

Chapter One - Introduction and Summary of Findings

INTRODUCTION

The Tax Exemption Study lists exemptions for the major state and local taxes in Washington and is authorized by the Revised Code of Washington (RCW) 43.06.400 [Appendix A].

Tax exemptions:

The term *tax exemption* includes a variety of preferences that reduce tax liability for taxpayers. Tax exemptions include:

- Exclusions;
- Deductions;
- Credits;
- Deferrals;
- Preferential tax rates; and,
- Exemptions.

Department of Revenue (Department) staff estimated the impact of each exemption. Sales and use tax exemptions for the same product or activity are included as a single estimate. In other cases, there are multiple estimates for a single statute to better illustrate the impacts.

The summary of each exemption includes:

- A brief description;
- The purpose of the exemption;
- Taxpayer savings;
- Potential revenue gains from a full repeal of the exemption; and,
- Additional information.

Taxpayer savings versus potential revenue gain:

Number of Incentives	STATE Taxpayer Savings (FY 2021)	STATE Revenues Realized from Repeal (FY 2021)
748	35,073,807,000	21,729,547,000

Savings to taxpayers do not indicate the potential revenue that governmental jurisdictions would accrue if the exemption did not exist. For example, some exemptions will not increase state revenues by the same amount as the taxpayer savings due to:

- Constitutional prohibitions against taxing certain activities;
- Possible changes in taxpayer reporting behavior; or,
- Actual cash receipts lower because of compliance factors.

In all cases, estimates assume a full repeal is effective July 1, 2020, resulting in no revenue gain in Fiscal Year 2020 and typically 11 months of revenue gain for Fiscal Year 2021.

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The Tax Exemption Study *does not* include:

- Locally administered taxes such as the municipal business taxes;
- Discussion regarding tax policy related to the exemption; or,
- Recommendations to keep or terminate existing exemptions.

Forecast:

All estimates use the March 2019 Economic and Revenue Forecast Council forecast unless otherwise noted.

Revised Code of Washington (RCW) Citation:

The full RCW citation is included if it was available at the time that the exemption was analyzed.

SUMMARY OF FINDINGS

The current study analyzes 748 tax exemptions. The state and local impacts of these tax exemptions combine for an estimated taxpayer savings of \$138.9 billion for the 2019-21 Biennium. Approximately 49 percent of the total, or \$68.3 billion, are exemptions from state taxes. Exemptions from local government taxes amount to \$70.6 billion.

Table 1 summarizes the number of exemptions and the distribution of state and local impacts for the various types of taxes considered in this study.

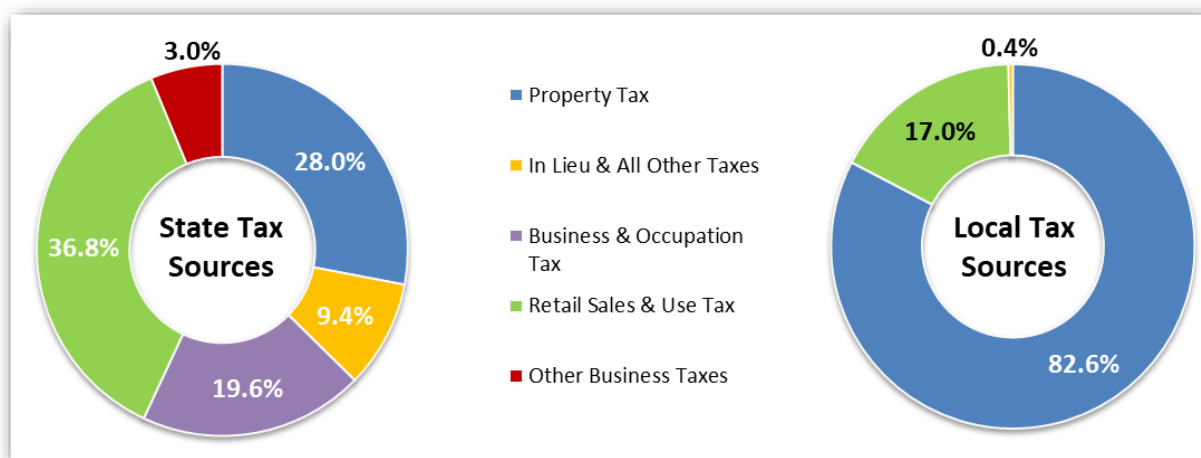
Table 1
Summary of Tax Exemption Impacts by Tax Source
Estimated Taxpayer Savings
2019-21 Biennium (\$ millions)

Tax Source	Number of Exemptions	State Tax Savings	Local Tax Savings	Total Savings for Biennium
Property Tax	118	\$19,104.884	\$58,294.621	\$77,399.505
In Lieu Excise Taxes	49	79.172	70.968	\$150.140
Business & Occupation Tax	195	13,374.365	0.000	\$13,374.365
Retail Sales & Use Tax	220	25,152.480	11,980.254	\$37,132.734
Other Business Taxes	94	4,277.526	0.000	\$4,277.526
All Other Taxes	72	6,308.024	204.323	\$6,512.347
Total	748	\$68,296.451	\$70,550.166	\$138,846.617

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Chart 1 shows tax savings by tax source as a percent of the total. Nearly 37 percent of the state impact is from retail sales and use tax exemptions, while more than 82 percent of local tax impact is from property tax exemptions.

Chart 1
Taxpayer Savings by Tax Source



Taxpayer savings versus potential revenue gains from a full repeal:

Savings to taxpayers do not indicate the potential revenue that governmental jurisdictions would accrue if the exemption did not exist. For this reason, each exemption provides the estimated taxpayer savings plus the potential revenue gain from a full repeal of the exemption.

- For many excise taxes there is a one-to-one relationship between the amount that taxpayers save and the amount that government gives up in potential revenues.
- Other exemptions may cause possible changes in taxpayer reporting behavior, which could restrict the potential revenues realized.
- Several exemptions exist because of constitutional reasons, and are not a reliable source of potential new governmental revenue.
- Depending on the year a property tax exemption is repealed, it may increase state revenues or shift property taxes back to currently exempt taxpayers.

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Table 2a shows the taxpayer savings for the 2019-21 Biennium, and the amount of potential revenue gains with a full repeal of the exemptions as of July 1, 2020. The potential gains reflect no collections in Fiscal Year 2020 and eleven months of collections in Fiscal Year 2021, the second year of the biennium.

Table 2a
Taxpayer Savings versus Potential Revenue Gains by Tax Source
2019-21 Biennium (\$ millions)

Tax Source	State			Local		
	State Tax Savings	Potential Revenue Gains	Difference	Local Tax Savings	Potential Revenue Gains	Difference
Property Tax	19,104.884	5,411.495	13,693.389	58,294.621	1,484.522	56,810.099
In Lieu Excise Taxes	79.172	34.215	44.957	70.968	20.606	50.362
Business & Occupation Tax	13,374.365	4,606.452	8,767.913	0.000	0.000	0.000
Retail Sales & Use Tax	25,152.480	9,267.407	15,885.073	11,980.254	4,678.880	7,301.374
Other Business Taxes	4,277.526	1,925.142	2,352.384	0.000	0.000	0.000
All Other Taxes	6,308.024	484.836	5,823.188	204.323	94.660	109.663
Total	68,296.451	21,729.547	46,566.904	70,550.166	6,278.668	64,271.498

Table 2b shows the taxpayer savings and potential revenue gains from a full repeal of the exemptions for the 2021-23 Biennium in order to include a full 24-month impact for both the savings and gains.

Table 2b
Taxpayer Savings versus Potential Revenue Gains by Tax Source
2021-23 Biennium (\$ millions)

Tax Source	State			Local		
	State Tax Savings	Potential Revenue Gains	Difference	Local Tax Savings	Potential Revenue Gains	Difference
Property Tax	20,815.450	20,645.712	169.738	63,093.244	5,840.322	57,252.922
In Lieu Excise Taxes	84.666	84.461	0.205	76.399	50.559	25.840
Business & Occupation Tax	14,500.813	10,511.281	3,989.532	0.000	0.000	0.000
Retail Sales & Use Tax	27,401.886	22,703.759	4,698.127	13,160.875	11,363.598	1,797.277
Other Business Taxes	4,267.719	4,149.700	118.019	0.000	0.000	0.000
All Other Taxes	6,713.502	3,040.337	3,673.165	211.562	211.562	0.000
Total	73,784.036	61,135.250	12,648.786	76,542.080	17,466.041	59,076.039

Taxpayer savings versus forecasted revenue collections:

Table 3 and Chart 2 compare the estimated taxpayer savings from exemptions for selected state taxes with the Economic and Revenue Forecast Council forecasted revenues for those same tax sources.

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The total taxpayer savings for these state taxes is nearly \$59 billion for the 2019-21 Biennium, which is nearly \$14 billion more than the forecasted revenues of \$45 billion.

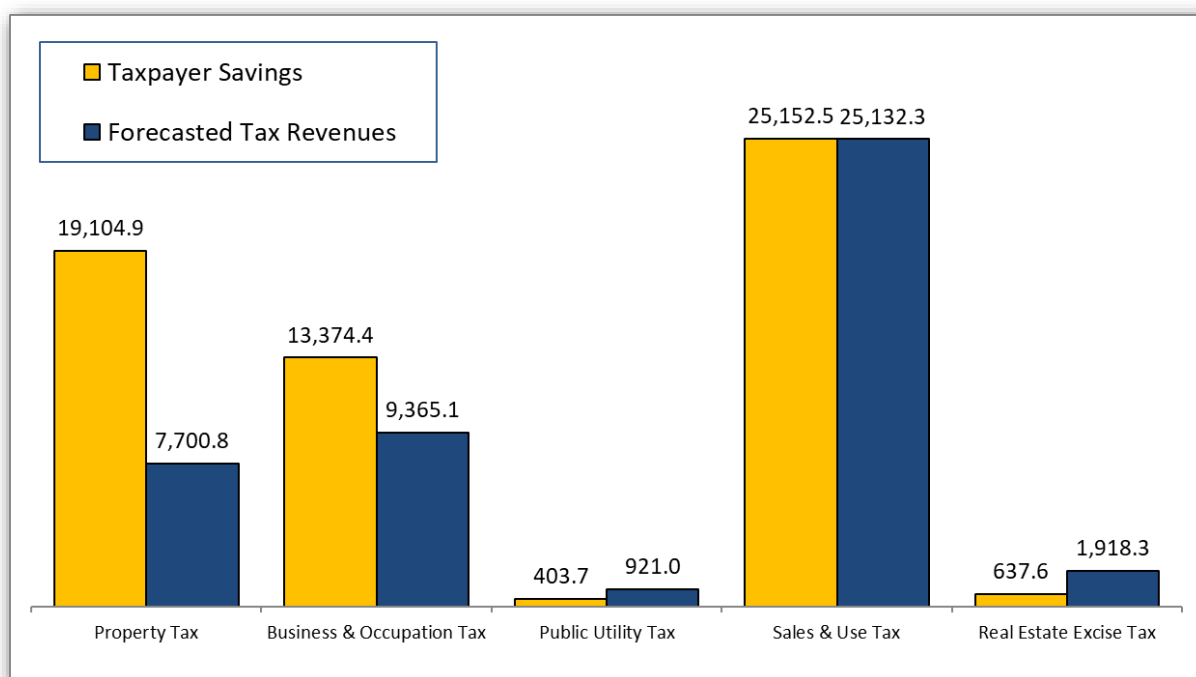
Table 3
Comparison between Taxpayer Savings and Revenues
Selected Major State Tax Sources
2019-21 Biennium (\$ millions)

State Tax Source	Taxpayer Savings from Exemptions	Forecasted Tax Revenues ¹	Exemptions as a Percent of Revenue
State Property Tax Levy	19,104.884	7,700.819	248.1%
State Business & Occupation Tax	13,374.365	9,365.125	142.8%
Public Utility Tax	403.652	921.049	43.8%
Retail Sales & Use Tax	25,152.480	25,132.343	100.1%
Real Estate Excise Tax	637.604	1,918.311	33.2%
Total	58,672.985	45,037.647	130.3%

¹Economic and Revenue Forecast Council (March 2019 Forecast)

Taxpayer savings for state property tax and the business and occupation tax exemptions are significantly higher than the forecasted revenues for these tax sources in the 2019-21 Biennium.

Chart 2
Comparison between Taxpayer Savings and Revenues
Selected Major State Tax Sources
2019-21 Biennium (\$ millions)



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Categorical Analysis:

Tax exemptions are established for a variety of reasons. In an attempt to present more meaningful data for the various types of exemptions, eight categories were developed. Each exemption is assigned to the category that most closely represents its general purpose or type of beneficiary (recognizing that many exemptions serve multiple purposes).

A brief description of the exemption categories appears below:

Category	Number of Exemptions	Brief Description of Category
Agriculture	60	There are a variety of property, B&O and sales tax, and other exemptions for agricultural businesses.
Business	263	These exemptions generally benefit business entities.
Government	88	Governmental jurisdictions include the federal government, the state of Washington, local governments and foreign countries.
Individuals	70	These exemptions generally benefit people, as opposed to businesses or other entities.
Interstate Commerce	21	The United States Constitution prohibits direct taxation of interstate commerce. The Legislature has enacted exemptions to assure that Washington does not violate this requirement.
Nonprofit	91	There are a variety of property, B&O and sales tax exemptions allowed for nonprofit organizations.
Tax Base	77	This category includes activities the Legislature purposefully excluded in the original tax base. For example, there is an exemption to assure employees are not subject to B&O tax, even though it was never the intent for tax to apply to salaries and wages.
Other	78	Some exemptions do not fit easily into one category. These are included in the "Other" category. As an example, the exemption for intangibles benefits the agricultural industry, businesses, and individuals.

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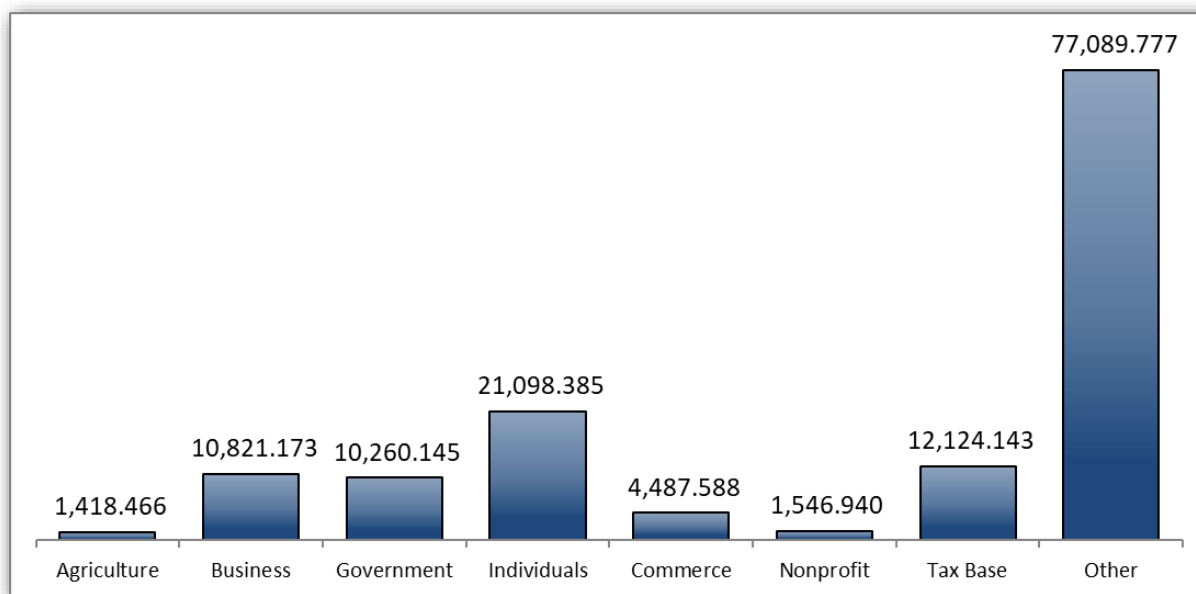
Table 4 summarizes the results of the categorical analysis. The other category represents over 55 percent of the total taxpayer savings, the majority of which are local tax savings. Of the \$77.1 million taxpayer savings in the other category, \$75.0 million comes from the following two exemptions:

- Property tax exemption on intangibles (\$62.0 million); and,
- Sales and use tax exemption on personal and professional services (\$13.0 million).

Table 4
Tax Exemptions by Category
2019-21 Biennium (\$ millions)

Category	Number of Exemptions	State Tax Savings	Local Tax Savings	Total Tax Savings	Percent of Total
Agriculture	60	880.268	538.198	1,418.466	1.0%
Business	263	7,936.939	2,884.234	10,821.173	7.8%
Government	88	3,632.198	6,627.947	10,260.145	7.4%
Individuals	70	14,930.826	6,167.559	21,098.385	15.2%
Interstate Commerce	21	4,013.700	473.888	4,487.588	3.2%
Nonprofit	91	1,000.349	546.591	1,546.940	1.1%
Tax Base	78	10,788.913	1,335.230	12,124.143	8.7%
Other	77	25,113.258	51,976.519	77,089.777	55.5%
Total	748	68,296.451	70,550.166	138,846.617	100.0%

Chart 3
Tax Exemptions by Category
2019-21 Biennium (\$ millions)



Exemption History

Tax exemptions enacted by year:

Until 1935, no more than a half dozen new exemptions appeared in any single year. With the adoption of the Revenue Act of 1935 came many new exemptions; 43 of which are still in statute today. These were associated with:

- Retail sales and use taxes;
- B&O tax; and,
- Various other new state excise taxes.

Table 5 shows the number of current tax exemption statutes over time, starting in Washington's territorial days.

Table 5
Current Tax Exemptions by Year of Enactment

Year Adopted	Number	Year Adopted	Number	Year Adopted	Number	Year Adopted	Number
1854	4	1949	14	1981	10	2002	6
1871	1	1951	13	1982	4	2003	29
1886	1	1953	2	1983	12	2004	18
1889	5	1955	7	1984	6	2005	24
1890	3	1957	1	1985	10	2006	14
1891	2	1959	3	1986	9	2007	19
1911	1	1961	5	1987	14	2008	13
1915	3	1963	4	1988	3	2009	33
1923	3	1965	9	1989	28	2010	7
1925	2	1967	19	1991	9	2011	9
1929	1	1970	12	1992	4	2012	7
1931	4	1971	17	1993	11	2013	11
1933	4	1972	1	1994	4	2014	6
1935	43	1973	5	1995	16	2015	20
1937	3	1974	5	1996	10	2016	5
1940	2	1975	10	1997	18	2017	12
1941	1	1976	11	1998	21	2018	2
1943	3	1977	4	1999	7	2019	25
1945	5	1979	12	2000	7		
1947	4	1980	13	2001	23	TOTAL	748

Exemption History

The following two charts show tax exemptions in current statutes:

- Enacted by year; and,
- The cumulative number by decade.

Chart 4
Current Tax Exemptions by Year of Enactment

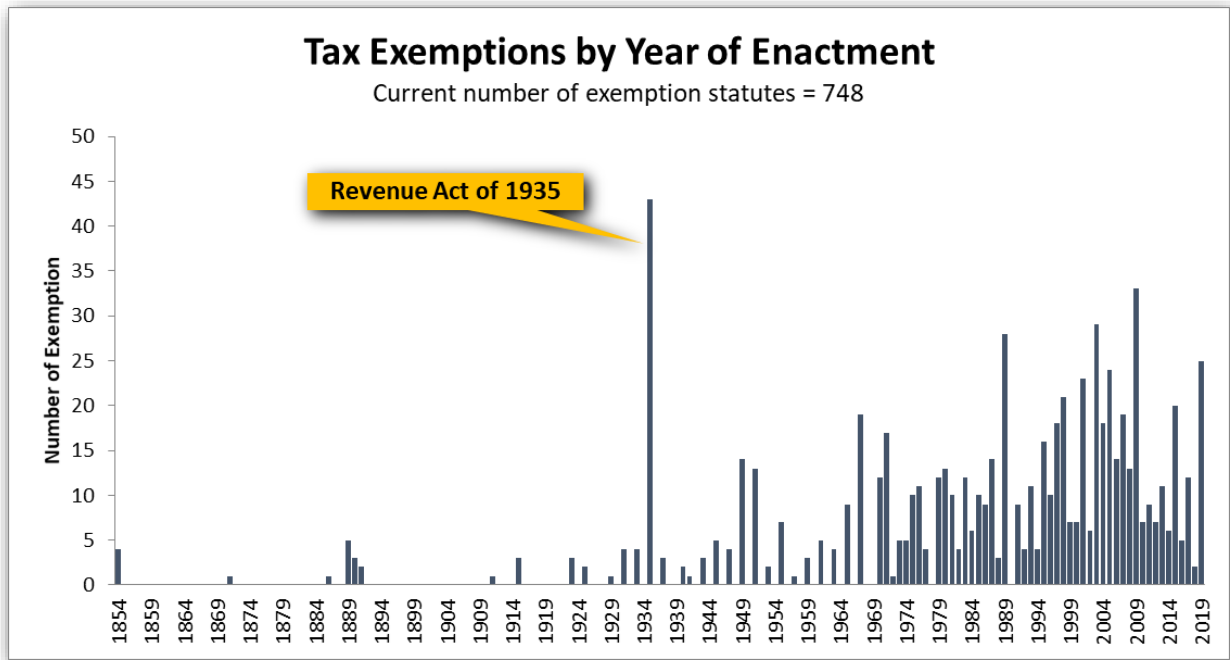


Chart 5
Cumulative Number of Tax Exemption Enacted by Decade

