

Washington State

# TAX BASICS

for nonprofits



5 THINGS  
TO KNOW



WASHINGTON NONPROFITS

Wayfind™

# Table of Contents

1. Registration with the Department of Revenue.....	1
Who Needs to Pay .....	1
How to Register .....	1
How Nonprofit Taxes are Paid .....	2
2. Types of Taxes.....	2
Business and Occupation Tax (B&O).....	2
Retail Sales Tax .....	2
Use Tax.....	3
Property Tax .....	3
Payroll Taxes .....	4
3. Lowering Taxes .....	5
Property Taxes .....	5
B&O Tax Exemptions .....	5
Entity-Based .....	5
Revenue-based .....	6
Activity-based .....	6
Credits.....	6
Reseller Permits .....	7
4. Audits .....	7
5. Consult with a CPA or Bookkeeper .....	8

## Thank you!

We are grateful for the following people who have contributed information and legal review for this toolkit.

Mark Hugh, Mark Hugh PLLC

Bob Heller, Clark Nuber PS

### THE FINE PRINT

This Toolkit includes high-level information about starting a nonprofit. It refers to other resources that go into more depth. It is designed for general use and not for the specific characteristics of an individual organization or person. It contains information about the laws impacting nonprofit organizations in Washington State. Legal information is not the same as legal advice. It is always a good idea to consult with an attorney to get advice as to how the law should be interpreted related to the specifics of your organization and situation. Also, laws impacting nonprofit organizations change over time. The information contained in this Toolkit may become out of date.



These materials provide you information on the top 5 things to know about Washington State nonprofit taxes.

A nonprofit can be exempt from paying *federal taxes* if the nonprofit is qualified as a 501(c)(3), 501(c)(4) or other eligible entity types. In Washington State nonprofits ARE subject to *state and local taxes*, but may be eligible for specific tax exemptions and deductions.

## 1. Registration with the Department of Revenue

### Who Needs to Pay

If your nonprofit has taxable gross income of \$12,000 (this means the total amount of money made by the nonprofit minus allowable exemptions or deductions from gross income) or more per year, or your nonprofit is required to collect or pay any taxes such as the sales tax, then the business is required to file business taxes.

### Ask the following questions

1. Will the nonprofit have \$12,000 or more of taxable gross income per year?
2. Is the nonprofit engaged in retail business activities and therefore required to collect retail sales tax from customers? See section 2 on Retail Tax.
3. Is the business required to collect any special taxes? See section 3, which covers industry guides, for further information.

If you answered *yes* to any of the above questions, then your nonprofit is required to apply for a business license with the Department of Revenue (DOR).

### How to Register

When you apply for a business license with the Department of Revenue, the registration starts the process to register for nonprofit taxes. (Information on applying for a business tax license can be found at: <http://bls.dor.wa.gov/file.aspx> and the BYOB video *How to Apply for a*

## TAX BASICS for nonprofits



*Business License Application*). Once you set up your DOR account, which is needed to apply for a business license, you will have an account to manage your nonprofit taxes online.

### **How Nonprofit Taxes are Paid**

Your nonprofit tax information will be submitted on the Combined Excise Tax Return, which can be accessed through your DOR account or submitted on a paper form. The forms can be accessed online at <https://dor.wa.gov/get-form-or-publication/forms-subject/excise>.

## 2. Types of Taxes

### **Business and Occupation Tax (B&O)**

Nonprofit are subject to B&O tax. The B&O tax is based on the gross receipts (this means the total amount the nonprofit receives from all sources during its annual accounting period, without subtracting any costs or expenses). The nonprofit must pay tax based on the value of its products, the gross proceeds of its sales, or the gross income of its services, as appropriate. Taxable gross receipts do not include allowable deductions such as donations, contributions (corporate sponsorships) or grants. The B&O tax is paid directly by the nonprofit. The B&O tax will differ based on the specific activity; to see a list of classifications go to:

[http://dor.wa.gov/Content/FileAndPayTaxes/BeforeIFile/doingBus\\_CommonBusActivities.aspx](http://dor.wa.gov/Content/FileAndPayTaxes/BeforeIFile/doingBus_CommonBusActivities.aspx)

and to see tax rates go to:

<http://dor.wa.gov/Content/FindTaxesAndRates/BAndOTax/BandOrates.aspx>.

Depending on the total amount of tax due in a year, the Department of Revenue will assign the nonprofit a monthly, quarterly or annual filing frequency. There are state B&O taxes and some cities also apply an additional B&O tax. While the additional charge is small, it is important to comply with all necessary B&O taxes. For information on local taxes go to <https://dor.wa.gov/get-form-or-publication/publications-subject/tax-topics/city-bo-tax-question>.

### **Retail Sales Tax**

The nonprofit must collect retail sales tax for any retail activity with its customers at the time of sale. A retail sale is every sale of a tangible or digital product. In general, it also includes the sale of services such as installation, repair, cleaning, altering, improving, construction, and

## TAX BASICS for nonprofits



decorating. Other services include improving real or personal property, certain amusement and recreational activities, lawn maintenance, and certain physical fitness activities. For more information go to: <https://dor.wa.gov/find-taxes-rates/retail-sales-tax#Whatis>.

When the nonprofit collects the retail tax from the customer, those funds are considered “trust funds” of the state and must be remitted to the Department of Revenue. If you or the person selling the item forgets to charge a customer the retail tax on a sale, the nonprofit is still required to pay the retail sales tax on the purchase.

### **Use Tax**

A use tax is paid by the consumer when there was no retail tax charged at the time of purchase. Use tax is most common when items are purchased over the internet from a seller in another state that is not registered to collect and remit Washington retail sales tax .

Washington provides an exemption for the use tax for activities that are also exempt under the sales tax.

There are also certain activities that are exempt from sale or use taxes. Some examples include: the sales of amusement, recreation or physical fitness services by a nonprofit youth organization to its members, sales by nonprofits for fundraising purposes, and sales of artistic or cultural objects to artistic or cultural organizations.

This issue would come up during an audit and there was no indication that taxes were paid on the sale. Keeping good records to account for all purchases, and if taxes were paid at the time of sale is very important to prevent additional taxes, interest, and penalties during an audit. This information should also be recorded on the Excise Tax Return.

### **Property Tax**

Property tax is administered by the county assessor and treasurer. For information on where to pay property tax go to: <https://dor.wa.gov/find-taxes-rates/property-tax/pay-my-property-tax-or-appeal-my-property-assessment>. Property tax items are listed on the Personal Property Listing Form due by April 30<sup>th</sup> of each taxable year.

## TAX BASICS for nonprofits



Both real and personal property are subject to property tax. Real property is land, structures, leasehold improvements and equipment permanently affixed to the land. Personal property includes items not affixed to land and that can be moved, such as office supplies, furniture, machinery, and equipment (including computers). Inventory is exempt from property tax.

### **Payroll Taxes**

The first thing to think about when hiring someone is if the person is a contractor or employee. This classification will affect what taxes the business must pay and if payroll taxes are required. For help on classifying workers go to: <https://www.esd.wa.gov/employer-taxes/independent-contractors>.

For employees, the nonprofit is required to have workers compensation insurance, administered by Labor and Industries (L&I). This registration is triggered when you apply for your business license and indicate that the nonprofit will hire employees. L&I will then contact you about the next steps. If you don't indicate that the nonprofit is hiring employees, you will need to reapply for a Business License, once you start hiring employees. For more information go to: <http://www.lni.wa.gov/ClaimsIns/Insurance/Learn/Open/Existing.asp>. The nonprofit is also required to pay unemployment insurance taxes, administered by the Employment Security Department (ESD). This tax requirement is also triggered by the business license registration. For information regarding unemployment taxes go to: <https://www.esd.wa.gov/employer-taxes/register-your-business>.

All contractors who are paid \$600 or more per year should receive an IRS form 1099 from the nonprofit. A good practice is to receive a W-9 when a contractor starts working with the nonprofit and then the nonprofit will have the necessary information to issue a 1099 form, if needed. For information from the IRS on paying contractors go to: <https://www.irs.gov/businesses/small-businesses-self-employed/forms-and-associated-taxes-for-independent-contractors>.

Also note that both L&I and ESD will require the nonprofit to prove that all their independent contractors are independently registered with the Department of Revenue before they will recognize the vendor as an independent contractor and not an employee subject to employment taxes. And this is true regardless that an independent contractor is not required to register with the Department of Revenue unless their taxable gross income is at least

## TAX BASICS for nonprofits



\$12,000. Therefore, nonprofits should verify that their vendors are registered with the Department of Revenue, and if not, require them to register and provide a copy of their business license. To verify who is registered, go to <https://secure.dor.wa.gov/gteunauth/>.

### 3. Lowering Taxes

#### **Property Taxes**

Washington State provides property tax exemptions for the certain nonprofit organizations, below are some examples:

- Churches
- Administrative offices of nonprofit recognized religious organizations
- Property used to provide character-building, benevolent, protective or rehabilitative social services
- Child care
- Housing for persons with disabilities or very low income
- Property used for the production of performance of musical, dance, artistic, dramatic or literary works for the benefit of the general public
- Property owned and used by humane societies

More information can be found at: <https://dor.wa.gov/content/property-tax-exemption-nonprofit-organizations>

#### **B&O Tax Exemptions**

There are three groups of B&O tax exemptions for non-profits: (1) entity-based, (2) revenue-based, and (3) activity-based.

#### **Entity-Based**

Entity-based exemptions are for specific types of organizations, here are some examples:

- Sheltered workshops, such as organizations that provide employment, rehabilitation, evaluation and work adjustment services to handicap individuals
- Adult family homes
- Assisted living families

## TAX BASICS for nonprofits



- Artistic or cultural organizations

### **Revenue-based**

Revenue-based exemptions are for specific types of revenue received, here are some examples:

- Membership dues and initiation fees
- Contributions and donations
- Grants and sponsorships
- Tuition fees from accredited educational institutions
- Gross revenue from trade shows, conventions, or educational seminars sponsored by trade or professional organizations
- Interstate sales

### **Activity-based**

Activity-based exemptions are for money received from certain activities, here are some examples:

- Fundraising
- Child welfare services, mental health services
- Convention and tourism promotion
- Credit and debt counseling
- Child care resource and referral services
- Day care services provided by churches

### **Credits**

Credits can lower your tax liability. The credit that is most likely to apply to nonprofit owners is the Small Business B&O Tax Credit. If the nonprofit is a service-based organization and has gross receipts under \$56,000 or is a retail-based nonprofit with gross receipts under \$178,556, the nonprofit may meet the criteria for the Small Business B&O Tax Credit. If you meet the criteria, the credit will offset the B&O tax and no B&O will be due! If you file online, the B&O tax credit will be automatically calculated. More information can be found in the Industry Guidelines, go to: <https://dor.wa.gov/doing-business/business-types/industry-guides/nonprofit-organizations>.

## TAX BASICS for nonprofits



### Reseller Permits

If your nonprofit buys products or inputs, modifies them, or sells them as is, a reseller permit will lower your tax liability. In a retail business, the retail tax is only intended to be paid by the end user. However, if your nonprofit is purchasing a product that is sold again by the nonprofit, the retail tax would be paid twice. With a reseller permit, you would present the permit to the business you are purchasing the product from and then you would not be charged retail sales tax. Here's a chart to explain the difference:

Without Reseller Permit	With Reseller Permit
<ol style="list-style-type: none"><li>1. Business buys t-shirt from wholesaler.</li><li>2. Wholesaler charges business sales tax.</li><li>3. Business sells t-shirt to customer.</li><li>4. Customer pays sales tax.</li></ol> <p>Tax is paid 2 times!</p>	<ol style="list-style-type: none"><li>1. Business buys t-shirt from wholesaler.</li><li>2. Business provides <i>reseller permit</i> to wholesaler.</li><li>3. Wholesaler verifies permit.</li><li>4. Business makes purchase with <i>no sales tax</i>.</li><li>5. Business sells t-shirt to customer.</li><li>6. <i>Customer pays sales tax</i>.</li></ol> <p>Tax is now only paid 1 time, saving the business money!</p>

For more information on reseller permits go to: <https://dor.wa.gov/find-taxes-rates/retail-sales-tax/reseller-permits>

## 4. Audits

Tax audits are common in Washington State. The audit will cover the last four years of records for the nonprofit, and cover the B&O tax, the sales tax, and the use tax. This is one of the many reasons that record keeping is very important. If you don't have accurate records, there can be interest, penalties, and an accumulation of unpaid taxes. You will need your records to prove that you have paid the necessary taxes. Remember that if you are audited and you don't agree with the findings, you have a right to appeal. For more information on auditing go to: <https://dor.wa.gov/doing-business/audits/audit-process-questions>.



## 5. Consult with a CPA or Bookkeeper

A CPA is “Certified Public Accountant” who has taken extensive classes related to accounting and is licensed, which requires the CPA to be up to date on current tax laws. Some CPAs do both bookkeeping and accounting, but CPAs are generally more expensive to work with due to their expertise.

Bookkeepers can help set up and maintain your record keeping system for all transactions and help with payroll. There are also many different types of software to help you with your bookkeeping needs. It is best to do some research online to see what best fits your needs. If software you are interested in or using seems confusing, working with a professional can be a great way to help you learn the system and then allow you to manage the businesses finances on your own.

When it comes to questions about the taxes that effect your business, a CPA will be able to help you.

As we’ve gone over parts of the resources, the WA Department of Revenue provides many resources that will help you handle your business taxes go to: <https://dor.wa.gov/>.