

**Initiative Measure****1098**

Proposed by initiative petition:

**Initiative Measure No. 1098 concerns establishing a state income tax and reducing other taxes.**

**This measure would tax “adjusted gross income” above \$200,000 (individuals) and \$400,000 (joint-filers), reduce state property tax levies, reduce certain business and occupation taxes, and direct any increased revenues to education and health.**

**Should this measure be enacted into law?**

**Yes**

**No**

The Official Ballot Title and the Explanatory Statement were written by the Attorney General as required by law. The Fiscal Impact Statement was written by the Office of Financial Management as required by law. The Secretary of State is not responsible for the content of arguments or statements (WAC 434-381-180). The complete text of Initiative Measure 1098 begins on page 66.

**Explanatory Statement**

Written by the Office of the Attorney General

**The Law as it Presently Exists**

The state of Washington does not currently impose an income tax or an excise tax on the receipt of income. The state does impose a business and occupation (B&O) tax on the privilege of engaging in various business activities in the state such as manufacturing,

selling, or providing services. Although there are some limited deductions, the tax is generally imposed on the gross income of the business. The law authorizes a credit against the tax that is taken on the tax return filed by the business. The credit reduces the amount of tax owed by the business. For most businesses, the credit is \$35 times the number of months covered by the tax return. For a business that files a tax return once a year, covering twelve months, the maximum credit is \$420 (\$35 x 12). For some businesses that provide services to their customers, the credit is \$70 times the number of months covered by the tax return. For such a business that files a tax return every month, the maximum credit that can be taken on the monthly return is \$70. If the tax exceeds the amount of the credit, the credit is reduced. If the tax owed is more than twice the amount of the credit, the credit is eliminated. The B&O tax is deposited in the state general fund.

The state, cities, counties, and other local jurisdictions are authorized to impose a property tax in varying amounts. The property tax is a tax based on the value of an owner’s taxable property. The state is authorized to impose a property tax for the support of the common schools. The state property tax is one component of the total property tax bill received by a property owner, which also includes property taxes levied by other authorized jurisdictions. The procedure for imposing the tax begins when the state levies the tax. The levy is the total amount of tax the state is authorized to collect. The levy is calculated based on certain constitutional and statutory requirements and limitations. Once the total amount of the state school levy is determined, it is divided by the value of all of the taxable property in the state to determine the rate of the tax. The rate of the property tax is also subject to certain constitutional and statutory requirements. The amount of state property tax a property owner pays is determined by multiplying the tax rate by the value of his or her taxable property. The state property tax is deposited in the state general fund and the student achievement fund for later distribution to the school districts.

**The Effect of the Proposed Measure, if Approved**

If approved, this measure would impose an excise tax on the receipt of taxable income beginning in 2012. For a married individual filing a joint return with his or her spouse and for every surviving spouse, the tax would be as follows:

Taxable Income	Tax
\$0-\$400,000	\$0
\$400,001-\$1,000,000	5% of the amount above \$400,000
\$1,000,001 and above	\$30,000 plus 9% of the amount above \$1,000,000

For every individual, other than a surviving spouse, who is not married, and for a married individual who does not file a joint return with his or her spouse, the tax would be as follows:

Taxable Income	Tax
\$0-\$200,000	\$0
\$200,001-\$500,000	5% of the amount above \$200,000
\$500,001 and above	\$15,000 plus 9% of the amount above \$500,000

This measure would also increase the credit against the B&O tax to \$4,800 a year. If the tax exceeds the amount of the credit, the credit would continue to be reduced. If the tax owed is more than twice the amount of the credit, the credit would continue to be eliminated.

This measure would also reduce the state property tax levy. The state levy would be calculated in the way it currently is, and that figure would be reduced by twenty percent. The reduced levy would be divided by the value of all of the taxable property in the state to determine the rate of the tax. The amount of state property tax a property owner pays would continue to be determined by multiplying the tax rate by the value of his or her taxable property. The twenty percent levy reduction would not apply to property taxes imposed by other jurisdictions.

Before spending the revenue generated by the tax imposed by this measure, the state treasurer would be required to calculate the loss to the general fund resulting from the increase in the B&O tax credit and the reduction of the state property tax levy, and deposit the revenue generated by the new tax into the state general fund to replace the lost revenue.

After the state treasurer has made the deposit to the general fund to replace the lost revenue,

the additional revenue generated by the tax imposed by this measure would be deposited in a dedicated account in the state treasury. Seventy percent of the revenue deposited in this dedicated account would be deposited in the education legacy trust account. Funds in the education legacy trust account may be used to enhance student achievement in grades K-12 by, for example, reducing class size, establishing special tutoring programs, or providing professional development for educators. The funds may also be used to expand access to higher education. Thirty percent of the funds deposited in the dedicated account would be used to supplement the state's basic health plan, provide for state and local public health services, provide long-term care services for seniors and people with disabilities, and for other health services.

The tax imposed by this measure would apply differently to residents and nonresidents of Washington. The tax is imposed on all of the taxable income of a resident. For a nonresident, the tax would be imposed on all the taxable income derived from sources within Washington. A resident of Washington would include an individual who lives in the state all year or claims Washington as his or her home for federal income tax purposes. It would also include an individual who considers Washington his or her residence, unless the individual does not maintain a permanent residence in Washington or any other place, and does not spend more than thirty days in Washington during the tax year. An individual who does not consider Washington his or her residence, but maintains a permanent residence in Washington and spends one hundred eighty-three (183) days in the state would be considered a resident unless the individual satisfies the Department of Revenue that he or she is only in Washington for temporary or transitory purposes.

The tax imposed by this measure would apply to taxable income. Taxable income is adjusted gross income, as determined under the federal internal revenue code, less two adjustments set out in the measure. First, taxable income would not include income that is exempt from state income tax under federal law. Second, because a nonresident's adjusted gross income may include income derived from sources outside of Washington, the measure sets out requirements to calculate a nonresident's taxable income that is derived from sources within Washington.

Employers would be required to withhold estimated tax and pay it to the Department of Revenue. The amount withheld would be a credit against any tax due during the taxable year. An employer who collected the estimated tax and failed to pay it to the Department would be personally liable to the state for the amount of the tax, plus interest and a penalty. An employer who fails to collect the estimated tax would be personally liable to the state for the amount of the tax, unless the failure was due to a reasonable cause and not willful neglect. It would be a gross misdemeanor for an employer to appropriate or convert the estimated taxes withheld. An individual, who is required to make estimated tax payments under the internal revenue code, must also make estimated payments to the Department.

Only married couples filing a joint return or a surviving spouse with taxable income in excess of \$400,000 or an individual with taxable income in excess of \$200,000 would be required to file a state tax return. If a married couple files a joint federal income tax return, they would be required to file a joint state tax return, unless one spouse is a Washington resident and the other is not. The date for filing the state tax return is the due date for the federal income tax return. The Department of Revenue would use the taxpayer's federal tax return as the main source of taxpayer information. Individuals subject to the tax imposed by this measure would be required to keep records, and the Department of Revenue would be authorized to inspect those records.

The Department of Revenue would be required to refund all taxes improperly paid or collected. State law governing the administration of other state taxes would also apply to the tax imposed by this measure. The Board of Tax Appeals would have jurisdiction over appeals relating to the taxes imposed by this measure.

The provisions of the internal revenue code would apply unless they are inconsistent with this measure. The internal revenue code is the United States Internal Revenue Code of 1986, and the amendments in effect on January 1, 2010. The Department of Revenue is authorized to adopt rules under the Administrative Procedure Act. The rules should be consistent with the internal revenue code, to the extent possible without being inconsistent with this measure.

The measure would provide that the tax imposed

may not be increased for any income level without a majority vote of the legislature and approval of the voters in an election.

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## **Fiscal Impact Statement**

Written by the Office of Financial Management

### **Fiscal Impact**

Beginning calendar year 2012, the income tax and tax relief are estimated to generate a net increase in state revenue of \$11.16 billion over five calendar years to be used exclusively for education and health services. The 20 percent state property tax levy reduction will allow some local property tax districts to levy an increased amount; this revenue impact is expected to be minimal. State implementation costs are estimated at \$39.3 million over five fiscal years; one-time computer programming costs are estimated at \$50,000 for the state and each university and local government with employees subject to the income tax.

### **State Revenues**

State revenues are estimated to increase by \$11.16 billion over five calendar years, as described on page 20, Figure 2.1.

### **State Income Tax Assumptions**

The tax will be based on the 2012 federal tax year and first imposed January 1, 2012. Therefore, employer withholding of tax and quarterly estimated tax payments begins in 2012. The first tax return will be due April 15, 2013.

Since 2005, the Washington State Department of Revenue has maintained an income tax model to estimate the revenue impacts of proposed legislation. This estimate is based on that model, which was most recently used during the 2010 legislative session to estimate the revenue impacts of Senate Bill 6250.

The model contains data for 2006 income for the 2007 federal tax year from 3.2 million state tax returns. Adjustments are made in the model for the June 2010 Washington State Economic and Revenue Forecast for personal income average growth of 3.6 percent, wages and salaries average growth of 3.44 percent and the United States implicit deflator. Adjustments are also made to the model for IHS Global Insight's national forecast for

dividends and interest income average growth of 7.8 percent, and proprietors income average growth of 7.4 percent.

It is estimated that the tax will be paid on an estimated 38,400 Washington state tax returns — 12,400 individual tax returns and 26,000 married joint, head of household and widower returns.

Growth in the tax is assumed to be 3 percent each year.

Compliance with the income tax is assumed at 90 percent for the first tax year.

### **State Property Tax Assumptions**

The state property tax levy reduction begins with the 2011 state levy, which is collected in 2012.

The state property tax levy reduction occurs after the levy is calculated each year, and does not affect the base levy amount.

Calendar years 2012 and 2013 state property tax levies are based on the June 2010 Washington State Economic and Revenue Forecast. For calendar years 2014–2016, the levies are estimated to increase, assuming that property market values and new construction grow at 6 percent per year, and state assessed properties grow at 3 percent per year.

### **State Business and Occupation Tax Credit for Small Business**

The increase in the tax credit begins with tax returns filed after January 1, 2012. For annual taxpayers, this includes the 2011 tax return; for quarterly taxpayers, this includes the fourth quarter tax return; and for monthly taxpayers, this includes the December 2011 tax return.

Using Washington State Department of Revenue excise tax return data for fiscal year (FY) 2009, the estimate assumes that the increased tax credit will exempt an estimated additional 118,000 taxpayers from all state business and occupation (B&O) taxes, and an additional 39,000 taxpayers will have a portion of their B&O tax liability reduced.

Growth in the tax credit is assumed to be 3.75 percent each year.

The amount of tax relief from the tax credit to be replaced in the State General Fund is the difference between current tax credit and the increased tax credit in the initiative.

### **Local Revenues**

The state Constitution limits the amount of property taxes that may be imposed on an individual parcel of real or personal property without voter approval to 1 percent of its true and fair value. When the 1 percent constitutional limit is exceeded, junior taxing district levies are prorated (reduced) as provided in RCW 84.52.010. The 20 percent reduction in the state property tax levy will create additional property tax capacity and allow some local property tax districts to levy an increased amount. This impact is expected to be minimal because few taxing districts are currently prorating due to the 1 percent constitutional limit. Additionally, this estimate assumes no local revenue impact from the state income tax or increased state B&O tax credit for small business.

### **State Expenditures**

Seventy percent of net revenue received by the Trust Fund must be deposited into the Education Legacy Trust Account to be used exclusively for education purposes described in RCW 83.100.230. Thirty percent of net revenues received by the Trust Fund are to be used exclusively for health services.

Before computing or spending net revenue in the Trust Fund, the State Treasurer must certify each year the revenue that would have been deposited into the State General Fund but for the state property tax levy reduction and the increased B&O tax credit for small business. The State Treasurer must then make deposits from the Trust Fund to the State General Fund as necessary to replace this revenue. Using these assumptions, the following are estimates of the additional amounts that are available for state expenditure. Estimates are described using the state's fiscal year (July 1, 2011, through June 30, 2012, is the fiscal year 2012).

The Washington State Department of Revenue will calculate the state property tax levy reduction in the normal levy process, which is completed by January 15 of each year. Therefore, it is assumed that the State Treasurer will certify and deposit to the State General Fund those amounts necessary to replace this revenue on February 1, 2012, and each February 1 thereafter.

Using filed excise tax returns, the Washington State Department of Revenue will calculate

every six months the reduced revenue from the increased B&O tax credit for small business. Assuming the Washington State Department of Revenue supplies this information to the State Treasurer on August 15 and March 15 of each year, the State Treasurer will certify and make deposits to the State General Fund to replace this revenue on September 1, 2012, and April 1, 2013, and each September 1 and April 1 thereafter.

The timing of deposits affects available funds, but does not generate new revenue to the State General Fund.

Assuming all deposits into the State General Fund must be completed before net revenues can be spent, the estimate assumes that net spending from the Trust Fund begins in FY 2013. (See page 20, Figure 2.2.)

### **State and Local Cost Estimate Assumptions**

The Washington State Department of Revenue will incur additional costs to administer the income tax. The largest cost will occur in FY 2012 from the purchase of computer hardware and off-the-shelf computer software to collect the tax, accept and audit tax returns, and process tax refunds and assessments. Costs also include additional staff, rule-making and policy activities, taxpayer mailings and workshops, supplies and materials. The increased state B&O tax credit for small business will result in cost savings from 41,000 taxpayers no longer being required to file excise tax returns who will be placed on active non-reporting status.

The Board of Tax Appeals will have jurisdiction over appeals related to income tax. Using appeal statistics from boards in other states with a state income tax to determine workload and staffing requirements, the board assumes 300 appeals each fiscal year. Costs are for additional staff, information technology upgrades, training, supplies and materials.

The following are net costs to the state, excluding costs for payroll system changes: (See page 20, Figure 2.3.)

Based on the Washington State Office of Financial Management's 2009 Personnel Detail Report and information from the Washington State Department of Personnel, University of Washington, Washington State University, Washington State Association of Counties and Association of Washington Cities, costs are

estimated up to \$50,000 total for computer programming changes to each payroll system for each jurisdiction with employees who are subject to tax. No costs are associated with the Washington State Department of Retirement Systems, assuming that the initiative does not require withholding of tax from public employee pensions.

Figure 2.1 State Revenue Increase					
Calendar Year	2012	2013	2014	2015	2016
Income Tax	\$2,213,000,000	\$2,937,000,000	\$3,025,000,000	\$3,116,000,000	\$3,209,000,000
Business & Occupation Tax Credit	(\$250,000,000)	(\$259,000,000)	(\$261,000,000)	(\$271,000,000)	(\$281,000,000)
Property Tax Relief	(\$383,000,000)	(\$393,000,000)	(\$403,000,000)	(\$414,000,000)	(\$425,000,000)
Total Net Revenue to Trust Fund	\$1,580,000,000	\$2,285,000,000	\$2,361,000,000	\$2,431,000,000	\$2,503,000,000

Figure 2.2 Additional Funds Available for State Expenditure					
Fiscal Year	2012	2013	2014	2015	2016
Education Legacy Account	\$0	\$1,106,000,000	\$1,599,500,000	\$1,652,700,000	\$1,701,700,000
Net Revenue in Trust Fund for Health Services	\$0	\$474,000,000	\$685,500,000	\$708,300,000	\$729,300,000
Total Revenue Available for Spending	\$0	\$1,580,000,000	\$2,285,000,000	\$2,361,000,000	\$2,431,000,000

Figure 2.3 State Net Costs					
Fiscal Year	2012	2013	2014	2015	2016
Department of Revenue	\$16,723,700	\$6,709,700	\$4,995,900	\$4,994,400	\$5,026,900
Board of Tax Appeals	\$0	\$41,000	\$260,000	\$257,000	\$259,000
Total State Costs	\$16,723,700	\$6,750,700	\$5,255,900	\$5,251,400	\$5,285,900

## Argument For Initiative Measure 1098

For years, Bill Gates Sr. called on Olympia to reform our tax code to lower taxes for the middle class and small businesses, but his pleas were ignored. That's why Gates Sr. and civic leaders proposed I-1098, which reduces taxes for the middle class and small businesses while raising dedicated funding to restore deep cuts to education and health care.

### Middle Class Tax Cuts

1098 will cut taxes for the middle class and help our economy: cut the state property tax on homeowners and businesses by \$357 million; eliminates B&O tax for small businesses: smallest 81 percent of businesses in Washington will no longer pay any B&O; income tax limited to the richest 3 percent – by law, there will not be one penny of income tax on income under \$400,000 a year for couples (\$200,000 for individuals).

Implements regular audits, requires a public vote for any change to the income tax.

### Levels the Playing Field

Washington ranks dead last – 50th of 50 states – in tax fairness. Middle class families pay *four times* the tax rate of the rich. 1098 restores fairness.

### Funding for Education, Health

Education and health care have been slashed – 3,000 teachers were laid off, 40,000 people lost basic health. With the wealthy paying their fair share, 1098 will net \$1 billion annually dedicated to funding K-12, college tuition, the Basic Health Plan and long-term care for seniors.

I-1098 benefits the middle class and small businesses – vote *yes*.

## Rebuttal of Argument Against

A small group of very rich people who benefit from the status quo are using fear tactics to attack 1098. The truth is 1098 slashes the state property tax 20 percent, eliminates the B&O tax for small businesses and boosts the economy. By law, the legislature is prevented from extending the tax on the rich to others or increasing it – any attempt would face a statewide vote. The people will have the final say.

## Argument Prepared by

**Bill Gates, Sr.**, tax reform advocate; **Janine Vaughn**, owner, Revival Lighting (Spokane), board, Main Street Alliance; **Sonya Langford**, 7th Grade teacher, Board member, Washington Education Association; **Walt Bowen**, President, Washington State Senior Citizens Lobby; **Linnea Hirst**, President, League of Women Voters of Washington; **Clair Ervin**, Tacoma small business owner, C. Ervin Construction LLC.

**Contact:** (206) 225-4610; info@Yeson1098.com; www.Yeson1098.com

## Argument Against Initiative Measure 1098

**Without your vote against Initiative 1098, Olympia will expand an income tax to everyone.**

Don't trust Olympia with a state income tax. Vote no on 1098 or a simple majority of the legislature will extend this income tax to everyone in just two years. Once in place, income tax rates will go up just like the sales tax.

Passing 1098 will impose new income taxes of almost \$2 billion in the first year alone. Earlier this year, the legislature already increased taxes by \$800 million per year. When our state economy desperately needs new jobs to recover from the recession, we don't need massive new tax increases.

Politicians in Olympia need to prioritize spending, not increase taxes.

**Income tax revenues will be spent as the legislature pleases.**

Supporters of 1098 claim the revenue will be used for education and health programs, but the truth is the money can be spent by the legislature on anything it wishes. Olympia raids "trust accounts" in the budget all the time. The modest business and property tax cuts in 1098 can be swept away in just two years, as well.

**A new state income tax will result in fewer new jobs.**

In urging voters to defeat 1098, *The Seattle Times* wrote, "I-1098 also takes away the most important tax-based advantage Washington has in attracting business and jobs here: our lack of a state income tax. This state needs that advantage..."

**Vote *no* on a state income tax.**

Visit [defeat1098.com](http://defeat1098.com) for the full story.

## Rebuttal of Argument For

1098 opens the door to a state income tax on everyone. Our state constitution allows a simple majority in Olympia to amend any initiative after two years. Every initiative passed in the last 20 years providing dedicated fund programs has been changed in Olympia.

The legislature has raided billions of dollars out of 74 dedicated budget accounts in recent years, including those for education and health programs.

Stop the largest tax increase in state history.

## Argument Prepared by

**Steve Appel**, President of the Washington Farm Bureau; **Don Brunell**, President of the Association of Washington Business; **John Drescher**, Executive Director of TechNet Northwest; **Steve Mullin**, President of the Washington Roundtable; **Mike Sotelo**, President, King County Hispanic Chamber of Commerce; **Joseph Zarelli**, State Senator.

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chapter 51.52 RCW to read as follows:

With respect to the rights and responsibilities of the department under this chapter, an industrial insurance insurer shall have the same rights and responsibilities under that chapter as does the department.

**NEW SECTION. Sec. 11.** Industrial insurance insurers who obtain a certificate of authority as provided in sections 2 and 3 of this act and provide coverage for industrial insurance benefits must provide benefits as set forth in chapters 51.32 and 51.36 RCW. Such industrial insurance insurers shall administer claims for benefits under chapter 51.32 RCW without involvement by the department, subject to the right to appeal any such claim decisions to the board and the courts pursuant to chapter 51.52 RCW.

**NEW SECTION. Sec. 12.** The exposure medium used by each carrier, self-insurer, or state fund to price their insurance product shall be based upon total payroll and will not be subject to any payroll limitation.

**NEW SECTION. Sec. 13.** (1) The joint legislative task force on private competition for industrial insurance is established. The task force shall consist of the following members appointed by the lieutenant governor:

- (a) One member from the house of representatives;
- (b) One member from the senate; and
- (c) The following members:
  - (i) Four members representing employers. At least one of the members must be from an employer with less than twenty employees, at least one of the members must represent an association with a retrospective rating program, and at least one of the members must be from a self-insured employer under Title 51 RCW;
  - (ii) Two members representing industrial insurance insurers; and
  - (iii) Four members representing employees. One member must be an employee of a self-insured employer and at least one member must be employed by an employer with fewer than twenty employees.

(2) The task force shall work with the commissioner and the department of labor and industries to develop proposed legislation to conform current statutes to the provisions of this act. The task force must provide its recommendations to the legislature by December 1, 2011.

(3) The task force shall expire upon completion of recommendations and transition of Washington's industrial insurance to a competitive market, but no later than December 31, 2012.

(4) No later than March 1, 2012, the legislature shall adopt such supplemental legislation as may be necessary to fully implement the policy directives of this act.

**NEW SECTION. Sec. 14.** Sections 2, 3, 11, and 12 of this act constitute a new chapter in Title 48 RCW.

**NEW SECTION. Sec. 15.** Sections 7 and 8 of this act take effect July 1, 2012.

**NEW SECTION. Sec. 16.** If any provision of this act or its application to any person or circumstance is held invalid, the remainder of the act or the application of the provision to other persons or circumstances is not affected.

-- END --

## Complete Text Initiative Measure 1098

AN ACT Relating to education, health care, and fiscal reform; adding a new section to chapter 82.04 RCW; amending RCW 82.04.4451; adding a new chapter to Title 82 RCW; and prescribing penalties.

BE IT ENACTED BY THE PEOPLE OF THE STATE OF WASHINGTON:

### PART I GENERAL PROVISIONS

**NEW SECTION. Sec. 101.** INTENT. It is the intent of the people to create a new trust fund dedicated to improving education and health services and providing middle class tax relief by reducing the state property tax by twenty percent and eliminating the business and occupation tax for all small businesses, to be funded by an excise tax on joint income in excess of \$400,000, or in the case of individuals \$200,000.

### PART II ESTABLISHING A NEW TRUST FUND DEDICATED TO EDUCATION AND HEALTH SERVICES AND MIDDLE CLASS TAX RELIEF, FUNDED BY AN EXCISE TAX ON JOINT INCOMES IN EXCESS OF \$400,000 (\$200,000 FOR INDIVIDUALS)

**NEW SECTION. Sec. 201.** (1) A new state trust fund is hereby established dedicated to funding education and health services and middle class tax relief. The trust is known and cited as the education, health services, and middle class tax relief trust and is funded by the excise tax on joint incomes in excess of \$400,000 (\$200,000 for individuals) imposed under this chapter.

(2) Net revenue received by the trust must be devoted to education and health services. Seventy percent of the net revenues received by the trust must be deposited into the education legacy trust account and used exclusively for the purposes of that account. Thirty percent of the net revenues received by the trust must be used exclusively to supplement amounts available to fund the basic health plan under chapter 70.47 RCW, to provide for costs of state and local public health services, and to provide for long-term care services for seniors and people with disabilities under chapter 74.39A RCW and other health services. Net revenue is that revenue received by the trust in excess of that necessary to fund the middle class tax relief adopted in Part III of this act.

(3) Before computing or spending net revenue, the state treasurer must each year certify the revenue that would have been deposited in the general fund but for the middle class tax relief adopted in Part III of this act, and must make such deposits as are necessary to replace the revenue eliminated by such middle class tax relief.

**NEW SECTION. Sec. 202.** The office of financial management must prepare an annual report summarizing how funds deposited in the trust have been spent and estimating the number of state residents benefited. Monthly disclosure of tax collection and spending under this chapter



must be posted on a web site maintained by the treasurer and the office of financial management and such disclosure must, at a minimum, include the information set forth in RCW 43.08.150.

### PART III

#### **ADOPTION OF MIDDLE CLASS TAX RELIEF BY REDUCING THE STATE PROPERTY TAX BY TWENTY PERCENT AND ELIMINATING THE BUSINESS AND OCCUPATION TAX FOR SMALL BUSINESSES**

**NEW SECTION. Sec. 301.** Beginning in 2012, the state property tax levy is reduced by twenty percent of the levy amount that would otherwise be allowed under this chapter without regard to this section.

**NEW SECTION. Sec. 302.** It is the intent of the voters that beginning in 2012, the business and occupation tax imposed in chapter 82.04 RCW on small business must be eliminated by increasing the business and occupation tax credit to four thousand eight hundred dollars per year, which will exempt approximately the smallest eighty percent of businesses in the state from the business and occupation tax and reduce the business and occupation tax for other businesses. The elimination of the business and occupation tax for small businesses must be carried out as provided in RCW 82.04.4451.

**Sec. 303.** RCW 82.04.4451 and 2010 c 23 s 1102 are each amended to read as follows:

(1) In computing the tax imposed under this chapter, a credit is allowed against the amount of tax otherwise due under this chapter, as provided in this section. ~~((Except for taxpayers that report at least fifty percent of their taxable amount under RCW 82.04.255, 82.04.290(2)(a), and 82.04.285, the))~~ The maximum annual credit for a taxpayer ((for a reporting period is thirty-five dollars multiplied by the number of months in the reporting period, as determined under RCW 82.32.045)) is four thousand eight hundred dollars. ((For a taxpayer that reports at least fifty percent of its taxable amount under RCW 82.04.255, 82.04.290(2)(a), and 82.04.285, the maximum credit for a reporting period is seventy dollars multiplied by the number of months in the reporting period, as determined under RCW 82.32.045.)) The department may by rule divide the credit into monthly or quarterly credits when monthly or quarterly returns are required.

(2) When the amount of tax otherwise due under this chapter is equal to or less than the maximum credit, a credit is allowed equal to the amount of tax otherwise due under this chapter.

(3) When the amount of tax otherwise due under this chapter exceeds the maximum credit, a reduced credit is allowed equal to twice the maximum credit, minus the tax otherwise due under this chapter, but not less than zero.

(4) The department may prepare a tax credit table consisting of tax ranges ~~((using increments of no more than five dollars))~~ and a corresponding tax credit to be applied to those tax ranges. The table shall be prepared in such a manner that no taxpayer will owe a greater amount of tax by using the table than would be owed by performing the calculation under subsections (1) through (3) of this section.

A table prepared by the department under this subsection must be used by all taxpayers in taking the credit provided in this section.

### PART IV DEFINITIONS

**NEW SECTION. Sec. 401.** The definitions in this section apply throughout this chapter unless the context clearly requires otherwise.

(1) "Adjusted gross income" means adjusted gross income as determined under the federal internal revenue code.

(2) "Individual" means a natural person.

(3) "Internal revenue code" means the United States internal revenue code of 1986 and amendments thereto, as existing and in effect on January 1, 2010.

(4) "Resident" includes an individual who:

(a) Has resided in this state for the entire tax year; or

(b) Is domiciled in this state unless the individual:

(i) Maintains no permanent place of abode in this state;

and

(ii) Does not maintain a permanent place of abode elsewhere; and

(iii) Spends in the aggregate not more than thirty days in the tax year in this state; or

(c) Is not domiciled in this state, but maintains a permanent place of abode in this state and spends in the aggregate more than one hundred eighty-three days of the tax year in this state unless the individual establishes to the satisfaction of the department that the individual is in the state only for temporary or transitory purposes; or

(d) Claims this state as the individual's tax home for federal income tax purposes.

(5) "S corporation" means an S corporation as defined in section 1361 of the internal revenue code.

(6) "Tax" means the tax imposed in this chapter, unless the context requires a different meaning.

(7) "Taxable income" means adjusted gross income as modified under sections 602 and 701 of this act.

(8) "Taxable year" means the taxpayer's taxable year as defined under the internal revenue code.

(9) "Taxpayer" means a person receiving income subject to tax under this chapter.

**NEW SECTION. Sec. 402.** DEFINITION OF TERMS GENERALLY. Except as provided in section 401 of this act and RCW 1.12.080, any term used in this chapter has the same meaning as when used in a comparable context in the internal revenue code.

### PART V DETERMINATION OF EXCISE TAX

**NEW SECTION. Sec. 501.** EXCISE TAX IMPOSED--RATES.

(1) An excise tax is imposed on the receipt of all taxable income of resident individuals and on all individuals deriving income from sources within this state for each taxable year based on the type of return filed and the amount of income in accordance with this section. An excise tax is not imposed on the assets held by a person resulting from income after its receipt, but only upon the receipt itself.

(2) For every married couple filing jointly with his or her spouse and for every surviving spouse, the excise tax is

determined in accordance with the following table:

If taxable income received is:	The tax is:
Not over \$400,000 .....	0
Over \$400,000 but not over \$1,000,000 .....	5.0% of the excess over \$400,000
Over \$1,000,000.....	\$30,000 plus 9.0% of the excess over \$1,000,000

(3) For every individual, other than a surviving spouse, who is not a married individual and for every married individual who does not make a single return jointly with his or her spouse, the excise tax is determined in accordance with the following table:

If taxable income received is:	The tax is:
Not over \$200,000 .....	0
Over \$200,000 but not over \$500,000.....	5.0% of the excess over \$200,000
Over \$500,000.....	\$15,000 plus 9.0% of the excess over \$500,000

**NEW SECTION. Sec. 502. CREDIT FOR INCOME TAXES DUE ANOTHER JURISDICTION.** (1) A resident individual is allowed a credit against the tax imposed under this chapter for the amount of any income tax imposed by another state or foreign country, or political subdivision of the state or foreign country, on income taxed under this chapter, subject to the following conditions, which must be imposed separately with respect to each taxing jurisdiction:

(a) The credit is allowed only for taxes imposed by the other jurisdiction on net income from sources within that jurisdiction; and

(b) The amount of the credit shall not exceed the smaller of:

(i) The amount of tax paid to the other jurisdiction on net income from sources within the other jurisdiction; or

(ii) The amount of tax due under this chapter before application of credits allowable by this chapter, multiplied by a fraction. The numerator of the fraction is the amount of the taxpayer's adjusted gross income subject to tax in the other jurisdiction. The denominator of the fraction is the taxpayer's total adjusted gross income as modified by this chapter. The fraction may never be greater than one.

(2) If, in lieu of a credit similar to the credit allowed under subsection (1) of this section, the laws of the other taxing jurisdiction contain a provision exempting a resident of this state from liability for the payment of income taxes on income earned for personal services performed in such jurisdiction, then the director is authorized to enter into a reciprocal agreement with such jurisdiction providing

a similar tax exemption on income earned for personal services performed in this state.

(3) The amount of the tax credit received by any taxpayer under this section may not exceed the total amount of tax due, and there may be no carryback or carryforward of any unused excess credits.

**NEW SECTION. Sec. 503. DUAL RESIDENCE.** If an individual is regarded as a resident both of this state and another jurisdiction for state personal income tax purposes, the department must reduce the tax on that portion of the taxpayer's income which is subjected to tax in both jurisdictions solely by virtue of dual residence, if the other taxing jurisdiction allows a similar reduction. The reduction must equal the lower of the two taxes applicable to the income taxed twice, multiplied by a fraction. The numerator of the fraction is the tax imposed by this state on the income taxed twice. The denominator of the fraction is the tax imposed by both jurisdictions on the income taxed twice. The fraction must never be greater than one.

**NEW SECTION. Sec. 504. PARTNERSHIPS AND S CORPORATIONS.** (1) Partnerships are not subject to tax under this chapter. Partners are subject to tax under this chapter in their separate or individual capacities on their distributive share.

(2) S corporations are not subject to tax under this chapter. Shareholders of S corporations are subject to tax under this chapter in their separate or individual capacities.

(3) "S corporation income" includes both distributed and undistributed federal taxable income of the S corporation.

## **PART VI TAXABLE INCOME MODIFICATION**

**NEW SECTION. Sec. 601. ABSOLUTE TAX THRESHOLD.** It is the intent of this act that in no event may excise tax be imposed upon joint adjusted gross income below \$400,000 (\$200,000 for individuals). No provisions of this chapter may allow the imposition of tax upon joint income below \$400,000 (\$200,000 for individuals).

**NEW SECTION. Sec. 602. FEDERAL OBLIGATIONS.** From adjusted gross income, deduct, to the extent included in adjusted gross income, income derived from obligations of the United States which this state is prohibited by federal law from subjecting to a net income tax.

## **PART VII DIVISION OF INCOME FOR NONRESIDENTS**

**NEW SECTION. Sec. 701. APPORTIONMENT AND ALLOCATION OF INCOME.** (1) For resident individuals, all income must be apportioned and allocated to this state.

(2) For nonresident individuals, income derived from sources within this state must be apportioned and allocated to this state.

(3) For purposes of this chapter:

(a) The adjusted gross income of a nonresident derived from sources within this state is the net amount of items of income, gain, loss, and deduction of the nonresident's adjusted gross income that are derived from or connected with sources in this state including any distributive share of partnership income and deductions.

(b) Items of income, gain, loss, and deduction derived from or connected with sources within this state are those items attributable to the ownership or disposition of any interest in real or tangible personal property in this state, and a business, trade, profession, or occupation carried on within this state. The department must issue rules to provide consistency of this section with other excise tax provisions.

(c) Deduction with respect to expenses, capital losses, and net operating losses shall be based solely on income, gains, losses, and deductions derived from or connected with sources in this state but shall otherwise be determined in the same manner as the corresponding federal deduction except as provided in this chapter.

(d) Income from intangible personal property, including annuities, dividends, interest, and gains from the disposition of intangible personal property, constitutes income derived from sources within the state of Washington only to the extent that such income is from property employed in a business, trade, profession, or occupation carried on within this state. However, distributed and undistributed income of an electing S corporation for federal tax purposes derived from or connected with sources within this state is income derived from sources within this state for a nonresident shareholder. A net operating loss of such corporation does constitute a loss or deduction connected with sources within this state for a nonresident shareholder.

(e) Compensation paid by the United States for service in the armed forces of the United States performed in this state by a nonresident does not constitute income derived from sources within this state.

(f) If a business, trade, profession, or occupation is carried on partly within and partly without this state, the determination of net income derived or connected with sources within this state as provided in this section must be made by apportionment and allocation of chapter 82.56 RCW.

## **PART VIII**

### **WITHHOLDING--ESTIMATED TAX**

**NEW SECTION. Sec. 801. EMPLOYER WITHHOLDING--REQUIREMENTS.** (1) Every employer making a payment of wages or salaries earned in this state, regardless of the place where the payment is made, and who is required by the internal revenue code to withhold taxes, must deduct and withhold a tax as prescribed by the department by rule. The rules prescribed must reasonably reflect the annual tax liability of the employee under this chapter. Every employer making such a deduction and withholding must furnish to the employee a record of the amount of tax deducted and withheld from the employee on forms provided by the department.

(2) If the employee is a resident of this state and earns income from personal services entirely performed in another state which imposes an income tax on the income, and the employer withholds income taxes under the laws of the state in which the income is earned, the employer is not required to withhold any tax imposed by this chapter on the income if the laws of the state in which the income is earned allow a similar exemption for its residents who earn income in this state.

**NEW SECTION. Sec. 802. LIABILITY OF EMPLOYER FORTAX WITHHELD.** Any person required to deduct and withhold the tax imposed by this chapter is liable under section 804 of this act to the department for the payment of the amount deducted and withheld, and is not liable to any other person for the amount of tax deducted and withheld under this chapter or for the act of withholding.

**NEW SECTION. Sec. 803. CREDIT FOR TAX WITHHELD--HOW CLAIMED.** The amount deducted and withheld as tax under sections 801 through 805 of this act during any taxable year is allowed as a credit against the tax imposed for the taxable year by this chapter. If the liability of any individual for taxes, interest, penalties, or other amounts due the state of Washington is less than the total amount of the credit which the individual is entitled to claim under this section, the individual is entitled to a refund from the department in the amount of the excess of the credit over the tax otherwise due. If any individual entitled to claim a credit under this section is not otherwise required by this chapter to file a return, a refund may be obtained in the amount of the credit by filing a return, with applicable sections completed, to claim the refund. No credit or refund is allowed under this section unless the credit or refund is claimed on a return filed for the taxable year for which the amount was deducted and withheld.

**NEW SECTION. Sec. 804. WITHHOLDING--FAILURE TO PAY OR COLLECT--PENALTIES.** (1) The tax required by this chapter to be collected by the employer is deemed to be held in trust by the employer until paid to the department.

(2) In case any employer, or a responsible person within the meaning of internal revenue code section 6672, having collected the tax herein imposed, fails to pay it to the department, the employer or responsible person must, nevertheless, be personally liable to the state for the amount of the tax. The interest and penalty provisions of chapter 82.32 RCW apply to this section. An employer or other responsible person who appropriates or converts the tax herein imposed is guilty of a gross misdemeanor as provided in chapter 9A.20 RCW.

(3) In case any employer or responsible person within the meaning of internal revenue code section 6672 fails to collect the tax herein imposed, the employer or responsible person must, nevertheless, be personally liable to the state for the amount of the tax unless it is shown that the failure was due to a reasonable cause and not willful neglect.

**NEW SECTION. Sec. 805. ESTIMATED TAX IMPOSED--DUE DATE OF ESTIMATED TAXES--AMOUNT OF ESTIMATED TAX--UNDERPAYMENT PENALTY.** (1) Each individual subject to taxation by this chapter, who is required by the internal revenue code to make payment of estimated taxes, must pay to the department on forms prescribed by the department the estimated taxes due under this chapter.

(2) The provisions of the internal revenue code relating to the determination of reporting periods and due dates of payments of estimated tax applies to the estimated tax payments due under this section.

(3) The amount of the estimated tax is the annualized tax divided by the number of months in the reporting period. No estimated tax is due if the annualized tax is less than

five hundred dollars. The provisions of RCW 82.32.050 and 82.32.090 apply to underpayments of estimated tax but do not apply to underpayments if the tax remitted to the department is either ninety percent of the tax due as shown on the current year's tax return or one hundred percent of the tax shown on the previous year's tax return.

(4) For purposes of this section, the annualized tax is the taxpayer's projected tax liability for the tax year as computed pursuant to internal revenue code section 6654 and the regulations thereunder.

## **PART IX ADMINISTRATIVE PROVISIONS**

### **NEW SECTION. Sec. 901. METHOD OF ACCOUNTING.**

(1) A taxpayer's method of accounting for purposes of the tax imposed under this chapter is the same as the taxpayer's method of accounting for federal income tax purposes. If no method of accounting has been regularly used by a taxpayer for federal income tax purposes or if the method used does not clearly reflect income, tax due under this chapter is computed by a method of accounting which in the opinion of the department fairly reflects income.

(2) If a person's method of accounting is changed for federal income tax purposes, it must be similarly changed for purposes of this chapter.

**NEW SECTION. Sec. 902. PERSONS REQUIRED TO FILE RETURNS.** (1) Only taxpayers with joint income in excess of \$400,000 (\$200,000 for individuals) are required to file a tax return with the department. The department must utilize such taxpayer's federal tax returns as a primary tool for obtaining taxpayers' information. The department may prescribe a simple supplement of no more than two pages for computing the excise tax owed under this chapter. Each person required to file a return under this chapter must, without assessment, notice, or demand, pay any tax due thereon to the department on or before the date fixed for the filing of the return.

(2) The department may by rule require that certain taxpayers file, on forms prescribed by the department, informational returns for any period. Each person required by rule to file an informational return must, without assessment, notice, or demand, pay any tax due thereon to the department on or before the date fixed for the filing of the informational return.

(3) If an adjustment to a taxpayer's federal return is made by the taxpayer or the internal revenue service, the taxpayer must, within ninety days of the final determination of the adjustment by the internal revenue service or within thirty days of the filing of a federal return adjusted by the taxpayer, file with the department on forms prescribed by the department a corrected return reflecting the adjustments as finally determined. The taxpayer must pay any additional tax due resulting from the finally determined internal revenue service adjustment or a taxpayer adjustment without notice and assessment. Notwithstanding any provision of this chapter or any other title to the contrary, the period of limitation for the collection of the additional tax, interest, and penalty due as a result of an adjustment by the taxpayer or a finally determined internal revenue service adjustment must begin at the later of thirty days following the final

determination of the adjustment or the date of the filing of the corrected return.

### **NEW SECTION. Sec. 903. DUE DATE FOR FILING A RETURN--EXTENSIONS--INTEREST AND PENALTIES.**

The due date of a return required to be filed with the department is the due date of the federal income tax return or informational return for federal income tax purposes. The department must have the authority to grant extensions of times by which returns required to be filed by this chapter may be submitted. The department must also have the authority to grant extensions of time to pay tax with regard to taxes imposed by this chapter. Interest at the rate as specified in RCW 82.32.050 accrues during any extension period and the interest and penalty provisions of chapter 82.32 RCW apply to late payments and deficiencies. Notwithstanding the limitation of RCW 82.32.090, in the case of the late filing of an informational return, there is imposed a penalty the amount of which is established by the department by rule. The penalty may not exceed fifty dollars per month for a maximum of ten months. RCW 82.32.105 applies to this section.

**NEW SECTION. Sec. 904. JOINT RETURN.** (1) If the federal income tax liabilities of both spouses are determined on a joint federal return for the taxable year, they must file a joint return under this chapter unless one spouse is a resident and the other is a nonresident.

(2) If neither spouse is required to file a federal income tax return for the taxable year, a joint return may be filed under this chapter under the same conditions under which a joint return may be filed for purposes of the federal income tax.

(3) If one spouse is a resident and the other is a nonresident, they must file separate returns under this chapter, unless they elect to determine their tax liabilities under this chapter on a joint return as if they were both residents, and:

(a) Their federal tax liability for the taxable year was determined on a joint federal tax return; or

(b) Neither spouse has filed a federal income tax return for the taxable year and they would be permitted to file a joint federal tax return for the taxable year.

(4) In any case in which a joint return is filed under this section, the liability of the spouses is joint and several, unless the spouse is relieved of liability under section 6013 of the internal revenue code.

(5) The department must take actions and adopt rules, forms, and procedures to implement this act consistently with RCW 26.60.015, notwithstanding any term or provision of this act except section 601.

**NEW SECTION. Sec. 905. RECORDS--RETURNS.** (1) Every taxpayer with joint income in excess of \$400,000 (\$200,000 for individuals) and all others required to deduct and withhold the tax imposed under this chapter must keep records, render statements, make returns, file reports, and perform other acts as the department requires by rule. Each return must be made under penalty of perjury and on forms prescribed by the department. The department may require other statements and reports be made under penalty of perjury and on forms prescribed by the department. The department may require any taxpayer and any person

required to deduct and withhold the tax imposed under this chapter to furnish to the department a correct copy of any return or document which the taxpayer has filed with the internal revenue service or received from the internal revenue service.

(2) All books and records and other papers and documents required to be kept under this chapter are subject to inspection by the department at all times during business hours of the day.

**NEW SECTION. Sec. 906. PROVISIONS OF INTERNAL REVENUE CODE CONTROL.** (1) To the extent possible without being inconsistent with this chapter, all of the provisions of the internal revenue code relating to the following subjects apply to the taxes imposed under this chapter:

(a) Time of payment of tax deducted and withheld under sections 801 through 805 of this act and this section;

(b) Liability of transferees;

(c) Time and manner of making returns, extensions of time for filing returns, verification of returns, and the time when a return is deemed filed.

(2) The department by rule may provide modifications and exceptions to the provisions listed in subsection (1) of this section, if reasonably necessary to facilitate the prompt, efficient, and equitable collection of tax under this chapter.

**NEW SECTION. Sec. 907. REFUNDS OF OVERPAYMENTS--OTHER ADMINISTRATIVE PROVISIONS.**

(1) The department must refund all taxes improperly paid or collected.

(2) The following sections apply to the administration of taxes imposed under this chapter: RCW 82.32.020, 82.32.050, 82.32.060, 82.32.070, 82.32.090, 82.32.100, 82.32.105, 82.32.110, 82.32.120, 82.32.130, 82.32.140, 82.32.150, 82.32.160, 82.32.170, 82.32.180, 82.32.190, 82.32.200, 82.32.210, 82.32.220, 82.32.230, 82.32.235, 82.32.237, 82.32.240, 82.32.245, 82.32.265, 82.32.290, 82.32.300, 82.32.310, 82.32.320, 82.32.330, 82.32.340, 82.32.350, 82.32.360, and 82.32.380.

**NEW SECTION. Sec. 908. RULES.** The department may adopt rules under chapter 34.05 RCW for the administration and enforcement of this chapter, including a phase-in for fiscal year taxpayers. The rules, to the extent possible without being inconsistent with this chapter, must follow the internal revenue code and the regulations and rulings of the United States treasury department with respect to the federal income tax. The department may adopt as a part of these rules any portions of the internal revenue code and treasury department regulations and rulings, in whole or in part.

**NEW SECTION. Sec. 909. APPEALS.** The board of tax appeals shall have jurisdiction over appeals relating to tax deficiencies and refunds, including penalties and interest, pursuant to this chapter. The taxpayer may elect a formal or informal hearing pursuant to RCW 82.03.140.

## **PART X MISCELLANEOUS**

**NEW SECTION. Sec. 1001. CONTEXT.** In 1932, more than seventy percent of Washington voters approved an

income tax initiative and simultaneously cut property taxes in half. The following year, the state supreme court, in an opinion that ultimately relied on United States supreme court cases that have long since been overruled, treated Washington's graduated income tax, as then drafted, as a nonuniform property tax. This threw the state's tax system into confusion and led to Washington's over reliance on high sales taxes and the business and occupations tax. The sales tax is regressive and stunts business growth. The business and occupation tax, which is peculiar to Washington state, discourages investment and encourages many potential employers to take their business elsewhere. The tax established by this initiative is intentionally structured as an excise tax on the receipt of income during a taxable year rather than as a property tax on money as an asset, after it has been received. As an excise tax rather than a property tax, this tax is intended to conform to the legal framework adopted by almost all states, consistent with United States supreme court rulings as they have evolved during the past eight decades. This initiative is also aimed at replicating the voters' 1932 action to reduce property taxes while installing a much fairer tax system overall and providing more stable funding to enable the state to meet its constitutional duty to provide for the education of all children, and to enable the state to better provide for the costs of health care.

**NEW SECTION. Sec. 1002. SEVERABILITY.** The provisions of this initiative are contingent upon the validity of the excise tax in section 501 of this act. Except as to this contingency, the voters intend the provisions of this initiative to be severable such that if any provision of this act or its application to any person or circumstance is held invalid, the remainder of the act or the application of the provision to other persons or circumstances is not affected.

**NEW SECTION. Sec. 1003. APPLICATION.** This chapter and sections 302 and 303 of this act apply to taxes collectible in 2012 and thereafter.

**NEW SECTION. Sec. 1004.** The excise tax rates in section 501 of this act may not be increased for any income level without a majority vote of the legislature and submission of the changes to the people for approval.

**NEW SECTION. Sec. 1005. CODIFICATION.** Sections 101 through 301 and 401 through 1004 of this act constitute a new chapter in Title 82 RCW.

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