation Impacts:

- [X] Cities:
- [ ] Counties:
- [ ] Special Districts:
- [ ] Specific jurisdictions only:
- [ ] Variance occurs due to:

Part II: Estimates

- [ ] No fiscal impacts.
- [X] Expenditures represent one-time costs:
- [ ] Legislation provides local option:
- [ ] Key variables cannot be estimated with certainty at this time:

Estimated revenue impacts to:

Jurisdiction	FY 2004	FY 2005	2003-05	2005-07	2007-09
City		(1,210,431)	(1,210,431)	(4,841,722)	(49,798,143)
County					
Special District					
TOTAL $		(1,210,431)	(1,210,431)	(4,841,722)	(49,798,143)
GRAND TOTAL $					(55,850,296)

Estimated expenditure impacts to:

Jurisdiction	FY 2004	FY 2005	2003-05	2005-07	2007-09
City		420,000	420,000	112,000	112,000
County					
Special District					
TOTAL $		420,000	420,000	112,000	112,000
GRAND TOTAL $					644,000

Part III: Preparation and Approval

Fiscal Note Analyst: Linda Kercher	Phone: (360) 725-5038	Date: 03/31/2003
Leg. Committee Contact:	Phone:	Date: 03/20/2003
Agency Approval: Louise Deng Davis	Phone: (360) 725-5034	Date: 04/16/2003
OFM Review: Doug Jenkins	Phone: 360-902-0563	Date: 04/16/2003

Part IV: Analysis

A. SUMMARY OF BILL

Provide a clear, succinct description of the bill with an emphasis on how it impacts local government.

This bill requires cities that levy a business and occupation tax to impose a model ordinance, which must provide for a uniform system of credits, small business tax threshold, tax reporting frequency, penalty and interest provisions, claim periods, refund provisions, tax classifications and definitions. Additionally, the bill includes a nexus requirement and a provision for apportionment of gross income among cities.

Section 2 limits the scope of this bill by excluding from municipal B&O tax services that historically have been taxed as a utility business.

Section 3 provides definitions for “business,” “city,” “business and occupation tax” or “gross receipts tax,” “value of products,” “gross income of the business” and “gross proceeds of sales.”

Section 4 requires cities to form a model ordinance development committee, working through the Association of Washington Cities, to develop a model ordinance. The section also requires that cities imposing a B&O tax adopt the mandatory provisions of the model ordinance. The section provides that mandatory provisions are:

· A system of credits
· A uniform, minimum small business tax threshold of $20,000 in gross income. If a city has in place a higher threshold as of Jan. 1, 2003, and chooses to drop below that threshold, it must notify all licensed businesses before implementing the lower threshold.
· Tax reporting frequencies
· Penalty and interest provisions
· Claim periods
· Refund provisions
· Definitions under Section 3 and tax classification definitions under Section 12

Section 4 also provides that a city may adopt its own provisions for tax exemptions, credits and deductions, and that if a city deviates from the mandatory provisions of the model ordinance, it must make available a description of differences.

Section 5 requires that a nexus with the city exist for city to impose a B&O tax. The section defines nexus as business activity conducted by a person sufficient to subject that person to the taxing authority of a city under interstate commerce standards established in the interstate commerce clause of the U.S. Constitution.

Section 6 requires that a city provide for a system of credits to prevent multiple taxation of the same income.

Section 7 requires that cities allow tax reporting and payment on a monthly, quarterly or annual basis. Due dates must coincide with the state’s reporting schedule, and monthly reporting may only be assigned if a taxpayer is remitting excise tax monthly to the state.

Section 8 and 9 require that a city compute interest and penalties on underpaid tax and on refunds and credits according to state provisions for tax administration.

Section 10 requires that a city’s provisions relating to claim periods for assessment or correction of assessment for additional taxes, penalties or interest be in accordance with state provisions for tax administration

Section 11 requires a city’s provisions relating to refund periods to be in accordance with state provisions for tax administration.

Section 12 provides tax classification definitions that the model ordinance must include. Software development may not be included in the definition of manufacturing activity. The section also requires that any additional tax classification created in the model ordinance be uniform among cities.

Section 13 requires that a city imposing B&O tax provide for allocation and apportionment of gross income among other cities according to the rules provided in this section.

Section 14 requires that cities imposing a B&O tax comply with Sections 2 through 13 by Dec. 31, 2004, or they are prohibited from imposing a tax on the privilege of engaging in business activities. Cities imposing a B&O tax after Dec. 31, 2004, must comply with Sections 2 through 13.

Section 15 requires the Department of Revenue (DOR) to conduct a study of the net fiscal impact of this act, especially the impact of apportionment and allocation under Section 13. DOR is to consult with businesses and local government in conducting its study. It is to report results to the governor and legislative fiscal committees Nov. 30, 2005. DOR is to provide progress reports in November of 2003 and 2004.

Section 16 requires DOR, by Dec. 31, 2004, to report on definitions used in the proposed model ordinance and estimated fiscal impact on taxpayers of deviations in definitions.

Section 18 provides that the effective date of Section 13, the apportionment section, is Jan. 1, 2008.

DIFFERENCES FROM ORIGINAL BILL:
Section 4 adds the requirement that cities, with an existing threshold higher than required under this bill, notify businesses if they choose to lower their small business threshold.

Section 14 provides that Sections 2 through 13 must be complied with by Dec. 31, 2004. The original bill required cities to comply with Sections 2 through 12.

B. SUMMARY OF EXPENDITURE IMPACTS

Briefly describe and quantify the expenditure impacts of the legislation on local governments, identifying the expenditure provisions by section number, and when appropriate, the detail of expenditures. Delineate between city, county and special district impacts.

The one-time expenditure impact under this bill is estimated to be $420,000 in FY05 for the 28 cities that have not adopted the existing model ordinance developed through the Association of Washington Cities (AWC). Ongoing expenditures are estimated at $56,000 per year, beginning in FY06. (See "Methodology" below)

DISCUSSION:
A model ordinance, as required under this bill, has been developed and has been adopted or is in the adoption process by nine cities to date (Bellevue, Bellingham, Bremerton, Burien, Everett, Seattle, Shelton, Tacoma and Tumwater), according to AWC. In Washington, 37 cities impose a local B&O tax. Twenty-eight cities have not yet adopted the model ordinance and would therefore be required to adopt it under this bill.

A large city, Tacoma reports that in implementing the existing model ordinance, it incurred a one-time cost of $20,000 to reprogram its computer system. Tacoma also incurred one-time costs for redrafting and taxpayer education. The city anticipates spending an additional $5,000 to $10,000 per year to make computer system adjustments for interest rate computation. Tacoma estimates that ongoing costs could be higher under this bill because of the requirements in Section 8 and 9 that cities compute interest, penalties and refunds and credits according to RCW statutory provisions. Additionally, by linking computation to RCW provisions, cities would incur costs to update systems as changes to statutes are made. Another ongoing cost, enforcement costs, would rise if a city experiences a rise in appeals due to confusion over the apportionment provisions in Section 13, according to Seattle. A small city, Tumwater estimates that it spent $15,000 on printing and postage costs in implementing the model ordinance, and has no significant ongoing costs.

According to a 2002 LGFN survey, cities estimated the one-time cost of implementing similar bills requiring adoption of a model B&O ordinance to be $33,000 each and ongoing costs to be $2,000 each a year for software updates and postage. Most of the cities responding to that survey have adopted the model ordinance. Therefore the one-time costs reported in 2002 are assumed to have been incurred by these cities already and are not reported in this analysis. However, additional one-time costs are expected to be incurred under this bill.

Note: Everett, Seattle and Tacoma report that together, they incurred a one-time cost of $595,151 in developing the existing model ordinance. Bellingham reports it dedicated up to 300 hours of staff time in the model ordinance development process.

ASSUMPTIONS:
The cities of Tumwater and Westport are assumed to be representative of the 28 smaller cities that have not yet adopted the model ordinance.

It is assumed that the notification requirement in Section 4 will have no significant expenditure impact, because few cities currently have a small business threshold in excess of the $20,000 threshold under this bill. Therefore, few cities would be able to lower the threshold and trigger the notification requirement.

While local government representatives would be required to serve on the committee to advise DOR in its fiscal impact study as required under Section 15, it is assumed the cost of participation will be minimal.

METHODOLOGY:
Estimates provided to LGFN in March 2003 by Tumwater and estimates provided for a 2002 LGFN survey, conducted in regard to similar bills, were used to estimate one-time costs and ongoing costs for cities adopting a model ordinance under this bill. Tumwater and Westport estimate one-time costs at approximately $15,000, which is used as the standard for one-time costs. The average ongoing cost reported to LGFN in 2002 was $2,000 per year, which is used as the standard for ongoing costs in this analysis. Twenty-eight cities have not yet adopted the model ordinance, but would be required to do so under this bill. The expenditure estimate is calculated as follows:
One-time cost to cities: $15,000 x 28 = $420,000 (FY05 expenditure)
Ongoing costs: $2,000 x 28 = $56,000 (Yearly expenditure for FY06 and beyond)

C. SUMMARY OF REVENUE IMPACTS

Briefly describe and quantify the revenue impacts of the legislation on local governments, identifying the revenue provisions by section number, and when appropriate, the detail of revenue sources. Delineate between city, county and special district impacts.

Revenue loss to cities under this bill is estimated at $1.2 million in FY05, $2.4 million in FY06 and FY07, $17.4 million in FY08 and $32.4 million in FY09.

DISCUSSION:
Cities imposing a B&O tax would incur revenue losses of varying degrees under this bill, depending on how similar a city's existing ordinance is to the requirements under this bill. The cities expected to experience the greatest impact under this bill are those that have not yet implemented the model ordinance developed through AWC. Of the 37 cities in Washington imposing a B&O tax, 28 have not implemented or have not begun the adoption process for the model ordinance. These are smaller cities that account for approximately 9 percent of the municipal B&O tax revenue generated statewide, according to 2001 data from the State Auditor Local Government Finance Reporting System (LGFRS). Most smaller cities were not able to estimate anticipated revenue loss under this bill.

REVENUE LOSS – APPORTIONMENT (Section 13)
Total revenue loss under Section 13 of the bill is estimated at nearly $30 million per year.

The apportionment loss estimated by 13 reporting cities totals $28.8 million. Individual estimates are as follows:

Bainbridge Island	$60,000
Bellevue	$2,100,000
Bellingham	$1,000,000
Everett	$3,700,000
Issaquah	$240,000
Kelso	$40,000
Lacey	$0 (Negligible loss estimated)
Long Beach	$0 (Negligible loss estimated)
Seattle	$16,500,000
Shelton	$11,274
Tacoma	$5,000,000
Tumwater	$150,000
Westport	$5,000

Total	$28,806,274

NOTE: Seattle reports that its estimate was determined by examining taxpayer information for industries, such as service industries, which are known to conduct business at customer sites in multiple locations and industries in which products are delivered outside of the city.

An additional loss of $1.2 million is projected for the balance of B&O cities that did not provide an estimate above. Those 24 cities are estimated to lose an average of 8.9 percent of B&O revenues due to the apportionment section.
(See "Methodology" below)

The estimated revenue loss for reporting and non-reporting cities combined totals $29,970,947.

REVENUE LOSS – OTHER PROVISIONS OF THE BILL

Interest, Penalties and Refunds
Revenue loss on interest, penalties and refunds under Sections 8 and 9 is estimated at $1.3 million per year by Seattle. Under the model ordinance already adopted by Seattle and eight other cities, the city computes interest for assessments using the federal short-term rate PLUS two percentage points, and it computes interest for refunds using the federal short-term rate MINUS two percentage points. Under the requirements of this bill, interest for both assessments on underpaid taxes and refunds is to be calculated using the federal short-term rate PLUS two percentage points. This change to the refund computation is estimated to result in a revenue loss of $1,313,000 for Seattle. Other cities could not produce estimates for losses under these sections, but do anticipate a loss of revenue over and above the loss incurred in implementing the model ordinance.

Small Business Threshold
Revenue loss under the small business threshold requirement in Section 4(2)(b) is estimated at $467,861 per year. (See "Methodology" below) Under this bill, cities levying a B&O tax must implement a minimum small business tax threshold of $20,000 in gross income annually. This is expected to have the greatest impact on small cities with a large base of small business activity and a low threshold. Tumwater is an example of a smaller city that has implemented the model ordinance, which includes the $20,000 threshold. Prior to

implementing the model ordinance, Tumwater exempted from its B&O tax businesses with a gross income below $6,000 annually. By raising the threshold to $20,000, the city estimates that it will lose $25,000 per year. The City of Westport currently has a $500 threshold. Westport estimates it will lose $10,000 per year, about 2 percent of its total B&O revenue, by raising its threshold to $20,000. Shelton reports could lose $3,000 under the raised threshold, while Yelm estimates a $2,000 loss. The loss cities would experience under this section of the bill would depend on what their current small business threshold is and the number of small businesses operating in their jurisdiction.

Reclassification
Revenue loss due to reclassifications of taxable activity under this bill is estimated at $640,000 per year by Seattle. This estimate is based on loss of revenue from taxing software development. Under the model ordinance adopted by Seattle, software development can be taxed as a manufacturing activity. Under Section 12 of this bill, software development may not be defined as a manufacturing activity. This reclassification is estimated to result in a revenue loss of $640,000 per year for Seattle. Other cities could not produce estimates for revenue loss due to reclassifications. The extent of loss would depend on how similar a city's existing classifications are to the requirements under this bill.

Together, losses from interest computation, the small business threshold and reclassifications total $2.4 million per year.

Summary of Losses:
FY05 = $1,210,431
Total accounts for six months of losses from interest computation, the small business threshold and reclassifications only. FY05 reflects six months of loss, as compliance is assumed to be required beginning Dec. 31, 2004.

FY06-07 = $2,420,861 per year
Total accounts for a full year of losses from interest computation, the small business threshold and reclassifications only.

FY08 = $17,406,335
Total accounts for losses from interest computation, the small business threshold and reclassifications, plus six months of loss due to apportionment under Section 13. The apportionment section of the bill takes effect Jan. 1, 2008. Therefore, the revenue impact estimate for FY08 reflects six months of revenue loss due to apportionment.

FY09 and beyond = $32,391,808
Total accounts for losses from interest computation, the small business threshold and reclassifications, plus a full year of loss due to apportionment under Section 13.

ASSUMPTIONS:
It is assumed that compliance with Sections 2 through 13 is required by Dec. 31, 2004.

A loss of 2.47 percent is assumed to calculate the small business threshold loss. (See "Methodology" below)

METHODOLOGY:
Apportionment
The overall apportionment loss estimate is composed of two parts -- 1) individual estimates made by individual cities and 2) projections for the remaining cities.

The first part of the apportionment impact estimate reflects information provided by 13 cities, which account for more than 90 percent of the municipal B&O tax revenue generated statewide, according to LGFRS data. The 13 cities reporting revenue loss are Bainbridge Island, Bellevue, Bellingham, Everett, Issaquah, Kelso, Lacey, Long Beach, Seattle, Shelton, Tacoma, Tumwater and Westport. Lacey and Long Beach report no loss or negligible loss because their existing ordinances are already similar to requirements under this bill. The reported loss estimates as a percentage of a city's overall B&O revenue vary widely, from 1 percent (Westport) to 25 percent (Everett). When taken as a whole, the overall percentage loss for the reporting cities is 15 percent. This figure was calculated by totaling the loss estimate for the 13 reporting cities and dividing that total by the total B&O revenue collected by those cities in 2001 -- ($28,806,274) divided by $190,555,182 = 15.1%

The remaining cities (non-reporting cities) that levy a B&O tax did not or could not provide an individual loss estimate. To arrive at an estimate, an 8.9 percent loss rate was applied to the total B&O revenue collected by the remaining cities in 2001. The loss rate of 8.9 percent is derived from loss estimates provided by reporting cities with less than $3 million in B&O revenue. All of the non-reporting cities have B&O revenue of less than $3 million each.

The loss projection for non-reporting cities is as follows:
Combined 2001 B&O Revenue = $13,086,219
$13,086,219 x (0.089) = ($1,164,673)

The overall apportionment loss estimate totals $29,970,947 per year.
($28,806,274) + ($1,164,673) = ($29,970,947)

Small Business Threshold
A loss rate of 2.47 percent is assumed under the small business threshold provision. This percentage is based on the average estimated loss reported by five cities. The loss reported by the five cities (Shelton, Tacoma, Tumwater, Westport and Yelm) totalled $565,083. That is equal to 2.47 percent of the total B&O revenue collected by those five cities in 2001, according to LGFRS data.

Total municipal B&O revenue for 2001, excluding those cities that have implemented the model ordinance, is $18,941,742, according to LGFRS data. The revenue loss estimate under the small business threshold was calculated as follows:
$18,941,742 x 0.0247 = $467,861

Interest computation and reclassifications
The revenue losses due to interest computation changes and reclassifications are based on projections provided by Seattle, which accounts for 60 percent of the municipal B&O tax revenue generated statewide, according to LGFRS data.

SOURCES:
Association of Washington Cities
City of Seattle
City of Tacoma
City of Tumwater
Department of Revenue
2002 LGFN fiscal notes for HB 2658, Substitute HB 2658 and HB 2555
State Auditor Local Government Finance Reporting System