

Seattle Rule 5-980 Payroll Expense Tax

Seattle Rule 5-980 Payroll Expense Tax

(1) Introduction: The City Council recognizes that the affordable housing crisis, homelessness emergency, and now the COVID-19 pandemic and the accompanying economic downturn and unemployment are deeply impacting the lives of people throughout Seattle. The JumpStart Seattle Progressive Revenue Plan will help to address these crises by funding investment in rental assistance programs, providing resources for non-profit affordable housing, the City's grocery voucher program and cash assistance to small businesses.

Effective January of 2021, the City of Seattle will impose a payroll expense tax on businesses operating in Seattle. The new payroll expense tax is based on a business's annual Seattle payroll expense attributable to employee annual compensation of \$150,000 or more in the current year. A business must have at least \$7 million in Seattle payroll in the prior calendar year to be subject to the tax.

(2) Definitions: For purposes of this rule, the following definitions will apply:

- (a) **"Compensation"** includes "Remuneration" as defined by the Washington State Family and Medical Leave program as currently or subsequently amended.
- (i) The name by which employee compensation is designated is immaterial and includes all payments for personal services, including commissions and bonuses and the cash value of all earnings paid in any medium other than cash.
 - (ii) Based on the guidance from the Washington State Employment Security Department, compensation **includes:**
 - (A) Salary or hourly wages;
 - (B) Cash value of goods or services given in the place of money;
 - (C) Commissions or piecework;
 - (D) Bonuses;
 - (E) Cash value of gifts or prizes;
 - (F) Cash value of meals and lodging when given as compensation;
 - (G) Holiday pay;
 - (H) Paid time off (vacation, sick leave, associated cash outs);
 - (I) Separation pay such as severance pay, termination pay, or wages in lieu of notice;
 - (J) The value of stocks at the time of transfer to an employee if part of a compensation package (i.e., stock grants, Restricted Stock Units (RSUs)); and
 - (K) Stipends and per diems (unless provided to cover a past or future cost incurred by the worker as a result of the worker's expected job functions).
 - (iii) In addition, for purposes of the payroll expense tax, compensation also includes:

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- (A) Employee contributions to deferred compensation plans (e.g. 401(k), 403(b), or other deferred compensation plans) in which a portion of an employee's salary or wages that are set aside to be paid at a later date;
 - (B) Net distributions, or incentive payments, including guaranteed payments earned for services rendered or work performed, whether paid directly or through an agent. "Net distribution" means the draws from net income by any owner of a pass-through entity. Taxable distributions are limited by the amount of draws or net income for that owner, whichever is less; and
- (iv) Compensation does **not** include:
- (A) Tips;
 - (B) Supplemental benefit payments as defined in WAC 192-510-025 made by an employer to an employee in addition to any paid family or medical leave benefits received by the employee;
 - (C) Employee exercised stock options (incentive stock options (ISOs) or non-qualified stock options (NQSOs));
 - (D) Payments provided to cover a past or future cost incurred by the worker as a result of the worker's expected job functions; or
 - (E) Employer contributions into retirement or disability plans; and
 - (F) Payments to an owner of a pass-through entity that are not earned for services rendered or work performed (i.e., return of capital, investment income, or other passive activities).

Example 1: Employee X is hired by Able Corp to work at their Seattle office. X's total compensation is \$175,000 per year and X decides to contribute 5% of their \$175,000 compensation into the Able Corp 401K plan. Assuming Able Corp is subject to the payroll expense tax, when Able Corp determines its payroll expense tax due, Able Corp must include employee X's total annual compensation of \$175,000. An employee's contributions to retirement plans are not excluded when determining compensation subject to the Seattle's payroll expense tax.

Example 2: In 2021, Employee Y is hired by Able Corp and has an annual salary of \$160,000. Employee Y also receives 4,000 Restricted Stock Units (RSUs) that vest at a rate of 25% a year. In 2021, the value of the stock at vesting is \$20,000. The value of stocks at the time of transfer (vesting) is part of a compensation package and is considered compensation for the payroll expense tax. Employee Y's total compensation for purposes of Able Corp's payroll expense tax is \$180,000 (\$160,000 salary + \$20,000 vested RSUs).

Example 3: Same as Example 2, except Employee Y receives 4,000 non-qualified stock options (NQSOs). Y exercises 1,000 options in 2021. Employee exercised stock options

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are not considered compensation, so they will not be included in Able Corp's payroll expense.

Example 4: While on paid medical leave, an employee receives 61% of the employee's typical weekly wage from the State of Washington and the employer paid the employee the remaining 39% of the employee's typical weekly wage as a supplemental benefit payment. The payments made to the employee from the State of Washington and the supplemental benefit payments from the employer are not compensation for purposes of the payroll expense tax.

- (b) **"Employee"** means any individual who performs work, labor or personal services of any nature for compensation paid by a business and includes:
- (i) Individuals who are members of limited liability companies, members of professional limited liability companies, partners, other owners of pass-through entities and sole proprietors; and
 - (ii) Independent contractors, who are individuals contracted to perform work or provide services to another entity and are not considered to be employees under the common law rules of the employer-employee relationship.

Example 5: LMN is a partnership based in Seattle and subject to the payroll expense tax because its prior calendar years' total compensation paid in Seattle was over \$7 million. During the current year, LMN had \$5 million of compensation paid in Seattle to non-partner employees and \$5 million in net distributions paid in Seattle to partners who performed work for LMN. Partners share of net distributions are considered compensation paid by the partnership under the payroll expense tax. Therefore, LMN's total payroll expense in Seattle is \$10 million.

Example 6: Same as Example 5, except that LMN also has limited partners in Seattle that do not provide services or perform work for the partnership. Rather, the limited partners are merely investors in the partnership. In addition to the \$10 million in compensation paid to the employees and general partners, LMN also distributes another \$2 million in net distributions to its limited partners. LMN's total compensation paid in Seattle is still \$10 million. LMN does not include the \$2 million paid to its limited partners in its total payroll expense because for the purposes of the payroll expense tax, compensation excludes payments made to owners of pass-through entities that are not earned for services rendered or work performed.

- (c) **"Payroll expense"** means compensation paid in Seattle to employees.
- (i) Compensation is paid in Seattle to an employee if:
 - (A) The employee is primarily assigned within Seattle;

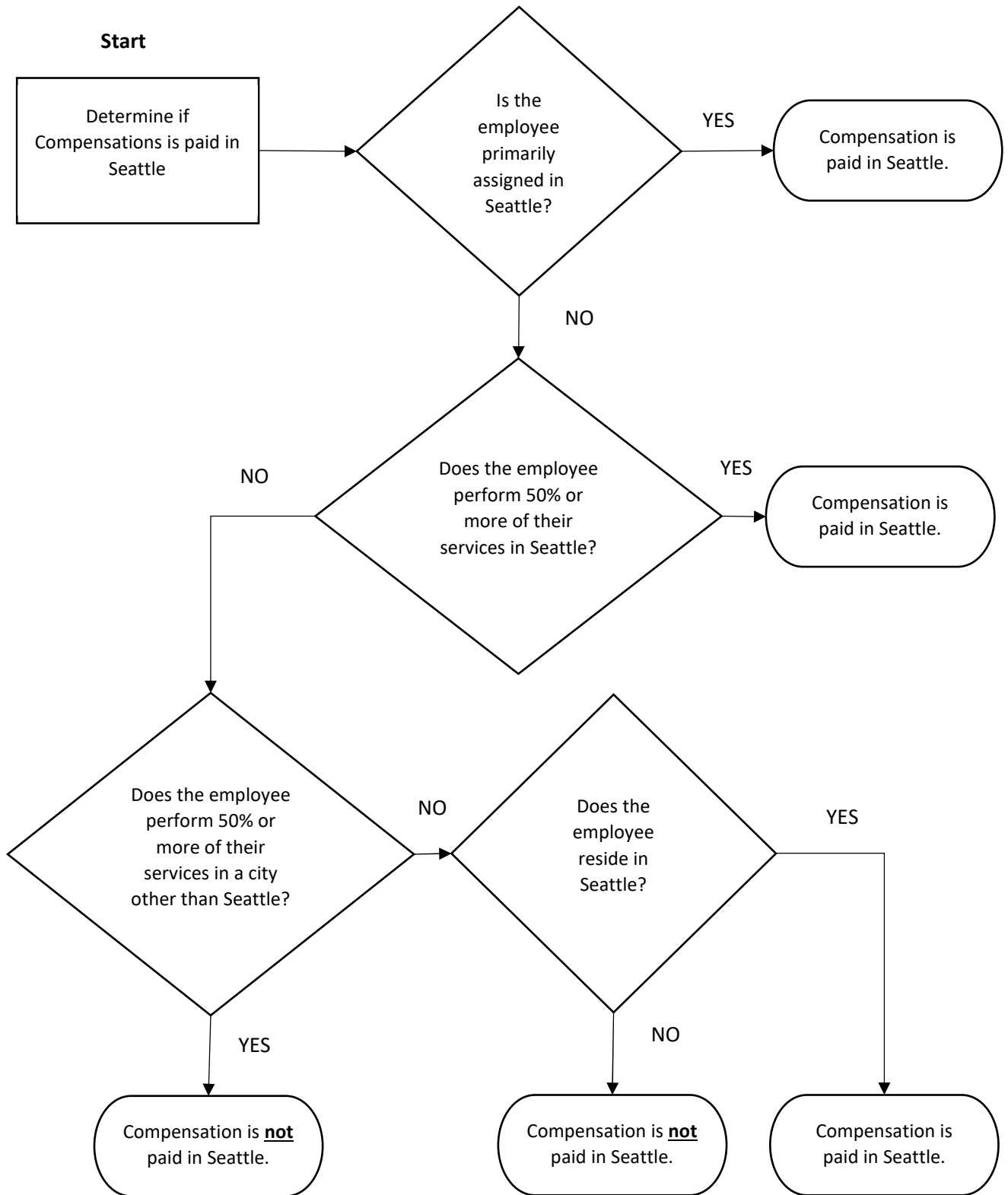
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- (B) The employee is not primarily assigned to any place of business for the tax period and the employee performs 50% or more of their service for the tax period in Seattle; or
 - (C) The employee is not primarily assigned to any place of business for the tax period, the employee does not perform 50% or more of their service in any city, and the employee resides in Seattle.
- (ii) “Tax period” means the calendar year during which tax liability is accrued.
- (d) **“Primarily assigned”** means the business location of the taxpayer where the employee performs their duties for the tax period. An employee that performs more than 50% of their duties at the business location of the taxpayer will be primarily assigned to that business location. An employee’s home is not a business location of the taxpayer.

The City of Seattle offers the following decision tree to aid businesses on how they should determine compensation paid in Seattle

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Compensation Paid in Seattle



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Example 7: Company A has three employees in Seattle in 2020, Employee X, Employee Y, & Employee Z. All three employees perform their duties at Company A's headquarters in Seattle. X, Y & Z are primarily assigned in Seattle because they perform their duties at Company A's business location in Seattle. Therefore, compensation paid to X, Y & Z is paid in Seattle and included in Company A's payroll expense.

Example 8: Same as Example 7, except Employee Z does not perform their duties at the Seattle headquarters for the tax period. Employee Z performs 60% of their service for the tax period at a client's worksite in Kent during the tax period. Therefore, only compensation paid to X and Y is paid in Seattle. Compensation paid to Employee Z is not paid in Seattle because Employee Z is not primarily assigned in Seattle and they perform 50% or more of their service at a location outside Seattle.

Example 9: Same as Example 7, except employees Y & Z telework from home. Employee Y's home is in Kent, WA and Employee Z's home is in Seattle, WA. Employee X performs their duties at Company A's business location in Seattle. Compensation paid to Employees X and Z is paid in Seattle because X is primarily assigned to Company A's office in Seattle and Employee Z performs 50% or more of their duties at Employee Z's home located in Seattle. Compensation paid to Y is not paid in Seattle because Y is not primarily assigned in Seattle and does not perform 50% or more of their duties in Seattle and does not live in Seattle.

(3) Tax rate and measure: Chapter 5.38.030 of the Seattle Municipal Code imposes a tax on the payroll expense of every person engaging in business within Seattle. The payroll expense tax has a progressive tax rate structure.

- (a) The payroll expense tax is computed on the total payroll expense paid in Seattle to employees with annual compensation of \$150,000 or more. Rates are applied to the total annual compensation paid in Seattle of employees with annual compensation of \$150,000 or more but less than \$400,000, and employees with annual compensation of \$400,000 or more. The tax rates also increase as a company's total compensation paid in Seattle increases.
- (b) The amount of the payroll expense tax due shall be the payroll expense of the business in the current calendar year (less deductions if applicable in subsection (5) of the rule) multiplied by the following rates:

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	Annual compensation \$0 - \$149,999.99	Annual compensation \$150,000 - \$399,999.99	Annual compensation Greater than \$400,000
Annual Payroll Expense less than \$100M	N/A	Rate = 0.7% (Seven-tenths percent)	Rate = 1.7% (One and seven-tenths percent)
Annual Payroll Expense greater than \$100M, but less \$1B	N/A	Rate = 0.7% (Seven-tenths percent)	Rate = 1.9% (One and nine-tenths percent)
Annual Payroll Expense of \$1B or greater	N/A	Rate = 1.4% (One and four-tenths percent)	Rate = 2.4% (Two and four-tenths percent)

Example 10: Company A has employees in Seattle. In 2020, Company A had \$9 million of Seattle payroll expense and \$10 million of Seattle payroll expense in 2021. In 2021, Company A has 55 employees that earn \$100,000 per year, 10 employees that earn \$200,000 per year, and 5 employees that earn \$500,000 per year.

Company A's 2021 Seattle Payroll Expense Tax would be:

COMPANY A					
Payroll in Seattle (Prior Year)		\$ 9 million			
Payroll in Seattle (Current)		\$ 10 million			
	# of Emp.	Ann. Salary	Payroll Exp	Rate	Tax
Not Taxable	55	\$100,000	\$5,500,000	N/A	\$0
Tier 1	10	200,000	2,000,000	0.70%	14,000
Tier 2	5	500,000	2,500,000	1.70%	42,500
TOTAL	70		\$10,000,000		\$56,500

Example 11: Company B has 11,100 employees in Seattle. In 2020, Company C had \$1.1 billion of Seattle payroll expense and \$1.2 billion of Seattle payroll expense in 2021. In 2021, Company B has 10,500 employees that earn \$100,000 per year, 500 employees that earn \$200,000 per year and 100 employees that earn 500,000 per year.

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Company B's 2021 Seattle Payroll Expense Tax would be:

COMPANY B					
Payroll in Seattle (Prior Year)		\$ 1.1 billion			
Payroll in Seattle (Current)		\$ 1.2 billion			
	# of Emp.	Ann. Salary	Payroll Exp	Rate	Tax
Not Taxable	10,500	\$100,000	\$1,050,000,000	N/A	\$0
Tier 1	500	200,000	\$100,000,000	1.40%	1,400,000
Tier 2	100	500,000	\$50,000,000	2.40%	1,200,000
TOTAL	11,100		\$1,200,000,000		\$2,600,000

Example 12: Same as Example 11, except Company B has \$750 million of Seattle payroll expense in 2021. In 2021, Company A has 6,600 employees that earn \$100,000 per year, 300 employees that earn \$200,000 per year, and 60 employees that earn \$500,000 per year.

Company B's 2021 Seattle Payroll Expense Tax would be:

COMPANY B					
Payroll in Seattle (Prior Year)		\$ 1.1 billion			
Payroll in Seattle (Current)		\$ 750 million			
	# of Emp.	Ann. Salary	Payroll Exp	Rate	Tax
Not Taxable	6,600	\$100,000	\$660,000,000	N/A	\$0
Tier 1	300	200,000	60,000,000	0.70%	420,000
Tier 2	60	500,000	30,000,000	1.90%	570,000
TOTAL	6,960		\$750,000,000		\$990,000

In 2021 (the current year), Company B's annual payroll expense is greater than \$100 million, but less than \$1 billion, therefore, Company B's rates are 0.7% of the payroll expense of employees with annual compensation of \$150,000 to \$399,999.99 and 1.9% of the payroll expense of employees with annual compensation greater of \$400,000 or more.

(4) Exemptions:

- (a) The following are exempt from the payroll expense tax:
 - (i) Any business having compensation paid in Seattle to employees of less than \$7 million in the previous calendar year.

Example 13: In the prior calendar year, 2020, Company A had Seattle payroll expense of \$9 million. In 2021, Company A has \$5 million of Seattle payroll expense. 25 employees

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earn \$100,000 per year, 5 employees earn \$200,000 per year and 3 employees earn \$500,000 per year.

Company A's 2021 Seattle Payroll Expense Tax would be:

COMPANY A					
Payroll in Seattle (Prior Year)		\$ 9 million			
Payroll in Seattle (Current)		\$ 5 million			
	# of Emp.	Ann. Salary	Payroll Exp	Rate	Tax
Not Taxable	25	\$100,000	\$2,500,000	N/A	\$0
Tier 1	5	200,000	1,000,000	0.70%	7,000
Tier 2	3	500,000	1,500,000	1.70%	25,500
TOTAL	33		\$5,000,000		\$32,500

The City of Seattle will impose a tax on businesses operating in Seattle with \$7 million or more in payroll expense in the previous year. Company A had more than \$7 million of payroll expense in 2020 and is subject to the payroll expense tax in 2021. (see subsection (1). However, because Company A had less than \$7 million of payroll expense in 2021, the company will not subject to the payroll expense tax in 2022 (see subsection (5)(a)(i)).

(ii) Any person engaged in a grocery business. **“Grocery business”** means a business where at least 70% of the gross income of the business for purposes of calculating the business license tax under SMC Chapter 5.45 is attributable to making retail or wholesales sales of food and food ingredients that will be exempt from the retail sales tax under RCW 82.08.0293.

Example 14: ABC is a retail supermarket chain that sells food and food ingredients. Seventy-five percent of ABC's retail sales are exempt from the retail sales tax. ABC is exempt from the payroll expense tax because 70% or more of its retail sales are exempt from the retail sales tax.

Example 15: DEF is a wholesaler of food and food ingredients who sells products to ABC a retail supermarket chain. When ABC resells DEF products, they are exempt from the retail sales tax. DEF is exempt from the payroll expense tax because its products are exempt from the retail sales tax when resold by ABC.

Example 16: QRS is a manufacturer of food and food ingredients. All of QRS's sales are wholesale sales to customers that are wholesalers who resell QRS products to retailers and other wholesale distributors. The wholesale sale of QRS food and food ingredients

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to QRS's customers are exempt from the retail sale tax. QRS is deemed a grocery business because more than 70% of its sales are exempt from the retail sales tax. Therefore, QRS is exempt from the payroll expense tax.

(iii) Compensation paid in Seattle to an independent contractor whose compensation is included in another business's payroll expense.

Example 17: Company R hires an individual independent contractor, Individual Z, for consulting services and agrees to pay them \$175,000 in 2021. Individual Z is a sole proprietor and is an independent contractor for purposes of the business license tax. Assuming Company R is subject to the payroll expense tax, Company R would include Individual Z's total annual compensation of \$175,000 in Company R's payroll expense. Individual Z is considered an employee of Company R for purposes of the payroll expense tax. Individual Z would not include payments received from Company R as compensation for purposes of the Seattle payroll expense tax because that amount is included in company R's calculation of its Seattle payroll expense.

Example 18: Same as example 17, except that Individual Z provides consulting services to Company R and Company S. Companies R and S each pay Individual Z \$175,000 in 2021 for consulting services. Assuming that both Company R and Company S are subject to the payroll expense tax, Company R will include \$175,000 of compensation paid to Z in its payroll expense and Company S will also include the \$175,000 of compensation it paid to Z in its payroll expense.

Example 19: In 2021, Company R hires an independent contractor Small Tech LLC, for consulting services and agrees to pay Small Tech LLC \$175,000 in consulting fees. Individual E is an employee of Small Tech LLC and is assigned by Small Tech LLC to perform the consulting services requested by Company R. In this example, Individual E's compensation is included in the payroll expense of Small Tech LLC because Individual E is an employee of Small Tech LLC. Company R would not include the consulting fees paid to Small Tech LLC in Company R's payroll expense because Small Tech LLC is not an individual independent contractor.

(iv) Any business engaged in business in Seattle that is preempted from taxation by cities under federal or state statutes or regulations, including, but not limited to, the following:

- (A) Insurance businesses and their appointed insurance producers whose revenue is exempt from the business license tax;
- (B) Businesses that only sell, manufacture, or distribute motor vehicle fuel;

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- (C) Businesses that only distribute or sell liquor defined as alcohol, spirits, wine, and beer, and all fermented, spirituous, vinous, or malt liquor, or combinations thereof;
 - (D) Federal and State government agencies and any local governmental entity.
- (b) To the extent that a business activities listed in Section (4)(a)(iv) that are pre-empted from taxation but also engages in activities not preempted from taxation, the business will be allowed to exclude the payroll expense attributable to those activities preempted from taxation by:
- (i) excluding compensation of employees exclusively engaged in supporting those activities preempted from taxation; and or
 - (ii) that portion of compensation paid to employees engaged in supporting those activities preempted from taxation but also not preempted from taxation equal to such employee compensation multiplied by a ratio equal to the gross income of the business from activities preempted from taxation over the total gross income of the business.

Example 20: Company L is a distributor of alcohol in Seattle. In addition to distributing alcohol products it also distributes some non-alcoholic drink items such as mixers and soda. Ninety percent of Company L's revenue is from the sales of alcohol and ten percent is from the sale of non-alcoholic items. In addition, all of Company L's employees support activities in selling and distributing both alcohol and non-alcoholic items. Assuming Company R is subject to the payroll expense tax, Company L would be able to exclude 90% of their payroll expense.

- (5) **Temporary or contracted employees:** Businesses that hire temporary or contracted employees shall include the temporary or contracted employees' compensation in their payroll expense, regardless of if the temporary or contracted employees are from an employment agency.

Example 21: Company A engages Temp Agency Corp to recruit and fill a temporary position at Company A. Temp Agency Corp performs all recruiting, interviewing, and background check services and identifies Individual T as its top candidate for Company A. Individual T is hired by Company A on a temporary basis. Company A is T's employer and responsible for T's employment costs (including but not limited to employment taxes and state unemployment insurance). Assuming Company A is subject to the payroll expense tax, compensation paid to Individual T is included in Company A's payroll expense tax calculation because individual T is an employee of Company A.

Example 22: Company B hires Temp Agency Corp to provide temporary staff. Temp Agency Corp employs several individuals that it hires out to companies that require

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temporary labor solutions. Company B contracts with Temp Agency Corp to fill two temporary positions for a project expected to last through the year. Temp Agency Corp assigns two of its employees, individuals X and Y to Company B. Temp Agency Corp regularly invoices Company B at the agreed rates for the temporary staff assigned to Company B during the year. Individuals X and Y are employed and paid by Temp Agency Corp for their services. Assuming Temp Agency Corp is subject to the payroll expense tax, Temp Agency Corp would include compensation paid to individuals X and Y in its payroll expense because X and Y are employees of Temp Agency Corp.

(6) Deductions:

- (a) From January 1, 2021, through December 31, 2023, taxpayers that are non-profit healthcare entities may deduct from the measure of the tax the payroll expense of employees with annual compensation of \$150,000 to \$399,999.99.
 - (i) **“Life Science”** means scientific research whose primary purpose is to understand human biology or pathology, or to improve human health, or to identify appropriate treatment (including ethical and policy aspects) of human disease, including basic research in non-human models (including in silica models).
 - (ii) **“Research and Development”** means activities performed to discover technological information, and technical and non-routine activities concerned with translating technological information into new or improved products, processes, techniques, formulas, inventions, or software.
 - (A) Research and Development includes exploration of a new use for an existing drug, device, or biological product if the new use requires separate licensing by the United States Food and Drug Administration under Chapter 21 in the Code of Federal Regulations, as amended.
 - (B) Research and Development does not include adaptation or duplication of existing products where the products are not substantially improved by application of the technology, nor does the term include surveys and studies not related to development, social science and humanities research, market research or testing, quality control, sale promotion and service, computer software developed for internal use, and research in areas such as improved style, taste, and seasonal design.

Example 23: Company M is a non-profit healthcare entity and has employees in Seattle. In 2020, Company M had \$9 million of payroll expense and \$10 million of payroll expense in 2021. In 2021, Company M has 55 employees that earn \$100,000 per year, 10 employees that earn \$200,000 per year, and 5 employees that earn \$500,000 per year. Assuming Company M is subject to the payroll expense tax, Company M would deduct the compensation of employees with annual compensation of \$150,000 to \$399,999.99 from their payroll expense.

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Company M's 2021 Seattle Payroll Expense Tax would be:

COMPANY M							
Payroll in Seattle (2020)		\$ 9 million					
Payroll in Seattle (2021)		\$ 10 million					
	# of Emp.	Ann. Salary	Payroll Exp	Deduction	Taxable Payroll Exp	Rate	Tax
Not Taxable	55	\$100,000	\$ 5,500,000		\$ -	N/A	\$0
Tier 1	10	200,000	2,000,000	(2,000,000)	\$ -	0.70%	0
Tier 2	5	500,000	2,500,000		\$ 2,500,000	1.70%	42,500
TOTAL			\$10,000,000		\$2,500,000		\$42,500

Company M may deduct the compensation of employees with annual compensation of \$150,000 to \$399,999.99 because it qualifies as a non-profit healthcare entity.

(7) Allocation and apportionment:

- (a) The tax administrator may adopt procedures to allow taxpayers who have payroll expenses consisting of work done and services provided within and outside Seattle to use a representative test period or conduct a survey based on factual data to arrive at a formula with which to calculate the percentage of payroll expense attributable to Seattle. Any formula so established will be subject to review and correction by the tax administrator. This section is strictly used to determine and establish a method to determine if an employee is primarily assigned to the business location of the taxpayer.
- (b) If the allocation and apportionment provisions of Chapter 5.38 of the Seattle Municipal Code, do not fairly represent the extent of the taxpayer's business activity in the city, the taxpayer may petition for or the tax administrator may require, in respect to all or any part of the taxpayer's business activity, the employment of any other method to effectuate an equitable allocation and apportionment of the payroll expense tax.
- (c) Taxpayers seeking an alternative apportionment calculation must submit a request to the tax administrator for approval prior to the application of any alternative apportionment formula
- (d) The party petitioning for, or the tax administrator requiring, the use of any method to effectuate an equitable allocation and apportionment of the payroll expense must prove by a preponderance of the evidence:
 - (i) That the allocation and apportionment provisions of this subsection (8) do not fairly represent the extent of the taxpayer's business activity in the city; and

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- (ii) That the alternative to such provisions is reasonable. The same burden of proof shall apply whether the taxpayer is petitioning for, or the tax administrator is requiring, the use of an alternative, reasonable method to effectuate an equitable allocation and apportionment of the taxpayer's income.
 - (e) If the tax administrator requires any method to effectuate an equitable allocation and apportionment of the taxpayer's income, the tax administrator cannot impose any civil or criminal penalty with reference to the tax due that is attributable to the taxpayer's reasonable reliance solely on the allocation and apportionment provisions of this subsection (7).
 - (f) A taxpayer that has received written permission from the tax administrator to use a reasonable method to effectuate an equitable allocation and apportionment of the taxpayer's income shall not have that permission revoked with respect to transactions and activities that have already occurred unless there has been a material change in, or a material misrepresentation of, the facts provided by the taxpayer upon which the tax administrator reasonably relied in approving a reasonable alternative method.
 - (g) Nothing in rule shall be construed as requiring the payment of any tax for engaging in business when such payment would be in violation of the Constitution or a statute of the United States or of the Constitution or a statute of the State of Washington.
 - (h) A business is allowed a credit to the extent necessary to preserve the validity of the City's tax, and still apply the City's tax to as much of the business's activities as may be subject to the City's taxing authority.
- (8) When due:**
- (a) All taxes due for the calendar year 2021 shall be due and payable on the fourth quarter tax filing due date of January 31, 2022. For tax years after 2021, the payroll expense tax shall be due and payable on a quarterly installment basis unless assigned a different reporting period by the director.
 - (b) For periods after December 31, 2021, if taxes are reported by a taxpayer on a basis more frequent than once per year, taxpayers may use the Seattle payroll expense in the prior calendar year to estimate reporting in the current calendar year and correct the reporting for the current year amount on the fourth quarter return. Amounts reported on the fourth quarter return would be adjusted in such a way to make correct the payroll expense due for the current calendar year.

Example 24: In 2021, Company A had total payroll expense of \$9 million. Of the \$9 million of total payroll expense it had \$1.5 million payroll expense of employees with annual compensation of \$150,000 to \$399,999.99 and, \$2,000,000 payroll expense of employees with annual compensation of \$400,000 or more. In 2021, Company A's total payroll expense tax due for 2021 was \$44,500. It was reported as follows:

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Company A				
2021 Payroll in Seattle = \$ 9 million				
	Employee Annual Compensation Range	Total Payroll Expense	Rate	Tax
Not Taxable	\$0 - \$149,999.999	\$5,500,000	N/A	\$0
Tier 1	\$150,000 - \$399,999.99	\$1,500,000	0.70%	\$10,500
Tier 2	\$400,000 or more	\$2,000,000	1.70%	\$34,000
TOTAL		\$9,000,000		\$44,500

In 2022, Company A decides to estimate its payroll expense tax using the prior calendar year information. Therefore, for each of quarters one, two and three Company A will estimate its returns by dividing the total payroll expense reported under each tier by 4 to arrive an estimated amount to report in quarter's one, two and three of 2022 and report those quarters as follows:

Quarter 1, 2022				
	Employee Annual Compensation Range	Total Payroll Expense	Rate	Tax
Not Taxable	\$0 - \$149,999.999	\$1,375,000	N/A	\$0
Tier 1	\$150,000 - \$399,999.99	\$375,000	0.70%	\$2,625
Tier 2	\$400,000 or more	\$500,000	1.70%	\$8,500
TOTAL		\$2,250,000		\$11,125

Quarter 2, 2022				
	Employee Annual Compensation Range	Total Payroll Expense	Rate	Tax
Not Taxable	\$0 - \$149,999.999	\$1,375,000	N/A	\$0
Tier 1	\$150,000 - \$399,999.99	\$375,000	0.70%	\$2,625
Tier 2	\$400,000 or more	\$500,000	1.70%	\$8,500
TOTAL		\$2,250,000		\$11,125

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Quarter 3, 2022				
	Employee Annual Compensation Range	Total Payroll Expense	Rate	Tax
Not Taxable	\$0 - \$149,999.999	\$1,375,000	N/A	\$0
Tier 1	\$150,000 - \$399,999.99	\$375,000	0.70%	\$2,625
Tier 2	\$400,000 or more	\$500,000	1.70%	\$8,500
TOTAL		\$2,250,000		\$11,125

At the end of 2022, before filing its fourth quarter return, Company A determines it had total payroll expense in 2022 of \$10,000,000. Of the \$10 million of total payroll expense it had \$2 million payroll expense of employees with annual compensation of \$150,000 to \$399,999.99 and, \$2,500,000 payroll expense of employees with annual compensation of \$400,000 or more. Company A's total annual payroll expense is summarized below:

COMPANY A					
Payroll in Seattle (2022) = \$ 10 million					
	# of Emp.	Ann. Salary	Payroll Exp	Rate	Tax
Not Taxable	55	\$100,000	\$5,500,000	N/A	\$0
Tier 1	10	200,000	2,000,000	0.70%	14,000
Tier 2	5	500,000	2,500,000	1.70%	42,500
TOTAL	70		\$10,000,000		\$56,500

When Company A prepares its fourth quarter return, it will need to adjust it such a way as to make correct the amount for the entire current calendar year. Therefore, the total left to be reported under the first tier is \$875,000 (\$2,000,000 for the entire year less \$1,125,000 [\$375,000 x3] reported in the first three quarters). The total left to be reported under the second tier is \$1,000,000 (\$2,500,000 for the entire year less \$1,500,000 [\$500,000 x 3] reported in the first three quarters.)

Company A will report the following on its fourth quarter return for 2022:

Quarter 4, 2022				
	Employee Annual Compensation Range	Total Payroll Expense	Rate	Tax
Not Taxable	\$0 - \$149,999.999	\$1,375,000	N/A	\$0

Seattle Rule 5-980 Payroll Expense Tax

Tier 1	\$150,000 - \$399,999.99	\$875,000	0.70%	\$6,125
Tier 2	\$400,000 or more	\$1,000,000	1.70%	\$17,000
TOTAL		\$3,250,000		\$23,125

Company A's total payroll expense tax due for 2022 was \$56,500 of which it made total estimated payments of \$33,375 in the first three quarters (\$11,125 x 3) and filed its fourth quarter return in such a way as to report \$23,125 tax due, making correct the amount due for the current year.

Example 25: Similar example 24, in which Company A had total payroll expense of \$9 million in 2021. Of the \$9 million of total payroll expense it had \$1.5 million payroll expense of employees with annual compensation of \$150,000 to \$399,999.99 and, \$2,000,000 payroll expense of employees with annual compensation of \$400,000 or more. Company A estimates its 2022 first, second, and third quarter returns based on its total payroll expense of 2021, same as in Example 24.

However, at the end of the year in 2022, Company A determines its total payroll expense for 2022 was only \$5 million. Of the \$5,000,000 total payroll expense it only had \$1 million payroll expense of employees with annual compensation of \$150,000 to \$399,999.99 and \$1,000,000 payroll expense of employees with annual compensation of \$400,000 or more. Therefore, in 2022 Company A's total payroll expense tax due for 2021 was \$44,500. It was reported as follows:

COMPANY A					
2022 Payroll in Seattle = \$5 million					
	# of Emp.	Ann. Salary	Payroll Exp	Rate	Tax
Not Taxable	30	\$100,000	\$3,000,000	N/A	\$0
Tier 1	5	200,000	1,000,000	0.70%	7,000
Tier 2	2	500,000	1,000,000	1.70%	17,000
TOTAL	37		\$5,000,000		\$24,000

When Company A prepares its fourth quarter return, it will need to adjust it such a way as to make correct the amount for the entire current calendar year.

Therefore, the amount to be reported in quarter four under the first tier is \$250,000 (\$1,000,000 for the entire year divided by 4) and the amount to be reported under the second tier is also \$250,000 (\$1,000,000 for the entire year divided by 4).

Company A will report the following on its fourth quarter return for 2022:

Seattle Rule 5-980 Payroll Expense Tax

Quarter 4, 2022				
	Employee Annual Compensation Range	Total Payroll Expense	Rate	Tax
Not Taxable	\$0 - \$149,999.999	\$750,000	N/A	\$0
Tier 1	\$150,000 - \$399,999.99	\$250,000	0.70%	\$1,750
Tier 2	\$400,000 or more	\$250,000	1.70%	\$4,250
TOTAL		\$1,250,000		\$6,000

Company A will then amend its prior returns for first, second, and third quarters to arrive at the correct amount due for the current year because it estimated and reported \$11,125 tax due based on the payroll expense of the prior calendar year. Therefore, each of quarters will be amended to reflect \$6,000 in payroll expense tax due. This will result in a refund to Company A equal to \$15,375 (3 x [\$11,125 reported less \$6,000 as amended]).

- (9) **Records to be kept by the taxpayer:** Businesses subject to the payroll expense tax are required to maintain and keep complete and adequate records. Records must be kept in such a manner as to enable the Director to determine the payroll expense tax liability of the taxpayer. Such records shall be retained for a period of not less than five (5) years. Records retained must be presented upon request of the Director and demonstrate the payroll expense of the business including but not limited to; where employees are primarily assigned, perform their duties, and reside, and employee compensation. Examples include but are not limited to; W-2 and earnings summaries and workpapers and other employment tax records; work location schedules; teleworking agreements between employee and employer; payroll expense reports; copies of state employment security returns and their workpapers; etc.
- (10) **Payroll expense tax is levied on employers:** The payroll expense tax is levied on employers, not on employees. Under no circumstance may the payroll expense tax be deducted or withheld from employee compensation. The payroll expense tax is levied upon the person engaging in the business activities and constitutes a part of the operating overhead or cost of doing business.