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In this installment of Skookum Tax News, the authors discuss Washington Gov. Jay Inslee — recently one of the Democratic presidential candidates and now running for a third term as governor. The article focuses on his gubernatorial legacy to date in state and local taxation.

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For his entire seventh year as governor of Washington, Jay Inslee (D) has been on the campaign trail. First, he joined over 20 other candidates for the Democratic nomination for president. His platform focused on a single statement: “Defeating climate change must be our

nation’s top priority.”¹ Inslee made it to the second round of presidential debates on July 31, but, like most of the crowded field of candidates, he never polled at more than 1 percent. The same day in August that he dropped out of that race, Inslee launched a campaign for a third term as Washington’s governor. As a lens for evaluating Inslee as a candidate, this article offers a summary of his legacy thus far in state and local taxation: his progress on his signature issue of climate change, increases to the state’s tax revenue, and Democratic efforts to reform Washington’s tax system to make it more progressive.

Fighting Climate Change With Taxes, Among Other Things

As Inslee embarked on his first term as governor in 2013, his objective was to make Washington a model for how states can combat climate change. That same year, he met with the governors of California and Oregon and the premier of British Columbia, resulting in the aspirational Pacific Coast Action Plan on Climate and Energy.² Inslee has tried several different approaches to bring about the types of changes discussed in the action plan.

First, in 2015, he pursued a carbon emissions cap-and-trade program.³ That law would have capped overall emissions and required the state’s largest stationary sources of emissions to pay for each metric ton of pollution emitted, while allowing the sale of excess emission allowances at an auction. The emphasis on stationary sources

¹ Jay Inslee, “Climate Change Is a Winning Campaign Issue — And President Trump Knows It,” *The New York Times*, July 28, 2019.

² Pacific Coast Collaborative, “Pacific Coast Action Plan on Climate and Energy” (Oct. 28, 2013).

³ Peter Jensen, “Inslee Cap-and-Trade Bill to Open Legislative Session’s Second Act,” *The Washington State Wire*, Mar. 12, 2015.

meant consumers or the transportation sector would not be directly affected.

Faced with strong legislative resistance, Inslee in 2016 took a different course: executive action in the form of the new Clean Air Rule — a set of regulations intended to cap and reduce carbon pollution.⁴ The regulations target major in-state stationary sources of greenhouse gas emissions and upstream producers, importers, and distributors of petroleum products in the state.⁵ But the regulations have become mired in litigation, particularly around whether the measures required legislative authorization. The trial court prevented implementation after holding that some parts of the rule were invalid. The state supreme court heard oral argument in the case in March,⁶ but as of the date of writing, no decision has been issued.

More recently, in 2017 and 2018, Inslee proposed bills that would have made Washington the first state to adopt a carbon tax, but he failed to garner enough legislative support. Washington voters similarly rejected carbon tax initiatives in the 2016 and 2018 elections.⁷ And the Legislature has not adopted proposed legislation to establish low-carbon fuel standards (LCFS) like those in California, Oregon, and British Columbia. The Puget Sound Clean Air Agency, however, has been considering a stringent regional LCFS program.⁸

The one measure Inslee has succeeded in passing through the Legislature has been this year's Clean Energy Transformation Act (CETA). CETA requires Washington electric utilities to remove coal from investments and depreciation payments, including coal plants owned in other states, by 2025.⁹ CETA requires the state to become

carbon-neutral by 2030 and sets a goal for the state to achieve fully carbon-free power by 2045.¹⁰ Whether the regulatory scheme to cap and reduce emissions through the Clean Air Rule survives remains to be seen. At any rate, even in a state with a strong environmental movement, and with Democratic control in both houses since 2019, Inslee has struggled to find a foothold for proposals around his signature issue.

Increasing State Revenue

Originally, Inslee espoused economic growth as the best route to meeting the state's increased revenue needs, including those posed by a school funding case decided shortly before Inslee took office as governor.¹¹ The case, *McCleary v. State of Washington*, held that the state was violating its duty under the state constitution to adequately fund K-12 education.¹² For six years, the Washington Supreme Court exercised oversight of the funding to comply with its holding in the case. It even held the Legislature in contempt until the court finally decided it had taken sufficient measures to meet its funding obligation.¹³ There have been other funding pressures during Inslee's tenure as governor, but *McCleary* represented by far the largest hurdle.¹⁴

During Inslee's time as governor, Washington has experienced an economic boom that, by itself, has greatly increased state revenues.¹⁵ Nevertheless, as early as 2014, Inslee started proposing budgets based on new taxes and fees, citing changed conditions since his 2012 campaign statements.¹⁶ The 2019 session, in which

¹⁰ *Id.*

¹¹ John Stang, "Inslee Unshaken on No-New-Taxes Promise," *Crosscut*, Nov. 14, 2012 ("he cited his campaign promise that the Legislature can raise money to meet a Washington Supreme Court mandate to increase school funding by creating enough new jobs to generate more state revenue — and without raising taxes").

¹² *McCleary v. State of Washington*, 173 Wn.2d 477, 269 P.3d 227 (2012).

¹³ *McCleary v. State of Washington*, No. 84362-7 (Wash. June 7, 2018) (order terminating retention of jurisdiction of court in case).

¹⁴ See, e.g., Washington State Department of Social and Health Services, "Trueblood Frequently Asked Questions" (regarding the 2018 settlement in the federal case *Trueblood v. Washington State Department of Social and Health Services* requiring additional state funding for psychiatric patients in the criminal justice system).

¹⁵ Steve Lerch, Washington State Economic and Revenue Forecast Council, "Economic and Revenue Growth Trends" (Jan. 22, 2019).

¹⁶ Jim Brunner, "Does Gov. Jay Inslee Support a State Income Tax? No, He Does Not," *The Seattle Times*, Sept. 12, 2016.

⁴ Washington State Department of Ecology, "Ecology Statement on Appeal Filed With Washington State Supreme Court," May 14, 2018.

⁵ Wash. Admin. Code chs. 173-441 and 173-442.

⁶ Rachel La Corte, "Washington Supreme Court Hears Case on Carbon Cap Rule," *The Seattle Times*, Mar. 19, 2019; and *Association of Washington Business v. Washington State Department of Ecology*, Docket No. 95885-8 (Wash.).

⁷ Carbon Tax Center, "Washington State (Initiative 1631)"; and Marianne Lavelle, "Washington State Voters Reject Nation's First Carbon Tax," *Inside Climate News*, Nov. 9, 2016.

⁸ Puget Sound Clean Air Agency, "Considering a Regional Clean Fuel Standard."

⁹ Molly Barker, "The Big Zero: Washington's Clean Energy Transition Act and the State's Big Shift to Zero Emissions," *NWLAWYER* (July/Aug. 2019).

Democrats enjoyed a majority in both houses of the Legislature, saw particularly large tax increases — over \$1 billion in new revenue for 2020.¹⁷ Even so, Inslee's 2019 budget plan proposed approximately twice as much in tax increases.¹⁸

The largest tax increases, in terms of dollar amounts, have been various property tax shifts in the last couple of years. For the most part, the shifts have been from local levies to the state tax levy. These have had varying effects on taxpayer pocketbooks depending on the year and local jurisdictions in which they occurred.¹⁹ The next largest increases are two business and occupation (B&O) tax surcharges for service activities affecting affiliates of advanced computing businesses and large financial institutions, starting January 1, 2020.²⁰ Following that is the amendment to the real estate excise tax, which creates a graduated rate based on value of the property sold and implements several other changes, also effective January 1, 2020.²¹ Lastly, under Inslee, the state's enforcement of its economic nexus rules against remote internet sellers and other out-of-state businesses has been aggressive even as the nexus thresholds keep changing. Starting January 1, \$100,000 in Washington sales will replace the prior nexus factor thresholds for all B&O tax classifications and sales tax collection.²² Together, along with Washington's continuing strong economic performance, these changes should significantly increase state tax collections.

Making Taxes More Progressive

Inslee and Democratic lawmakers have not only argued for increased state revenues but also for making Washington's tax system more progressive. In his 2019 budget proposal, Inslee explained, "More than half our revenue comes from retail sales taxes, which disproportionately

impact people at the lower end of the economic scale and allow the very wealthiest individuals and most prosperous businesses to pay relatively less in taxes."²³ The state has one of the highest sales tax rates in the nation and no personal income tax. The lack of personal income tax has been a source of contention for years, as shown most recently in litigation over Seattle's effort to create its own standalone personal income tax.²⁴ Inslee, however, has not favored an income tax, which makes sense considering voters' repeated rejection of a constitutional amendment many consider necessary under Washington law.²⁵

Instead, Inslee proposed a capital gains tax that would raise nearly a billion dollars for the 2019-21 biennium.²⁶ In a state without any personal income tax — and no system for individual income tax reporting — this type of tax is controversial. Lawmakers have tried to address some of the most pressing concerns, such as exempting personal retirement accounts. A new capital gains tax would also present possible legal impediments: Taxing gains measured by a basis established long before the tax existed would amount to a retroactive tax that would arguably offend due process principles. Strangely, this point has not been part of the debate. The 2019 legislative session did not see the creation of this new tax, however, because lawmakers could not agree on whether to add the new tax to the existing tax regime or to instead offset it with cuts to the sales tax and property tax.²⁷

The only measure adopted that might address regressivity concerns is the change to the state real estate excise tax paid on the transfer of real property whether by deed or controlling interest. Rather than applying the same tax rate (usually approximately 1.8 percent after adding the local tax component) regardless of the value of the property, the tax will be graduated, with slightly lower rates on lower-value properties and increasing rates for higher-value properties.²⁸

¹⁷ Rich Smith, "Senate Democrats Killed the Capital Gains Tax. Here's What Happened," *The Stranger*, May 3, 2019.

¹⁸ Jay Inslee, "Proposed 2019-21 Budget & Policy Highlights," at 5.

¹⁹ See, e.g., Ch. 410, Laws of 2019 (S.B. 5313).

²⁰ Ch. 406, Laws of 2019 (H.B. 2158); Ch. 420, Laws of 2019 (H.B. 2167).

²¹ Ch. 424, Laws of 2019 (S.B. 5998).

²² Ch. 8, Laws of 2019 (S.B. 5581).

²³ Inslee, *supra* note 18, at 5.

²⁴ *Kunath v. City of Seattle*, 444 P.3d 1235 (Wash. Ct. App. 2019).

²⁵ Michelle DeLappe and Norman Bruns, "Seattle's Income Tax Quest: An Impossible Dream?" *State Tax Notes*, July 10, 2017, p. 171.

²⁶ Inslee, *supra* note 18, at 10.

²⁷ Smith, *supra* note 17.

²⁸ Ch. 424, Laws of 2019 (S.B. 5998).

Conclusion

Of course, no article about Inslee's legacy in state and local tax should skip over the Boeing tax incentives adopted in 2013 in a special legislative session — but for that, we recommend Billy Hamilton's excellent article on the subject.²⁹ In the end, Inslee's SALT legacy has been a road full of twists and turns and ups and downs — and even a mugging, as Inslee characterized the Boeing incentives when interviewed on *The Daily Show*.³⁰ Every indication is that Washington will have Inslee for governor for another four years, but who knows? Many have speculated that his presidential campaign was in part a prelude to vying for a cabinet appointment if a Democrat prevails in the presidential race.³¹ Inslee has denied any interest in such a position, however — though some take that with a grain of salt given Inslee's 2012 stance against new taxes compared with the later reality.³² ■

²⁹ Billy Hamilton, "Boeing and Washington: A Love So Right Turns Out to Be So Wrong," *State Tax Notes*, May 6, 2019, p. 519.

³⁰ *Id.*

³¹ Melissa Santos, "Gov. Inslee's Re-election Bid Cools Other Democrats' Ambitions — For Now," *Crosscut*, Aug. 22, 2019.

³² *Id.*

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