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Governor

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March 28, 2013

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Governor Inslee releases Working Washington budget priorities
Proposal will boost education funding, set new accountability measures

OLYMPIA – Governor Jay Inslee today released his Working Washington 2013–15 budget priorities which call for $1.2 billion in new, targeted education investments tied to strong accountability measures.

"I feel deeply that my number one priority is to help rebuild our economy, get people working again and take important steps toward building a workforce for the future," Inslee said. "And that begins with education."

Inslee's budget moves the state forward in meeting state Supreme Court-mandated basic education obligations. In addition to providing more support for basic school operations, Inslee's plan includes funding for full-day kindergarten in all high-poverty schools and reducing kindergarten and first grade class sizes, early reading intervention, dropout prevention programs and more professional development opportunities for educators. Outside of the definition of basic education, Inslee also proposes adding $35 million to expand preschool opportunities.

Inslee has said repeatedly that the state cannot fund its basic education obligations by making deeper cuts to vital services for children, seniors and vulnerable adults. Instead, the governor proposes closing tax breaks and continuing tax rates set to expire June 30 — a 0.3 percent business and occupation tax surcharge paid by doctors, lawyers, accountants and other professionals, and a 50-cent-per gallon beer tax.

"Today, I choose education over tax breaks. I choose fulfilling our constitutional and moral duty to ensure high-quality schools for our children," Inslee said. "When we give these tax breaks a hard look, they just don't measure up to our urgent need to better fund education."

The governor's budget priorities also:

- Promote policies and opportunities to grow jobs
- Step up efforts on Lean management so state agencies operate more effectively and efficiently, within available resources
- Protect vital services to seniors, children and disabled individuals, and improve access to health care through expansion of Medicaid
- Reinvest in Washington's quality of life with renewed investments in state parks

"I believe I have laid out a plan that takes a big step toward making sure every child receives an excellent education and that every worker has the skills he or she needs to succeed in today's economy."

Inslee's proposal also addresses a projected budget shortfall totaling more than $2 billion over the next two years and leaves more than $500 million in reserves.

# # #

Working Washington: Budget Priorities 2013–15

"Our number one priority is revitalizing Washington's economy and building a 21st century workforce. To do that, we must start with a strong commitment to education — and we must ensure that our investments get results."

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Message from the Governor

Our state has been tested these past few years by an economic storm of historic proportions. But we are emerging from the recession, and I believe we now have an opportunity before us to rebuild our economy so it is more diverse and resilient than ever. As governor, I will do everything in my power to seize this moment.

Our number one priority is revitalizing Washington's economy and building a 21st century workforce. To do that, we must start with a strong commitment to education — and we must ensure that our investments get results. That is the driving principle behind my Working Washington Agenda, which lays out my vision for revitalizing our economy and creating jobs.

At a time when the state is failing to meet its obligations to education, these investments include important accountability measures so we can be sure your dollars are being spent wisely.

Today, I am putting forward my priorities for the 2013–15 budget — priorities that I believe take a big step to ensure that every child receives an excellent education and every worker gains the skills he or she needs to succeed in today's economy. At a time when the state is failing to meet its obligations to education, these investments include important accountability measures so we can be sure your dollars are being spent wisely.

My budget priorities also protect our most vulnerable citizens and make strategic investments in clean energy research and development as well as key industry sectors such as aerospace and agriculture. Another key priority is to significantly expand state government's performance management work so we deliver better services while we make the most of every tax dollar.

I recognize that others may have different priorities. But as we construct a budget for the next two years, we must take a broader and more critical view than we have in the past. It's time to start giving tax exemptions and loopholes the same level of scrutiny we've given the rest of the state budget. And I believe it is time to end tax breaks that simply do not outweigh Washington's urgent need to better fund education.

In this document you will find the details of investments I believe need to be made now to help us rebuild the economy and take steps to adequately fund education.

Budget Priorities for a Working Washington

A commitment to education, rebuilding our economy

Washington's economy continues to recover from the worst recession in modern times. But we are bouncing back at a far slower pace than we did from previous recessions. Too many businesses are still struggling and too many people remain out of work. While there are encouraging signs, consumer confidence still lags well below pre-recession levels and state revenue growth remains sluggish.

Governor Inslee is committed to getting Washington back on its feet and back to work. A key part of his strategy is a budget focused on rebuilding the state's economy and meeting our education obligations while preserving essential services. This document outlines the Governor's budget priorities.

When Governor Inslee took office in January, the state was facing a projected budget shortfall — the difference between the cost of all current obligations and anticipated revenue — totaling nearly $1 billion for the next biennium (2013–15). Over the past two weeks, that projection has grown to more than $1.2 billion. On top of that basic shortfall, the state will need to spend at least $1 billion over the next two years to begin meeting its basic education responsibilities and complying with the state Supreme Court's McCleary decision.

Governor Inslee believes we must take a bold and balanced approach in addressing our $2 billion-plus budget challenge. First and foremost, the Inslee administration is committed to building and sustaining a thriving economy that spurs job growth in every industry sector and every corner of the state. That is why his top budget priority is his "Working Washington Agenda," which makes important investments in education — the foundation of a strong economy — and strategic investments to create jobs.

A key part of Governor Inslee's Working Washington strategy is a budget focused on rebuilding the state's economy, meeting our education obligations and preserving essential services.

The Governor's budget priorities hold the line on most state agency spending, adding enhancements only to protect the most vulnerable, ensure public safety and address shortfalls in a few critical areas. He is stepping up the state's efforts on Lean management so state agencies provide services more effectively and efficiently, within available resources.

The Governor is not proposing any new taxes, and instead proposes closing certain tax breaks and extending tax rates already in place. His plan would leave healthy reserves totaling more than $500 million.

Meeting obligations with targeted investments, accountability

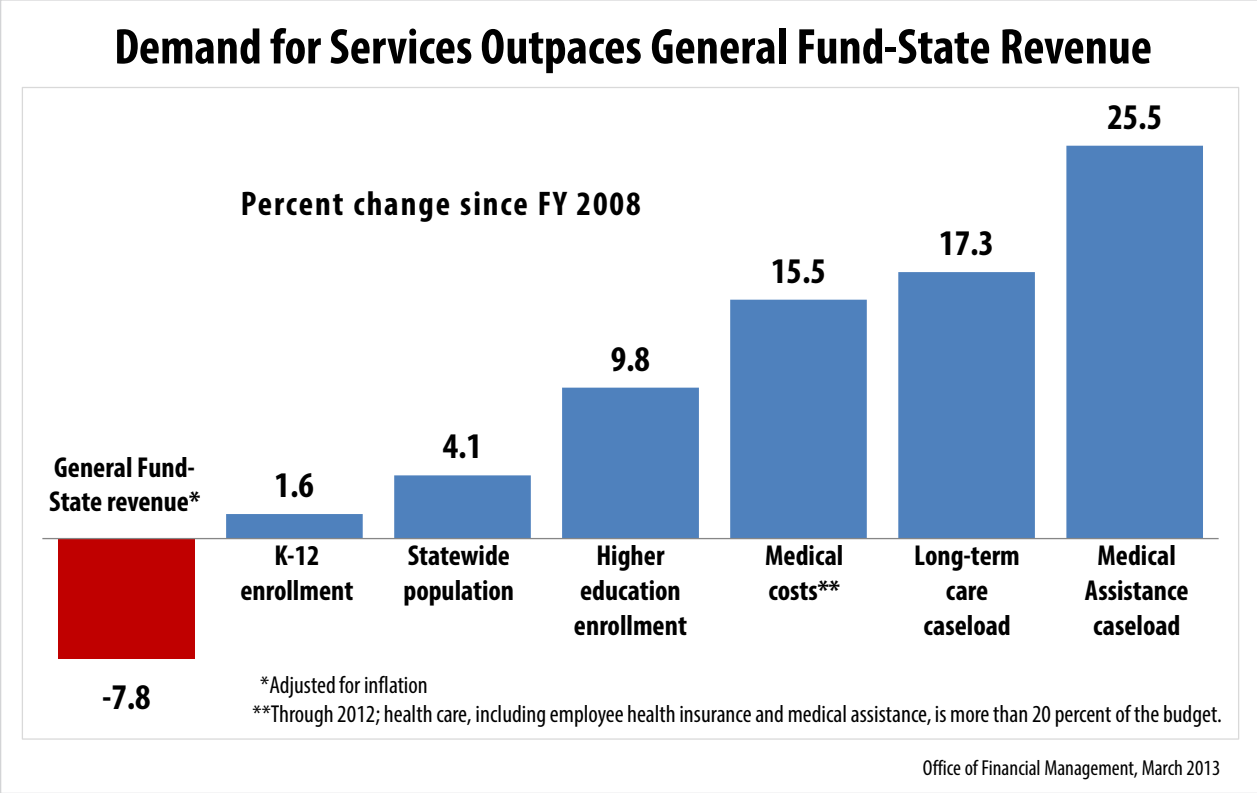
The state Supreme Court has made a clear statement: Washington is not living up to its constitutional obligation to adequately fund basic education. Meeting those obligations will require significant new funding over the next six years.

Governor Inslee is proposing a $1.2 billion "down payment" in the 2013–15 biennium to begin meeting the state's basic education responsibilities. Besides providing more support for basic school operations, his plan includes funding for full-day kindergarten expansion and

reducing kindergarten and first grade class sizes, early reading intervention, dropout prevention programs and more professional development opportunities for educators. Outside of the definition of basic education, the Governor also proposes adding $35 million to expand preschool opportunities.

The Governor's Working Washington Agenda includes a broad range of proposals to improve the state's business climate, educate a 21st century workforce, advance Washington's leadership in aerospace and promote clean energy development. To achieve these, the Governor's proposal promotes tax relief for new businesses in high-growth sectors and additional funding for STEM (science, technology, engineering and math) and aerospace training opportunities in our secondary and higher education systems.

The Governor proposes investments in a few critical areas, such as adding child and adult protective services caseworkers. His plan funds collective bargaining agreements that don't include any general wage increases. The 3 percent pay cuts most state employees took in the current biennium are restored. And he believes the state must step up to address critical funding shortfalls, including those in our parks system and the College Bound Scholarship program.



Finding savings after years of cutting

According to the latest forecast, state revenue collections are just now returning to fiscal year 2008 levels. But by next year, our budget will be serving a state population that will have grown by 350,000 since 2008.

Demand for state services has also continued to mount. For example, compared to 2008, we have today 235,000 more people on medical assistance, 16,400 more K-12 students and nearly 8,800 more people receiving state-supported, long-term care services.

While the number of people state government serves continued to rise during the Great Recession, the state cut existing and projected spending by more than $11 billion. Since 2008, the state:

- Made deep cuts to our social safety net, including the Basic Health Plan and Disability Lifeline program.
- Sharply reduced General Fund support for higher education, increasing the burden on students and their families. Tuition has risen nearly 60 percent at our baccalaureate institutions and more than 30 percent at our community and technical colleges.
- Shrank the general government workforce by more than 12 percent, to fewer than 60,000 employees, and cut employee take-home pay.

Given the reductions that have already taken place — and the fact that roughly two-thirds of the state General Fund budget is protected by constitutional, contractual and federal requirements — there are few places left to turn to for big savings.

Under Governor Inslee's budget priorities, the state will save $321 million by again suspending the teacher cost-of-living raises required under Initiative 732. And the Governor is fully embracing Medicaid expansion, which will save the state nearly $300 million as the federal government picks up the full cost of covering an estimated 255,000 adults newly eligible for health care.

A sharp focus on better management of state government

Governor Inslee has honed a clear vision of how his team will manage state government transparently, efficiently and effectively on behalf of Washingtonians. Whether the work is to protect children, license caregivers, issue licenses or build roads — all core responsibilities of state government — the Governor holds his Cabinet and agency leadership responsible for achieving results that the taxpayers deserve and to which he is committed.

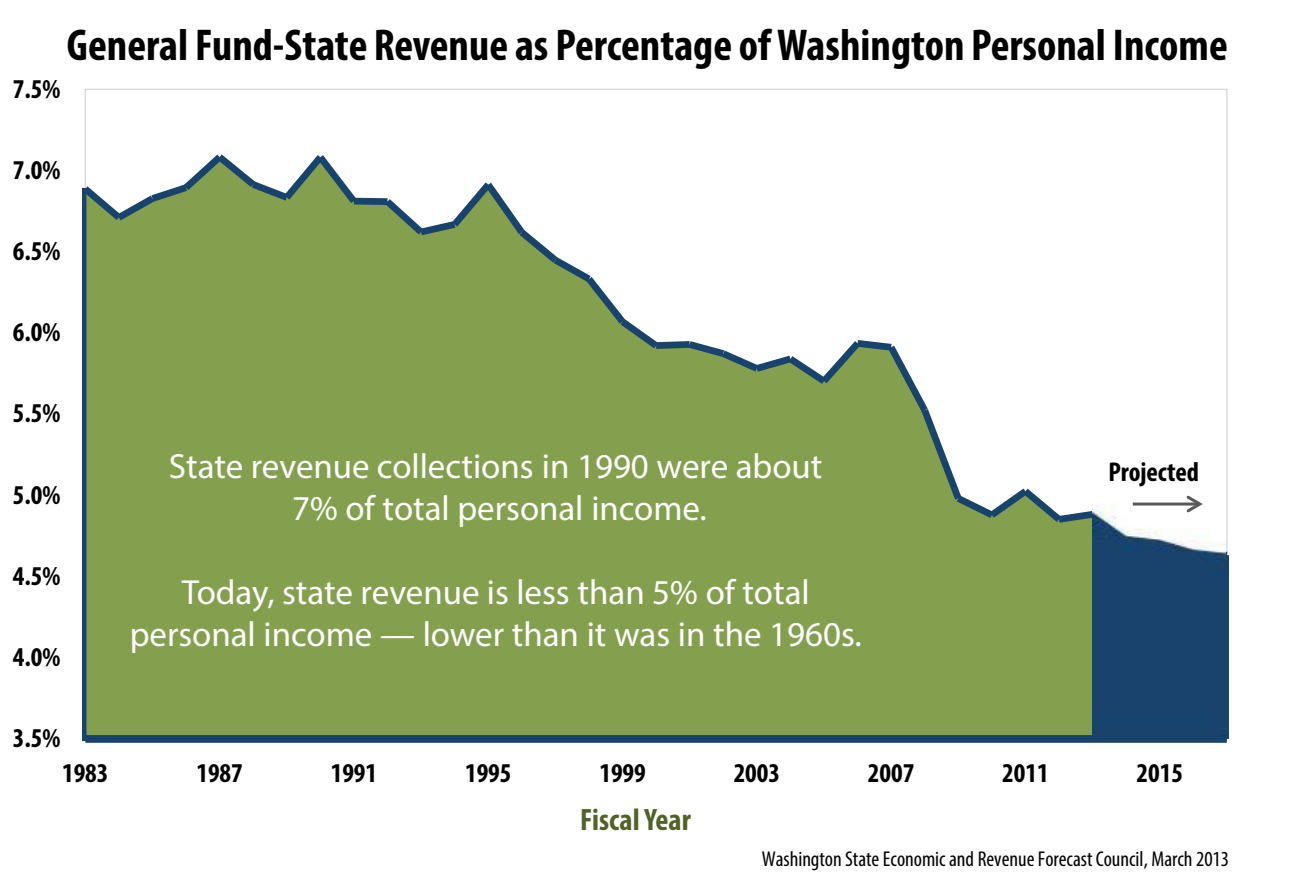
This includes their collaborative, dedicated efforts to develop and maintain a culture that makes continuous improvement a habitual behavior that extends through the employee front lines to management to leadership.

The Governor proposes to build on successes achieved through such tools as Washington's Government Management Accountability and Performance program. Its successes include quicker responses to allegations of child abuse and shorter wait times for a driver's license. Another tool is Lean, a continuous improvement strategy developed in private industry and already test-driven in our state with the help of loaned private-sector executives.

These and other strategies will form the backbone of a new initiative to boost the quality and efficiency of state programs, especially in the priority areas of the economy, education, health care and government reform. As a result, state government will operate more openly to the public with more efficiency and at greater value.

A Lean fellowship program will be developed through the loaning of staff members from agencies for up to a year to support a select group of early adopter agencies. These practitioners will receive training from Lean experts so they support enterprise-wide improvement. Each practitioner will then be expected to offer process-improvement workshops with targets for boosting quality, shrinking delays and saving money. Practitioners will return to their agencies and lead efforts there to sustain a continuous improvement process.

Revenue



Closing tax breaks to fund education and meet other obligations

Washington's fragile economic situation requires a thoughtful, strategic and focused approach to funding education and other budget obligations. Governor Inslee does not believe this is the time for general tax increases. And he has stressed that we will not meet our education funding responsibilities by making deeper cuts to other vital services for children, seniors and vulnerable adults.

Instead, Governor Inslee is putting forward a funding solution that will meet our basic education needs while minimizing the impact on our economy. First, he proposes eliminating tax breaks that have either proven to be ineffective at improving economic outcomes or whose benefits simply do not outweigh the needs of our students. Second, he proposes extending tax rates that are already in place.

Almost $1.2 billion of the new revenue will be dedicated to the Education Legacy Trust Account to make significant improvements in education.

Many tax breaks serve an obvious benefit. For example, the voter-approved sales tax exemption on food is estimated to save consumers more than $2.7 billion in state and local taxes during the current biennium. But many other tax breaks are harder to justify, especially when weighed against educating children.

The Joint Legislative Audit and Review Committee has recommended several dozen exemptions be given additional scrutiny, terminated or allowed to expire. But the Legislature has acted on very few of those recommendations, and many more tax breaks have yet to be reviewed by the committee.

Governor Inslee's budget office worked with the Department of Revenue to review dozens of tax breaks. Based on that review, the Governor is proposing eliminating or modifying a dozen tax breaks worth more than $500 million in the 2013–15 biennium.

In addition, the Governor proposes trimming the break that many industries get on their business and occupation (B&O) tax rates. The state's B&O tax code now includes preferential tax rates that benefit about 40 industries, from the manufacturers of certain agricultural products to travel agencies and international investment management. Industries with a preferential rate do not pay the same B&O tax rate other businesses pay for their specific classification.

Many of these preferential rates have been enacted in the past 15 years, often without any specific, measurable public policy objectives. For example, income from royalties, which is classified as a service, would normally require payment of the standard service B&O tax rate of 1.5 percent, but instead requires payment of a much lower rate of 0.484 percent.

The Governor proposes to reduce the value of these special tax rates by 25 percent for all industries except aerospace and radioactive waste cleanup by the federal government.

The Governor also supports continuing certain tax rates that are set to expire June 30. In 2010, lawmakers approved a 0.3 percent increase to the B&O tax paid by doctors, lawyers, accountants and others, and a 50-cent-per-gallon beer tax. Continuing both — and including small brewers in the beer tax — will yield more than $660 million in the next biennium.

Balance Sheet for 2011–13 and 2013–15 Budgets

Including 2013 Supplemental Budget

General Fund-State, Education Legacy Trust, Opportunity Pathways and Budget Stabilization Accounts

	Dollars in millions	
	2011–13	**2013–15**
Resources		
Beginning fund balance	**(60.4)**	**157.8**
March 2013 revenue forecast	31,006.0	32,865.0
Transfer to Budget Stabilization Account	(267.7)	(307.4)
Other enacted fund transfers	378.6	
Align with financial statements	(5.0)	
Adjustment to working capital (HB 2822)	238.0	
Transfer to Child/Family Reinvestment Account		(5.0)
Governor's proposed budget		
HB 1920 estate tax clarification		160.3
Budget driven revenue/fees/fund transfers	2.0	598.3
Jobs agenda tax credits		(31.1)
Tax breaks repeals/modifications		565.2
Continuation of existing taxes		661.6
Total Resources (including beginning balance)	**31,291.5**	**34,664.7**
Expenditures		
Enacted budget with 2012 supplemental	31,249.2	
Actual reversions in fiscal year 2012	(105.9)	
Assumed reversions in fiscal year 2013	(60.0)	
Subtotal	**31,083.3**	
Governor's Proposed Budget		
Reduced reversion assumption	13.5	
Expenditure changes for 2011–13	36.9	
2013–15 expenditures		34,433.2
Total Expenditures	**31,133.7**	**34,433.2**
Reserves		
Projected ending balance	157.8	231.4
Budget Stabilization Account beginning balance	0.6	268.4
Net transfer/interest earnings	267.8	31.8
Total Reserves	**426.2**	**531.6**

Note: Some totals may not add exactly due to rounding.

Balance Sheet Detail

General Fund-State, Education Legacy Trust, Opportunity Pathways and Budget Stabilization Accounts

Budget-driven revenues, fees, fund transfers	Dollars in millions
Additional Dept. of Revenue tax auditors	9.6
Lottery budget driven revenue	(1.2)
Judicial Stabilization Account fee renewal	9.0
Prohibit delinquent taxpayers from renewing liquor licenses	2.1
Budget Stabilization Account	276.0
Public Works Fund	162.0
Local Toxics Control Account	62.5
Life Sciences Discovery Fund	22.0
State Toxics Control Account	21.6
Treasurer's Service Account	20.0
Waste Reduction, Recycling, Litter Account	11.7
Flood Control Assistance Account	2.0
Financial Services Regulation Account	1.0
Subtotal	**598.3**
Jobs agenda tax credits	Dollars in millions
Tradable research and development tax credits	(15.0)
Tax credits to businesses hiring veterans (SB 5812)	(10.0)
New businesses in high-growth areas (HB 1693)	(4.0)
Aviation services sector (HB 1707/SB 5622)	(2.1)
Subtotal	**(31.1)**
Tax break repeals/modifications	Dollars in millions
Limit trade-in exemption to first $10,000 of value	94.8
Repeal sales tax exemption for local residential telephone service (HB 1971)	83.2
Extend sales tax to custom computer software	78.5
Trim preferential B&O rates for most industries by 25%	66.2
Repeal sales tax exemption for non-residents	63.7
Repeal sales tax exemption on bottled water	51.5
Repeal use tax exemption for extracted fuel, except hog fuel	40.8
Eliminate preferential tax rate for resellers of prescription drugs	29.0
Repeal B&O tax exemption for long-term rental of commercial real estate	27.8
Narrow tax exemption for import commerce	24.1
Repeal sales tax exemption for farm auction purchases	5.6
Subtotal	**565.2**
Extended revenues	Dollars in millions
0.3% B&O tax surcharge	534.0
50 cent beer tax, including small brewers	127.6
Subtotal	**661.6**

Education

Building a new foundation for excellent schools

For too long, Washington has failed to provide adequate funding for its public schools. This issue has been debated in the Legislature and the courts for decades. Governor Inslee proposes a new approach for meeting and targeting our basic education funding needs: close tax breaks and tap existing revenue sources to provide a funding foundation, and focus new spending where it's needed most, with strong accountability to ensure our investments yield strong outcomes. With new state funding comes an obligation to use resources effectively to improve student learning. Districts that do not meet specified expectations will be required to implement research-proven best practices.

The state constitution requires the Legislature to define and fund a program of education that serves all children in the state. In the 1970s, the state Supreme Court ruled that Washington had not met its constitutional obligation to fund schools. Decades later, in last year's McCleary v. State decision, the court reaffirmed that the state is again not meeting its education funding obligation. While important, the ruling confirms we must do better for our students in both funding and results. While it is true that insufficient resources diminish the effectiveness of our schools, taxpayer resources are limited and new funding for schools must result in better student outcomes.

Washington's graduation rate of 77 percent is unacceptable. We have large achievement gaps between low-income and higher-income students throughout the kindergarten-through-12th grade system and in all academic subjects. Our students face unacceptable and persistent opportunity gaps based on race and ethnicity. More troubling is the fact that these achievement and opportunity gaps are not narrowing. We have significant room for improvement in our schools, and we owe it to our children to make those improvements — their careers and lives depend on it. And there's more at stake: Washington's economy is dependent on a better-educated and more skilled workforce.

In 2009 and 2010, the Legislature made sizable new statutory commitments to increase school funding over the next six years. Estimates of the cost to fully meet these commitments over the next three biennia vary from $3.2 billion to more than $4.5 billion per biennium. Regardless,

Early learning

Budget priority: Giving our youngest citizens a great start in the classroom to ensure future education and economic success

Expand preschool opportunities. The state's **Early Childhood Education and Assistance Program** (ECEAP) supplements the federal Head Start program in providing preschool for low-income 3- and 4-year-old children. Research is clear that for many children, access to high-quality early learning programs improves kindergarten readiness, success in school, graduation rates and outcomes in adult life. Together, however, Head Start and ECEAP serve just two-thirds of the state's eligible preschool population.

The proposal gives access to 3,035 more eligible children and includes quality improvements such as more class time for preschoolers, educator professional development and site visits. *($35.0 million)*

Targeted investments to meet Washington's education needs

Priorities	Actions
Invest in early learning *$279.2 million*	√ Expand preschool opportunities for children in poverty *($35.0M)** √ Expand full-day kindergarten to all high-poverty schools *($116.2M)* √ Reduce class sizes from 24 to 20 for kindergarten & 1st grade for all high-poverty schools *($128.0M)*
Reduce dropouts *$59.7 million*	√ Ensure 3rd grade literacy *($12.5M)* √ Provide support for students exiting the bilingual program *($21.9M)* √ Use evidence-based practices for schools not meeting 3rd grade literacy targets √ Offer additional supports for students in pivotal years: 6th–9th grade *($25.3M)* √ Use evidence-based practices for districts with high dropout rates
Increase courses in middle and high school *$97.7 million*	√ Increase secondary course offerings by hiring 1,400 new teachers
Improve instruction and leadership *$132.0 million*	√ Provide principal and teacher professional development time for the school year — 1 hour every other week. State sets topic. *($90.4M)* √ Support new teachers with additional time and mentoring *($37.5M)* √ Offer pilot of yearlong principal residency program, starting in 2014–15 school year *($4.1M)**
Ensure strong outcomes *$23.4 million*	√ Fund school turnaround programs *($12.5M)** √ Design statewide strategy to improve STEM education *($10.9M)**
Fund basic operations *$664.3 million*	√ Fully fund new transportation formula in 2013–14 school year *($197.5M)* √ Fully fund utilities, insurance & professional development in Materials, Supplies and Operating Costs formula *($466.8M)*
Total 2013–15 *$1.26 billion*	**Indicates outside the definition of basic education*

substantial, smart funding increases for K-12 schools during the next two years are critical to building the foundation for future investments and innovations to improve education outcomes.

The Governor proposes to build that foundation with $1.3 billion in targeted new investments, which will be paid for by extending tax rates and closing tax exemptions that cannot be justified in the face of our pressing education needs.

A strong start in the elementary grades

The proposal offers two investments for our young learners to give them a solid start on their education path:

» Reduce **sizes of kindergarten and first-grade classes** from 24 to 20 students in all high-poverty elementary schools. Smaller classes in these grades will extend the advantages of early learning and full-day kindergarten programs, especially for students with greater needs; half the state's kindergarteners and first graders will benefit. An additional 900 teachers will be funded to serve these students. *($128.0 million)*

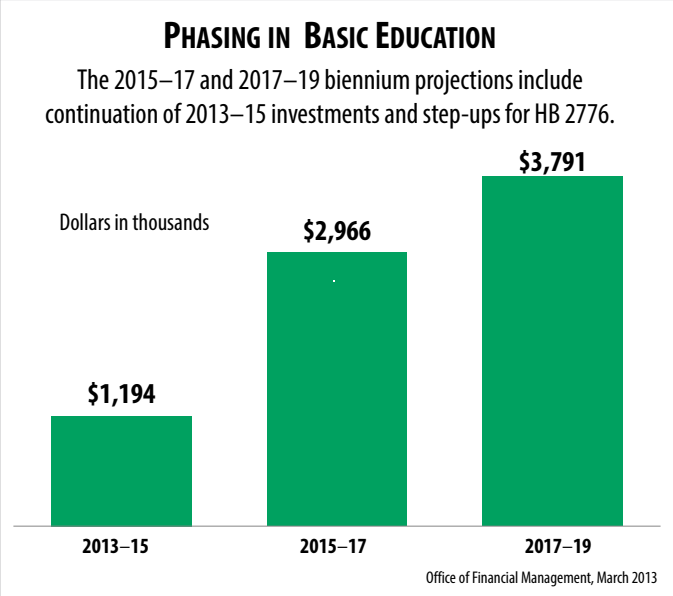
» Provide **full-day kindergarten classes** at all high-poverty elementary schools during the 2013–15 biennium. This enhancement also builds on the Governor's expansion of preschool programs. An additional 288 schools will receive funding to serve 11,500 more kindergarteners. An additional 650 teachers will also be funded. *($116.2 million)*

High-quality instruction and leadership

Having a highly qualified, skilled teacher is the most important school-based factor in student achievement. Teachers need principals with strong leadership skills. Governor Inslee proposes two investments in basic education to support high-quality instruction and a pilot program, which is outside the definition of basic education, to test a new principal residency model:

» Provide for one hour of **professional development time,** set by the state, every other week outside of regular classroom instruction time. A new state funding formula will give teachers and principals an additional 1.25 percent of the state's salary allocation. Across the state, teachers and principals are already embracing the new professional evaluation system and changes in standards-based instruction. For the 2013–15 biennium, the statewide focus will be successfully implementing the new teacher and principal evaluation program. This will allow principals and teachers to collaborate on improving their practices, make changes in the classroom and monitor improvement. *($90.4 million)*

» Fund the **Beginning Educator Support Team** (BEST) approach for all teachers in their first three years on the job. About 2,000 first-year teachers are hired in Washington each year, and as the state emerges from the recession, our schools will be hiring more. Research shows students of well-supported first-year teachers demonstrate achievement gains equivalent to the students of fourth-year veterans. BEST supports new teachers by including additional paid time for weekly meetings with mentors and more opportunities for peer observation and feedback on teaching. Mentor teachers will receive compensation for taking on this important leadership role. *($37.5 million)*



◆ Element of Governor's Working Washington plan to create jobs

All funds General Fund-State unless otherwise noted.

» Offer the **Principal Residency Program.** Because schools need excellent principals, the proposal includes piloting a new model for principal training. This yearlong residency program would match 50 principal candidates with 50 veteran principals for a job shadow. Principals who apply to the Office of Superintendent of Public Instruction (OSPI) to serve as a mentor principal must have earned a high ranking on the new evaluation system. Candidates will be screened and matched with a mentor principal in their region. Starting with the 2014–15 school year, OSPI will support the cost of the resident principal by providing the state's allocation for salary, fringe benefits and health care. *($4.1 million)*

Dropout prevention: Identification, assistance and interventions

It's past time to meet our state's dropout problem head on. The data tell us that students who are not reading proficiently by third grade are four times more likely than their peers to leave school without a diploma. Last year, 31 percent of Washington's third graders did not meet the standard for reading. By looking at absence rates, behavior issues and academic struggles, students as early as grades six through nine can be identified as being at risk of dropping out. The proposal includes three additional supports to boost student achievement and prevent students from dropping out:

» **Ensure third-grade literacy.** Districts will receive a larger allocation for the Learning Assistance Program, which offers extra instructional help to struggling students, based on the prior year's count of students who did not meet state standard for third grade literacy. Districts will implement literacy activities that work best in their own communities. *($12.5 million)*

We will identify schools where fewer than 60 percent of students meet the state third-grade literacy standard, with measures adjusted for students learning English in the Transitional Bilingual Instruction Program, and with the 2012–13 school year serving as the baseline measure. Starting with the 2014–15 school year, schools identified as not meeting the literacy requirement will be required to implement evidenced-based, K-3 literacy instruction strategies with their state basic education funds.

» Close the **achievement gap** with supplemental instruction for students who have recently demonstrated English language proficiency. Data show there is a gap between the state standard for reading and the state standard for demonstrating English proficiency in the bilingual program. Districts will receive additional funds to provide instructional support for students for two years after they exit the Transitional Bilingual Instruction Program. *($21.9 million)*

Research shows it takes four to seven years for students to learn English at a level that enables them to succeed in school. Across the state, more than 19 percent of bilingual students have been in bilingual programs for more than five years. Districts in which the average student time to gain proficiency is more than five years will be required to implement research-based bilingual instruction strategies.

» Prevent students in grades six through nine from **dropping out.** Though districts are able to identify students in these grades who are at risk of dropping out, they need more resources to support them and keep them engaged. School districts will receive additional learning assistance funding based on 15 percent of students in grades six through nine. This money can be used for academic liaisons, tutoring or small-group instruction. Supports will help students who are behind academically to catch up, including those who need additional instructional assistance due to suspensions or expulsions. Again, districts will tailor these research-proven support strategies so they offer the most effective ones to meet their students' needs. *($25.3 million)*

OSPI currently calculates a district's dropout rate, which consists of students who started in ninth grade and who within four years no longer participate in an education program and do not

graduate. Starting with the 2014–15 school year, a district identified as having a four-year dropout rate of more than 14 percent will implement evidenced-based dropout prevention and re-entry programs. School districts with fewer than 20 ninth-grade students will be excluded.

Ensure strong outcomes

» Fund school **turnaround programs**. The state will provide funding for school turnaround programs for the lowest-performing schools in the state as identified through the required action district process, which is built on a partnership among the State Board of Education, OSPI and local school districts. *($12.5 million)*

» In the past 10 years, science, technology, engineering and math (STEM) jobs have grown three times faster than non-STEM jobs. Skills learned through STEM education are essential in a wide range of employment fields. Governor Inslee's proposal creates the **STEM Education Innovation Alliance** to implement a bold, results-driven approach to align the work of state agencies and resources with a comprehensive preschool-through-graduate school strategy to improve the quality of STEM education. The Alliance's membership of business, labor, nonprofit and education organization partnerships is dedicated to help accomplish the state's education goals. The proposal also calls for building a talent pipeline from high school to college, and then career, by expanding industry-developed high school skills programs and allowing credits earned in high school to transfer to college. *($10.9 million)*

Middle and high school courses

The Legislature has committed to increasing learning time for the state's middle and high school students by the 2017–18 school year. Our students need the learning and skills growth benefits of more instructional time sooner. Offering more courses will lead to improved learning and skills development, which will enrich the education experience and make students more attractive to employers.

» Hire 1,400 **additional middle and high school teachers** to extend student learning time. Average instructional hour offerings will increase from 1,000 to 1,080 hours per year, starting in the 2014–15 school year. *($97.7 million)*

Basic operations

Some of the need for improved state funding for schools is truly basic — state school funding formulas provide insufficient resources today for basics such as heating, lighting, insurance and supplies, and for operating costs such as buses to transport children to and from school.

Part of the down payment this biennium must include such funding:

» Increase funds for the **MSOC formula** to keep the lights on. Starting with the 2013–14 school year, the proposal improves funding of the formula called MSOC, for materials, supplies and operating costs. The change will provide 100 percent of the formula enhancements for the utilities, insurance, professional development and school security components of the state funding commitment. This change is equivalent to an average annual increase of $241 per student above maintenance level. *($466.8 million)*

» **Fully fund pupil transportation.** Multiple studies have called for reforms to how the state funds student transportation. The proposal funds 100 percent of the new pupil transportation funding formula, beginning next school year, one year ahead of the schedule set forth in House Bill 2776. Districts will receive state allocations as provided under OSPI's expected cost model, which is based on statistical analysis of all 295 school districts to determine each district's expected cost of operations. *($197.5 million)*

Higher education

Tuition

Tuition will remain at 2013 levels for the next two years at the community and technical colleges as they serve thousands of students who need high-quality job training and academic instruction. Tuition growth of up to 3 percent each year at the regional universities (Eastern Washington, Central Washington, Western Washington universities and The Evergreen State College) will allow them to serve their higher enrollments and support student services. Greater, but still limited, tuition growth of up to 5 percent per year at the research universities (University of Washington and Washington State University) will help preserve and enhance their research and instruction mission, which allows them to foster new industry growth and to prepare leaders and employees for the new economy.

Decisions on tuition levels are made by the regents or trustees of the individual universities and the State Board for Community and Technical Colleges. Should a board of regents or trustees approve tuition at a rate higher than proposed in the state budget, the institution is responsible for providing increased financial aid.

Investments

STEM enrollment pool

Budget priority: Increasing the supply of qualified engineers and getting more Washington students to fill high-tech job vacancies

» Create a competitive **enrollment pool for the public four-year universities.** This will help industry fill positions with qualified employees, especially those in STEM fields. Winning proposals must demonstrate innovation and cost efficiency. Such new investment allows us to grow the workforce that our economy needs. *($11.0 million)* ◆

» Create an **enrollment pool for the community and technical colleges**. This will help them graduate students ready to work for STEM, aerospace and other manufacturing firms that need employees for the new economy. *($5.0 million)* ◆

Financial Aid

Budget priority: Ensuring low-income students have access to Washington's postsecondary education and training system

» Boost funding for **College Bound scholarships** to meet a shortfall. This will fulfill the state's promise of a college education for low-income students who meet certain criteria. This program has energized middle school students who have been preparing for college during high school. The first cohorts are entering college, and funding will allow nearly 4,000 students to pay no tuition at the public institutions. *($35.0 million)*

» Increase award amounts in the **State Need Grant and State Work Study programs** to keep pace with the modest tuition increases proposed in the budget. These increases mean recipients will be shielded from higher costs in the 2013–15 biennium. *($24.7 million)*

Clean Energy Research

Budget priority: Ensuring that the global leaders of the clean energy industry are based in Washington

» Create a **Clean Energy Institute** at the University of Washington to focus on next-generation energy storage and solar energy. Additional staff, advanced computing support and, most importantly, a clear mission will make the institute a global model in this emerging sector. *($12.0 million)* ◆

» Invest in Washington State University's **Center for Bioproducts and Biofuels** in the Tri-Cities to leverage new federal and private grants and scale up its promising efforts. Ramping up research funding will help keep the region at the forefront of alternative and biofuels research. *($5.2 million)* ◆

STEM capacity in the community and technical colleges

Budget priority: Ensuring that communities meet the needs for highly skilled, high-demand workers

» **Expand capacity** in a variety of high-cost programs from aerospace to nursing. More Washington residents need training in industries that are hiring right now. The community and technical colleges need to be flexible and adaptable to local employment trends, but the state needs to step up when the high cost of providing training becomes a barrier to serving students and industry. *($20.0 million)* ◆

Reductions/Savings

Save **$320.5 million** by suspending Initiative 732 cost-of-living salary increases for K-12 and certain higher education employees. The proposal restores salary reductions of 1.9 and 3.0 percent for classified and certificated education employees, and maintains current health benefit contribution rates.

Save **$29.8 million** by limiting state funding for alternative learning experience (ALE) programs in certain cases. In response to recent state audit findings, the state will limit funding of ALE programs to districts predominantly serving their own students, providing online courses solely from state-approved providers and/or demonstrating minimum face-to-face teacher/student contact time for out-of-district students. These reforms will preserve innovative ALE programs while avoiding inappropriate uses of taxpayer dollars.

Save **$21.1 million** by streamlining and improving state-mandated, K-12 student assessments. By implementing new assessments developed through the multi-state Smarter Balance Assessment Consortium, Washington can reduce the cost of elementary and middle school assessments while providing schools with more timely results that teachers can use to inform instruction. In addition, the state will consolidate currently separate 10th grade reading and writing assessments into a single language arts test that saves money and student learning time while meeting state education standards and federal testing requirements.

Other

The Governor supports OSPI as it allocates funds through the School Construction Assistance Grant Program for the reconstruction of Crestline Elementary School in the Evergreen School District in Clark County. The school was destroyed by a January 2013 fire.

Climate, Energy and Natural Resources

Investments

Budget Priority: Taking actions to reduce greenhouse gas emissions and adapt to climate change that create jobs and protect the environment

Provide grants through a revolving fund to not-for-profit lenders able to match the state grant with private capital. Grants will be used to **increase financing for building energy efficiency** as well as for small and medium-scale renewable energy projects. The not-for-profit lenders will make loans to fund projects such as residential and commercial energy retrofits, residential and community-scale solar installations, anaerobic digesters to treat dairy waste, and combined heat and power projects using woody biomass as a fuel source. *($20.0 million capital budget)* ◆

Fund grants to public utilities and entities that will match funds to implement solutions that **manage intermittent renewable and distributed energy.** Winning grants will advance the development of an industry standard for dispatching energy storage resources from utility control rooms and use power management technologies that could lower costs for utility customers. *($20.0 million capital budget)* ◆

Provide matching funds to research institutions such as the University of Washington and Washington State University to make them more attractive as they compete for federal funds to develop **clean energy solutions.** Funds will also support Washington's efforts to compete for federal funding for advanced manufacturing centers. *($10.0 million capital budget)* ◆

Reduce greenhouse gas emissions by tripling the number of miles that can be traveled by **electric vehicles** (from 550 million to more than 1.5 billion miles). Funds will be used to construct 40 to 50 fast-charging (level 3) stations along interstates (82, 90, 205 and 405) and state routes (12, 97, 167 and 518) as well as in key urban areas. These installations would cost approximately $6 million. In addition, $3 million would be used for public and private workplace charging facilities (level 2) at approximately 150 locations statewide. *($9.0 million capital budget)* ◆

Construct 30 **biofuel storage, distribution and fueling facilities** to ensure local and state governments achieve their alternative fuel goals and create jobs (assuming costs of approximately $300,000 per location, with one-third of the cost funded locally). These structures will offer ease of storage and distribution of commercial biofuel blends, especially in proximity to major state ferry and state and local government vehicle refueling centers. *($6.0 million capital budget, $3.0 million matching funds)* ◆

Implement the priority recommendations of the blue-ribbon **Ocean Acidification Panel** to monitor and reduce impacts of acidic water on the state's shellfish industry and native shellfish. *($3.3 million total: $2.0 million State Toxics Control Account; $820,000 Aquatic Lands Enhancement Account; $510,000 Resource Management Cost Account)*

Fund grants and loans to public/private partnerships that offer innovative, effective **biofuel production methods.** This will boost the production of biofuels, shrink dependence on imported fuels and encourage the growth of oilseed farms. Funding will require a minimum of a 1-to-1 local/private match. *($3.0 million capital budget)* ◆

Support the work of the Governor's **Climate Legislative and Executive Work Group** to develop policies and actions to reduce greenhouse gas emissions that meet legislatively established emission limits. *($250,000 supplemental budget; $377,000 biennial budget)*

Budget Priority: Managing and restoring Puget Sound and coastal marine resources

Invest operating budget funds for **restoring and monitoring Puget Sound** in areas such as stormwater management and forest practices implementation. Capital budget funds will support habitat and water quality restoration efforts throughout the basin. Puget Sound is an invaluable natural resource and economic driver for the region. The Governor directs state agencies to continue their efforts to collaborate with the Puget Sound Partnership. Together, they will coordinate state investments with their federal, local and tribal partners to ensure actions taken will produce clean water and better habitat for salmon and shellfish. *($490.4 million total, multiple fund sources: $23.1 million various operating accounts; $461.1 million various capital accounts; $6.2 million transportation)*

Continue **marine spatial planning** on the Washington coast to improve management of the state's coastal resources. *($2.0 million Marine Resources Stewardship Trust Account)*

Budget Priority: Maintaining the state parks system for current and future generations, and preserving lands for farms, outdoor recreation and other purposes

Provide support to the **State Parks and Recreation Commission** for free and discounted passes, work performed by the commission to preserve the state's environmental, historic and cultural heritage, and other essential activities to maintain operations of the state parks system. Revenue from the Discover Pass has not been sufficient to meet these expenses. Without additional funding, up to 60 state parks could be closed year round or seasonally. *($23.7 million)*

Add funding to the **Washington Wildlife and Recreation Program** for such activities as land protection, habitat conservation, farmland preservation and outdoor recreation facilities construction. *($75.5 million capital budget)*

Budget Priority: Supporting local governments and citizens to implement vital environmental programs

Design and construct priority projects to improve the **Yakima River Basin water supply,** including initiation of the purchase of the Teanaway property. This will help restore fisheries and meet agricultural, municipal and domestic water needs. *($45.0 million capital budget)*

Provide training through the Department of Ecology to local governments and developers on using stormwater-reducing, **low-impact development practices** and incorporating them in local land-use ordinances. This funding is in addition to the $109 million in previously approved grants to local governments to implement stormwater permits and capital projects. The Governor directs the Department of Ecology to develop a comprehensive, statewide stormwater financial assistance program to be implemented no later than the 2015–17 biennium for future appropriations. *($2.0 million State Toxics Control Account)*

Provide grants to Thurston and Chelan counties to implement the **Voluntary Stewardship Program** on a pilot basis to protect critical areas while maintaining agricultural production. Additional counties may join the program if federal funds become available. *($546,000 General Fund-State, $1.0 million General Fund-Federal)*

Develop non-lethal options for the Department of Fish and Wildlife to implement the agency's **wolf management plan.** *($300,000 State Wildlife Account)*

Support the creation of a **Model Toxics Control Act Investment Work Group** to develop recommendations on how to invest state

resources most effectively to clean up and reduce toxics in the environment. (complete with existing resources)

Budget Priority: Maintaining the state wildlands for current and future generations

Provide funding to the departments of Natural Resources and Fish and Wildlife, and the State Patrol for **suppression and mobilization costs** for last summer's wildland fires. *($46.0 million supplemental budget)*

Reductions/Savings/Transfers

Fund Centennial Clean Water grants to local governments for wastewater and other clean water projects with state bonds to free up the State and Local Toxics Control accounts for transfer to General Fund-State. *($50.0 million capital budget)*

Shift a portion of Department of Ecology costs from GF-S to the State Toxics Control Account, some on a one-time and some on an ongoing basis, for activities in the air quality, water quality, environmental assessment, shorelands and administration programs. *($29.1 million from GF-S to State Toxics Control Account)*

Reduce funding on a one-time basis for litter prevention and waste reduction programs. *($8.9 million Waste Reduction, Recycling and Litter Control Account)*

Shift funding for programs related to aquatic invasive species, commercial shellfish management, hatchery operations and hydraulic permit approval at the Department of Fish and Wildlife from GF-S to the Aquatic Lands Enhancement Account. *($5.6 million GF-S to Aquatic Lands Enhancement Account)*

Reduce grants and staff at the Department of Ecology for assisting local groups in implementing local watershed plans. Funding is maintained for assistance to groups in the Dungeness, Walla Walla and Wenatchee watersheds, as well as other basins in Eastern Washington. *($2.9 million)*

Human Services, Health and Public Safety

Taking care of our most vulnerable citizens and ensuring public safety are among the most fundamental responsibilities of state government. As we identify funding sources for our public education system, cutting services for individuals with developmental disabilities, those with mental illness and children who are abused or neglected is not acceptable. After earlier rounds of reductions, the Governor proposes modest increases in vital areas.

Investments

Children's Administration

Budget priority: Improving outcomes for children and families in the child welfare system

Offer **Family Assessment Response** (FAR) as an alternative to Child Protective Services. Lower-risk families will receive a comprehensive assessment of child safety, risk of subsequent child abuse or neglect, family strengths and basic needs. *($8.3 million)*

Lower caseloads for **Child Protective Services** workers to reduce response and investigation times. Current caseloads are higher than the recommended level of 15 cases per caseworker. *($5.9 million)*

Developmental Disabilities and Long-Term Care

Budget priority: Protecting the most vulnerable citizens by providing personal care, housing and employment services

Fund interest arbitration award for **individual providers** and parity for **agency providers** who offer personal care services to elderly and disabled clients in their homes. *($146.1 million)*

Serve 219 additional individuals with developmental disabilities graduating from high school by moving 553 state-only employment clients to the **Medicaid waiver** to leverage federal funds. The 106 employment clients who are not now eligible for the Medicaid waiver will still be served with state funds. *($7.0 million in federal funds)*

Reduce **Adult Protective Services** caseloads and improve response and investigation times for vulnerable adults residing in their own homes by adding 22.7 staff. *($3.6 million)*

Add community placements to maintain services for 51 **individuals with developmental disabilities** who are living in state residential settings including foster care placements, mental health institutions, and juvenile rehabilitation and Department of Corrections facilities. *($3.0 million)*

Reduce caseloads for **residential care investigators** who investigate abuse, neglect and financial exploitation of adults in residential settings by adding 20.4 employees. *($1.3 million)*

Economic Services

Budget priority: Providing assistance to vulnerable individuals and families

Use **Temporary Assistance for Needy Families** grant funds to move homeless children and families to stable housing, leveraging housing funds in the Department of Commerce. *($10.0 million)*

Terminate the **disabled grant program** to maximize the refinancing of Medicaid expansion. Services provided through the Essential Needs and Housing Support program in the Department of Commerce will provide housing and other supports, such as transportation vouchers. The aged grant program will continue.

Mental Health

Budget priority: Providing mental health services to those in crisis, promoting client and staff safety in institutions, and treating individuals in appropriate settings

Implement the **Involuntary Treatment Act** sooner to treat individuals at risk to themselves and their communities. *($15.8 million)*

Provide funding to Eastern and Western State hospitals to promote **safety for patients and staff** and continue state mental hospital accreditation. One-time capital improvements will also be made for such items as secondary fencing and metal detectors. *($10.1 million)*

Establish **enhanced service facilities** in the community to provide an alternative placement to a state institution for individuals with dementia or traumatic brain injury. *($1.5 million)*

Health Care Authority

Budget priority: Keeping health care affordable by promoting programs that lead to better health

Fund **adult dental services** for currently eligible Medicaid and newly eligible Medicaid adults as a result of Medicaid expansion. Dental coverage for newly eligible adults will be fully paid by the federal government. *($23.8 million)*

Align **Medicaid plan benefits** for all eligible adults with the 10 essential health benefit categories identified in the Affordable Care Act. Services include physical and occupational therapy, shingles vaccinations and mental health services. *($7.9 million)*

Expand **employee wellness programs** to improve employee health and wellness and reduce the growth in medical costs. *($5.0 million)*

Continue policy of **not requiring cost-sharing** for Medicaid clients.

Department of Corrections

Budget priority: Ensuring the safety of those who work in the state's correctional facilities

Fill 28 critical staff **custody positions** and provide **radio system infrastructure** to improve staff and offender safety in medium- and minimum-security prisons. *($3.5 million)*

Provide funding for ballistic and stab-resistant body armor, security cameras and electronic control systems to open and lock doors to improve **prison staff safety.** *($1.6 million)*

Reductions/Savings

Capture **$296.0 million** in savings through Medicaid expansion. The federal government will cover 100 percent of the health care costs for approximately 255,000 newly eligible, low-income adults. Beginning in state fiscal year 2017, the federal share will decrease to 95 percent and to 90 percent by 2020.

Save **$260.0 million** by continuing the hospital safety net assessment, which was set to expire June 30, 2013.

Capture **$70.0 million** in savings from lower WorkFirst and Working Connections Child Care caseloads. WorkFirst helps low-income Washington parents get back to work.

Save **$36.5 million** by freezing Medicaid nursing home reimbursement rates at fiscal year 2013 levels.

Save **$13.4 million** by eliminating Social Security Income facilitators for disabled childless adults. This function will be shifted to the counties as part of safety net reform.

General Government

Investments

Budget priority: Promoting business development in the state to grow jobs and encouraging tourism

Set up **"MyAccount,"** an integrated, single portal for business interactions with state agencies, to help small businesses move smoothly through the licensing and regulatory process. Operating on Lean principles, MyAccount will let small businesses spend less time worrying about compliance and more time focused on expanding and hiring more employees. MyAccount will come online in three phases over the next four years. *($8.0 million)* ◆

Increase funding to the **Department of Commerce Business Services Division** to expand business recruitment and retention opportunities as well as restore capacity to support trade missions, export assistance and other efforts to create and retain jobs. New business sector leads will be added in fields such as life sciences, military, information/communications technology, clean technology and advanced manufacturing. In addition, the state will contract for services to market Washington products abroad and attract new investment opportunities to the state. *($5.4 million General Fund-State, $4.0 million Economic Development Strategic Reserve Account-State)* ◆

Boost funding to forge partnerships with the private sector to enhance the economic impact of **tourism** on Washington's economy. In conjunction with the Washington Tourism Alliance, the state will provide bridge funding to make destination information more available to prospective visitors and fund promotional activities in international markets with the goal of attracting more tourists to the state. *($1.8 million)* ◆

Budget priority: Ensuring the safety of Washington's information technology systems and data

Enhance **security services** for state information technology systems and provide delivery of common infrastructure and services through Consolidated Technology Services to state agencies for early warning and responses to security threats. *($10.5 million Data Processing Revolving Account-Nonappropriated)*

Budget priority: Promoting military mission retention and expansion through investments prior to potential Base Realignment and Closure rounds or other Department of Defense budget reduction efforts

Provide funding to the Department of Commerce for **capital improvements** for the following projects: Joint Base Lewis-McChord Center Drive interchange *($2.0 million)*, Kitsap County/Hood Canal Naval Undersea Warfare Center training range encroachments *($2.0 million)*, Puget Sound Naval Shipyard pedestrian tunnel safety improvements *($1.3 million)* and acquisition of land within the encroachment zone at Fairchild Air Force Base *($2.7 million). (total $8.0 million capital budget)*

Budget priority: Ensuring the integrity of the worker's compensation system

Adopt industry benchmark ratios of nurses-to-claim managers at the Department of Labor and Industries to resolve worker's compensation **time-loss claims** in a more timely manner. The goal is to resolve 50 percent or more of time-loss claims in six or fewer months. *($4.1 million Medical Aid Account-State)*

Budget priority: Ensuring public safety

Fund additional **liquor enforcement officers** to address public safety concerns associated with an increase in the number of on- and off-premise liquor licensees, product theft and smuggling,

and underage alcohol consumption. These new officers will educate licensees and conduct investigations and undercover compliance checks. *($2.1 million Liquor Revolving Account-State)*

Budget priority: Ensuring better management of state government

Establish a **Lean fellowship program** to train agency staff in the principles of Lean management to improve the quality and efficiency of state programs. The Government Management Accountability and Performance program will provide training and staff to further this effort. *($2.7 million Performance Audits of Government Account-State)*

Reductions/Savings

Capture **$27.2 million** in savings through lower charges to state agencies for back-office support and information technology support services. The consolidation of five state agencies into the Department of Enterprise Services and Consolidated Technology Services continues to generate savings, about 40 percent of which will benefit the General Fund.

Capture **$3.7 million** in savings through elimination of the STARS (Strategically Targeted Academic Research) team and Entrepreneurs-in-Residence program at the University of Washington and Washington State University.

Save **$3.2 million** from elimination of pass-through grants at the Department of Commerce for Northwest agricultural incubators, global health technology research, microenterprise business support and community mobilization against violence and substance abuse.

Save **$1.5 million** in advertising costs at the Washington State Lottery Commission. An audit by the Joint Legislative Audit and Review Committee found that lottery sales are influenced more by economic conditions and the size of lottery jackpots than by targeted advertising.

Budget Priorities for a Working Washington

- √ Make significant and targeted investments in education to meet our constitutional obligations under the McCleary decision
- √ Step up efforts on Lean management so state agencies operate more effectively and efficiently, within available resources
- √ Close tax breaks whose benefits do not outweigh the needs of our schoolchildren
- √ Promote policies and opportunities to grow jobs
- √ Prepare Washington for a vibrant, thriving economy
- √ Protect vital services to seniors, children and disabled individuals

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Tax Exemption Fact Sheets

Office of Financial Management

March 2013

Limit trade-in exemption to first $10,000 of value

Repeal sales tax exemption for local residential telephone service (HB 1971)

Repeal sales tax exemption for custom computer software

Trim preferential B&O rates for most industries by 25%

Repeal sales tax exemption for non-residents

Repeal sales tax exemption on bottled water

Repeal use tax exemption for extracted fuel, except hog fuel

Eliminate preferential tax rate for resellers of prescription drugs

Repeal B&O tax exemption for long-term rental of commercial real estate

Narrow tax exemption for import commerce

Repeal sales and use tax exemption for farm auction purchases

Limit trade-in exemption to first $10,000 of value

Description

This proposal would limit the exclusion of trade-in value from retail sales and use tax to $10,000 for motor vehicles, recreational vehicles, boats and other items.

Current Law

When a consumer purchases tangible personal property, the measure of sales or use tax excludes the value of like-kind property traded in at the time of sale. Consequently, the trade-in value is deducted from the selling price that is subject to sales tax. (RCW 82.08.010(1) and 82.12.010(1))

Original Purpose and Current Analysis

The trade-in exclusion was approved by voter initiative in 1984 to encourage purchases of new items, especially motor vehicles.

Trade-ins of motor vehicles average $7,500, so limiting deductible trade-in values to $10,000 benefits most households. The current unlimited deduction primarily benefits high-income purchasers with the lowest tax burdens in Washington. Setting a limit would reduce the regressivity of the current tax system.

Citizen Commission Recommendation

The Citizen Commission has not reviewed the trade-in exclusion.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$44.6	$50.2	$94.8	$52.6	$54.3	$106.9

Notes:

- *This proposal impacts an estimated 85,000 taxpayers.*
- *Estimates assume a July 1, 2013, effective date, representing 11 months of collections for FY 2014.*

Repeal the sales tax exemption for local residential telephone service (HB1971)

Description

Repeals the sales tax exemption for local residential telephone service.

Current Law

- Telecommunications services (e.g., wireless, VoIP and landline voice services) are generally subject to state and local retail sales taxes.
- RCW 82.08.0289 exempts local residential telephone service from retail sales tax, but long-distance service is subject to retail sales tax.

Original Purpose and Current Analysis

To relieve the tax burden for the "necessary" portion of telephone service (i.e., local calls by individuals). Enacted in 1983.

The advent of cellular and VoIP phone service has blurred the distinction between local residential telephone service and long-distance service subject to the sales tax. The Department of Revenue has held that only traditional landline local service qualifies for the exemption because neither cellular nor VoIP phone service operates under tariffs regulated by the Utilities and Transportation Commission. The department's interpretation is currently subject to court challenge, and a court win could have a large negative financial impact on the state if a court decision extends the exemption to wireless and cable providers. The simplest solution would be to eliminate the deduction as outmoded, given the technological changes over the past 30 years.

Citizen Commission Recommendation

The Citizen Commission has not reviewed this item.

Revenue Impact

General Fund impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$39.8	$43.4	$83.2	$43.4	$43.4	$86.8

- *This proposal impacts an estimated 100 taxpayers.*
- *Estimates assume a July 1, 2013 effective date, resulting in 11 months of collections for FY 2014.*

Repeal sales tax exemption for custom computer software

Description

Tax and exemption
This proposal would repeal the sales tax exemption on the service of creating custom software. The following would continue to be exempt:

- Custom software services purchased for resale,
- Custom software services consumed as a component of a new product produced for sale. "Product" means tangible personal property, digital products, remote access software or both pre-written and custom software.

Use tax
Custom software used by the purchaser, except as a component of a new product for resale, would be subject to use tax.

Royalties
Treatment of software licenses taxed under the royalties classification would be the same for custom software as for prewritten software.

Current Law

Custom computer software services are not subject to sales or use tax. Providers of these services are taxable under the service classification of the business and occupation tax, currently 1.8% of gross income.

Original Purpose and Current Analysis

To reflect the fact that producing customized software was considered to be a service.

In today's economy, the distinction between custom software and standard prewritten software has become much more indistinct. Repealing the sales tax exemption would reduce the B&O tax rate to the retailing rate of 0.471%.

Citizen Commission Recommendation

The Citizen Commission has not reviewed this tax preference.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$36.8	$41.7	$78.5	$46.1	$51.0	$97.1

- *This proposal will impact an estimated 3,300 taxpayers.*
- *Estimates assume a July 1, 2013, effective date, representing 11 months of collections for FY 2014.*

Trim preferential B&O tax rates for most industries by 25%

Description

This proposal would reduce the value of preferential B&O tax rates for all industries except aerospace and radioactive waste cleanup by the federal government.

Current Law

The state's B&O tax code now includes preferential tax rates that benefit about 40 industries, from the manufacturers of certain agricultural products to travel agencies and international investment management. Industries with a preferential rate do not pay the standard B&O tax rate for their specific classification.

Many of these preferential rates have been enacted in the past 15 years, often without any specific, measurable public policy objectives. For example, income from royalties, which is classified as a service, would normally require payment of the standard service B&O tax rate of 1.5 percent, but instead requires payment of a much lower rate of 0.484 percent.

Citizen Commission Recommendations

The Citizen Commission for Performance Measurement of Tax Preferences recently recommended terminating the preferential B&O tax rate for several industries due to a lack of evidence that the tax preference is achieving any specific public policy objective.

Revenue Impact

General Fund impacts *($ millions)*:

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$30.9	$35.3	$66.2	$43.9	$46.4	$90.3

- *This proposal impacts an estimated 7,524 taxpayers.*
- *Estimate assumes a July 1, 2013 effective date, representing 11 months of collections for FY 2014.*

Repeal sales tax exemption for non-residents

Description

This proposal would repeal the nonresident sales tax exemption.

Current Law

Under RCW 82.08.0273, bona fide residents of a state, U.S. possession or territory, or province of Canada that does not impose a sales tax or similar consumer tax of 3% or more, may purchase tangible personal property for use outside this state without paying Washington's sales tax.

The seller is not required to make a tax-free sale to a nonresident, but if the seller does:

- The purchaser must provide proof of exemption to the seller, and
- The seller must retain a record of the proof.

Original Purpose and Current Analysis

To enable Washington sellers, especially those along the Oregon border, to compete with merchants in other states that either do not levy a retail sales tax or levy a sales tax with a low rate. Enacted in 1965.

No other state has seen the need to provide similar preferential treatment to nonresidents.

Citizen Commission Recommendation

The Citizen Commission recommended that the Legislature review and clarify the exemption.

Revenue Impact

General Fund impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$29.8	$33.9	$63.7	$35.3	$36.7	$72.0

- *This proposal impacts an estimated 4,436 taxpayers.*
- *Estimates assume a July 1, 2013, effective date, resulting in 11 months of collections for FY 2014.*

Repeal sales tax exemption on bottled water

Description

This proposal would repeal the sales tax exemption on sales of bottled water to consumers. The tax would apply to both portable-sized bottles *and* to bulk bottled water sales (sales of water in large, reusable containers).

Current Law

Under current law, sales tax does not apply to retail sales of bottled water.

- Until Jan. 1, 2004, sales of bottled water were subject to sales tax.
  - At that time, legislation to conform to the Streamlined Sales and Use Tax Agreement (SSUTA) took effect and sales of bottled water became exempt from sales tax.
  - In 2010, the SSUTA was amended to allow member states to separately tax bottled water sales.
- In 2010, Senate Bill 6143 imposed sales tax on sales of bottled water beginning July 1, 2010, until Dec. 2, 2010, when the sales tax on bottled water was repealed by Initiative 1107.

Original Purpose and Current Analysis

To conform to definitions of SSUTA. However, SSUTA has been amended to allow taxation of bottled water.

Citizen Commission Recommendation

Not reviewed by Citizen Commission.

Revenue Impact

General Fund impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$24.4	$27.1	$51.5	$27.5	$27.9	$55.4

- *This proposal impacts an estimated 195,000 taxpayers.*
- *Estimates assume a July 1, 2013, effective date, resulting in 11 months of collections for FY 2014.*

Repeal use tax exemption for extracted fuel, except hog fuel

Description

This proposal would limit the use tax exemption for fuel produced by the extractor or manufacturer when the fuel is directly used in the same extracting or manufacturing operation that produced the fuel. Only wood byproducts, also referred to as "hog fuel," would be eligible for the exemption.

Current Law

Fuel consumed by manufacturers or extractors is exempt from use tax when the fuel is used in the process of manufacturing or extracting at the same plant.

- The fuels for which the exemption applies are generally wood byproducts, also referred to as "hog fuel," and refinery fuel.
- Approximately 180 wood product manufacturers and 5 petroleum products refineries are eligible for the exemption.
- In its preliminary 2011 Tax Preference Review Report, the Joint Legislative Audit and Review Committee notes that while no refineries existed in the state when the exemption was enacted in 1949, refinery fuels account for approximately 98% of the estimated value of the exemption.

Original Purpose and Current Analysis

To support the fuel manufacturing and extracting industry.

However, the biggest beneficiaries of this exemption are oil refineries that did not even exist when this statute was originally enacted. Other industries pay tax when they use materials that they manufacture themselves.

Citizen Commission Recommendation

The Citizen Commission recommended that the Legislature review and clarify because the public policy objective and intended beneficiaries are not clear.

Revenue Impact

General Fund impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$20.1	$20.7	$40.8	$20.3	$22.0	$42.3

- *This proposal impacts an estimated 5 taxpayers.*
- *Estimates assume a July 1, 2013 effective date, resulting in 11 months of collections for FY 2014.*

Eliminate preferential tax rate for resellers of prescription drugs

Description

This proposal eliminates the preferential business and occupation (B&O) tax rate of 0.138% for resellers of prescription drugs. It instead applies the wholesaling B&O tax rate of 0.484% or the retailing B&O tax rate of 0.471% to these activities.

Current Law

A preferential B&O tax rate of 0.138% is provided in RCW 82.04.272 to persons who warehouse and resell prescription drugs to retailers, hospitals, clinics, health care providers or other providers of health care services.

Purpose

This tax preference was enacted to encourage out-of-state prescription drug companies to build warehouses in Washington. Enacted in 1998.

The state was unable to restrict the preferential rate only to companies with in-state warehouses, so it now provides tax relief to out-of-state wholesalers with nexus in Washington. This negates the purpose of the preferential rate.

Citizen Commission Recommendation

The Citizen Commission has not reviewed this tax preference.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$13.4	$15.6	$29.0	$16.6	$17.7	$34.3

Notes:

- *This proposal will impact an estimated 40 taxpayers.*
- *Estimates assume a July 1, 2013, effective date, representing 11 months of collections for FY 2014.*

Repeal B&O tax exemption for long-term rental of commercial real estate

Description

This proposal would apply business and occupation (B&O) tax at the service and other activities rate on income derived from all long-term (30 days or more) rentals of commercial real estate, such as:

- Rental of commercial buildings, mini-storage facilities, apartments and leased departments,
- Rental of a boat moorage slip, parking space or airplane hangar for assigned spaces where the rental is for 30 days or longer, and
- Sale of lodging by a hotel, motel or other lodging establishment for 30 continuous days or longer.

Current Law

Under current law, income from long-term property rental is not taxed by the state, both for commercial and residential property, except income from granting a license to use real estate, for example, renting hotel rooms for fewer than 30 days or leasing space in a building.

Original Purpose and Current Analysis

To reflect a court ruling. In 1959, the Legislature extended the B&O tax to the rental of real estate, but in Schumacher (1960), the Washington Supreme Court ruled that it was an unconstitutional non-uniform property tax.

Later court decisions have called into question the continued validity of the decision, but it remains unclear if the court would overturn Schumacher and uphold a B&O tax on long-term rental income.

Citizen Commission Recommendation

The Citizen Commission has not reviewed this tax preference.

Revenue Impact

General Fund Impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$8.6	$19.2	$27.8	$29.7	$40.8	$70.5

- *This proposal impacts an estimated 10,000 taxpayers.*
- *Estimates assume a July 1, 2013, effective date, resulting in 11 months of impact for FY 2014.*

Narrow tax exemption for import commerce

Description

Amends the current exemption from business and occupation (B&O) tax and retail sales tax for imports and exports by companies with sufficient nexus in the state so that it applies only to exports and to imports of aerospace components.

Current Law

RCW 82.04.610 provides an exemption from B&O tax for the sale of tangible personal property in import or export commerce.

RCW 82.08.990 provides an exemption from retail sales tax for sales of tangible personal property if the sale is exempt from B&O tax under RCW 82.04.610.

Original Purpose and Current Analysis

To codify the Department of Revenue's historical treatment of imports and exports as reflected in WAC 458-20-193C.

Under current law, importers with nexus in Washington have an unfair advantage over instate manufacturers and wholesalers because the latter must pay B&O tax on their instate sales and collect retail sales tax on retail sales to instate customers, while importers are exempt.

Citizen Commission Recommendation

Not reviewed by the Citizen Commission.

Revenue Impact

General Fund impacts ($ millions)

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$7.4	$16.7	$24.1	$25.7	$35.3	$61.0

Notes:

- *This proposal impacts an estimated 1,000 taxpayers.*
- *Estimates assume a July 1, 2013, effective date, representing 11 months of collections for FY 2014.*

Repeal sales and use tax exemption for farm auction purchases

Description

This proposal would repeal the retail sales and use tax exemption for property bought at a farm auction.

Current Law

Under current law, neither retail sales nor use tax applies to sales of tangible personal property sold at an auction conducted on a farm. The exemption applies to items used on a farm, including farm machinery, equipment, vehicles, recreational items and household goods.

Typically, farm auctions occur on a farm with several farmers owning the property to be auctioned. There is no requirement that persons purchasing property at a farm auction be a farmer.

Original Purpose and Current Analysis

To support the agricultural industry.

Eliminating the exemption levels the playing field for sales of farm machinery, equipment and other farm implements sold by dealers or at on-farm auctions.

Citizen Commission Recommendations

The Citizen Commission for Performance Measurement of Tax Preferences endorsed a 2008 Joint Legislative Audit and Review Committee recommendation that the Legislature should require the reporting of information for on-farm auction sales and review the policy of this exemption. The reason JLARC provided for this recommendation is that Washington does not have uniform tax treatment for used farm machinery and equipment.

Revenue Impact

General Fund impacts *($ millions)*:

Fiscal Year 2014	Fiscal Year 2015	2013-15 Biennium	Fiscal Year 2016	Fiscal Year 2017	2015-17 Biennium
$2.6	$3.0	$5.6	$3.1	$3.1	$6.2

- *This proposal impacts an estimated 10,000 taxpayers.*
- *Estimate assumes a July 1, 2013 effective date, representing 11 months of collections for FY 2014.*

A New Foundation for Excellent Schools

By the Numbers

	Current school year (2012–13)	Governor Inslee's plan (2013–14)
Early Learning Investments		
Expanding preschool enrollment	8,391	11,426
Boosting state-funded full-day kindergarten for low-income kids		
Percent of kindergarteners served	22%	50%
Number of full-day kindergarten students funded	8,853	20,389
Number of schools funded	223	511
Reducing K-1 class sizes – high-poverty schools	24.1	20
Literacy Support and Dropout Prevention		
Additional students receiving extra reading support (LAP)		23,161
Exiting bilingual students receiving additional support (TBIP)		20,850
At-risk 6th through 9th graders receiving additional support (LAP)		47,693
Increase Courses in Middle and High School*		
Increasing annual hours of instruction (grades 7 to 12)*		80
Increasing the number of teachers funded (grades 7 to 12)*		1,429
Instruction Improvements		
Additional salary allocation to cover 18 hours of professional development for teachers/principals		1.25 %
Added support for new teachers		
First-year teacher stipend		$2,200
Second- / third-year teacher stipend		$1,000
Mentoring stipend for first-year teacher		$2,500
Mentoring stipend for second -/ third-year teacher		$1,250
Number of future principals in new one year residency program*		50
Basic Operations		
Percent of local pupil transportation funded by the state	76%	100%
School operations funding (MSOC) per student**	$555	$789

*Program starts in 2014–15
**School Year 2014–15 MSOC rate per student will be $829