

Summaries for the Current Tax System

Retail Sales and Use Tax

Tax Base: Purchases of tangible personal property and some services by individuals and business consumers. Includes construction, repair, lodging, participatory recreational activities, and some services such as telephone. Major exemptions: most personal & business services, motor vehicle fuel, utility services, groceries and manufacturing machinery.

Tax Rate:

State:	6.5% (no change since 1983)
Local:	0.5% - 2.4% (average of 1.7%)
Maximum:	8.9% in southern Snohomish Co.

Collections (FY 2001):

State:	\$5.92 billion (52% of general fund state sources)
Local:	\$1.68 billion (approx. 20% of all local taxes)

Advantages based on findings:

- Productive
- Broad-based
- Not lumpy
- Administratively simple for businesses, individuals and DOR.
- Surveys show that it is perceived by the general population to be the most equitable tax.

Disadvantages based on findings:

- Is inadequate in the long run as measured by a long run elasticity of .93 for sales tax and .89 for use tax. Erosion of the sales tax base by services and remote sales is one of the causes.
- Is the most volatile of all of Washington's major taxes.
- Encourages some tax avoidance by shopping in Oregon or via remote sales, thus causing economic inefficiencies as well as inequities for Washington retailers that must collect sales tax.
- Is the least exportable of Washington's current taxes for business. Individuals cannot deduct it from federal taxes.
- Cost of collecting sales tax is a burden on retailers.
- Raises the cost of plant and equipment and thus may discourage business investment.
- Regressive, especially at the extreme low and high ends.

Business and Occupation Taxes

Tax Base: Gross receipts derived from engaging in business within the state. Major exemptions: sale and rental of real estate, agricultural production, interest on 1st mortgages, investment income of non-financial firms.

Major Tax Rates:

Manufacturing, wholesaling	-	0.484%
Retailing	-	0.471%
Services & hospitals	-	1.5%

Lower rates (0.275% or 0.138%) remain for selected activities such as meat processors, fruit & vegetable packers, travel agents, etc.

Collections (FY 2001):

State: \$2.01 billion (17.3% of general fund state sources)

Advantages based on findings:

- Less volatile than corporate income tax.
- More broad-based than corporate income tax.
- Low government administration costs compared to corporate income tax.
- A higher percentage of this tax can be exported out of state and to the federal government, compared to other major Washington excise taxes.
- Contributes to a relatively low tax burden on high profit margin industries compared to other states.

Disadvantages based on findings:

- Burdensome to firms in their unprofitable years.
- Contributes to a relatively large tax burden on low profit margin industries compared to other states
- As with other business taxes, the portion of the tax that is passed down to consumers is not transparent
- Pyramids approximately 2:1. Pyramiding can cause inefficient vertically integrated operations.
- Lumpy for small taxpayers
- Inconsistencies in local B&O cause administrative burdens on taxpayers.

Property Tax

Tax Base: Assessed value of all taxable real and personal property. County assessors determine the value of real property and business owners report the value of equipment and supplies. The state determines the values of inter-county utilities, commercial vessels, and forestlands.

Levy Rates - taxes due in 2001 (\$ per \$1,000 of assessed value):

State levy	-	\$ 3.16
Aggregate of all local levies	-	<u>9.80</u>
Total nominal rate (average)	-	\$12.96
Ave. effective rate (% of market value)	-	1.16%

Levies due in 2001:

State	-	\$1.40 billion (12.0% of G.F. state)
Local regular	-	2.34 billion
Local special	-	<u>1.97 billion</u>
Total levies	-	\$5.71 billion

Share of total levies:

Schools	-	56.0%
Counties	-	17.9
Cities	-	14.0
Junior taxing districts	-	12.1

Advantages based on findings:

- Contributes to long run adequacy as measure by a long run elasticity of 1.1.
- Taxpayers can deduct property taxes on their federal tax returns thereby exporting a portion of the tax burden to the federal government.
- Correlates somewhat with benefits received since a portion of collections pays for local services
- Transparent

Disadvantages based on findings:

- Regressive (though not as regressive as sales tax)
- Lumpy
- Burdensome for homeowners if assessed value grows faster than income.
- Perceived to be unfair because the tax burden is not necessarily related to income or ability to pay.
- Exemptions cause a direct shift to other taxpayers.

- Provides uncertain funding for schools. School levies must be passed with a 60% favorable vote.
- Creates geographic inequities, some taxing districts are “poor” (lower per capita assessed values), resulting in lower revenues and/or higher tax rates.
- Complex valuation/assessment system makes it expensive to administer.

Major Selective Sales Taxes

Tax Base/Rate:

Gas tax	-	23 cents per gallon
Cigarette tax	-	\$1.425 per pack
Liquor taxes (spirits only)	-	20.5% of wholesale price + \$2.44 per liter

Collections (FY 2001):

Gas tax	-	\$611.7 million (5.2% of all state taxes)
Cigarette tax	-	\$244.6 million (2.1% of all state taxes)
Liquor taxes	-	\$125.0 million (1.1% of all state taxes)

Advantages based on findings:

- Gas tax is tied to benefits received.
- To the extent that smoking and drinking are related to higher health costs, cigarette tax and liquor tax is a tax on externalities.
- Collection costs are low; taxes are collected by wholesalers/distributors

Disadvantages based on findings:

- More regressive than general sales tax
- Very high cigarette tax rates encourage tax evasion.
- Gas tax based on volume, not price - revenues do not keep up with the economy