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Governor Inslee Proposes \$1.5 Billion of New Revenue, Including a 7 Percent Personal Tax on Capital Gains

Tax Legal Update

Washington Governor Jay Inslee recently released his proposed budget for 2015-17, which includes approximately \$1.5 billion of new and increased taxes the Governor is marketing as “improving Washington’s unfair and outdated tax system.”

Capital Gains Tax

The centerpiece of the Governor’s tax increase proposals involves a new 7 percent capital gains tax that would be imposed on individuals. The capital gains tax is estimated to generate nearly \$800 million in its first year and represents more than half of the proposed tax increase. Washington does not currently have an income tax or other tax imposed on individuals.

Carbon Pollution Reduction Program

Another large revenue driver would be the Governor’s proposed Carbon Pollution Accountability Act, which he describes as “a new market-based carbon pollution reduction program.” The proposed Act would require certain businesses to purchase carbon emission allowances at public

auction. The proposal is expected to raise \$379 million in new revenue for the state's general fund (to be used to fund K-12 education programs), while another \$568 million would be dedicated to other purposes (and therefore is not considered part of the \$1.5 billion in new general fund revenue), including \$400 million toward transportation.

Repeal of Tax “Breaks”

The Governor's proposed budget seeks another \$282 million by repealing five “tax breaks”:

- Cap trade-in vehicle exemption (\$105 million): The sales and use tax exemption for the trade-in value of motor vehicles, boats and other vehicles would be capped at \$10,000.
- Eliminate use tax exemption for most extracted fuels (\$51 million): The use tax exemption for fuel used in manufacturing or extracting would be limited only to wood byproducts (aka “hog fuel”), effectively increasing taxes paid by oil refineries.
- Elimination of point-of-sale tax exemption for residents from non-sales-tax states (\$52 million): Currently, residents of states without a sales tax can buy goods in Washington tax-free upon proof of residency. The Governor's proposal would replace the exemption with a post-sale refund program, applicable only to the state portion of sales tax (not any local portion), and only for purchases of \$25 or more.
- Elimination of sales tax exemption for bottled water (\$44 million): The Governor proposes eliminating a sales tax exemption for bottled water that would overturn a voter initiative retaining the exemption in 2010.
- Elimination of preferential B&O tax rate for royalties (\$30 million): The Governor also proposes eliminating the preferential B&O tax rate (0.484 percent) for royalties. Instead, the catch-all service and other activities classification rate of 1.5 percent would apply.

Sin Taxes

The Governor's budget would increase the cigarette tax by \$0.50 per pack to raise \$38 million in revenue, and impose a tax on e-cigarettes and vapor products based on the “other tobacco products” tax for an additional \$18 million in revenue.