BUSINESS OF THE CITY COUNCIL
CITY OF MERCER ISLAND

AB 6791
November 4, 2025
Regular Business

AGENDA BILL INFORMATION

TITLE:	AB 6791: B&O Tax Code Amendment (Ordinance. No. 25C-23, First Reading)	☐ Discussion Only ☒ Action Needed: ☒ Motion ☐ Ordinance ☐ Resolution
RECOMMENDED ACTION:	Conduct first reading of Ordinance No. 25C-23 to update City Code related to business & occupation tax and set it for second reading and adoption.	

DEPARTMENT:	Finance
STAFF:	Matthew Mornick, Finance Director
COUNCIL LIAISON:	
EXHIBITS:	1. Ordinance No. 25C-23
CITY COUNCIL PRIORITY:	n/a

EXECUTIVE SUMMARY

The purpose of this agenda is to introduce a mandatory revision to the Mercer Island City Code to bring it into compliance with state requirements.

- Over the summer the Association of Washington Cities (AWC) formed a city working group to review required changes to the Business and Occupation (B&O) tax model ordinance in response to the passage of Senate Bill (SB) 5814. The new law expands the state and local retail sales tax to a list of services for which retail sales tax did not previously apply.
- The B&O tax model ordinance is the standard legal framework cities use to incorporate the B&O tax structure into their municipal code (RCW 35.102). Ordinance 25C-23 (Exhibit 1) incorporates the changes from SB 5814 into Chapter 4.10.020 of the Mercer Island City Code (MICC).
- Many cities in Washington state collect a local B&O tax, calculated as a percentage of a business's gross revenue in each city each year. In cities using a tiered system, businesses pay a percentage depending on their classification or business type.
- The City of Mercer Island charges a 0.10% tax on gross revenue earned from local business activities each year, regardless of a business's tax classification.
- Changes outlined in Exhibit 1 do not increase the City's B&O tax rate for any business segment, do not expand the City B&O tax on any business segment that is not currently subject to the tax, and therefore have no material impact on the City's forecasted B&O tax revenues.

The City Council must adopt Ordinance No. 25C-23 before the end of the year to take effect by January 1, 2026 to comply with state requirements.

BACKGROUND

A total of 53 cities in Washington state impose a local B&O tax on the gross receipts of businesses engaging in business in their city. Since 2004, cities with local B&O taxes were required to adopt the B&O tax model ordinance with mandatory uniform provisions related to a minimum threshold, tax classification definitions, engaging in business definition, and allocation and apportionment for activities occurring in more than one jurisdiction (RCW 35.102). The latest revisions to the model ordinance focused on tax classification definitions.

Over the summer, the Association of Washington Cities (AWC) formed a working group of City finance directors and tax managers to review changes to the B&O model ordinance in response to the passage of SB 5814. The new legislation changed the taxation classification of certain activities from services to retail sales. As a result, B&O tax cities must amend their tax code to align with the model ordinance by January 1, 2026.

ISSUE/DISCUSSION

Ordinance No. 25C-23 updates Chapter 4.10.020 MICC to bring it into compliance with the latest changes to the business and occupation tax model ordinance (Exhibit 1). The AWC work group limited revisions to the model ordinance to changes necessary to implement the state's changes to sales at retail in SB 5814. Specifically, the passage of SB 5814 expanded the state's retail sales tax to a list of services for which retail sales tax did not previously apply. In the past, sales tax was mainly on physical goods. It now applies to:

- Advertising services
- Live presentations
- Information technology services
- Custom website development services
- Investigation, security, and armored car services
- Temporary staffing services
- Sales of custom software and customization of prewritten software

When a service is subject to the state's retail sales tax, it is also subject to the state's "retailing" B&O tax classification. For cities using a tiered a tiered system for applying a B&O tax, the local B&O tax rate for "retailing" is typically lower than the rate for "service and other activities."

For example, the City of Issaquah applies a B&O tax rate on a business's gross income based on how that business is classified for taxing purposes. Businesses that fall within the "services and other business activities" classification pay a 0.15% tax on gross receipts. Businesses that fall within the "retailing" classification pay a lower tax on gross receipts at a rate of 0.12%.

The City of Mercer Island applies a flat B&O tax rate of 0.10% on gross receipts for all businesses and all classifications. The City does not use a tiered system to apply a B&O tax rate. As a result, the City's revenue from business and occupation taxes will not be impacted by the changes to the model ordinance.

NEXT STEPS

Staff seeks to answer questions from the City Council and schedule a second reading of Ordinance No. 25C-23 at the November 18, 2025 City Council meeting. Upon adoption, MICC chapter 4.10 will be revised, and staff will notify AWC and the Washington state Department of Revenue of the adopted code amendments.

RECOMMENDED ACTION

Set Ordinance No. 25C-23 for second reading and adoption.