Washington Research Council

Policy Brief

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I-1366: A Choose Your Own Tax Adventure for Legislators

Briefly

- I-1366 would reduce the state sales tax from 6.5 percent to 5.5 percent unless the Legislature refers a constitutional amendment to voters for approval.
- The constitutional amendment would require two-thirds legislative approval to increase taxes.
- It would also require a majority vote of the Legislature for fee increases.
- A supermajority was first required to raise taxes when I-601 was approved in 1993.
- Since then, it has been suspended by the Legislature and reaffirmed by voters many times.
- The state Supreme Court ruled it unconstitutional in 2013.
- If the sales tax is reduced by 1 percent, it would reduce state revenues by $1.590 billion in 2015–17 and by $3.066 billion in 2017–19.
- Such a loss of sales tax revenues would significantly impact the state budget.
- Some may consider the crisis atmosphere created by a sales tax reduction an opportunity to increase other taxes or levy entirely new ones.

Over 20 years Washington voters had consistently approved supermajority requirements for tax increases, but the state Supreme Court ruled such requirements to be unconstitutional in 2013. This November, voters will again have an opportunity to weigh in on the question with Initiative 1366.

If approved by voters, I-1366 would reduce the state sales tax from 6.5 percent to 5.5 percent on April 15, 2016—unless the Legislature puts to voters a constitutional amendment requiring that any tax increases be approved by two-thirds of the Legislature (or be approved by voters) and that any fee increases be approved by a majority of the Legislature. If the sales tax is reduced, the Legislature would not be able to restore the current sales tax rate for two years with a simple majority vote (they could do so before then with a two-thirds majority).

Tax increases are defined as

> *any action or combination of actions by the state legislature that increases state tax revenue deposited in any fund, budget, or account, regardless of whether the revenues are deposited into the general fund.*

Revenue Impact

If the Legislature does not send such a constitutional amendment to voters, the Department of Revenue (DOR) estimates that the sales tax reduction would reduce state revenues by a net of $1.590 billion in 2015–17, by $3.066 billion in 2017–19, and by $3.329 billion in 2019–2021 (DOR 2015). (Collections from the sales tax are deposited into the general fund–state (GFS) and the performance audit account, so both accounts would be affected.)

Table 1: State Revenue Impact, If Sales Tax Reduced (Dollars in Thousands)

	2016	2017	2018	2019	2020	2021
GFS, Sales Tax	(163,804)	(1,432,025)	(1,504,173)	(1,571,928)	(1,653,576)	(1,686,820)
GFS, B&O Tax	818	7,149	7,509	7,847	8,255	8,421
Performance Audit, Sales Tax	(263)	(2,295)	(2,411)	(2,519)	(2,650)	(2,703)
Total	**(163,249)**	**(1,427,171)**	**(1,499,075)**	**(1,566,600)**	**(1,647,971)**	**(1,681,102)**

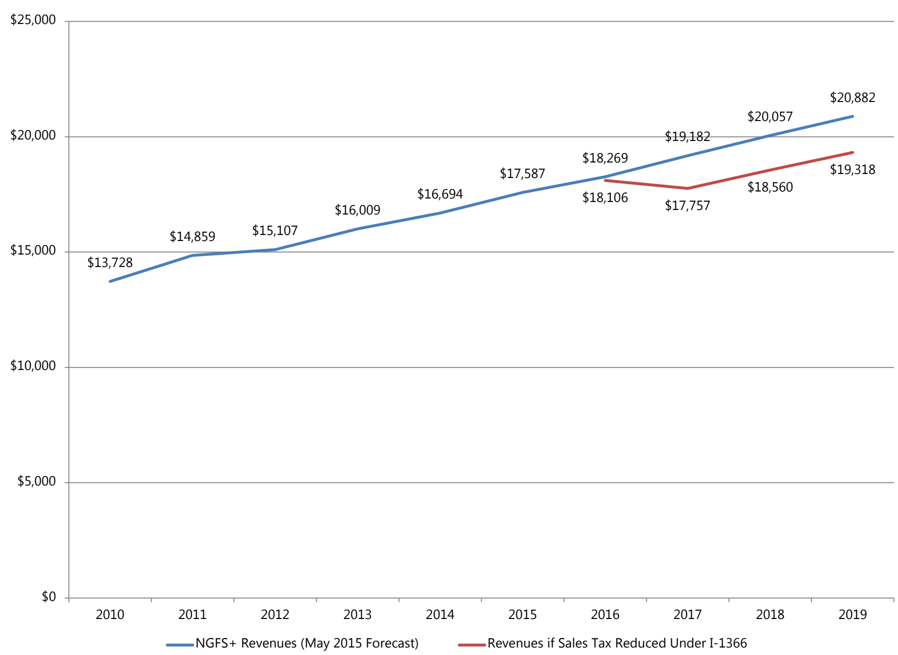
Table 2: Local Revenue Impact, If Sales Tax Reduced (Dollars in Thousands)

2016	2017	2018	2019	2020	2021
4,623	40,414	42,451	44,363	46,667	47,605

According to DOR, the estimate includes the effects of a reduction in the use tax rate, which is statutorily tied to the sales tax rate (RCW 82.12.020(4)(a)). It also takes into account the likelihood that taxable sales would increase as the lower sales tax rate induces consumers to spend more than they otherwise would have. Thus, business and occupation (B&O) tax collections would be expected to increase, as would local revenues.

Local revenues are estimated to increase by $45.0 million in 2015–17, by $86.8 million in 2017–19, and by $94.3 million in 2019–2021.

Chart 1: Near General Fund–State Plus Opportunity Pathways Revenues (Dollars in Millions)



History of Washington's Supermajority Requirement

The supermajority requirement for raising taxes has been in and out of the state law books since 1993, when voters approved I-601. It was reaffirmed as part of Referendum 49 in 1998. The Legislature has suspended the requirement several times, and voters have reinstated the requirement in Initiatives 960, 1053, and 1185 (see the timeline on page 3).

The Legislature was able to suspend the supermajority requirement because under the state constitution (Article II, Section 1(c)), initiatives may be amended or repealed after a period of two years following enactment. (They may be amended within the two year period if approved by a two-thirds majority of the Legislature.)

Since I-601 was approved, there have been questions about the constitutionality of the supermajority requirement, but the state Supreme Court didn't settle the matter until 2013. In 2011, the League of Education Voters and others had filed a lawsuit arguing that the requirement was unconstitutional. The Supreme Court agreed in 2013. The Court cited the "plain language" of Article II, Section 22 of the constitution, which states, "No bill shall become a law unless . . . a majority of the members elected to each house be recorded thereon as voting in its favor" (*LEV v. State* 2013).

According to the Center on Budget and Policy Priorities, 16 states require supermajority votes of the Legislature for some or all tax bills. In seven of those states, the constitution requires the supermajority (CBPP 2015).

Table 3: Law Changes Related to the Supermajority Requirement

1993	Voters approve I-601 (51.21% - 48.79%)
1998	Voters approve Ref. 49 (57.14% - 42.86%)
2002	Supermajority requirement suspended for the 2001-03 biennium (SB 6819)
2005	Supermajority requirement suspended from 7/1/2005 through 6/30/2007 (SSB 6078)
2006	Supermajority requirement reinstated by Legislature beginning 7/1/2006 (ESSB 6896)
2007	Voters approve I-960 (51.24% - 48.76%)
2010	Supermajority requirement suspended from 2/24/2010 through 7/1/2011 (ESSB 6130)
2010	Voters approve I-1053 (63.75% - 36.25%)
2011	League of Education Voters sues over constitutionality of supermajority requirement
2012	Voters approve I-1185 (63.91% - 36.09%)
2013	State Supreme Court finds the supermajority requirement unconstitutional

Amending the Constitution

Given the state Supreme Court decision, in order to reinstate a supermajority requirement for tax increases, the constitution will have to be amended. The state Senate passed SJR 8213 in 2014, which would have done so, but the House did not take it up.

Voters may not amend the constitution via initiative—per Article XXIII of the constitution, amendments must be proposed by the Legislature. If two-thirds of the Legislature votes for an amendment, it must then be approved by a majority of voters.

A lawsuit was filed to keep I-1366 off the ballot on the grounds that it represents an attempt to amend the constitution via initiative. The state Supreme Court has unanimously ordered that the initiative will be on the ballot. A written opinion has not yet been released, but according to the Court's order, it will retain the appeal for a future "decision on the merits" (*Huff et al. v. Wyman et al.* 2015). Therefore, even if voters approve the initiative, it may not stand.

Comment

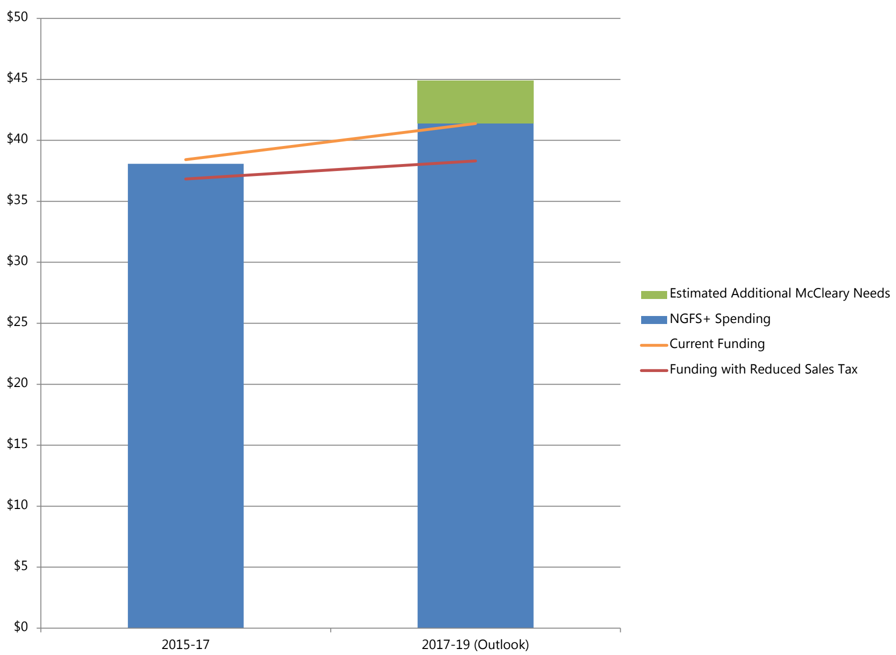
By approving the supermajority requirement, voters have consistently shown that they want it to be more difficult to increase taxes. If I-1366 passes, legislators will have to either refer to voters a constitutional amendment enshrining the supermajority requirement in the constitution (and effectively protecting it from legislative meddling forever), or accept a reduction in the sales tax rate (which could be undone after two years with only a majority vote).

The less permanent of the two options may be more attractive to legislators. But it is hard to see how the state could afford the loss of the sales tax revenue. Retail sales and use tax collections accounted for 46.6 percent of total state tax collections in 2014. Because the state is so dependent on the sales tax, the 1 percent reduction contemplated by I-1366 would significantly impact the state budget.

The July 2015 four-year budget outlook estimates that the state will end 2015–17 with reserves totaling $1.237 billion. Total reserves after 2017–19 are estimated to be $1.344 billion (ERFC 2015). (Those numbers include amounts in the budget stabilization account, which would only be able to be tapped with approval of three-fifths of the Legislature. The unrestricted ending fund balance for 2015–17 is $343 million and for 2017–19 is negative $23 million.)

If I-1366 passes, and if the Legislature allows the sales tax reduction to go into effect, over $4.5 billion will be lost by the end of fiscal year 2019, putting the 2015–17 budget and the outlook for 2017–19 in the red (even if using budget stabilization account funds). And that's not counting the additional funds that the Legislature will need related to the

Chart 2: Impact on the State Budget (Dollars in Billions)



McCleary decision in 2017–19—many observers estimate that it will come to about $3.5 billion.

In 2012, we wrote of the supermajority requirement,

> *The restraint has led to bipartisan decision-making and a more thoughtful approach to priority-based budgeting. In recent years, we've seen fiscal improvements, including pension reform, steps to control health care costs, and a four-year balanced budget requirement. Arguably, these measures were adopted because tax increases were the more difficult option.* (WRC 2012)

That said, the state continues to face real budget challenges. If the sales tax is reduced, the Legislature will have to find billions of new dollars just to continue the current level of services. While supporters of I-1366 presumably think that will encourage legislators to choose the constitutional amendment option, others may consider the crisis atmosphere created an opportunity to increase other taxes or levy entirely new ones.

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