SENATE BILL REPORT
SB 5733

As of February 10, 2023

Title: An act relating to creating a business and occupation tax deduction and increasing the tax rate for persons conducting payment card processing activities.

Brief Description: Creating a business and occupation tax deduction and increasing the tax rate for persons conducting payment card processing activities.

Sponsors: Senators Mullet, Wilson, L. and Gildon.

Brief History:
Committee Activity: Business, Financial Services, Gaming & Trade: 2/14/23.

Brief Summary of Bill

- Creates a business and occupation (B&O) tax deduction for amounts received by a payment card processing company in the form of interchange fees or network fees.
- Establishes a B&O tax rate of 3 percent for certain contracted payment card processing activities.

SENATE COMMITTEE ON BUSINESS, FINANCIAL SERVICES, GAMING & TRADE

Staff: Alia Kennedy (786-7405)

Background: Business and Occupation Tax. The state business and occupation (B&O) tax is Washington's primary business tax. It is a gross receipts tax measured on the value of products, gross proceeds of sale, or gross income of the business. There are no deductions from the B&O tax for labor, materials, taxes, or other costs of doing business. The B&O tax rate varies by classification (activity). The major rates are: 0.471 percent for retailing activities, 0.484 percent for manufacturing and wholesaling activities, and for service and other activities, either 1.5 percent or 1.75 percent, depending upon the amount of annual

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gross income of the business. The state B&O tax includes a number of preferential tax rates, credits, exemptions, and deductions as well as several increased rates or surcharges.

Workforce Education Funding. Since April 1, 2020, the B&O tax has two rates under the service and other activities classification. The tax rates replace the Workforce Education Investment Surcharge that was created in 2019. Service and other activities of $1 million or more in the prior calendar year are taxed at a B&O rate of 1.75 percent. A portion of the revenue generated from the 1.75 percent B&O rate is deposited into the Workforce Education Investment Account to support higher education programs, state-funded student aid, and workforce development. Activities below the gross receipts threshold are subject to a B&O tax rate of 1.5 percent.

Business and Occupation Surcharge on Financial Institutions. Since January 1, 2020, a surcharge is imposed on financial institutions with an annual net income of at least $1 billion for the previous calendar year. The surcharge is 1.2 percent and applies to the business' income subject to the B&O tax under the service and other activities tax classification. All receipts from the surcharge are deposited into the state general fund.

Tax Preferences. State law provides for a range of tax preferences that confer reduced tax liability upon a designated class of taxpayer. Tax preferences include tax exclusions, deductions, exemptions, preferential tax rates, deferrals, and credits. Washington has over 700 tax preferences, including a variety of sales and use tax exemptions. Legislation that establishes or expands a tax preference must include a tax preference performance statement that identifies the public policy objective of the preference, as well as specific metrics the Joint Legislative Audit and Review Committee can use to evaluate the effectiveness of the preference. All new tax preferences automatically expire after ten years unless an alternative expiration date is provided.

Summary of Bill: Busniess and Occupation Tax Deduction for Certain Credit Card Processing Fees. A B&O tax deduction is allowed for amounts received by payment card processing companies in the form of interchange fees or network fees.

Interchange fees are fees set by a payment network, or by agreement between an issuing bank and a merchant or merchant bank, that an issuing bank retains from the amounts settled to the merchant as compensation for the services the issuing bank provides in issuing a credit, debit, or prepaid card to a cardholder, advancing proceeds to settle a credit, debit, or prepaid card transaction, and incurring a portion of the risks relating to the transaction.

Network fees are fees a payment network charges and receives as compensation for its services, including for facilitating the payment of a credit, debit, or prepaid card transaction from cardholders to a merchant through its network.

Business and Occupation Tax Rate on Payment Card Processing Activities. Payment card processing activities are subject to a B&O tax rate of 3 percent. The new B&O tax rate

applies to any gross income derived from the merchant discount of those merchants with which the payment card processing company has directly or indirectly contracted to perform payment card processing activities.

Payment card processing activities subject to the new B&O tax rate of 3 percent are also subject to the surcharge on financial institutions and the a workforce education investment surcharge.

For payment card processing activities in which more than one payment card processing company receives a portion of the merchant discount, each company is required to include in its gross income the portion of the merchant discount it is entitled to retain.

"Merchant discount" means the aggregate fee, or negotiated discount, incurred by a merchant for the processing of payment card transactions under its contract with a payment card processing company when it accepts a payment network-branded credit, debit, or prepaid card in a sale transaction.

"Payment card processing activities" means acquiring, either directly or indirectly, credit, debit, or prepaid card transactions from merchants, facilitating the submission of those transactions to payment networks, and facilitating the payment of proceeds of those transactions to merchants.

Tax Preference Performance Requirements. The B&O tax deduction for amounts received by payment card processing companies in the form of interchange fees or network fees is permanent and not subject to tax preference performance review.

Retroactivity Clause. The bill applies prospectively and retroactively to any penalties or interest assessed on delinquent taxes, including any disputed assessments pending before the Department of Revenue, Board of Tax Appeals, or any court of law. Any tax not previously paid must be paid within 90 days of the effective date of the act, but is not subject to penalties or interest.

Appropriation: None.

Fiscal Note: Requested on February 9, 2023.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: The bill takes effect on October 1, 2023.