



With the Income Tax, Washington Adds a New, Volatile Layer of Taxation

Briefly

Under ESSB 6346, a 9.9% tax will be imposed on Washington income over \$1 million beginning Jan. 1, 2028. All the provisions in the bill, including the tax rate and the \$1 million standard deduction, are statutory, so they could be changed by the Legislature at any time.

The determination of taxable income begins with the taxpayer's federal adjusted gross income (AGI), and several additions and subtractions are made to form Washington taxable income. The Washington income tax is explicitly levied on individuals. However, business income from pass-through entities will be subject to the tax.

In addition to imposing an income tax, ESSB 6346 also reduces some taxes (by repealing many changes made in ESSB 5814; ending the temporary B&O tax surcharge early for certain industries; increasing the small business B&O tax credit; and exempting diapers, over-the-counter drugs, and certain grooming and hygiene products from sales tax) and expands eligibility for the working families tax credit. These changes will be effective Jan. 1, 2029, if the income tax is not invalidated by the Supreme Court. Some additional targeted tax reductions will be effective July 1, 2026, and are not contingent on the income tax remaining law.

The bill does not make any appropriations, nor does it require that income tax revenues be used to increase funding for any specific purpose (aside from the expansion of eligibility for the working families tax credit).

The income tax itself is expected to increase state revenues by \$2.698 billion in FY 2029 (the second year of the 2027–29 biennium) and by \$6.899 billion in 2029–31. The net impact of ESSB 6346 to funds subject to the outlook is -\$46.4 million in 2025–27, \$2.309 billion in 2027–29, and \$5.372 billion in 2029–31. After accounting for tax reductions and increased appropriations for the working families tax credit, the state will effectively retain about 70% of income tax revenues each year that could be appropriated for any purpose.

A lawsuit challenging the constitutionality of the income tax has already been filed, and signatures are being gathered for a potential initiative to repeal the tax. Thus, the state Supreme Court or Washington voters could overturn the tax before it goes into effect.

If it remains law, the income tax will be a major change to Washington's tax system. But instead of broadly reducing other taxes in a revenue-neutral reform, the Legislature layered the income tax on top of an already uncompetitive tax structure. Even though this generates substantial new revenues for the state, it does not solve the state's ongoing budget problem. Further, the income tax will make state revenues more volatile, which will make it more difficult to craft sustainable budgets in the future.

The Washington state Supreme Court ruled in 1933 that income is property and subject to constitutional restrictions on property taxes. Consequently, an income tax with a graduated rate (in which the tax would not be “uniform upon the same class of property”) or a rate higher than 1% is considered unconstitutional. Nevertheless, in 2026, the Legislature adopted an income tax.

The income tax bill, ESSB 6346, imposes the income tax and makes some targeted reductions to other taxes. All the provisions in the bill, including the tax rate and the \$1 million standard deduction, are statutory, so they could be changed by the Legislature at any time.

Individual Income Tax

Under ESSB 6346, a 9.9% tax will be imposed on Washington income over \$1 million beginning Jan. 1, 2028. Taxes on 2028 income will be due in April 2029. If taxpayers have a federal filing extension, they will pay the estimated amount in April and it will be trued up in October. (Tax return due dates are tied to federal income tax return due dates.) Tribal income will be exempt from the tax.

Determination of the Tax. The determination of taxable income begins with the taxpayer’s federal adjusted gross income (AGI). Several additions and subtractions are made to form Washington base income. Then, additions and subtractions are made to Washington base income to form Washington taxable income. The 9.9% tax rate is applied to Washington taxable income. (See the diagram on page 3.)

Washington Base Income. Because Washington already has a separate capital gains tax, which calculates taxable capital gains differently from the federal government, the Washington income tax determination removes federal capital gains from federal AGI and adds back income subject to the Washington capital gains tax. It also adds in the Washington capital gains tax standard deduction. It does not add back the capital gains tax deductions for charitable donations or for interest in qualified family-owned small businesses. Further, capital gains income exempt from Washington capital gains tax (like gains from real estate and retirement accounts) are not added into Washington base income.

Additionally, the Washington income tax treats carryover losses differently from the federal income tax. Federal law allows individuals to deduct business losses from prior years in calculating AGI. This federal deduction is generally limited to 80% of taxable income (IRS 2024). These net operating losses will be added back into Washington base income. Then, 80% of the amount of net operating loss carryover that was deducted in federal AGI will be subtracted, if the losses are apportioned to Washington. Effectively, the Washington income tax will allow less business income to be offset with losses than federal income tax.

Other additions and subtractions are made, as shown in the diagram on page 3. This forms Washington base income.

Washington Taxable Income. Next, deductions are allowed against Washington base income. Two major deductions are the standard deduction and the charitable contributions deduction. The standard deduction is initially set at \$1 million per individual or couple. This deduction will be adjusted for inflation, but only every other year. The standard deduction will be adjusted for nonresidents based on the ratio of the taxpayer’s Washington base income to the taxpayer’s federal AGI.

The deduction for charitable contributions is limited to \$100,000 per individual or couple. This deduction will not be adjusted for inflation, and it is limited to Washington charities.

Other deductions and an addition are shown in the diagram on page 3. This forms Washington taxable income.

FIGURE 1

Determining the Tax

Start ⇒ Federal Adjusted Gross Income (AGI)

Total gross income from all sources:

wages, tips, interest, dividends, business income, retirement income, net short- and long-term capital gains, net operating loss, gambling, stock options, other

Less adjustments:

certain business expenses, educator expenses, deductible retirement contributions, deductible self-employment taxes, other

Minus

- Long-term federal capital gains
- 80% of net operating loss carryover deducted in federal AGI
- Any income WA is prohibited from taxing

Plus

- + Long-term federal capital losses
- + WA capital gains plus capital gains tax standard deduction
- + Interest on non-WA state and local bonds
- + Taxes on income that are deducted in federal AGI
- + Taxes deducted for federal purposes for which B&O or public utility tax credits are allowed
- + Amounts deducted in federal AGI that were carried over from before 1/2028
- + Amounts of net operating loss carryover deducted in federal AGI since 1/2028
- + Income from nongrantor trust funded with incomplete gift



Washington Base Income

Washington Base Income

Minus

- \$1 million standard deduction
- Charitable contributions up to \$100,000
- Commercial cannabis activities business expenses
- 90% of WA wagering losses
- Amount deposited in a merchant marine capital construction fund

Plus

- + Pass-through entity tax expense, if deducted in federal AGI



Washington Taxable Income

Washington Taxable Income x 9.9%

Minus

- Credit for income taxes due to another state or local government
- Credit for B&O and public utility taxes paid
- Credit for WA capital gains tax paid
- Credit for pass-through entity tax payments



Washington Income Tax Due

Credits. After calculating the amount of income tax due, taxpayers are allowed certain credits, which reduce the amount owed. These include credits for B&O and capital gains taxes paid. Credits may not exceed the tax due, and credits may not be carried forward or backward.

Paying the Tax. Under ESSB 6346, only those owing the tax will be required to file returns, and there is no provision in the law for withholding. However, estimated payments will be required if the estimated tax is more than \$5,000. Any estimated payments will begin after July 1, 2029, and will follow federal estimated payment quarterly reporting periods, with estimated tax payments due in April, June, September, and January.

Who Will Pay? The Department of Revenue estimates that there will be 21,000 income tax filers. According to the Internal Revenue Service (IRS), there were 21,530 filers with AGI of \$1 million or more in Washington in 2022, which is the most recent year of data (IRS 2025).

The tax will be imposed regardless of filing status. The standard deduction is \$1 million and the charitable deduction is \$100,000, regardless of whether the taxpayer is single or married. This means that there is a marriage penalty. For example, a single person with taxable income of \$600,000 would not be subject to the income tax. If two people are married and each make \$600,000, their combined taxable income would be subject to income tax.

Assuming individuals have taxable income over the standard deduction, they will pay Washington's income tax if they are residents and, in some cases, if they are nonresidents.

For purposes of the income tax, individuals are residents of Washington if they are domiciled in Washington. State rules for the capital gains tax define "domicile" as

"a permanent place of abode, coupled with the intent to make the abode one's home. It is the place that you intend to return to even if you visit or temporarily reside elsewhere. Thus, actual presence in a location at any given time is not necessarily determinative of a person's domicile. An individual can have only one domicile at a time." (WAC 458.20.301(2)(c))

State rules also note that the Department of Revenue makes determinations about domicile on "a case-by-case basis" (WAC 458.20.301(6)(c)). ESSB 6346 specifies that if taxpayers are considered domiciled in Washington but have no permanent residence in Washington and have a permanent residence outside Washington, they will be considered residents of Washington for purposes of the income tax if they spend more than 30 days in Washington during the calendar year. Additionally, individuals who were not domiciled in Washington but maintained a residence here and spent more than 183 days in Washington during the calendar year will also be considered Washington residents. (This definition is the same as the definition of a resident for purposes of Washington's capital gains tax.)

ESSB 6346 states that for residents, "all income must be allocated" to Washington. For nonresidents, "income derived from sources within this state must be allocated to this state." However, there is a five-day safe harbor for nonresidents: If they work five or fewer days in Washington during a year, no income is allocated to Washington. The five-day safe harbor does not apply to nonresident professional or student athletes or nonresident entertainers.

For nonresident professional athletes, compensation will be apportioned to Washington based on the ratio of duty days within Washington to the total number of duty days in the year. The tax would be owed on income apportioned to Washington for any professional athlete earning total compensation of

over \$1 million (not adjusted for inflation). For nonresident student athletes, income from commercial use of their name, image, or likeness will be allocated to Washington “if the publicity services provided by the student athlete related to such commercial use of the student athlete’s name, image, or likeness primarily occur in Washington.”

Impact on Businesses. The Washington income tax is explicitly levied on individuals. However, many businesses are structured as pass-through entities. (ESSB 6346 defines pass-through entities as partnerships, limited liability companies, and S corporations.) As such, their business income is taxed via the owners’ individual income taxes. For example, in 2022, 60.2% of federal income tax returns filed by Washington residents with AGI over \$1 million included net income from partnerships or S corporations (IRS 2025). However, the B&O and public utility tax credits would reduce the amount of Washington income tax paid.

Under ESSB 6346, owners of pass-through entities may elect to make the entity itself subject to the Washington income tax. In that case, the owner of the entity may take a credit against the income tax that is equal to the owner’s share of the tax paid by the entity. Such an election would not change the amount of tax due to Washington, but it would provide federal tax advantages to the taxpayer. Under current federal law, the state and local tax deduction is limited for individuals. But the state and local tax deduction is unlimited for business entities.

Additionally, some business activity could become newly subject to tax in Washington. For example, income from renting real estate for periods of more than a month is not subject to the B&O tax because the state Supreme Court held in 1960 that taxing rental income would be an unconstitutional property tax (DOR 2024). If ESSB 6346 is upheld by the Supreme Court, rental income would be subject to state income tax. Indeed, rental income is included in federal AGI and thus forms part of Washington taxable income for individuals and pass-through entities. Further, if ESSB 6346 is upheld, rental income could become subject to B&O tax, which would also affect C corporations.

Interactions with the Capital Gains Tax. Washington already has a free-standing capital gains tax, and several forms of capital gains that are taxed at the federal level (through the income tax code) are not taxed in Washington (e.g., gains from real estate and retirement accounts). Consequently, as noted above, in determining Washington base income, capital gains are removed from federal AGI and then Washington capital gains are added. The switch assures that income from the sale of a house, for example, will not be subject to Washington income tax.

However, in many respects, the capital gains tax and income tax are not harmonized:

- The capital gains tax has an additional rate tier. The Washington capital gains tax rate is 7%. For gains exceeding \$1 million, an additional 2.9% tax is imposed. Thus, both the Washington capital gains tax and income tax apply a 9.9% tax rate on income over \$1 million.
- The standard deduction is \$278,000 in tax year 2025 for the capital gains tax. We estimate that it will be \$301,000 in tax year 2028, when the income tax standard deduction is \$1 million.
- The \$278,000 standard deduction for the capital gains tax is adjusted *annually* for inflation, but the \$1 million standard deduction for the income tax is adjusted for inflation *only every other year*. The capital gains tax bracket (the point at which the rate is 9.9% instead of 7%) is not adjusted for inflation at all.

- The capital gains tax charitable deduction is \$111,000 for tax year 2025. It is adjusted annually for inflation; we estimate it will be \$120,000 in tax year 2028. To take this deduction, a taxpayer must have made minimum donations to Washington charities of at least \$278,000 (adjusted annually for inflation). The income tax deduction for charitable contributions is limited to \$100,000 (not adjusted for inflation), and it is limited to Washington charities (but there is no requirement that total giving exceeds a certain amount). The determination of the income tax excludes the capital gains tax charitable donation amount. Consequently, for tax year 2028, if a taxpayer makes \$301,000 in charitable donations, they could take a \$120,000 deduction from their capital gains tax and another \$100,000 deduction from their income tax.

The impact of these differences on tax burden will depend on a taxpayer's situation.

Other. ESSB 6346 amends RCW 1.90.100 (I-2111, which was approved by the Legislature in 2024) to allow the state to impose an income tax, if the standard deduction is at least \$1 million. Counties, cities, and other local jurisdictions will still be prohibited from imposing personal income taxes.

The bill includes a null and void clause such that “if a court of final jurisdiction invalidates” the income tax, then the entire bill—except for the tax relief provisions that are effective in 2026 (see below)—is null and void.

Planned Uses of Income Tax Revenues

In addition to imposing an income tax, ESSB 6346 also reduces some taxes and expands eligibility for the working families tax credit. Some of these changes are effective only if the income tax is not invalidated by the Supreme Court. The bill does not make any appropriations.

Sales Tax on Services. In 2025, the Legislature enacted ESSB 5814. The bill extended sales and use taxes to various services, including, for example, custom website development, temporary staffing, and advertising (WRC 2025). ESSB 6346 repeals the 2025 changes for all the services newly subject to sales tax, except advertising. This is effective Jan. 1, 2029.

In the meantime, ESSB 6346 makes several targeted changes to ESSB 5814. First, temporary staffing services are defined to exclude their use by hospital-based clinical providers. Second, live presentations are defined to exclude before and after school care, presentations by nonprofits, performances, tutoring, and music lessons. Third, various services to libraries and schools are explicitly not subject to sales tax. These targeted changes are effective July 1, 2026, regardless of whether the income tax is held to be invalid.

With the repeal of many of the ESSB 5814 changes, services that are currently subject to sales tax will revert to being taxed at the B&O service and other activities rate. They may also be subject to the workforce education investment surcharge or the financial institutions surcharge.

Targeted Changes to Temporary B&O Tax Surcharge. In 2025, the Legislature imposed a temporary B&O tax surcharge of 0.5% on taxable income over \$250 million (WRC 2025). It is scheduled to be in place from Jan. 1, 2026, through Dec. 31, 2029. ESSB 6346 makes hospitals, prescription drug warehousing and reselling, and health care services exempt from the surcharge, effective Jan. 1, 2029.

Additionally, ESSB 6346 makes wholesale sales of food and food ingredients exempt from the temporary surcharge, effective July 1, 2026. This change is effective regardless of whether the income tax is held to be invalid. (The fiscal note estimates it will affect six wholesalers.)

Small Business B&O Tax Credit Increased. ESSB 6346 increases the small business B&O tax credit so that about \$300,000 of business income will be exempt, with a full phase out at about \$600,000. (Currently,

about \$125,000 is exempt, with a full phase out at about \$250,000.) Additionally, the B&O tax filing threshold will increase from \$125,000 to \$250,000. These changes are effective Jan. 1, 2029.

New Sales Tax Exemptions. ESSB 6346 exempts grooming and hygiene products from sales and use taxes, effective Jan. 1, 2029. Grooming and hygiene products are narrowly defined as “soaps and cleaning solutions, shampoo, toothpaste, mouthwash, antiperspirants, and sun tan lotions and screens.”

Additionally, ESSB 6346 exempts diapers and over-the-counter drugs from sales and use taxes, effective Jan. 1, 2029.

Working Families Tax Credit (WFTC). ESSB 6346 expands eligibility for the WFTC, effective Jan. 1, 2029. Despite its name, the WFTC is structured as an entitlement program for which funds are appropriated in the state operating budget. Although premised on the expectation that recipients have paid sales taxes, there is no connection between the amount of sales taxes paid and the amount of the remittance. Instead, the minimum remittance is \$50, and the maximum remittances are currently \$335 for an individual with no children, \$660 for an individual with one child, \$995 for an individual with two children, and \$1,330 for an individual with three or more children (the amounts are adjusted for inflation). The amount of the remittance is phased down based on income.

Currently, eligibility is limited to individuals who are 25 to 65 years old (unless they have qualifying children). Under ESSB 6346, any individual may qualify if they are at least 18 years old.

TABLE 1

Working Families' Tax Credit Income Thresholds

(Assuming ESSB 6346 Changes Effective for Tax Year 2025)

	No Children	One Child	Two Children	Three Children	Four or More Children
<u>Current Law</u>					
Phase-out Begins					
Single Filers	\$16,604	\$45,434	\$52,310	\$56,555	\$56,555
Joint Filers	\$23,714	\$52,554	\$59,430	\$63,675	\$63,675
Maximum Income					
Single Filers	\$19,104	\$50,434	\$57,310	\$61,555	\$61,555
Joint Filers	\$26,214	\$57,554	\$64,430	\$68,675	\$68,675
<u>ESSB 6346</u>					
Phase-out Begins					
Single Filers	\$43,292	\$67,528	\$84,196	\$109,948	\$132,772
Joint Filers	\$70,028	\$84,196	\$109,948	\$132,772	\$132,772
Maximum Income					
Single Filers	\$45,792	\$72,528	\$89,196	\$114,948	\$137,772
Joint Filers	\$72,528	\$89,196	\$114,948	\$137,772	\$137,772

Note: The table shows single versus joint filers to provide an apples-to-apples comparison, but the income thresholds in ESSB 6346 are based on the number of people in the household, not filing status.

Additionally, under current law, the WFTC income limit is tied to the federal earned income tax credit (EITC) limit, which is adjusted annually for inflation and is dependent on income tax filing status. Under ESSB 6346, the maximum qualifying income will be the greater of the federal EITC limit or the individual's "need and payment standards for cash assistance" (WAC 388-478-0015). Eligibility for various state assistance programs is already based on this standard, which is adjusted annually by the state Department of Social and Health Services by rule (RCW 74.04.770). Currently, the standard is based on the University of Washington's self-sufficiency standard (DSHS 2026). The need and payment standard is substantially higher than the EITC limit, and it is based on the number of people in the household (not tax filing status).

Table 1 on page 7 shows the maximum income eligible for the credit and the income level at which the credit begins to be phased out, under both current law and ESSB 6346. (This is a hypothetical comparison that assumes the changes in ESSB 6346 are effective now. These thresholds will change by 2029.) Table 2 provides some examples of the remittances given varying income levels and number of children.

Note that ESSB 6346 does not increase the amount of the WFTC remittance. A single filer with no children and income of \$16,000 gets a remittance of \$335 under current law. Under ESSB 6346, a single filer with no children making \$36,000 would also get a remittance of \$335.

Potential Spending. Income tax revenues will mainly be deposited in the general fund–state (GFS). However, beginning in FY 2030, 5% of income tax revenues from the prior fiscal year will be deposited in the fair start for kids account (FSKA). The FSKA may only be used for child care and early learning, but it currently has no revenue source. There is nothing in ESSB 6346 that would prevent the state from supplanting current funding for child care with the new money in the FSKA. (The FSKA is a fund subject to the outlook.)

TABLE 2
Estimated Working Families' Tax Credit Amounts
(Assuming ESSB 6346 Changes Effective for Tax Year 2025)

	Income	Estimated Remittance	
		Current Law	ESSB 6346
Single Filer, No Children	\$16,000	\$335	\$335
Single Filer, No Children	\$20,000	\$0	\$335
Single Filer, No Children	\$36,000	\$0	\$335
Single Filer, One Child	\$45,000	\$660	\$660
Single Filer, One Child	\$70,000	\$0	\$363
Joint Filer, Two Children	\$64,000	\$310	\$995
Joint Filer, Two Children	\$110,000	\$0	\$987
Joint Filer, Four Children	\$65,000	\$1,092	\$1,330
Joint Filer, Four Children	\$135,000	\$0	\$929

The intent section of ESSB 6346 includes several non-binding ideas for spending the revenues: to fund free school meals, create a city and county fiscal health account, and “[i]ncrease state funding for K-12 education in order to improve outcomes for Washington’s students by strengthening high quality instruction and expanding student supports.”

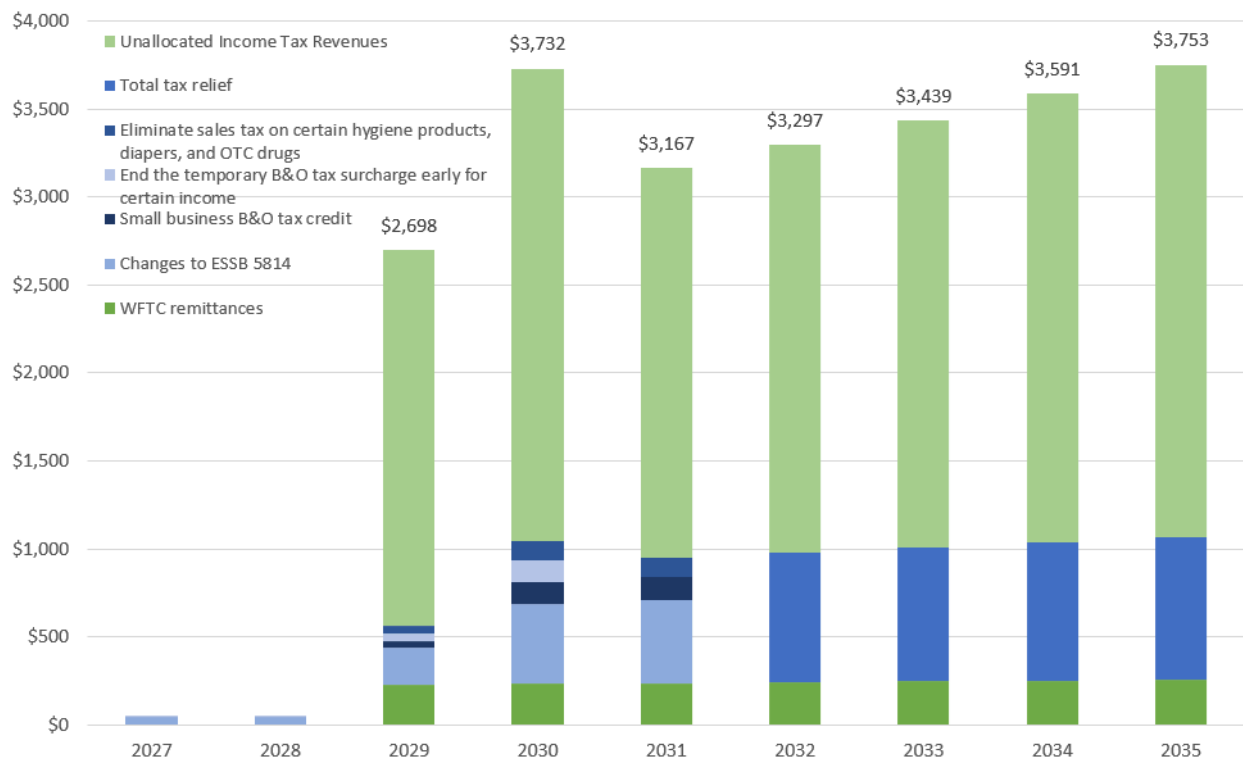
As part of the 2026 supplemental budget, the Legislature assumed, in the outlook for 2027–29, \$140 million for free school meals and \$200 million for the proposed city and county account. However, these are not appropriations, they are suggestions that the next Legislature may accept or reject. Because most income tax revenues are deposited in the GFS, some of the revenues will likely be used for education, health care, and human services. But there is nothing in ESSB 6346 that requires the income tax revenues to be used for those purposes or that requires increasing funding for those purposes.

The Income Tax Will be a Major New Tax Source

On net, ESSB 6346 is expected to increase revenues to funds subject to the outlook (NGFO) by 6.2% in 2029–31. The income tax will be the state’s fourth-largest tax source, behind the sales tax, B&O tax, and property tax.

According to the fiscal note for ESSB 6346, the income tax itself is expected to increase state revenues by \$2.698 billion in FY 2029 (the second year of the 2027–29 biennium) and by \$6.899 billion in 2029–31. ESSB 6346 also impacts state B&O tax revenues and state and local sales tax revenues. The net impact of ESSB 6346 to the NGFO is -\$46.4 million in 2025–27, \$2.309 billion in 2027–29, and \$5.372 billion in 2029–31.

CHART 1
NGFO Revenue Impact from Income Tax Bill
(Dollars in Millions)



Source: DOR

The fiscal note estimates that there will be a spike in revenues in FY 2030, due to normal payment timing issues and the beginning of required estimated payments. FY 2030 revenues will include final tax year 2028 payments collected in October 2029 (which is in FY 2030), four quarters of estimated payments for tax year 2029, and the first quarterly estimated payment for tax year 2030.

Additionally, the fiscal note estimates that the expansion of the WFTC will increase appropriations by \$226.0 million in FY 2029 and \$467.0 million in 2029–31. Effectively, after accounting for the tax

TABLE 3

Estimated Fiscal Impacts of ESSB 6346

(Dollars in Millions)

	2027	2028	2029	2030	2031	2025-27	2027-29	2029-31
Income Tax Revenues	\$0.0	\$0.0	\$2,698.0	\$3,732.0	\$3,167.0	\$0.0	\$2,698.0	\$6,899.0
Tax reductions								
Repeal most of ESSB 5814								
State	-\$41.5	-\$46.3	-\$215.7	-\$466.1	-\$483.5	-\$41.5	-\$262.0	-\$949.6
Local	-\$20.6	-\$25.2	-\$128.6	-\$346.6	-\$359.4	-\$20.6	-\$153.8	-\$706.0
Total	-\$62.1	-\$71.5	-\$344.3	-\$812.7	-\$842.9	-\$62.1	-\$415.8	-\$1,655.6
Increase small business B&O tax credit and filing threshold								
	\$0.0	\$0.0	-\$37.1	-\$127.4	-\$130.4	\$0.0	-\$37.1	-\$257.8
End the temporary B&O tax surcharge early for certain income								
	-\$5.0	-\$6.0	-\$47.0	-\$126.0	\$0.0	-\$5.0	-\$53.0	-\$126.0
Eliminate sales tax on certain grooming and hygiene products								
State	\$0.0	\$0.0	-\$31.2	-\$76.2	-\$77.4	\$0.0	-\$31.2	-\$153.6
Local	\$0.0	\$0.0	-\$11.6	-\$35.3	-\$35.8	\$0.0	-\$11.6	-\$71.1
Total	\$0.0	\$0.0	-\$42.8	-\$111.5	-\$113.2	\$0.0	-\$42.8	-\$224.7
Eliminate sales tax on diapers								
State	\$0.0	\$0.0	-\$7.5	-\$18.6	-\$19.1	\$0.0	-\$7.5	-\$37.7
Local	\$0.0	\$0.0	-\$2.8	-\$8.6	-\$8.9	\$0.0	-\$2.8	-\$17.5
Total	\$0.0	\$0.0	-\$10.3	-\$27.2	-\$28.0	\$0.0	-\$10.3	-\$55.2
Eliminate sales tax on over-the-counter drugs								
State	\$0.0	\$0.0	-\$6.1	-\$15.4	-\$16.2	\$0.0	-\$6.1	-\$31.6
Local	\$0.0	\$0.0	-\$2.3	-\$7.1	-\$7.5	\$0.0	-\$2.3	-\$14.6
Total	\$0.0	\$0.0	-\$8.4	-\$22.5	-\$23.7	\$0.0	-\$8.4	-\$46.2
Total tax reductions								
State	-\$46.5	-\$52.3	-\$344.7	-\$829.7	-\$726.6	-\$46.5	-\$397.0	-\$1,556.4
Local	-\$20.6	-\$25.2	-\$145.3	-\$397.6	-\$411.6	-\$20.6	-\$170.5	-\$809.2
Total	-\$67.1	-\$77.5	-\$490.0	-\$1,227.3	-\$1,138.2	-\$67.1	-\$567.5	-\$2,365.6
Net Revenue								
NGFO	-\$46.4	-\$51.4	\$2,360.6	\$2,916.7	\$2,455.4	-\$46.4	\$2,309.2	\$5,372.1
Multimodal account (transportation budget)	\$0.0	-\$0.9	-\$6.6	-\$13.1	-\$13.6	\$0.0	-\$7.5	-\$26.7
Performance audits account	-\$0.1	-\$0.1	-\$0.6	-\$1.4	-\$1.4	-\$0.1	-\$0.7	-\$2.8
State total	-\$46.5	-\$52.3	\$2,353.3	\$2,902.3	\$2,440.4	-\$46.5	\$2,301.0	\$5,342.6
Local governments	-\$20.6	-\$25.2	-\$145.3	-\$397.6	-\$411.6	-\$20.6	-\$170.5	-\$809.2
WFTC Remittances								
	\$0.0	\$0.0	\$226.0	\$231.0	\$236.0	\$0.0	\$226.0	\$467.0
Unallocated State Income Tax Revenues								
Percent of Income Tax Revenues			\$2,127.3	\$2,671.3	\$2,204.4		\$2,127.3	\$4,875.6

Source: DOR

reductions and the increased appropriations for WFTC, the state will retain about 70% of income tax revenues each year that could be appropriated for any purpose.

Nevertheless, income tax revenues will not be sufficient to solve the operating budget problem; the state will still need to limit spending growth to below the long-term average in order to close the gap between spending and revenues (WRC 2026b, Makings 2026).

Impact on the Transportation Budget and Local Governments. In 2025, the Legislature adopted 2SSB 5802, which directed 0.1% of revenues from the sales tax to the multimodal account, effective FY 2028. Thus, the changes to the sales tax in ESSB 6346 are estimated to reduce revenues to the state multimodal account (which is appropriated in the transportation budget) by \$7.5 million in FY 2029 and by \$26.7 million in 2029–31.

Similarly, the sales tax changes in ESSB 6346 are expected to reduce local government revenues by \$20.6 million in FY 2027 (the second year of 2025–27), \$170.5 million in 2027–29, and \$809.2 million in 2029–31.

Washington’s Tax Structure Will Be Less Competitive and More Volatile

According to the Tax Foundation, Washington’s tax structure as of July 1, 2025 was the sixth-least competitive in the country (Fritts et al. 2025). Further, Washington ranks fourth worst for corporate tax and second worst for both sales tax and unemployment insurance tax. This poor showing does not even reflect most of the tax increases that were adopted in 2025, including ESSB 5814 (WRC 2026a).

Washington will join 41 other states that have income taxes, but our income tax will be added on top of an already uncompetitive structure. ESSB 6346 did not meaningfully reduce B&O or sales taxes to counteract the new income tax. (Indeed, the most significant piece of tax relief in ESSB 6346 is the repeal of most of ESSB 5814, but because ESSB 5814 was not yet included in the Tax Foundation analysis, its repeal won’t improve our competitiveness ranking.) Further, many of the specifics of Washington’s income tax may make it less competitive than income taxes in other states.

In evaluating state income taxes, the Tax Foundation considers, for example, the top tax rate, inflation adjustments, and the treatment of married couples. Assuming other states don’t change their top rates by 2028, Washington’s income tax rate would tie Oregon’s for the fifth highest. Washington’s standard deduction will be adjusted for inflation only every other year, and the charitable deduction won’t be indexed at all. Washington’s tax includes a marriage penalty (the standard deduction is not doubled for taxpayers who file jointly).

Meanwhile, although Washington’s tax structure is uncompetitive, it has traditionally had the benefit of producing stable revenues. Pew estimates that for the 15 years ending in 2024, Washington had the nation’s fifth-least volatile revenues (Robyn et al. 2026). As Pew notes, general sales taxes are “historically one of the least volatile major tax streams” (Robyn et al. 2026). Income taxes are more volatile than sales taxes. Further, the Urban Institute reports, “state tax revenues have become far more volatile over the past decade due to states’ growing reliance on volatile nonwage income sources, particularly capital gains and stock-based compensation” (Dadayan 2026).

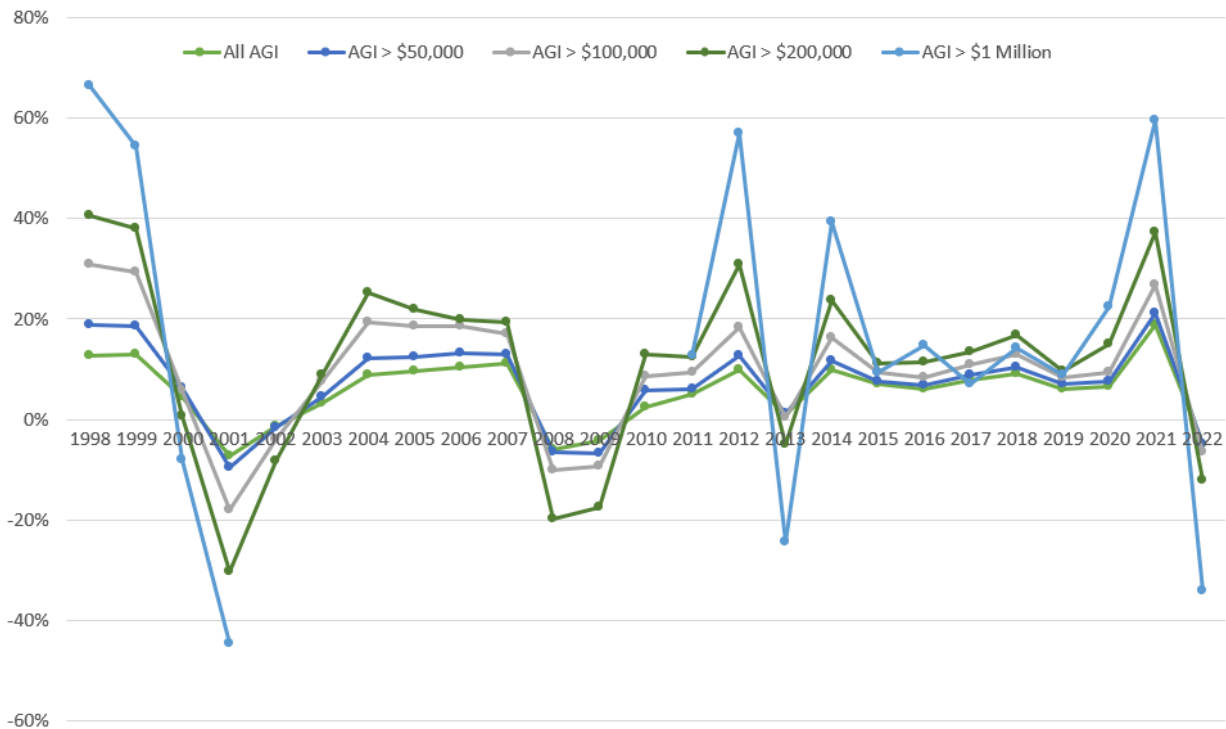
Washington’s income tax, with a standard deduction of \$1 million, will be more volatile than an income tax with a lower standard deduction. Chart 2 on page 12 shows the percentage change in total AGI of Washington residents; total AGI over \$50,000 per return; total AGI over \$100,000 per return; total AGI over \$200,000 per return; and total AGI over \$1 million per return (IRS 2025). Effectively, this

approximates how hypothetical income tax revenues would have changed given various exemption levels. (The IRS data does not break out AGI over \$1 million for years 2002 through 2009, and 2022 is the most recent data available.) As the exemption level rises, the peaks are higher and the troughs are lower.

As Washington becomes more reliant on income taxes—especially those targeted at high earners and capital gains—state revenues will become more volatile. That means the state will need to increase reserves to ensure that we are saving enough money in good times to avoid service disruptions when revenues decline.

CHART 2

Year-Over-Year Percentage Change in Washington AGI



Source: IRS

 Washington Research Council

Comment

A lawsuit challenging the constitutionality of the income tax has already been filed, and signatures are being gathered for a potential initiative to repeal the tax. Thus, the state Supreme Court or Washington voters could overturn the tax before it goes into effect.

If it remains law, the income tax will be a major change to Washington’s tax system. But instead of broadly reducing other taxes in a revenue-neutral reform, the Legislature layered the income tax on top of an already uncompetitive tax structure. Even though this generates substantial new revenues for the state, it does not solve the state’s ongoing budget problem. Further, the income tax will make state revenues more volatile, which will make it more difficult to craft sustainable budgets in the future.

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