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Title

Department of Finance Director's Rules Nos. 5-045 and 5-930, Implementing Seattle Business Tax Ordinance.

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Rule No. 5-045 **Allocation and Apportionment Methods**

(1) Introduction. Beginning January 1, 2008, RCW 35.102.130 established new allocation and apportionment requirements for cities with a gross receipt business tax. The new allocation procedure requires businesses to allocate or source their sales of tangible personal property to the local jurisdiction where delivery takes place. The new apportionment procedures require businesses that report under the service and other business activities tax classification to apportion their gross income based on a two-factor formula. The two factors are "payroll" and "service revenue." (See allocation and apportionment procedures below.)

In an effort to recoup a major portion of the tax revenue lost under RCW 35.102.130, the City of Seattle imposed the square footage business tax on any taxpayer who received a tax reduction benefit from RCW 35.102.130. (See Seattle Rule 5-930 for the square footage business tax information.) The square footage business tax was imposed starting January 1, 2008.

For many taxpayers, these allocation and apportionment requirements have created confusion and administrative hardships. The intent of this rule is to provide guidance on the new allocation and apportionment methods.

(2) Reporting Instructions. Any taxpayer whose sales and services are delivered wholly within the city of Seattle (does not engage in any business activity outside of Seattle) is allowed to take a 100% credit against their square footage business tax. Since all of their sales and services are delivered within Seattle the new allocation and apportionment procedures do not effect their tax reporting requirements. They should report the business license tax in the same manner as they have historically reported and then take a 100% credit against their square footage business tax.

(3) Extracting, Manufacturing, Printing, Transporting Freight for Hire, Processing for Hire, and Tour Operator reporting instructions. For periods both before and after January 1, 2008, taxpayers engaged in extracting, manufacturing, printing, transporting freight for hire, processing for hire and tour operator activities, shall report the activity in the location where the activity takes place. This means that there will be no change in their reporting requirements. Persons engaged solely in such activities are exempt from the square footage business tax.

(4) Royalty Income. Gross income derived as royalties from the granting of intangible rights shall be allocated to the commercial domicile (headquarters) of the taxpayer.

(5) Retail/Wholesale reporting methods. In order to compute the amount of square footage business tax credit, the following explains the methods for reporting revenue under the retailing/wholesaling classifications of the business license tax:

(a) Retail/Wholesale revenue assignment prior to January 1, 2008. Revenue reported under either the retailing or wholesaling classification of the business license tax is assigned to the City of Seattle as follows:

(i) A person who maintains an office or place of business in the City shall be taxable on the gross income, gross proceeds of sales, or value of products derived from the business activities rendered by, generated from, or attributable to the office or place of business located within the City, unless specific deductions or exemptions apply.

(ii) A person engaging in business activities in the City who does not maintain an office or place of business in the City shall allocate to the City that portion of the taxpayer's gross income or gross proceeds of sales that are derived from business activities performed in the City.

(iii) A person who maintains an office or place of business in the City and also elsewhere.

(A) Shall be taxable on that portion of his gross income or gross proceeds of sales, or value of products that is derived from business activity rendered by, generated from, or attributable to the office or place of business located within the City, unless specific deductions or exemptions apply; and

(B) Shall allocate to the City and be taxable on gross income, or gross proceeds of sales, from business activities performed in the City but supported by the office or place of business located outside the City, where the business activity performed in the City is a significant factor in making or holding the market for the goods or services sold; and

(C) Delivery of product or the performance of services occurs in Seattle; or

(D) The customer is located in Seattle.

(iv) The amount derived from goods delivered outside of the State of Washington by the seller may be deducted from the gross income.

(v) The amount derived from goods delivered into other cities or local jurisdiction that maintain an eligible gross receipts tax and subject to the tax may be deducted from the gross income. Also see the provisions for the Multiple Activity Tax Credit (MATC) when goods are extracted, manufactured, or printed in Seattle or in another city that imposes an eligible gross receipt tax.

(b) Retail/Wholesale revenue assignment beginning January 1, 2008. Revenue earned after December 31, 2007 and reported under either the retailing or wholesaling classification of the business license tax is assigned to the City of Seattle if the goods or services are delivered within the city and the taxpayer has nexus within the city. Goods delivered by a Seattle seller to a point outside of the city may be deducted from the gross proceeds of sales (includes both intrastate and interstate deliveries).

(6) Service Income Reporting Methods. In order to compute the square footage business tax credit, the following explains the different methods for reporting income reportable under the service and other business activities classification of the business license tax:

(a) Service revenue assignment prior to January 1, 2008. This section instructs taxpayers which revenues reported under the service and other business activities classification of the business license tax will be assigned to the City as taxable. Once the amount subject to tax in Seattle is determined according to this section, then the credit or deductions contained in SMC 5.45.070 and SMC 5.45.075 may be calculated, if applicable.

(i) A person who maintains an office or place of business in the City shall be taxable on the gross income, gross proceeds of sales, or value of products derived from the business activities rendered by, generated from, or attributable to the office or place of business located within the City, unless specific deductions or exemptions apply.

(ii) A person engaging in business activities in the City who does not maintain an office or place of business in the City shall allocate to the City that portion of the taxpayer's gross income or gross proceeds of sales that are derived from business activities performed in the City.

(iii) A person who maintains an office or place of business in the City and also elsewhere.

(A) Shall be taxable on that portion of his gross income or gross proceeds of sales, or value of products that is derived from business activity rendered by, generated from, or attributable to the office or place of business located within the City, unless specific deductions or exemptions apply; and

(B) Shall allocate to the City and be taxable on gross income, or gross proceeds of sales, from business activities performed in the City but supported by the office or place of business located outside the City, where the business activity performed in the City is a significant factor in making or holding the market for the goods or services sold, and

(C) Delivery of product or the performance of services occurs in Seattle; or

(D) The customer is located in Seattle.

(iv) Allocations of amounts shall be made in accordance with and in full compliance with the provisions of the interstate commerce clause of the United States Constitution where applicable.

(v) In cases where the taxpayer maintains only one office or place of business in Seattle and conducts activities outside of Washington which create taxing nexus and the person has licensed and pays any applicable taxes, then the apportionment of revenue shall be made using a two-factor formula of payroll and service income. In this case the payroll and service income factors will be computed based upon Multi-State Tax Commission guidelines as follows:

(A) The payroll factor is based on employees' (FICA employees) compensation paid within Seattle compared to total employees' compensation. Payroll is paid within Seattle if:

(1) The employee's service is performed entirely within Seattle.

(2) The employee's service is performed both within and without Seattle, but the service performed without Seattle is incidental to the employee's service within Seattle. "Incidental" means any service which is temporary or transitory in nature.

(3) If the employee's services are performed both within and without Seattle the employee's compensation will be attributed to Seattle: (i) if employee's base of operation is in Seattle; or (ii) if the place from which the service is directed or controlled is in Seattle; or (iii) if the base of operations or the place from which the service is directed or controlled is not in any city in which some part of the service is performed but the employee's residence is in Seattle.

(B) The service income factor is based on the income produced within Seattle compared to total income produced. Income is produced within Seattle if:

(1) The income producing activity is performed wholly within Seattle; or

(2) The income producing activity is performed both in and outside of Seattle and a greater proportion of the income producing activity is performed in Seattle than any other location, based on cost of performance. "Cost of performance" means direct costs determined in a manner consistent with generally accepted accounting principles. Included in the taxpayer's cost of performance are taxpayer's payments to an agent or independent contractor for the performance of personal services and utilization of tangible and intangible property which give rise to the particular item of income directly to the taxpayer's customer. If this subsection (6)(a)(v) applies and you have questions concerning the procedures, then contact the Revenue and Consumer Affairs Division to ask for assistance.

(vi) If the Director determines that the allocation of gross income from business activities for a person subject to subsection (6)(a) above and taxable under the "other business activities" classification (SMC 5.45.050 G) does not fairly reflect gross income derived from business activities within the City, the Director shall determine such gross income by either of the following methods: (a) by a fair and equitable formula agreed upon by the Director and the taxpayer after a consideration of the facts; or (b) by the ratio that the cost of doing business within the City bears to the cost of doing business both within and without the City. For apportionment purposes, all costs must be assigned to an office location.

(b) Service revenue apportioned beginning January 1, 2008. Gross income derived from service and other business activities taxed under SMC 5.45.050 G after January 1, 2008 shall be apportioned to the City by multiplying the service and other business activity income by a fraction, the numerator of which is the payroll factor plus the service and other business activity income factor and the denominator of which is two (2).

(i) The payroll factor is a fraction, the numerator of which is the total amount paid for compensation in the City during the tax period by the taxpayer and the denominator of which is the total compensation paid everywhere during the tax period. Compensation is paid in the City if:

(A) The individual or employee is primarily assigned within the City;

(B) The individual is not primarily assigned to any place of business for the tax period and the employee performs fifty percent (50%) or more of his or her service for the tax period in the city; or

(C) The individual is not primarily assigned to any place of business for the tax period, the individual does not perform fifty percent (50%) or more of his or her service in any city, and the employee resides in the city.

(ii) The service and other business activity income factor is a fraction, the numerator of which is the total service and other business activity income of the taxpayer in the City during the tax period, and the denominator of which is the total service and other business activity income of the taxpayer everywhere during the tax period. Service and other business activities income is in the City if:

(A) The customer location is in the City; or

(B) The income-producing activity is performed in more than one (1) location and a greater proportion of the service-income-producing activity is performed in the City than in any other location, based on costs of performance, and the taxpayer is not taxable at the customer location; or

(C) The service and other business activity income producing activity is performed within the City, and the taxpayer is not taxable in the customer location.

(iii) The definitions in this subsection apply throughout this rule.

(A) "Compensation" means wages, salaries, commissions, and any other form of remuneration paid to individuals for personal services that are or would be included in the individual's gross income under the federal Internal Revenue Code.

(B) "Individual" means any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee of that taxpayer.

(C) "Customer location" means the city or unincorporated area of a county where the majority of the contacts between the taxpayer and the customer take place.

(D) "Primarily assigned" means the business location of the taxpayer where the individual performs his or her duties.

(E) "Service-taxable income" or "service income" means gross income of the business subject to tax under the service and other business activity classification, including but not limited to royalty income.

(F) "Taxable in the customer location" means either that a taxpayer is subject to a gross receipts tax in the customer location for the privilege of doing business, or that the government where the customer is located has the authority to subject the taxpayer to gross receipts tax regardless of whether, in fact, the government does so.

(7) Examples. The following examples identify a number of facts and then state a conclusion. The tax status of each circumstance must be determined after a review of the agreement and all of the facts and circumstances.

(a) Company ABC is a retail store located in Seattle. They ship approximately 25% of their merchandise to customers outside of Seattle. Of the 25% shipped outside of Seattle, 5% are shipped in their own trucks into other cities with a gross receipt tax such as Bellevue, Burien, and Everett. Under the new allocation procedure ABC can deduct the twenty-five percent (25%) that they deliver outside Seattle. However they would incur Seattle's new square footage business tax if they take that deduction. They would have to compute and pay 20% (twenty percent) of the square footage business tax computed (25% less the 5% delivered into other gross receipt B & O tax cities).

(b) BAM Company is a Seattle CPA firm that conducts audits and provides consulting services to business both within and outside Seattle. Beginning January 1, 2008, BAM should report under the new apportionment procedures and use the two-factor formula of payroll and service revenue. BAM will incur Seattle's new square footage business tax in the same percentage that they benefit by the twofactor formula when compared to the old code method of reporting all of their intrastate revenues and taking a deduction for any services rendered within other gross receipts B & O cities and having paid their tax.

(c) Company MMM that reports under the service and other business activity classification has its only business location in Seattle. It maintains traveling managers who visit independent contractors who sell the company's services. The independent contractors are paid by commissions. The independent contractors are located partly outside of the state and partly within the state. The traveling managers are assigned to the Seattle office. Company MMM has nexus outside of the state due to their independent contractors working with MMM's ultimate customer. MMM should compute their taxable service and other income using the two-factor method. Since their employees and the traveling managers are assigned to the Seattle office, 100% of the payroll is assigned to Seattle. The service and other income generated by their independent contractors in out-of-city locations will be sourced to outside of Seattle and only that service and other income generated from employees or independent contractors within the city shall be assigned to Seattle. Assuming that 75% of the service and other income is generated outside of Seattle and 25% inside of Seattle, then the two factor apportionment would be as follows:

$100\% \text{ (Seattle payroll factor)} + 25\% \text{ (Seattle income factor)} / 2 = 62.5\% \text{ apportionment factor.}$ 62.5% of MMM's service and other income would be assigned to Seattle for tax purposes.

Effective: April 18, 2008.

Rule No. 5-930 **Square Footage Business Tax (Square Footage Tax)**

(1) Introduction. In 2003, the Washington State Legislature passed a law (RCW 35.102.130) that changes how cities can impose their gross receipts Business and Occupation (B&O) taxes (such as Seattle's business license tax) on certain types of business activities. The most notable changes of the new law, which went into effect on January 1, 2008, are:

(a) Income from providing services shall now be apportioned for tax purposes between the city where the employee providing the service is based (payroll) and the place where the majority of contacts with the customer occurs (service revenue source).

(b) Income from the sale of tangible personal property shall be allocated for taxation purposes to the location where delivery to the buyer takes place.

Seattle's square footage business tax applies to businesses located in Seattle and is based on the amount of square feet used to conduct its business activities. The square footage business tax is computed by applying tax rates against the square footage of a business.

All businesses located within Seattle subject to the business license tax shall be subject to the square footage business tax, unless specifically exempt from the tax. Businesses subject to the square footage business tax may take credits against the tax as provided below.

Seattle businesses that do not ship goods or provide services outside of Seattle are entitled to a 100% credit of the square footage tax. Therefore, Seattle businesses such as restaurants, hospitals, hotels, theaters, barbers, hair salons, and grocery stores, or such other retail stores where the customers pick up all merchandise at the store would be entitled to a 100% credit against the square footage tax.

Seattle businesses that ship goods or provide services outside of Seattle, and benefit under the new allocation and apportionment law, will have their business square footage taxed on the same percentage basis as they received benefit under the new tax provisions.

For example, a Seattle business that ships 30 percent of its goods to locations outside of Seattle, but within Washington, would receive a tax benefit under the new business license tax law because it can now deduct those sales from the measure of the business license tax. The business license tax would decrease by 30 percent. This same Seattle business would therefore be required to pay 30 percent of its square footage business tax and take a credit for the other 70 percent.

The business will be required to complete the square footage tax portion of the business license tax return and take the applicable credits to reduce or eliminate the tax.

The square footage business tax law also provides that a Seattle business ordinarily should not pay any more total tax under the combined square footage tax and the new allocation and apportionment provisions of the business license tax than it would have paid before these two new tax provisions were imposed. This is accomplished through a maximum square footage business tax credit as described below.

(2) Definitions. For purposes of this rule and Seattle Municipal Code ("SMC") Chapter 5.46, the following definitions apply for the square footage business tax:

(a) "Business floor space" means rentable square feet of an office or place of business and includes the proportionate share of the building service areas such as lobbies, corridors and other common areas in a building. The rentable square footage shall be computed by measuring to the inside finish of permanent outer building walls and shall include space used by columns and projections necessary to the building. Business floor space does not include vertical penetrations through the building such as stairs, elevators, or heating, ventilation, air conditioning, utility, or telephone systems. Business floor space does not include other floor space as defined in subsection B below. If the business floor space is owned by the taxpayer, the business floor space shall be calculated in the same manner as above and as if the area was rented.

(b) "Other floor space" means rentable square feet used for dining areas, exercise areas, or warehouse space.

(1) "Dining area" means any space used exclusively by employees for the purpose of purchasing, preparing, or consuming meals.

(2) "Exercise area" means any space used exclusively by employees for the purpose of physical exercise not related to an employee's normal job duties.

(3) "Warehouse space" means any space used exclusively for the storage of merchandise or commodities.

Other floor space shall be measured in the same manner as business floor space whether owned or rented.

(c) "Headquarters space" is the portion of business floor space and other floor space used in Seattle exclusively to administer and manage other offices or places of business located outside of

Seattle.

(3) Measuring and computing the Square Footage Business Tax.

(a) The square footage business tax is computed by applying tax rates against the square footage of a business located in Seattle. The square footage business tax is imposed using two tax rates. "Business floor space" shall be taxed at a rate of \$0.39 per square foot per quarter (\$1.56 annually). "Other floor space" shall be taxed at a rate of \$0.13 per square foot per quarter (\$0.52 annually). These tax rates will be adjusted annually for inflation.

(b) Headquarters space is not included in the computation of the square footage used by the business. Space used for the administration and management of Seattle locations is included in the computation.

(c) The following credits are available to offset the square footage business tax:

(i) Persons who owe no business license tax under SMC 5.45.050 due to deductions contained in SMC 5.45.100 (with the exception of subsection SMC 5.45.100 W which covers intrastate sales delivered outside of Seattle) may take a credit against the square footage business tax for the total amount of the tax. In short, if your business activities have remained the same and you have not paid the business license tax due to deductions available to you under the business license tax code then you will not owe any square footage business tax.

(ii) Persons whose taxable gross income on an annual basis is below the minimum tax threshold of \$80,000 owe no square footage tax.

(iii) Persons who pay the business license tax under SMC 5.45.050 on all of their gross income, excluding interstate sales and sales taxed by another Washington gross receipts B & O tax city, generated from the Seattle business location(s) may take a credit for 100 percent of their square footage business tax.

(iv) Retailers and wholesalers. Persons selling tangible personal property from a Seattle business location may take a credit against the square footage business tax equal to the square footage tax owed for the reporting period multiplied by the ratio of adjusted gross income to total gross income. Adjusted gross income for retailers and wholesalers is the taxpayer's total gross income less those sales delivered from the Seattle business location(s) to the buyer at a location outside of Seattle but within Washington, where a local government has not taxed the goods under an eligible gross receipts tax.

(v) Service businesses. Persons providing services (subject to tax under SMC 5.45.050 G) from a Seattle business location(s) may take a credit equal to the square footage tax owed for the reporting period multiplied by the ratio of adjusted gross income to total gross income generated by the Seattle business location. Adjusted gross income for service businesses is computed by subtracting from the total gross income (subject to the service and other business license tax) the difference between the taxable service income under Seattle's method of computing taxable service income prior to January 1, 2008 (SMC 5.45.080) and under the new two-factor method of computing taxable service income (SMC 5.45.081 C or RCW 35.102.130(3) which takes effect after January 1, 2008).

(vi) Combined retailing/wholesale and services. A business engaging in retailing or wholesaling and also in a service and other business activity shall compute the adjusted gross income for each

activity and then combine the computations to arrive at the proper credit percentage to use in computing their square footage business tax.

(vii) Maximum square footage business tax credit. A taxpayer should not pay any more tax under the new tax provisions of RCW 35.102.130 and SMC Chapter 5.46 (square footage business tax) than the taxpayer would have paid if both of those provisions had not taken effect. If the gross receipts business license tax and the square footage business tax combine to result in a tax increase for the taxpayer when compared to the amount of tax that would have been due prior to the implementation of RCW 35.102.130 on January 1, 2008, then an additional credit may be taken against the square footage business tax for the amount of such tax increase.

(viii) The calculation of the square footage business tax credits in (ii) through (vii) above, does not include royalty income, which must be allocated 100 percent to the headquarters or domicile of the business, as specifically required by State law (RCW 35.102.103(2)).

For subsections (i) through (iii) of this subsection, the square footage tax shall be computed and then a 100% credit applied against the tax owing.

Computation worksheets are available to assist in computing the square footage business tax and any credits that are available. Such worksheets are available at <http://www.seattle.gov/rca/taxes/Taxforms.htm>

(4) Exemptions from the square footage business tax. The following businesses are exempt from the square footage business tax:

(a) Persons who conduct only activities which the City is preempted from taxing, pursuant to federal or state statutes, including but not limited to: insurance businesses; the selling, manufacturing, or distributing of motor vehicle fuel pursuant to the Revised Code of Washington (RCW) 82.36.440; and the distributing or selling of liquor pursuant to RCW 66.08.120. Persons engaging in these exempt activities, but also engaged in taxable activities, shall use only the square feet involved in the non-exempt activity when computing the square footage business tax.

(b) Banks and other financial institutions, whose income is apportioned according to WAC Chapter 458-28.

(c) Persons taxable under the utility tax pursuant to SMC Chapter 5.48 are exempt from SMC Chapter 5.46 (square footage business tax) provided they generate no gross income from activities taxable under SMC 5.45.050 (business license tax). If utility businesses generate income subject to the business license tax, only the square footage used in generating those revenues shall be included in the computation of the square footage business tax and any related credits.

(d) Persons exempt from the business license tax pursuant to SMC 5.45.090.

(e) Business and other floor space used in the following activities: Manufacturing, extracting, printing, processing for hire, transporting freight for hire, and tour operators.

(5) Changes in floor space.

(a) A person who moves outside the city or closes their business during the tax reporting period shall prorate the number of square feet based on a ratio of days that the space was occupied to total days of the tax reporting period.

(b) A person whose business floor space or other floor space changes during the tax reporting period shall prorate the square footage based on a weighted average of the floor space occupied during the different segments of the reporting period.

Example for change in floor space: A business occupied business floor space of 8,000 sq. ft. for the first 30 days and then 5,000 sq. ft. for the remaining 60 days of the quarter. To compute the number of square feet subject to tax during the tax quarter, the following weighed average calculation is made:

$(8,000 \text{ sq. ft.} \times 30 \text{ days}) + (5,000 \text{ sq. ft.} \times 60 \text{ days})$ divided by 90 days = 6,000 sq. ft. The 6,000 sq. ft. would be used in computing the square footage business tax. .TX: (6) Rental or Lease of floor space. Generally, the person or business occupying the space will be responsible for the square footage business tax only if the person or business has exclusive right of control and occupancy to the space, e.g., the person or business controls such things as lighting, heating, cleaning, repairing, and opening and closing the premises, etc.

Space rented for the storage of goods in a warehouse where no walls separate the goods, and exclusive right to the space is not provided, shall be included in the other floor space of the warehouse business.

(7) Examples.

(a) Taxpayer A Retailer or Wholesaler.

Taxpayer A is located in Seattle and sells and delivers \$1 million worth of goods to customers located in unincorporated King County or other cities that do not impose an eligible gross receipts tax. Total gross income from sales is \$4 million, generated from 8,000 square feet of business floor space (all other sales are delivered within Seattle).

Adjusted gross income and credit percentage computation:

\$4 million (Total gross sales) less \$1 million (Unincorporated King County and other city sales) = \$3 million (Adjusted Gross Income).

The credit percentage against the square footage is equal to:

Adjusted gross income \$3 million = 75 %

Total gross income \$4 million

75 % of the gross sales were in Seattle and subject to the business license tax; therefore Taxpayer A would pay only 25 % of the calculated square footage business tax.

Square footage tax computation:

8,000 sq. ft (business floor space) X \$1.56 (annual business floor space tax rate) X 25 % (percentage of tax owed) = \$3,120 (annual square footage business tax owed after credit).

Under the business license tax, with the new deduction for sales delivered outside of Seattle, and the new square footage business tax, the total tax for Taxpayer A would equal:

Business license tax: \$3 million X .00215 (retailing tax rate) = \$6,450.

Square footage tax = \$3,120.

Total tax due under new provisions = \$9,570 (\$6,450 + \$3,120)

Under the old business license tax provisions Taxpayer A would have paid tax on the \$4 million dollars at the .00215 tax rate.

Business license tax due under the old tax provisions: \$4 million X .00215 = \$8,600

Maximum square footage tax credit computation:

To determine eligibility for the maximum square footage tax credit, you must compute the business license tax liability that would have been imposed under the tax provisions in effect prior to January 1, 2008 (SMC 5.45.080). If this number is less than the business tax imposed under the current tax provisions, effective January 1, 2008, you are eligible for the maximum square footage tax credit.

In this case, Taxpayer A owes \$9,570 under the new tax provisions (prior to taking the maximum square footage credit) while under the tax provisions in effect prior to January 1, 2008, Taxpayer A would have owed \$8,600.

\$9,570 minus \$8,600 = \$970 (maximum square footage business tax credit)

\$3,120 (sq. ft. tax) minus \$970 (maximum sq. ft. tax credit) = \$2,150 (actual square footage business tax owed after all credits)

Total tax due by Taxpayer A after all credits. \$9,570 minus \$970 = \$8,600.

(b) Taxpayer X Retailer or Wholesaler with sales into other B & O cities.

Taxpayer X is located in Seattle and sells and delivers \$1 million worth of goods to customers located in unincorporated King County or other cities in Washington that do not impose an eligible gross receipts tax. Taxpayer X sells and delivers \$1 million worth of goods to customers located in other cities in Washington that subjects the sales to an eligible gross receipts tax. Total gross income from sales is \$4 million, generated from 8,000 square feet of business floor space (all other sales are delivered within Seattle).

Adjusted gross income and credit percentage computation:

\$4 million (Total gross sales) less \$1 million (Unincorporated King County and other non B & O city sales) = \$3 million (Adjusted Gross Income).

The credit percentage against the square footage is equal to:

Adjusted gross income \$3 million = 75%

Total gross income \$4 million

75% of the gross sales were in Seattle and subject to the business license tax; therefore, Taxpayer X would pay only 25% of the calculated square footage business tax.

Square footage tax computation:

8,000 sq. ft (business floor space) X \$1.56 (annual business floor space tax rate) X 25% (percentage of tax owed) = \$3,120 (annual square footage business tax owed after credit).

Under the business license tax, with the new deduction for sales delivered outside of Seattle, and the new square footage business tax, the total tax for Taxpayer X would equal:

Business license tax: \$2 million X .00215 (retailing tax rate) = \$4,300.

Square footage tax = \$3,120.

Total tax due by Taxpayer X under new provisions = \$7,420 (\$4,300 + \$3,120)

Under the old business license tax provisions Taxpayer X would have paid tax on the \$3 million dollars at the .00215 tax rate. (Tax would not have been paid on the sales into other eligible gross receipts tax cities.)

Business license tax due under old tax provisions: \$3 million X .00215 = \$6,450.

Maximum square footage tax credit computation:

To determine eligibility for the maximum square footage tax credit, you must compute the business license tax liability that would have been imposed under the tax provisions in effect prior to January 1, 2008 (SMC 5.45.080). If this number is less than the business tax imposed under the current tax provisions, effective January 1, 2008, you are eligible for the maximum square footage tax credit.

In this case, Taxpayer X owes \$7,420 under the new tax provisions (prior to taking the maximum square footage credit) while under the tax provisions in effect prior to January 1, 2008, Taxpayer X would have owed \$6,450.

\$7,420 minus \$6,450 = \$970 (maximum square footage business tax credit)

\$3,120 (sq. ft. tax) minus \$970 (maximum sq. ft. tax credit) = \$2,150 (actual square footage business tax owed after all credits)

Total tax due by Taxpayer X after all credits = \$7,420 minus \$970 = \$6,450.

(c) Taxpayer B Service business.

Taxpayer B, located in Seattle, received \$2 million for audit services it provided to businesses located outside of Seattle but within Washington (audit work was predominately completed at customers' locations). Taxpayer B also provided audit services in Seattle totaling \$2 million. Taxpayer B's total gross income equals \$4 million. All payroll is primarily assigned to the Seattle business location. Taxpayer B maintained 10,000 square feet of business floor space. The new method under SMC 5.45.081 C or RCW 35.102.130(3) requires the taxpayer to use a two-factor formula (payroll and service income) for computing the taxable service income under the business license tax.

Adjusted gross income and credit percentage computation:

(payroll factor + service factor) X total revenue = service income 2 subject to tax in Seattle

or,

(100 % + 50 %) X \$4 million = \$3 million subject to the business 2 license tax.

Prior to January 1, 2008, the service income generated by the Seattle office was taxable by the City of Seattle unless another eligible gross receipts tax city taxed a portion of the service income. Assuming that no other city with an eligible gross receipts tax subjected any of the gross income to tax, the entire \$4 million in service income was subject to tax.

Based on these facts, the adjusted gross income and the credit percentage are calculated as follows:

\$4 million (total gross income) less \$1 million (difference between previous tax code and new tax code) = \$3 million adjusted gross income.

The credit against the square footage business tax would be:

\$3 million (adjusted gross income) = 75% credit against sq. ft. tax \$4 million (total gross income)

Square footage tax computation:

Taxpayer B would pay 25% of its square footage business tax. 10,000 sq. ft X \$1.56 (tax rate) X 25 percent = \$3,900 in annual square footage business tax.

Under the business license tax, using the new two-factor formula, and the new square footage business tax, the total tax due by Taxpayer B would equal:

Business license tax: \$3 million X .00415 (service tax rate) = \$12,450. Square footage business tax = \$3,900.

Total tax due under the new provision: 12,450 + \$3,900 = \$16,350

Maximum square footage business tax credit computation:

\$4 million in service income multiplied by the service tax rate of .00415 results in a tax that would have been due under the provisions in effect prior to January 1, 2008 of \$16,600. Since this is more than the \$16,350 owed by Taxpayer B under the new provisions, there is no maximum square footage business tax credit available.

(d) Taxpayer C -Combination business with retail/wholesale and service activities.

Taxpayer C is located in Seattle and maintained 18,000 square feet of business floor space. Taxpayer C generated Washington retail and wholesale sales of \$8 million of which \$1 million were to other B & O cities and \$3 million were into unincorporated areas or into cities without an eligible gross receipt tax. The remaining \$4 million were sold within Seattle.

Service income of \$2 million was generated within Seattle (where the majority of contacts with the taxpayer took place). Additional service income was generated by Taxpayer C by providing services outside of Seattle, but within Washington, (where the majority of contacts with the taxpayer took place) totaling \$2 million. Total service income was \$4 million. All service payroll is sourced to Seattle. Of the \$2 million in service provided outside of Seattle, \$1 million was provided within other B & O cities.

Total income equals \$12 million.

Adjusted gross income and credit percentage computation:

Retail/wholesale.

\$8 million in sales less \$3 million delivered into unincorporated areas and non B & O cities = \$5 million adjusted gross income.

Service income.

100% payroll + 50% revenue = 75% then multiply by \$4 million revenue = \$3 million

2

Adjust gross service income:

\$4 million in service income less \$1 million in service income that is excluded from the business license tax because of the two-factor formula per Taxpayer C above - adjusted service gross income is equal to \$3 million.

Total adjusted gross income = \$8 million (\$5 million plus \$3 million)

To compute the square footage business tax credit:

\$8 million = 67 % credit against the sq. ft. tax. 33% of the square footage tax due.

\$12 million

Square footage tax computation:

To compute the square footage business tax due:

18,000 sq. ft X \$1.56 (tax rate) X 33 percent = \$9,266 in sq. ft. tax is due.

Total taxes due for Taxpayer C above using tax code after 1-1-08:

Square footage business tax \$ 9,266 Retailing/wholesaling business license tax (\$4 million X .00215) \$ 8,600 Service and other business license tax (\$3 million X .00415) \$12,450 Total taxes due under new tax provisions \$30,316

Maximum square footage business tax credit computation:

If the square footage business tax and the new requirements contained in SMC 5.45.081 and RCW 35.102.130 had not taken effect, the total taxes due would have been:

Retailing/wholesaling business license taxes (\$7M X .00215)* \$15,050 Service business license taxes (\$3M X .00415)* \$12,450 Total business license taxes due \$27,500 *Does not include selling or service income provided into other gross receipts B & O cities.

The increase in tax due under the square footage business tax and new business license tax provisions is as follows:

Total taxes due under new tax provisions \$30,316 Total taxes due under SMC 5.45 without new tax provisions \$27,500 Increase in total taxes owed-amount of maximum credit \$ 2,816

\$2,816 would then be credited against the square footage business tax due as computed for Taxpayer C above. This would result in the following total square footage business tax due, after all credits:

Total square footage tax due for Taxpayer C above \$9,266 Less maximum square footage business tax credit \$2,816 Square footage business tax due \$6,450

Effective: April 18, 2008.



Seattle City Council

Office of the Mayor

Office of the City Clerk

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