GOV. JAY INSLEE’S
2017-19 BUDGET/REVENUE
RECOMMENDATIONS

March 2017

OFFICE OF FINANCIAL MANAGEMENT
Revenue growth is not keeping pace with higher costs and demand for services.

On top of that, the state faces an enormous obligation to fund public schools.
Our budget needs, obligations and revenue projections

Projected Spending Needs

- **2015-17 BUDGET**
- **2017-19 MAINTAIN SERVICES AT CURRENT LEVELS**
- **+ BASIC EDUCATION OBLIGATIONS**
- **+ POLICY ENHANCEMENTS**

Projected Revenue

- Pessimistic Forecast (25% chance of occurring)
- Baseline Forecast (40% chance of occurring)
- Optimistic Forecast (15% chance of occurring)

Revenue forecast as of Sept. 2016, less 1% to Budget Stabilization Account, plus other resources
Governor’s proposed budget

- Fully funds basic education
- Invests in high-quality teachers, closing the opportunity gap
- Overhauls mental health system
- Freezes college/university tuition and expands financial aid
- Begins major restructure of services for children and families
- Combats homelessness and opioid crisis
- Protects safety net for vital services
Fully funding K-12 education

- Meets court order to fully, sustainably fund basic education
- $2.7 billion to pay state’s full share of teacher compensation
- Includes salary increase for beginning teachers
- Every district will receive more money from state
- Local school taxes reduced by at least $250 million per year
- No increase in state property tax
- Alleviates decades-long funding disparities among districts
- Budget includes another $1 billion to:
  - Continue shrinking early elementary class sizes
  - Boost teacher mentoring and other proven strategies
  - Address opportunity gaps
State revenue remains well below historic growth trend

major revenue changes.

addressing other needs will require

Fully funding K-12 education and
Over the past 30 years, state revenue collections as a share of the economy have fallen by nearly 30%.

**GENERAL FUND-STATE REVENUE AS PERCENTAGE OF WASHINGTON PERSONAL INCOME**

Washington's 82-year-old tax system has not evolved with changing economy.
Since 1974, services as a share of Washington's economy have doubled.

1974:
- Services: 11%
- Manufacturing: 29%
- Wholesaling: 29%
- Retailing: 20%

2015:
- Services: 23%
- Manufacturing: 23%
- Wholesaling: 20%
- Retailing: 20%

Share of Washington's Gross Business Income

Washington's tax system was founded on a goods-based economy—we don't tax services to the extent we tax goods and commodities. As our economy shifts, our tax system fails to keep pace with economic growth.

Due to our heavy reliance on sales taxes, Washington's state tax system is by far the most regressive in the region and the nation.
Lowest-income families in Washington face the nation’s highest state & local tax burden

**COMPARING ALL 50 STATES**

A family in the **lowest income** quintile pays 16.8% of income in state and local taxes.

Washington ranks **1st** among the 50 states and D.C.

- **California**
- **Idaho**
- **Oregon**
- **Washington**

**Top 1% of earners**
Taxes as share of income: **2.4%**
Rank: **47th**

*Nonelderly taxpayers

Source: Institute on Taxation and Economic Policy, 2015 "Who Pays?" Report
Tax regressivity: How Washington compares

**WASHINGTON**

Shares of family income for non-elderly taxpayers

- Lowest 20%: 16.8%
- Second 20%: 11.7%
- Middle 20%: 10.3%
- Fourth 20%: 8.5%
- Next 15%: 6.6%
- Next 4%: 6.6%
- Top 1%: 2.4%

- Income Range: Less than $21,000
- Income Range: $21,000 - $40,000
- Income Range: $40,000 - $65,000
- Income Range: $65,000 - $100,000
- Income Range: $100,000 - $197,000
- Income Range: $197,000 - $507,000
- Income Range: $507,000

**OREGON**

Shares of family income for non-elderly taxpayers

- Lowest 20%: 8.1%
- Second 20%: 7.3%
- Middle 20%: 7.8%
- Fourth 20%: 7.2%
- Next 15%: 7.2%
- Next 4%: 7.4%
- Top 1%: 6.5%

- Income Range: Less than $19,000
- Income Range: $19,000 - $34,000
- Income Range: $34,000 - $55,000
- Income Range: $55,000 - $189,000
- Income Range: $189,000
- Income Range: $172,000
- Income Range: $173,000
- Income Range: $571,000

**CALIFORNIA**

Shares of family income for non-elderly taxpayers

- Lowest 20%: 10.5%
- Second 20%: 9.2%
- Middle 20%: 8.2%
- Fourth 20%: 7.7%
- Next 15%: 7.4%
- Next 4%: 8.7%
- Top 1%: 8.7%

- Income Range: Less than $21,000
- Income Range: $21,000 - $38,000
- Income Range: $38,000 - $61,000
- Income Range: $61,000 - $101,000
- Income Range: $101,000 - $127,000
- Income Range: $127,000 - $146,000
- Income Range: $146,000

**IDAHO**

Shares of family income for non-elderly taxpayers

- Lowest 20%: 8.5%
- Second 20%: 8.5%
- Middle 20%: 7.6%
- Fourth 20%: 8.2%
- Next 15%: 7.5%
- Next 4%: 6.4%
- Top 1%: 6.4%

- Income Range: Less than $18,000
- Income Range: $18,000 - $31,000
- Income Range: $31,000 - $35,000
- Income Range: $35,000 - $52,000
- Income Range: $52,000 - $58,000
- Income Range: $58,000
- Income Range: $154,000
- Income Range: $576,000

Source: Institute on Taxation and Economic Policy, 2015 "Who Pays?" report
Washington has fallen far behind the national average for state tax collections.
Washington has fallen behind other states in revenue as a share of the economy.

If Washington’s tax system were at the U.S. average, we would be generating about $6.8 billion more in state and local taxes per biennium.

WASHINGTON: $94.31 (RANK: 35)

In the mid-1990s, Washington ranked 11th nationwide. In the most recent ranking, our state has fallen to 35th.

Creating a more sustainable revenue system

- Governor proposes balanced mix of revenue changes to address short-term and long-term needs, obligations
- Majority of $4.4 billion in new revenue dedicated to education
- Revenue proposal rooted in fairness for working families
- Proposed revenue changes are not new
Revenue package elements: B&O on services

- Increases state B&O tax on services from 1.5% to 2.5%
- Applies to broad range of personal, professional services
- More than doubles filing threshold to $100,000
- Increases small-business tax credit to $125 per month
- Estimated 38,000 more small businesses would receive some tax relief
- Generates $2.3 billion next biennium
Revenue package elements: capital gains tax

- 7.9% capital gains tax on sale of stocks, bonds, other assets
- Applies to earnings above $25,000 for individuals, $50,000 for joint filers
- Affects only a tiny fraction of the state’s wealthiest taxpayers
- Exempts retirement accounts, homes, farms, forestry
- Earned income from salaries/wages is not capital gains and would not be taxed
- Creates reserve fund to protect against volatility
- Generates $821 million next biennium
What a capital gains tax would have looked like over the past decade

ESTIMATED REVENUE OF A 7.9% CAPITAL GAINS TAX

Great Recession

Calculations assume a $25,000 exemption for individuals and a $50,000 exemption for joint filers, and a B&O deduction allowed on capital gains that are taxable under the proposed capital gains tax and B&O tax.

Revenue package elements: carbon pollution tax

- Tax on emissions from production, consumption of fossil fuels
- Emissions taxed at $25 per ton, starting May 2018
- Tax increases 3.5% annually, plus inflation
- Generates nearly $2 billion per year at outset
- Half of revenue to fund education needs
- Remainder to be reinvested
  - Fund clean energy and transportation projects
  - Build water infrastructure
  - Improve forest health
  - Offset carbon tax impacts on business, low-income households
Revenue package elements: closing loopholes

- Repeal sales tax exemption on bottled water – $57 million
- Refund state portion of sales tax to nonresidents – $49 million
- Repeal use tax exemption for extracted fuel – $52 million
- Repeal sales tax exemption for trade-ins valued over $10,000 – $91 million
- Limit REET exemption on foreclosure sales by lenders – $59 million