Washington Research Council

Policy Brief

December 7, 2018 PB 18-10

Washington Revenue Review: Revenues Are Still Growing Strong, But for How Long?

Briefly

Washington's tax structure brings in revenues that are proportional to those in other states. Meanwhile, growth in state and local taxes from 2015 to 2016 was highest in Washington.

In its November revenue forecast, the Economic and Revenue Forecast Council estimates that near general fund–outlook (NGFO) revenue will be $45.799 billion in 2017–19, $50.002 billion in 2019–21 (an increase of 9.2 percent), and $53.795 billion in 2021–23 (an increase of 7.6 percent). For 2017–19 and 2019–21, the new forecast adds a total of $1.735 billion since the February forecast (on which the 2018 supplemental budget was based). However, the forecast also suggests that growth may be slowing.

Washington's tax structure is unusual, but it yields revenues that are similar to other states by multiple metrics. Further, the state has experienced exceptionally high revenue growth in recent years (13.8 percent in 2015–17 and an estimated 17.3 percent in 2017–19). The November revenue forecast indicates that revenue will continue to grow in the next biennium, but it also points to slowing growth in some of Washington's largest revenue sources.

Revenue Sources

Washington is one of seven states that do not tax income. Instead, the state relies more heavily than other states on sales and property taxes. Washington's sales tax accounts for 44.6 percent of state taxes, compared to a U.S. average of 31.3 percent (Census n.d.).

Washington's property tax accounts for 9.3 percent of state taxes, compared to a U.S. average of 2.0 percent (Census n.d.).

Chart 1: All State Taxes, FY 2016

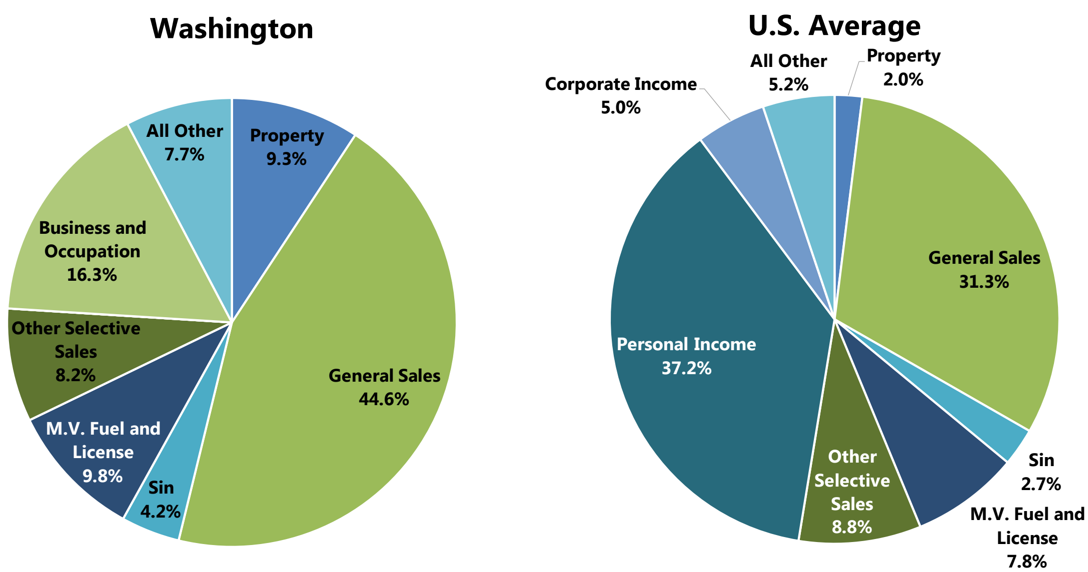


Chart 2: Tax Revenue Volatility Score, 1998–2017

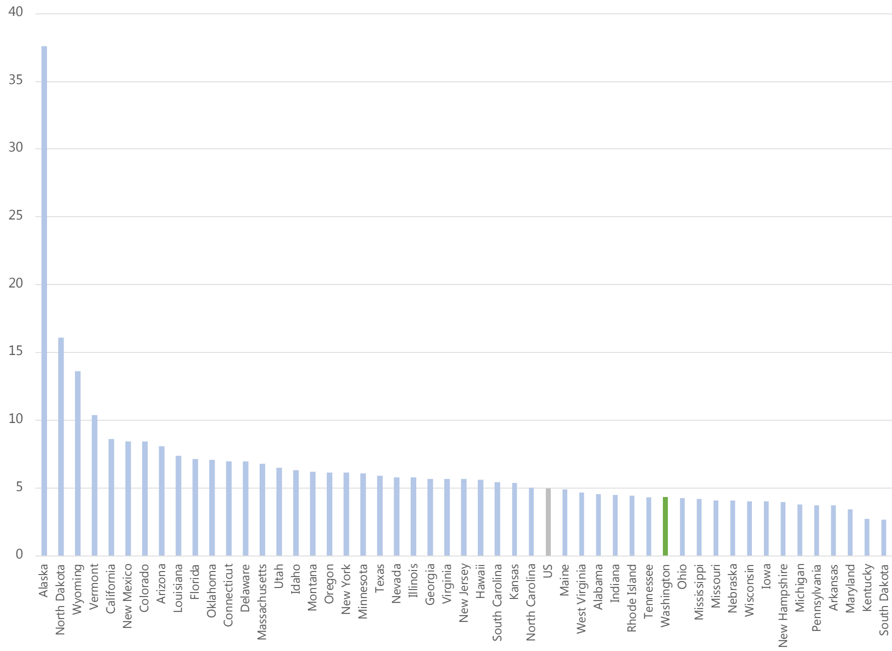
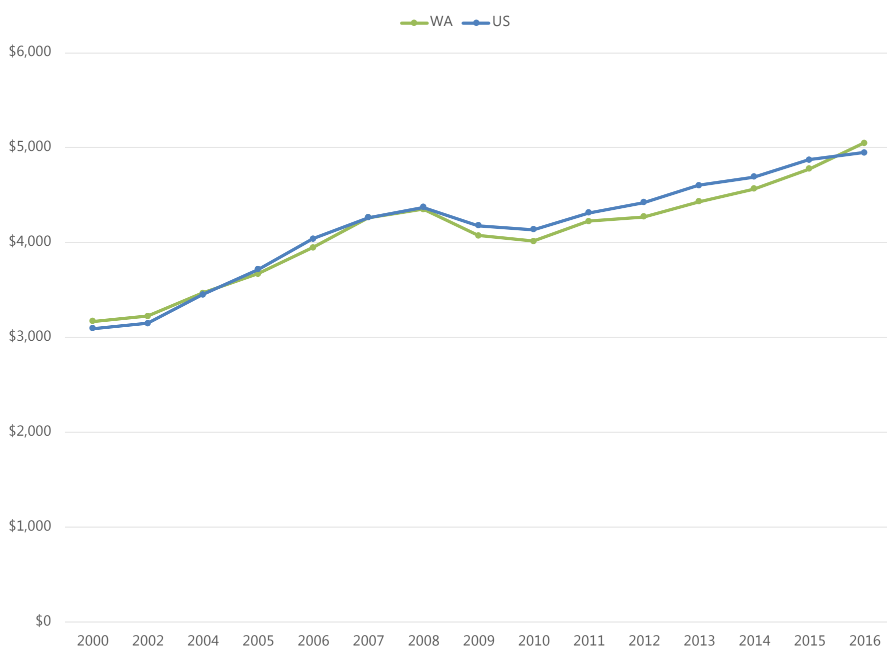


Chart 3: State and Local Taxes Per Capita



(In other states, property taxes are primarily levied at the local level.) According to the most recent revenue forecast, state property taxes in Washington will increase over the next several years. A second state property tax was enacted in 2017 to help support the increase in school funding required by the state Supreme Court's McCleary decision (WRC 2017). The state property tax rate was $1.89 per $1,000 of assessed value in calendar year (CY) 2017; with the 2017 legislation and amendments made in 2018, the combined state property tax rate is $2.70 per $1,000 in CY 2018 and it will be $2.40/$1,000 in CY 2019, $2.70/$1,000 in CY 2020, and $2.70/$1,000 in CY 2021 (RCW 84.52.065).

Additionally, through CY 2021, the two state property taxes are not subject to Washington's statutory 101 percent revenue growth limit (WRC 2017). This means that until 2022, property tax revenues will be reflective of property values. If property values are increasing, more revenues could be collected than if the limit was in place. But declining property values could result in reduced property tax revenues.

The other significant difference between Washington's tax structure and those of other states is Washington's business and occupation (B&O) tax, which accounts for 16.3 percent of state taxes. The B&O tax's counterpart in most states is the corporate income tax, which makes up just 5.0 percent of state taxes in the U.S. on average. (Census n.d.)

The revenues produced by Washington's tax structure are the 14th least volatile in the country (Pew 2018). Further, increasing the proportion of the state's revenue from the new state property tax levied as part of the state's response to the McCleary decision will make Washington's revenues still less volatile. (Property taxes are exceptionally stable from year to year, particularly when they are subject to growth limits.) Revenue stability is an important aspect of the tax structure because large revenue swings from year to year can make funding sources for spending programs unreliable.

Comparative Revenues Over Time

Despite its lack of an income tax, Washington's state and local taxes per capita have largely tracked the national average (see Chart 3 on page 2). In 2016 (the most recent data available), Washington's state and local taxes per capita were $5,050, above the national average of $4,946. By this measure, Washington ranked 17th in the nation. (Census n.d.)

As a share of personal income, Washington's state and local taxes rank near the middle of the pack at 28th among the states (Census n.d.). Washington's rank is lower by this measure than per capita because its personal income per capita is consistently higher than the national average. In 2017, Washington ranked ninth highest in the country in personal income per capita (BEA 2018).

Revenue Outlook

Washington's recent revenue growth has been strong by national standards. Indeed, Washington's state and local tax growth from 2015 to 2016 was the nation's highest (Census n.d.).

Similarly, state revenue growth in Washington has outpaced the nation since 2015, and it ranked 10th highest among the states in 2017 (Pew 2018). (See Chart 6 on page 4.) Other states have not performed as well. Adjusted for inflation, revenues in 16 states have still not recovered to their pre-recession peaks (Pew 2018).

Looking forward, the Economic and Revenue Forecast Council (ERFC) estimates that Washington's state revenues will continue to increase through the forecast window (2017–19 through 2021–23). In the November 2018 revenue forecast, the ERFC estimates that near general fund–outlook (NGFO) revenues will be $45.799 billion in 2017–19, an increase of 17.3 percent over 2015–17 (a 13.2 percent increase, adjusted for inflation). (This is an increase of $809.2 million, or

Chart 4: State and Local Taxes as a Share of Personal Income

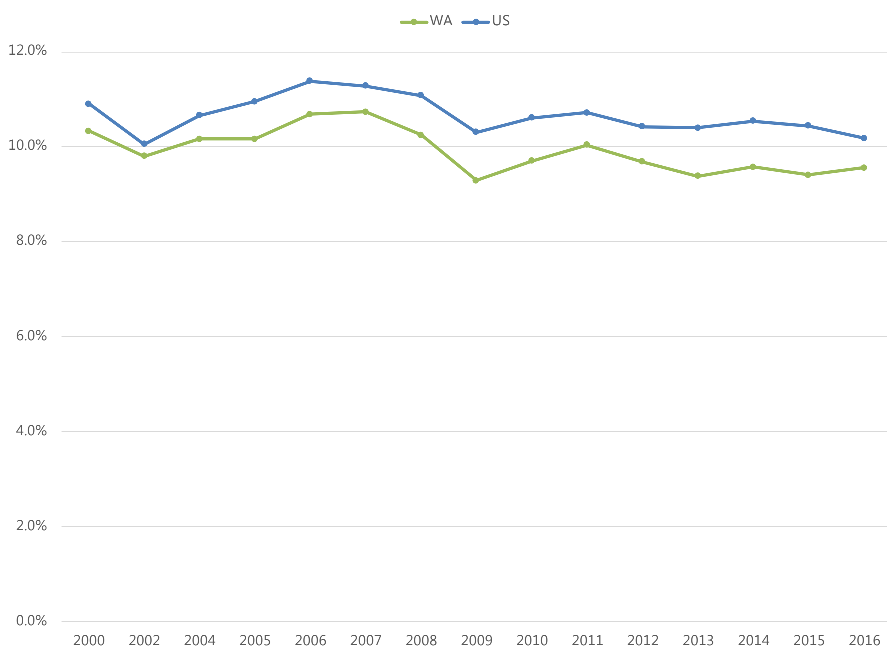


Chart 5: Personal Income Per Capita

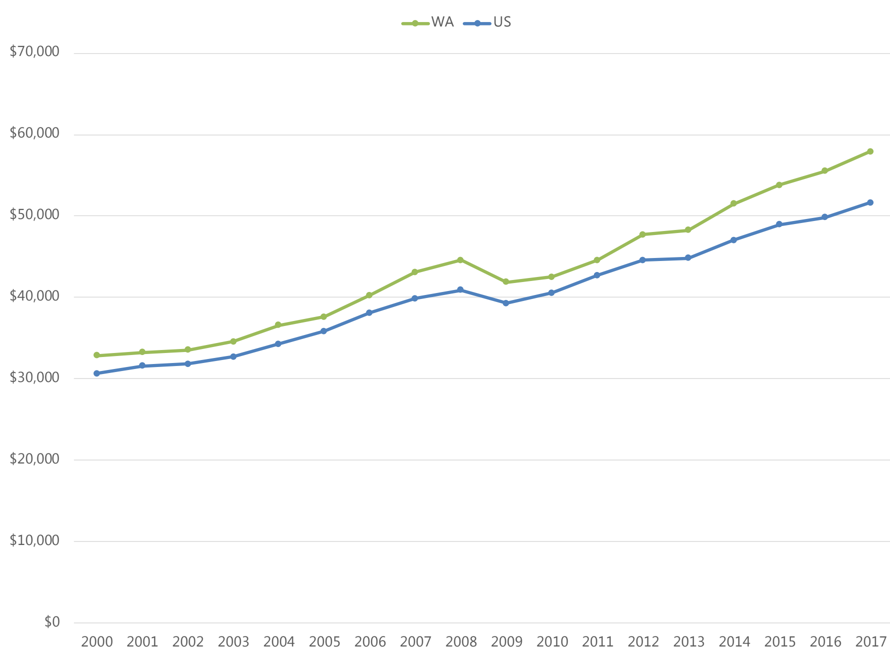


Chart 6: State Revenue Since the Pre-Recession Peak

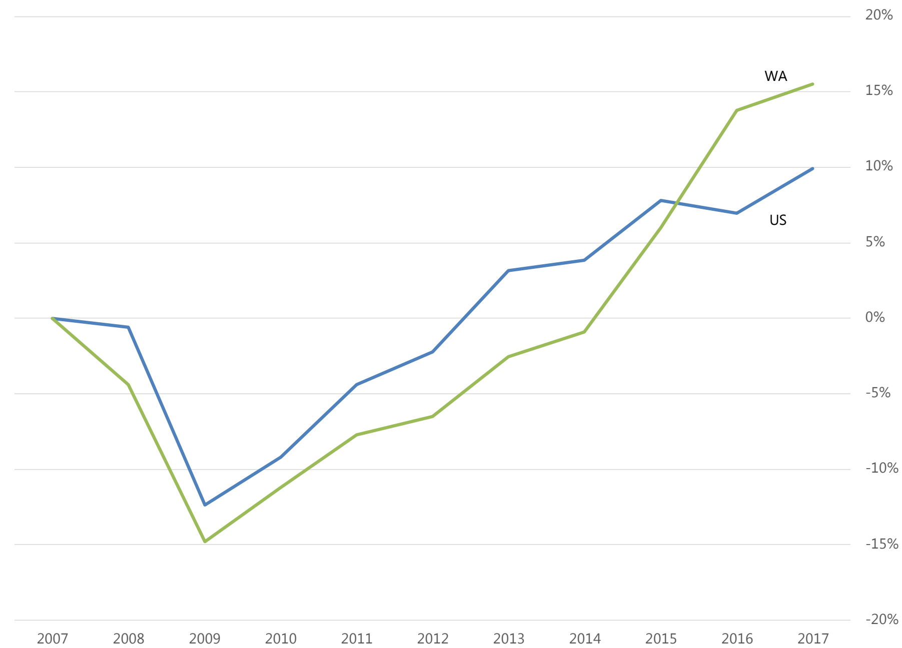
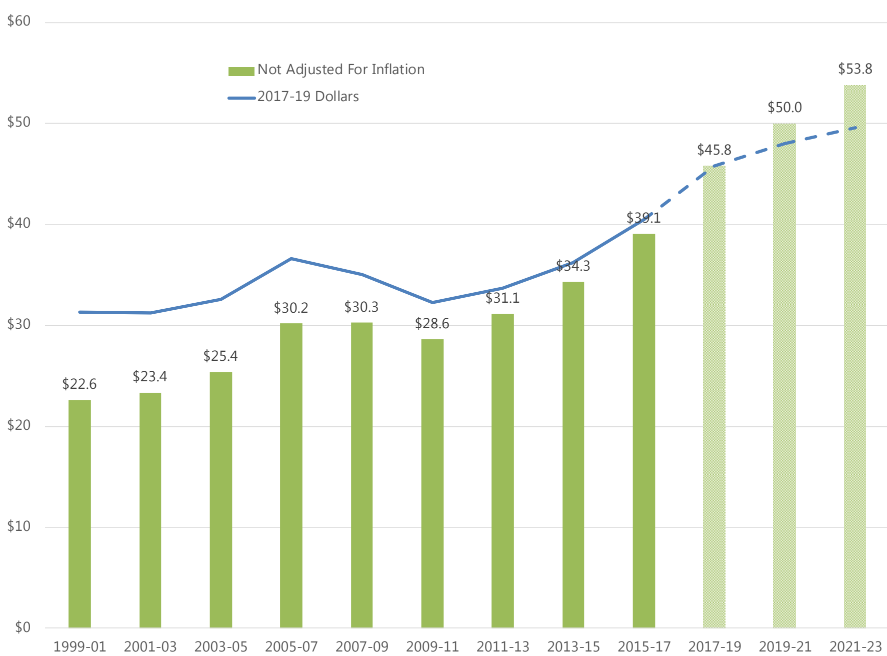


Chart 7: NGFO Revenues (Dollars in Billions)



1.8 percent, since the February 2018 forecast, on which the 2018 supplemental to the 2017–19 budget was based.) NGFO revenues in 2017–19 are estimated to be 51.8 percent higher than the pre-recession peak in 2005–07 (25.1 percent higher, adjusted for inflation). (ERFC 2018)

For 2019–21, the ERFC estimates that NGFO revenues will total $50.002 billion, an increase of 9.2 percent over 2017–19 (an increase of 4.8 percent, adjusted for inflation). (This is an increase of $925.3 million, or 1.9 percent, since the February forecast). Revenues for 2021–23 are estimated to be $53.795 billion, an increase of 7.6 percent (an increase of 3.3 percent adjusted for inflation). (ERFC 2018)

The November revenue forecast gave some reasons to be cautious about the future. Revenue Act taxes (retail sales and use, B&O, public utility, and non-cigarette tobacco products taxes), which make up about 75 percent of the state's revenue sources, were revised downward; personal income is growing slower than in recent years; and real estate excise taxes are "assumed to have reached a near-term peak in the first quarter of 2018" (ERFC 2018).

Comment

Washington's tax structure, though unconventional, produces significant revenues. Taxes per capita compare favorably with other states. Washington's substantial wealth drives revenue growth that has exceeded the national average since 2015. Moreover, despite high personal income, taxes as a share of personal income in Washington still rank in the middle of the pack nationally.

Funds Subject to the Outlook (NGFO)

In recent years, legislative fiscal committee staffs have based budget presentations on a synthetic "account" that rolls up the general fund–state (the state's primary budget account) with the education legacy trust account and the opportunity pathways account, because they believe that it better reflects the entire budget situation. Previously called the near general fund–state plus opportunity pathways (NGFS+), it is now more simply called "funds subject to the outlook" or the near general fund–outlook (NGFO). (Under the four-year balanced budget requirement, a positive ending balance is required in the current biennium on an NGFO basis.)

The November 2018 revenue forecast delivered $1.7 billion in new revenue for the 2017–19 and 2019–21 biennia and estimates that revenues will continue to grow in the near term. However, it also suggests that growth may be slowing. Legislators should not expect that recent exceptional revenue growth will continue forever and should plan accordingly.

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