

Rational Steps #6: Looming 2023 Tax Hikes Will Exacerbate the Affordability Crisis

Welcome to the sixth installment of this series, which identifies and explores important issues facing our state and recommends workable policy solutions.

The Senate Republican Caucus' top three priorities for the 2022 session were: addressing affordability; improving public safety; and restoring trust in government. This focuses on the first priority.

- **Issue:** A series of new and higher taxes on income, property, sales, and driving are set to take effect beginning in January 2023, thanks to actions in the past two Democrat-controlled legislative sessions.
- **Rational Step Toward a Better Washington:** Legislators need to be more cognizant of the cumulative effect of their tax policies and the burdens they place on working- and middle-class Washingtonians.

I. The Affordability Context

Washingtonians will pay several new and higher taxes in 2023. Before delving into those, it's necessary to provide some contextual background.

A. Comparatively High Tax Burden: Washingtonians Already Pay \$900 More Per Capita in State and Local Taxes than Median State

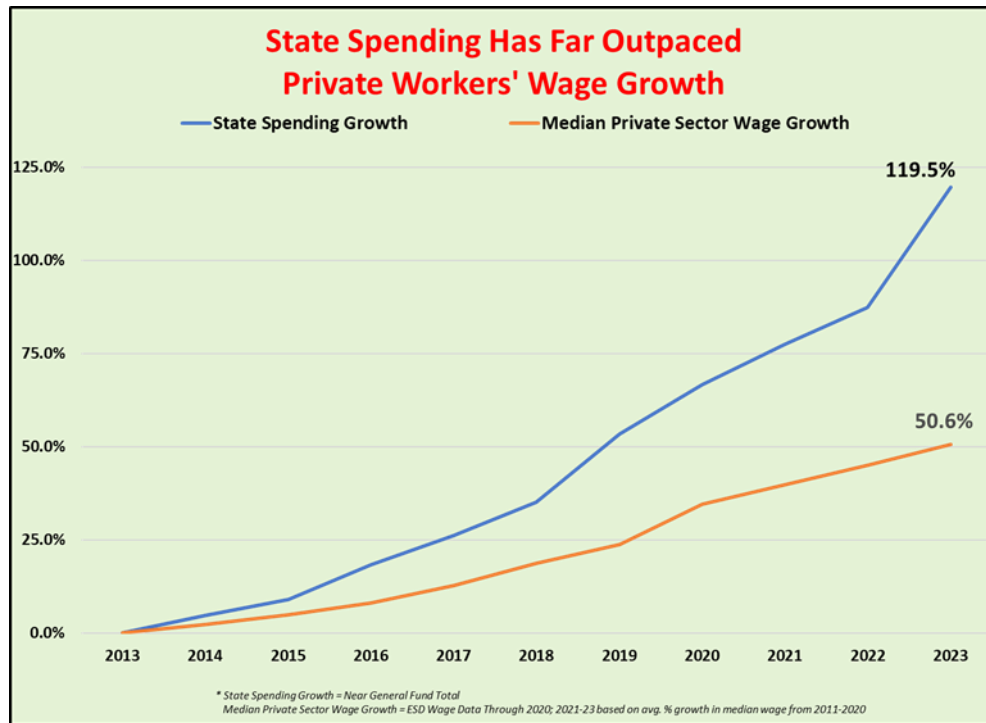
Washingtonians, according to our own state Department of Revenue, pay the 14th highest state and local taxes per capita in the country. The tax burden was at \$6,111 in fiscal year 2019.¹

This is more than \$900 above the median state, New Hampshire.²

Important to note: This tax ranking, and comparison to the median state, is before any of the tax increases to be mentioned later.³

B. State Spending Has More Than Doubled in Past 10 Years, Far Outpacing Worker Wage Growth

State spending in the past decade has been robust, to say the least – growing at more than twice the rate of private-sector median wages:



C. Washingtonians Facing 40-Year Highs in Inflation

Nationally, inflation grew at 8.5% over the past 12 months – the highest increase since 1981. The largest price increases affect essentials such as food and gas, and therefore disproportionately impact those with fixed or lower incomes.⁴

Here in Washington, inflation has been outpacing even the national average and could hit double digits soon.⁵

II. The Looming 2023 Tax Hikes

The many pending 2023 tax increases all stem from legislation passed in the 2021 and 2022 sessions. Let's break them into distinct categories: income, property, sales, and driving.

A. Income Tax Hikes

- **Capital-Gains Income Tax (First Tax Collection: April 15, 2023)**

Talk about disrespecting voters: In 2021 the Democrat-controlled Legislature imposed a state income tax, even though Washingtonians have rejected an income tax **every time** they've been asked to vote on the issue – that's 11 times in a row, dating to 1934.⁶

This includes a November 2021 advisory vote, in which over 61% of voters recommended repealing the tax, which is on income from capital gains.⁷

Democrats knew this opposition was likely, so in an egregious use of the legislative process they included language in the bill that denied Washington voters the opportunity to overturn the resulting law using their constitutional right of referendum.⁸

Make no mistake, the tax – which went into effect Jan. 1, 2022, with the first payment due on April 15, 2023 - is an income tax.

- **"Income tax" is used 11 separate times in the bill**
 - Despite the attempts to characterize the tax as an excise tax, the phrase "income tax" is used 11 different times in the legislation.
- **Diagramming the bill's language: So this is what you *really* mean . . .**
 - "Beginning January 1, 2022, an excise tax is imposed on the sale or exchange of long-term capital assets . . . which equals seven percent multiplied by an individual's Washington capital gains." (sec. 5)
 - "Washington capital gains" means an individual's adjusted capital gain" (sec. 4(13))
 - "Adjusted capital gain" means federal net long-term capital gain" (sec. 4(1))
 - "Federal net long-term capital gain" means the net long-term capital gain **reportable for federal income tax purposes**" (sec. 4(3), *underline added*)
- **How will the Department of Revenue calculate tax liability?**

- Taxpayers owing capital gains tax must file their **federal income tax return** with the agency (sec. 12(2 & 6))

On March 1, to no one's surprise, a Superior Court judge declared the tax unconstitutional.⁹ This also aligns with how the IRS and all other states in the country classify capital gains as an income tax.¹⁰ It is expected the state Supreme Court will be the final arbiters on the constitutionality of this tax, and while no one can predict the outcome, Democratic budget writers continue to assume the projected income-tax revenue will be available.

- **Long-Term Care Payroll Tax (July 1, 2023)**

Remember the fervor in the fall of 2021 as working people across Washington realized they soon would have to pay 0.58% of every paycheck for the rest of their working lives to state government? In the face of that potential political backlash, Democrats made a "suspension" of the LTC payroll tax their first bill action of the 2022 session.¹¹

But – and this is a big “but” – the payroll tax was suspended for only 18 months, meaning it will take effect July 1, 2023.¹² From then on, the tax will take over \$2.5 billion every budget cycle out of the wages of working Washingtonians.¹³

The program's 0.58% tax rate is actuarially unsound, by \$15 billion – meaning the rate will have to go up in the long run to stay financially solvent.¹⁴

As with a state income tax, voters have been asked their opinion – in an advisory vote, and on a constitutional amendment. Both times they rejected the concept by wide margins.¹⁵

- **Tax Rate Increase on Paid Family Medical Leave (Jan. 1, 2023)**

Due to financial insolvency in the Paid Family Medical Leave program, the rate of the supporting tax is forecast to increase from 0.6% of wages now to 0.8% in 2023.¹⁶

Lawmakers have known about the program's financial insolvency and the looming tax hike. During this past session I proposed a solution in the form of [Senate Bill 5959](#), which would have used a portion of the state's \$15 billion budget surplus to provide this popular program with an ongoing revenue source.¹⁷

Because lawmakers chose not to address the looming solvency problem, workers and employers are now faced with a projected tax hike beginning in January – an increase that could have been avoided, had there been the will.

B. Property Tax Hike

- **Property Tax Hike for "Ghost Students" (Jan. 1, 2023)**

Since the pandemic began, K-12 public school enrollment has declined by more than 40,000 students statewide. The vast majority are either now home-schooled or in private school, and may not return to public schools.¹⁸

The local property-tax levy requests that help fund public schools are typically based on the number of students enrolled in each respective district. Yet during this year's session, Democrats voted to allow 2023 local school levies to be based on 2019 school-district enrollment if that level was higher than present school-year enrollment.¹⁹

The result? Districts can typically raise local funds up to \$2,500 per student, so this legislation could conceivably cost taxpayers \$100 million more in property taxes for students that are no longer enrolled in public schools. This, when we should be looking instead at providing substantial, progressive property-tax relief, as was proposed in my SB 5463!

C. Sales Tax Hike

- **0.1% Non-Voter Approved Sales Tax Hike (July 1, 2022 Authority)**

The tax increases already mentioned are all tied to 2023; this tax increase is actually eligible to go into place in just two months!

Five years ago, Chicago had the highest sales-tax rate of any major city in the country, at 10.25%.²⁰ Our two largest cities, Seattle and Tacoma, were both outside the top five, at 9.6%.²¹

Today, Tacoma has the highest in the country at 10.3%, while Seattle is tied for second (with Chicago and three California cities) at 10.25%.²²

That's right. While the state sales tax has remained flat at 6.5%, the local sales-tax rates in Tacoma and Seattle have gone up by 0.7% and 0.65% respectively, over the past five years.

Under SB 5974 (Transportation Resources), both Tacoma and Seattle – and each jurisdiction in the state that has a Transportation Benefit District (TBD) – will likely see their sales tax rise by an additional 0.1%, as the new law gives TBDs the councilmanic authority (meaning the council decides, without the vote of the people) to raise the sales tax by that amount.²³ A 0.1% tax increase statewide is equivalent to roughly \$500 million per biennium in additional tax.²⁴

That means, come July 2022, Tacoma and Seattle could have the highest sales-tax rates of any major city in the United States, increasing by 0.8% and 0.75% respectively, in the past five years. All of this is due to legislatively granted local authority to increase sales tax.

Even so, Tacoma and Seattle still would not have the highest sales-tax rates in the state. Many Snohomish County cities already exceed them, with Edmonds, Mountlake Terrace, and Woodway clocking in at 10.4%. But none tops Lynnwood, at 10.5%. Notably, that city is

represented by the author of the additional 0.1% sales-tax authority found in SB 5974: Sen. Marko Liias, chair of the Transportation Committee.

D. Increasing the Cost of Driving

Perhaps the most regressive tax one can enact is to raise the cost of driving. Four Democratic policies going into effect in 2023 will do exactly that.

- **Low Carbon Fuel Standard Rule (Jan. 1, 2023)**
- **Carbon Cap-and-Tax Policy (Jan. 1, 2023)**

These two are the biggies. The former requires lowering the carbon in fuel from present levels, while the latter is a *de facto* gas tax that is expected to bring in over \$5 billion in coming years. Both are due to legislation passed in the 2021 session.²⁵

We need look no further than California to see the future impact to Washingtonians from these two policies. California implemented the low-carbon fuel standard in 2011, with cap-and-tax following a few years later.

Prior to either policy being enacted, California's gas prices were 31 cents above the national average.²⁶ Today California has the highest gas prices in the country, over \$1.54 above the national average.²⁷

While there are some additional policies in California that affect that state's gas prices, these two policies make up the vast bulk of the present price difference between Washington gas (\$4.73 a gallon) and California (\$5.75 a gallon).²⁸

The irony? Washington is already a very low carbon-emission state, ranking fifth-lowest per capita in the country in energy-related carbon emissions.²⁹ On a per capita basis, our emissions have declined from 14.7 metric tons per person in 1999 to 9.6 tons in 2019 – a decline of nearly 35%.³⁰

- **License Plate Fee Increase (July 1, 2022)**
- **Drivers' License Fee Increase (Oct. 1, 2022)**

In another example of regressive tax policies that hit lower-income residents disproportionately hard, the SB 5974 law created this year also tripled the cost of replacing license plates (to \$30, from \$10), and quintupled the price of getting the initial plates (to \$50, from \$10).³¹

Additionally, the price of a driver's license is increasing by a minimum of \$18.³²

Together, these policies are expected to take another nearly \$100 million a year out of Washingtonians' wallets.³³ All this is on the horizon as inflation climbs to a rate that is predicted to cost an average household \$5,200 more per year.³⁴

Conclusion

In coming months, Washingtonians will see a host of tax increases – from those taken directly out of their wages, to higher sales and property taxes, to increased costs of driving – all due to policies enacted by the Democrat-controlled Legislature in 2021 and 2022.

Footnotes

1. Comparative State and Local Taxes, Fiscal Year 2019 (Washington State Dept of Revenue), p. 15 https://dor.wa.gov/sites/default/files/2022-03/Comparative_2019.pdf?uid=6271419acbf5d
2. Id.
3. It is worth noting that, since FY 2019, the date of the comparative tax analysis, the Democrat-controlled legislature in Washington has passed more than two dozen new taxes.
4. <https://www.bls.gov/news.release/cpi.nr0.htm>
5. The most recent month for Seattle-area reported inflation (Feb. 2022) had annual inflation exceeding the national average for the same time by 0.2%. https://www.bls.gov/regions/west/news-release/consumerpriceindex_seattle.htm
6. Rejections of an income tax by a vote of the people have occurred in 1934, 1936, 1938, 1942, 1944, 1970, 1973, 1975, 1982, 2010, and 2021.
7. Results for Advisory Vote #37 (Nov. 2021, Office of Secretary of State website)
8. Sec. 5, sub (2) of ESSB 5096 (2021): <https://lawfilesexternal.leg.wa.gov/biennium/2021-22/Pdf/Bills/Session%20Laws/Senate/5096-S.SL.pdf?q=20220503101603>
9. <https://www.king5.com/article/news/politics/state-politics/overturms-washington-states-capital-gains-tax/281-41326c01-0ad3-49bf-8dac-5bf3374f881b>
10. <https://www.washingtonpolicy.org/library/docLib/WPC-cap-gains-decl.pdf>
11. <https://lawfilesexternal.leg.wa.gov/biennium/2021-22/Pdf/Bills/Session%20Laws/House/1732-S.SL.pdf?q=20220503105447>
12. Id.
13. Milliman 2020 Actuarial Study, page 43 <https://leg.wa.gov/osa/additionalservices/Documents/Milliman2020WALTSSTrustActuarial%20Study.pdf>
14. <https://leg.wa.gov/osa/additionalservices/Documents/Actuarial.Status.WA.Cares.Fund.Program.22-96.03-22.pdf> The report indicates a \$15 billion actuarial liability (deficit) over 75 years.
15. Advisory Vote #20 (2019, voters advised repealing the tax by a 62.9% vote) <https://results.vote.wa.gov/results/20191105/advisory-votes-advisory-vote-no-20.html>
Voters the following year rejected a constitutional amendment concerning investments of tax revenue to support the fund (SJR 8212, rejecting the constitutional amendment by a 54.4% vote) <https://results.vote.wa.gov/results/20201103/engrossed-senate-joint-resolution-no-8212.html>

16. Email from ESD on March 7, 2022.
17. <https://app.leg.wa.gov/billsummary?BillNumber=5959&Initiative=false&Year=2021>
18. https://cfc.wa.gov/Monitoring/ComSch_Enrollment.pdf
19. Sec. 3 of HB 1590 (2022):
<https://app.leg.wa.gov/billsummary?BillNumber=1590&Chamber=House&Year=2021>
20. <https://taxfoundation.org/sales-tax-rates-major-cities-midyear-2016/>
21. Id.
22. <https://taxfoundation.org/publications/sales-tax-rates-in-major-cities/>
23. Sec. 406 of ESSB 5974: <https://lawfilesexternal.leg.wa.gov/biennium/2021-22/Pdf/Bills/Session%20Laws/Senate/5974-S.SL.pdf?q=20220503120027>
24. See fiscal estimate for SB 5932, which proposed reducing state sales tax by 1%.
25. E3SHB 1091 (Low Carbon Fuel Standard):
<https://app.leg.wa.gov/billsummary?BillNumber=1091&Initiative=false&Year=2021>
E2SSB 5126 (Carbon Cap and Tax):
<https://app.leg.wa.gov/billsummary?BillNumber=5126&Year=2021&Initiative=false>
26. Senate Transportation Committee staff memo to SB 5126.
27. As of 5/3/2022, national average is \$4.20 and California average is \$5.75. <https://gasprices.aaa.com/state-gas-price-averages/>
28. Id.
29. Table 4: <https://www.eia.gov/environment/emissions/state/>
30. Id.
31. ESSB 5974, section 202
32. Id., sec. 205
33. Item 4: <http://leap.leg.wa.gov/leap/Budget/Detail/2022/ctResourceBillConferenceSummary.pdf>
34. <https://www.bloomberg.com/news/articles/2022-03-29/u-s-households-face-5-200-inflation-tax-this-year-chart>