

WASHINGTON STATE TAX STRUCTURE STUDY

Administrative Simplicity - Findings

Department of Revenue Costs

- The long-term costs to the Department of Revenue to administer the state and local taxes it is responsible for have averaged 0.75%, or 75 cents per \$100 of tax collected.
- Relative collection costs have been declining in recent years, due to lower staffing levels and technological enhancements. Costs in Fiscal Year 2001 were 69 cents per \$100.
- Tax sources that are dedicated to fund specific programs are generally more complex and more costly to administer. Examples are the hazardous substance tax (\$4.26 per \$100) and the litter tax (\$12.94 per \$100).
- Taxes that are costly for the Department to collect are also generally difficult and costly for taxpayers to comply with.

Costs to Retailers to Collect and Remit State and Local Sales Taxes

- Retailers are unpaid agents of state and local government in the collection and remittance of the sales tax. More than one-half of the sales tax states compensate retailers for collection costs.
- Costs of collection for state and local sales taxes range from \$6.47 per \$100 for small retailers to \$0.97 per \$100 for large retailers.
- Costs for local sales tax only range from \$3.30 per \$100 for small retailers to \$0.31 per \$100 for large retailers.

Record Keeping Obligations for Taxpayers

- The majority of taxpayers use much of the information gathered to file the state portion of their state tax return for other purposes as well.
- Most taxpayers collect and organize data required to file the local portion of their state tax return only for this purpose.
- The lack of uniform definitions of activities between cities, and between the cities and the state system, adds to taxpayer costs to comply with city-imposed B&O taxes based on gross receipts. Rules for allocation of income between entities are inconsistent, and apportionment of income rarely occurs.

Simplicity

- 1) Does our tax system impose record keeping and/or paperwork obligations on taxpayers above and beyond that required for normal business operations and federal tax obligations?
- 2) How much does the tax system cost the state to administer compared to collections?
- 3) Do different local taxes cause administrative burdens for businesses located in more than one local jurisdiction?
- 4) Is there an additional compliance burden caused by different agencies being involved in collecting different taxes?

Costs of Business Taxpayer Compliance

Businesses pay their taxes to DOR either annually, quarterly, or monthly. Large businesses file more frequently than small businesses in most circumstances. About 66,500 taxpayers report monthly, about 148,000 quarterly and 140,000 annually. Approximately 250,000 do not report because their income is below the minimum threshold of \$28,000.

Because Washington does not have a personal income tax, it is one of nine states that do not require individuals to file tax returns.

Reasons for Collecting and Organizing Information

In order to determine tax liability and file tax returns, businesses use some information that is collected for other purposes, such as federal income tax or other business operations. However, some information is collected only for purposes of filing the Washington State Combined Excise Tax Return (CETR). In the 2001 Taxpayer Satisfaction Survey, taxpayers were asked about which information had to be kept solely for the purpose of filing the Washington State CETR. The table below summarizes the responses.

Percentage of Taxpayers that Collect and Organize Information Solely for the CETR or for Other Reasons

	Determination of Gross Income by Tax Classification	Deduction Information	Local Retail Sales Tax Coding Information
Collect for CETR only	30.7%	36.1%	64.3%
Collect for other purposes but collect more for CETR	40.3%	26.9%	14.1%
Collect mostly for other purposes	22.4%	11.1%	1.3%
Not applicable	6.5%	25.8%	20.3%

Based on the 2001 Taxpayer Satisfaction Survey, taxpayers spend an average of 7 hours and 20 minutes collecting and organizing data for filing the CETR each reporting period. Of the 7 hours, about 65% is devoted to information for determining gross income tax classifications, 15% to information for determining deductions and 20% to information for local retail sales tax coding.

The survey results also indicated that taxpayers spend an average of four hours filling out and filing the tax return. Of the four hours, about 60% is spent filling out gross income by tax class, 16% is spent filling out deduction information and 20% is spent filling out the local retail sales tax detail.

The table below details the amount of time spent collecting and organizing data and filling out and filing the CETR each period for monthly, quarterly and annual taxpayers.

Hours Spent Per Reporting Period Collecting and Organizing Data, and Filing Out and Filing the CETR

Type of taxpayer	Time spent collecting and organizing data	Time spent filling out and filing CETR
Monthly	6.6 hours	4.6 hours
Quarterly	6.5 hours	3.8 hours
Annually	7.6 hours	3.6 hours

Filing Requirements for Other Agencies

In addition to filing tax returns to the Department of Revenue, employers must report on a quarterly basis to the Departments of Employment Security and Labor and Industries. The quarterly due date for both agencies is the last day of the first month following the quarter end. This due date corresponds with the due date for Quarterly Combined Excise Tax Return filers; however, for monthly reporters, the Department of Revenue's Combined Excise Tax Return is due on the 25th of the month following the tax period.

Local Government Taxes

Thirty-seven Washington cities impose a local Business and Occupation (B&O) tax. There is no statutory requirement of uniformity in the local B&O tax base either between cities or with the state B&O tax. However, the Association of Washington Cities has developed a model B&O tax ordinance for cities to voluntarily adopt to bring greater uniformity, simplicity, and consistency among cities levying a B&O tax. Several cities have begun the process of adopting the model B&O ordinance.

Allocation and apportionment of income between cities is currently conducted on a case-by-case basis. However, the model B&O tax ordinance includes standardized methods of allocation and apportionment of income among cities. Because adoption of the model B&O ordinance is

voluntary, not state-mandated, businesses claim that this benefit is temporary at best. Local B&O taxes are paid directly to each of the local governments.

Administrative Costs of Collecting Taxes

Over the last 30 years, the Department spent an average of about 75 cents to collect \$100. In the last eight years costs in relation to collections have declined due to declining staffing levels since 1995. The decline can also be attributed to technological enhancements during this period. In Fiscal Year 2001, the Department spent about 69 cents to collect \$100.

Some taxes are much more costly to collect than other taxes. The table below shows estimates of collection costs by tax type for the major taxes. (Costs of all taxes are included in Appendix 1.)

Costs to the Washington State Department of Revenue of Collecting State Taxes

Tax type	Cost per \$100 of collections
Retail Sales Tax	\$0.27
Use Tax	\$3.06
Business and Occupation Tax	\$0.75
Public Utility Tax	\$1.18

State and local property taxes are collected both by county treasurers, while valuation functions and other administrative duties are the responsibility of local county assessors and the Department of Revenue. Cost information for the local government portion of these administrative functions is not readily available.

The Washington State Department of Revenue also collects and distributes local sales taxes. Local taxes cost \$1.06 per \$100 to collect.

Generally, the cost of collecting taxes correlates with the cost to taxpayers of complying with Washington's tax system; taxes that are difficult for the Department of Revenue to collect are generally difficult for taxpayers to file.

Dedicated taxes are generally more complex by nature, both for taxpayers and for the administering agency. Consequently, they are more costly to collect. For example, the hazardous substance tax costs \$4.26 for each \$100 of collections. The litter tax costs \$12.94 for each \$100 of collections.

Costs to Retailers of Collecting State and Local Sales Tax

One reason that the cost of collecting retail sales tax is so low is that a large portion of the collection burden falls on retailers. The 1998 DOR study, "Retailers' Cost of Collecting and Remitting Sales Tax," estimated that the total cost of collecting and remitting sales tax is 6.47% of total state and local sales tax collections for small retailers, 3.35% for medium retailers and 0.97% for large retailers. For purposes of the study, small retailers are defined as those with gross annual Washington sales between \$150,000 and \$400,000, medium retailers with sales

between \$400,000 and \$1,500,000 and large retailers with sales over \$1,500,000. The costs include any activity the retailer has to perform related to sales tax collections and remittance that they would not have to do if they not obligated to collect and remit sales tax. The table in Appendix 2 details the costs of collections by type of cost.

The costs associated with collecting local sales tax are estimated to be 3.3% of total local collections for small retailers, 1.89% of total collections for medium retailers and 0.31% of total collections for large retailers.

As of 1998, 26 of the 45 states that have a retail sales tax allow vendors to keep a portion of the sales tax collections as a way of compensating retailers for collecting and remitting sales tax as agents for state and local government. Washington State does not compensate retailers in this way. In some of these states, costs to retailers are substantially higher because retailers must remit sales taxes to each local government separately.

Answers to the Questions

- 1) Does our tax system impose record keeping and/or paperwork obligations on taxpayers above and beyond that required for normal business operations and federal tax obligations?

According to responses from a survey of taxpayers, the majority of taxpayers collect and organize much of the information that is required to file the state portion of the Washington State Combined Excise Tax Return for other purposes. About a third of taxpayers collect this information only for purposes of filing the state portion of the Washington CETR. However, most taxpayers collect and organize the data required to file the local retail sales tax portion only for the purpose of filing the Washington State CETR.

Taxpayers spend an average of 7 hours and 20 minutes each reporting period collecting and organizing data plus an additional four hours filling out and filing the CETR.

In most states and the federal government, quarterly filing is required for corporate taxpayers. About 10% percent of Washington business taxpayers are required to file monthly CETRs.

Individuals not engaged in business do not file tax returns in Washington State.

- 2) How much does the tax system cost the state to administer compared to collections?

In Fiscal Year 2001, Washington State Department of Revenue spent 69 cents for every \$100 of collections. Cost of collections varies by tax type. Dedicated taxes are generally more costly to collect than other taxes.

Retailers and other businesses that collect retail sales tax incur costs of collecting retail sales tax for the state. Average retailers incur an estimated cost of between 0.97% and 6.47% (based on size of retailer) of total state and local collections.

- 3) Do different local taxes cause administrative burdens for businesses located in more than one local jurisdiction?

Retailers and other businesses that collect retail sales tax also incur costs associated with collecting local sales tax. The average costs associated with local sales tax collections are estimated to total between 0.31% and 3.3% of local tax collections depending on the size of the retailer.

Thirty-seven Washington cities impose a local business and occupation tax. There is no statutory requirement of uniformity in the local B&O tax base either between cities or with the state B&O tax. Widespread municipal adoption of the Association of Washington Cities' model B&O tax ordinance may lead to greater uniformity, simplicity, and consistency among cities levying a B&O tax. Administrative burdens should correspondingly decrease. Local B&O taxes are paid directly to each of the local governments.

- 4) Is there an additional compliance burden caused by different agencies being involved in collecting different taxes?

Businesses in Washington State must report to the Departments of Revenue, Employment Security, and Labor and Industries. Quarterly reporting due dates are consistent among agencies. Larger Department of Revenue taxpayers must report monthly. These taxpayers file more frequently and on a different reporting schedule than they do for other agencies.

Appendix 1

**DEPARTMENT OF REVENUE COLLECTION COST
BY REVENUE SOURCE - 1996**

STATE TAXES	COST PER \$100 COLLECTED
Retail Sales	\$0.27
Use	3.06
Business and Occupation	0.75
Public Utility	1.18
Cigarette	0.28
Liquor Sales	0.03
State Property	*
Timber Excise	6.46
PUD Privilege	0.15
Leasehold Excise	3.60
Estate	0.44
Tobacco Products	2.14
Litter	12.94
Real Estate Excise	0.18
Convention Center	2.01
Hazardous Substance	4.26
Refuse Collection	2.22
Wood Stove Fee	61.22
Refuse Collection	34.23
Carbonated Beverage Syrup	3.01
Brokered Natural Gas	2.15
Oil Spill	2.94
Rental Car	2.25
<i>State Taxes Subtotal</i>	\$0.63
LOCAL TAXES	
Sales & Use	\$0.76
Transit	0.55
Criminal Justice	0.95
Public Facilities	6.83
Hotel/Motel	3.81
Juvenile Correctional Facilities	14.42
Rental Car - Stadium	28.25
King Co Food & Beverage	16.85
Stadium Taxes	71.86
Local Rental Car	15.59
<i>Combined Local Excise Tax Subtotal</i>	\$1.06
TOTAL	\$0.70

*Property taxes are collected by the county treasurers and administered by both the Department of Revenue and the county assessors.

Appendix 2

**Retailers' Costs of Collecting and Remitting Washington State Sales Tax
Summary of All Costs**

As a percent of total state and local sales tax collections

	Small	Medium	Large	Total, weighted by number	Total, weighted by dollars
Additional clerk/cashier hours	--	--	--	--	--
Additional/more complex POS equipment	1.59%	--	--	0.69%	0.06%
Additional customer service	0.15%	0.18%	0.006%	0.13%	0.03%
Additional training	--	--	--	--	--
POS rate and base changes	0.32%	0.72%	0.07%	0.42%	0.14%
Credit and debit card fees	0.89%	0.74%	0.76%	0.81%	0.76%
Total audit costs	0.012%	0.041%	0.001%	0.021%	0.006%
Storage cost	0.03%	0.02%	0.003%	0.02%	0.006%
Appeals cost	--	0.001%	0.0001%	0.0004%	0.0002%
Total cost of filing tax return	3.27%	1.35%	0.08%	1.94%	0.34%
Cost of mistakes	0.17%	0.30%	0.05%	0.20%	0.08%
Total Costs	6.47%	3.35%	0.97%	4.23%	1.42%
Float	0.51%	0.40%	0.40%	0.45%	0.40%
Lower B&O	0.18%	0.20%	0.23%	0.20%	0.22%
Total Benefits	0.69%	0.60%	0.63%	0.65%	0.62%

Table entries with no cost indicate that costs are less than 1/1,000th of a percent.