



TaxNewsFlash

United States



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Washington State: Penalties on unified annual reconciliation of apportionable income

The Washington State tax authority continues to impose penalties as high as 29% on taxpayers that do not file an [Annual Reconciliation of Apportionable Income Form \(ARAI\)](#) [PDF 293 KB]. Thus, all businesses that report apportionable income on timely filed Washington State combined excise tax returns in 2021 may need to file the ARAI by October 31, 2022, even when the reconciliation results in a “no change” return.

In addition, those taxpayers that reported revenues under only the retailing, wholesaling, or manufacturing classifications may wish to file the ARAI if there is any potential for a reclassification of receipts into an apportionable income category (e.g., services and other).

Background

The Washington State business and occupation (B&O) tax is a gross receipts tax measured by the value of products, gross proceeds, or gross income of a business. The B&O tax employs various tax classifications—most commonly “retailing,” “wholesaling,” “manufacturing,” and “service and other” activities. The service and other classification captures any activity not explicitly taxed under another B&O tax classification. Income from certain business activities, such as service and other, is deemed apportionable income. This means that the taxpayer must apply an apportionment factor to calculate the deduction for income derived outside Washington State to arrive at income subject to Washington State B&O tax. Most taxpayers are required to file and remit B&O tax on a monthly basis, while certain other taxpayers file and remit B&O tax on a quarterly or annual basis.

Taxpayers reporting apportionable income are permitted to calculate the receipts factor for the current tax year based on the most recent calendar year for which information is available for all 12 months. Alternatively, taxpayers may calculate the receipts factor based on current year information. In either case, RCW 82.04.462(4) requires a taxpayer to file an annual reconciliation by October 31 of the following tax year that corrects the reporting for the current year. WAC 458-20-19402 makes clear that the reconciliation must be filed regardless of whether a refund or additional tax is due. If the annual reconciliation is not filed with any additional tax paid by October 31, penalties apply on any additional tax due. Penalties are assessed at a rate of 9% if the reconciliation is not filed and tax has not been paid by the due date; 19% after 30 days, and 29% after 60 days.

The tax authority takes the position that the 29% penalty for failing to file an annual reconciliation applies to any additional tax assessed on apportionable income even if the taxpayer did not report any apportionable income

on its timely filed original returns. It is not uncommon for taxpayers that do not otherwise report apportionable income on their returns to be assessed tax on apportionable income on audit. This can occur for a variety of reasons. For example, the tax authority may reclassify a taxpayer's receipts from retailing to service and other receipts, which are taxed at a higher B&O rate than retailing receipts. Another common scenario is that a taxpayer may have receipts—such as intercompany receipts—that it failed to include on its timely filed returns. As a result, there is a risk that taxpayers could be assessed tax on apportionable income on audit and be subject to the 29% penalty even if they are currently filing only under non-apportionable income B&O tax classifications (e.g., retailing, wholesaling, or manufacturing).

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