FINAL BILL REPORT
ESSB 6346

C 238 L 26
Synopsis as Enacted

Brief Description: Establishing a tax on millionaires.

Sponsors: Senate Committee on Ways & Means (originally sponsored by Senators Pedersen, Chapman, Frame, Bateman, Orwall, Slatter, Alvarado, Hunt, Lovelett, Riccelli, Shewmake, Valdez, Wellman, Hasegawa, Robinson, Lovick, Conway, Trudeau, Cleveland, Kauffman, Wilson, C., Dhingra, Stanford, Nobles, Saldaña and Salomon).

Senate Committee on Ways & Means
House Committee on Finance

Background: Federal Individual Income Taxes. Federal individual income taxes are based on a taxpayer's adjusted gross income (AGI), which represents total income from all taxable sources minus certain allowable adjustments, such as retirement or health savings account contributions or student loan interest paid on certain higher education loans. From AGI, taxpayers subtract either the standard deduction or itemized deductions to arrive at taxable income, the amount actually subject to tax. The United States uses a bracketed tax rate structure where taxable income is divided into brackets, with each bracket taxed at a higher marginal rate as income rises; taxpayers don't pay their top rate on all income, only on the portion that falls within that bracket. The federal individual income tax has seven tax rates ranging from 10 percent to 37 percent.

Pass-through Entities. For federal income tax purposes, partnerships, limited liability companies, and certain corporations, referred to as S corporations, are considered disregarded entities. These entities are not taxed at the entity level and the various items of income, gains, losses, and expenses are passed through to the individual owners.

Capital Construction Fund. A capital construction fund (CCF) is a special account authorized under federal law that allows eligible vessel owners or operators to defer federal income taxes on money deposited into the fund. Those deposits must later be used to construct, reconstruct, or, under limited circumstances, acquire fishing vessels with before-tax dollars. A contribution to a CCF reduces federal taxable income, not federal AGI.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not part of the legislation nor does it constitute a statement of legislative intent.

State Individual Income Taxes. Approximately 41 states impose a broad-based individual income tax. Nine states have a flat-rate income tax system, which means that all income levels are taxed at the same rate. The other states use a bracketed rate structure, similar to the federal government. A majority of state income tax systems use AGI as the starting point for calculating state taxes. Others use federal taxable income as the starting point and a small number of states do not use either federal AGI or taxable income as a starting point, instead establishing their tax base independently.

Allocation and Apportionment. Under the United States Constitution, state taxes are required to be fairly apportioned, connected to activity within the state, and not unduly burdensome or discriminatory against interstate commerce. States have various methodologies to assign income to the state for nonresident individuals and businesses conducting activity in multiple states.

Working Families Tax Credit. In 2021, the Legislature established the Working Families Tax Credit (WFTC) Program, based in part on the federal Earned Income Tax Credit Program (EITC). It provides a refundable credit for retail sales or use tax paid by low-to-moderate income Washington residents who meet certain eligibility requirements. Individuals may apply for any WFTC payments for which they were eligible, but did not claim, for up to three years. To be eligible for credit payments, a person must:

- have filed a federal tax return;
- meet the requirements for the EITC, or would otherwise meet the requirements for the EITC, but are filing with an Individual Taxpayer Identification Number;
- be at least 25 and under 65 years of age, or have a qualifying child; and
- have lived in Washington for more than 183 days, or be the spouse of someone who does.

The Department of Revenue (DOR) administers the WFTC Program. The credit amount varies depending on the number of qualifying children in the household and the filer's income level. Qualifying income levels are based around the maximum adjusted gross income for the federal EITC, which changes annually. The maximum credit amount for the WFTC is reduced by varying percentages depending on income levels. DOR adjusts the rate of credit reductions annually to maintain the minimum credit being received at the maximum qualifying income level.

Small Business Business and Occupation Credit. Qualifying businesses may take a credit against B&O tax due up to $55 per month in the tax reporting period. The credit phases out as the B&O tax liability exceeds $55, phasing out completely when the tax due exceeds $110. For service businesses, the monthly credit is $160 per month in the tax reporting period. This credit phases out as the B&O tax liability exceeds $160, phasing out completely when the tax due exceeds $320. Roughly speaking, these credit amounts correlate to exempting the first $125,000 of business income, which phases out completely for businesses generating more than $250,000 in business income during the year. DOR

provides credit tables for use by all taxpayers, which applies the credit in $5 increments. The annual B&O tax return filing threshold is $125,000.

Business and Occupation Surcharge. Beginning January 1, 2026, an additional B&O tax was imposed on businesses in Washington with at least $250 million in Washington taxable income. The tax is 0.5 percent of the business's annual Washington taxable income in excess of $250 million and is in addition to the other B&O taxes imposed on the income. This surcharge expires December 31, 2029.

Retail Sales and Use Tax. Retail sales taxes are imposed on retail sales of most articles of tangible personal property, digital products, and some services. A retail sale is a sale to the final consumer or end user of the property, digital product, or service. If retail sales taxes are not collected when the user acquires the property, digital product, or service, then use tax applies to the value of property, digital product, or service when used in this state. The state, all counties, and all cities levy retail sales and use taxes. The state sales and use tax rate is 6.5 percent; local sales and use tax rates vary, depending on the location.

The Legislature made significant changes to the sales and use tax in 2025. Pursuant to ESSB 5814 beginning October 1, 2025, the following select services were classified as retail services and subject to the retail sales tax and the retailing B&O tax:

- custom software and customization of prewritten software;
- custom website design, support, and development services;
- information technology related training services, technical support, and other services;
- investigation, security services, security monitoring, armored car services, but excluding locksmith services;
- temporary staffing, except for temporary staff provided at hospitals;
- advertising services, but excluding:
    1. web hosting services;
    2. domain name registration;
    3. services rendered in respect to newspapers, printing, or publishing;
    4. certain radio and television broadcasting;
    5. out-of-home advertising, including billboards;
    6. street furniture advertising;
    7. transit advertising;
    8. place-based advertising, such as in-store displays or point-of-sale advertising;
    9. dynamic or static signage at live events;
    10. naming rights; and
    11. fixed signage advertising; and
- live presentations.

The following digital automated services are also classified as retail services and subject to the retail sales tax and the retailing B&O tax:

- any service that primarily involves the application of human effort by the seller;

- live presentations;
- advertising services; and
- digital processing services.

The sale of services between members of an affiliated group are not considered a retail service for purposes of the retail sales tax and the retailing B&O tax.

Fair Start For Kids Account. In 2021, the Legislature created the Fair Start for Kids Account. Funds from the account must be used for child care and early learning purposes.

Initiative 2111. In 2024, an initiative to the Legislature was passed by the Legislature without change. Initiative 2111 prohibits the state, counties, cities and other local jurisdictions from imposing a tax on any form of an individual's personal income. Income has the same meaning as gross income as provided in the federal tax code.

Tax Preference Performance Statement. State law provides a range of tax preferences that confer reduced tax liability upon a designated class of taxpayer. Tax preferences include tax exclusions, deductions, exemptions, preferential tax rates, deferrals, and credits. Legislation that establishes or expands a tax preference must include a Tax Preference Performance Statement (TPPS) that identifies the public policy objective of the preference, as well as specific metrics that the Joint Legislative Audit and Review Committee (JLARC) can use to evaluate the effectiveness of the preference. All new tax preferences automatically expire after ten years unless an alternative expiration date is provided or the tax preference is exempted from expiration.

Summary: Imposition of Tax. Beginning January 1, 2028, a 9.90 percent tax is imposed on the receipt of Washington taxable income. Only individuals are subject to payment of the tax. The first tax payments and returns begin in calendar year 2029.

Determining Washington Base Income. The determination of Washington taxable income starts with federal AGI and incorporates the following modifications to arrive at Washington base income:

- long-term capital gains:
    1. exclude all long-term capital gains and losses from federal AGI;
    2. add net long-term capital gains subject to Washington's capital gains tax;
    3. add the Washington capital gains tax standard deduction, to the extent the deduction reduced the amount of long-term capital gains subject to the Washington capital gains tax;
- state and local debt obligations:
    1. add interest income from debt obligations of other states;
    2. interest income from Washington-based state and local debt obligations are excluded from federal AGI;
- state and local taxes
    1. add state and local income taxes and B&O and PUT taxes to the extent these

taxes have been deducted in determining federal AGI;

- carryovers
    1. add any loss carryforwards that have been deducted in computing federal adjusted gross income and then deduct 80 percent of the amount of net operating loss carryover that has been deducted in computing federal adjusted gross income if the loss carryover is from losses apportioned to Washington and the loss carryover is carried over from taxable years ending after January 1, 2028;
- incomplete nongrantor trusts
    1. add income from an incomplete nongrantor trust;
- tribal income
    1. deduct tribal treaty income, income received by any member of a federally recognized tribe when the individual worked or received income within their own tribe's Indian country, income received by any member of a federally recognized tribe that is derived directly from lands or funds held in trust by the federal government, income derived from a federally recognized tribe when such income is received by a member of a federally recognized tribe or by a beneficiary of an Indian health program, and any other income exempt under federal law; and
- federal debt obligations
    1. deduct interest income from federal debt obligations to the extent it is included in federal AGI.

After making the modifications described above, a nonresident individual will allocate income attributable to sources or activity in Washington as described in the following allocation and apportionment section, to arrive at Washington base income.

Income earned by a nonresident participating as a keynote speaker, panelist, presenter, moderator, or similar role at a convention trade show or business event held in this state may be excluded under certain conditions.

Determining Washington Taxable Income—Standard Deduction, Charitable Deduction, Capital Construction Fund, Wagering Losses, Cannabis Business Expenditures, and Pass-Through Entity Tax Payments. From Washington base income, three deductions and one income increase are applied to arrive at Washington taxable income.

First, a taxpayer may deduct from Washington base income a standard deduction of $1 million per individual, or in the case of spouses or domestic partners, their combined standard deduction is limited to $1 million, regardless of whether they file joint or separate returns. The standard deduction is adjusted annually for inflation beginning with taxes collected in 2030 and every second year thereafter. The standard deduction is reduced for an individual who was not a resident for the entire year. The reduction is based on a fraction, which equals the individual's Washington base income divided by their total federal AGI.

Second, a taxpayer may deduct from their Washington base income the amount of charitable contributions they claimed for the taxable year under section 170 of the internal revenue code, up to a maximum deduction of $100,000 per individual, or in the case of spouses or domestic partners, their combined charitable deduction is limited to $100,000, regardless of whether they file joint or separate returns. A charitable contribution must be made to a nonprofit organization or other organization that is eligible to receive a charitable contribution under the federal tax code and principally directed and managed within the state of Washington.

Third, a taxpayer must add to the taxpayer's Washington base income the taxpayer's distributive share of the tax expense incurred by a pass-through entity making an election to pay the tax at the entity level.

Fourth, a taxpayer may deduct from the taxpayer's Washington base income the amount deposited in a CCF to be later used for the construction, reconstruction, or acquisition of fishing vessels, if the contribution amount has reduced the taxpayer's federal taxable income for the taxable year.

Fifth, a taxpayer may deduct an amount equal to 90 percent of any Washington allocated wagering losses for the tax year. The amount of the losses deducted cannot be more than the Washington allocated wagering income included in the taxpayer's Washington base income. Wagering losses may not be carried forward or backward.

Sixth, a taxpayer may deduct from the taxpayer's Washington base income the amount of expenditures disallowed pursuant to section 280E of the Internal Revenue Code so long as the expenditures are related to the commercial cannabis activities by a person licensed under state law.

Tax Credits. A resident individual may claim a tax credit for any income tax paid to another state, or to a political subdivision of that state, on income that is also subject to tax under this bill.

A tax credit is available against taxes owed under the bill for any B&O tax or public utility tax paid on the same income that is subject to the new tax.

A tax credit is also available for any Washington capital gains tax paid on capital gains taxed under the bill.

Distribution of Revenues. Beginning July 1, 2029, and each July 1st thereafter, the state treasurer will deposit 5 percent of the revenues collected from the tax during the previous fiscal year into the Fair Start for Kids Account. The remainder of taxes, interest, and penalties are deposited into the state general fund.

Allocation and Apportionment. For resident individuals, all income is allocated to the state

of Washington.

For nonresident individuals, income derived from sources within this state is assigned to Washington based on various allocation and apportionment methodologies described below.

A nonresident individual is subject to tax on the portion of federal AGI derived from employment within the state of Washington, regardless of the location of the commercial domicile of the employer. Compensation for services performed by a nonresident as part of their employment is allocated to this state to the extent the services are rendered within the state. If the services are performed both within and outside the state, the compensation will be apportioned based on the ratio of days worked in the state to total days worked, or by another reasonable method approved by DOR.

For a nonresident operating a business within and outside the state, income is assigned to the state generally following a model law called the Uniform Division of Income for Tax Purposes Act (UDITPA) developed by the Multistate Tax Commission. Under UDITPA, income from a business, trade, or profession carried on in this state, including any distributive share of a pass-through entity of a business, trade, or profession carried on in this state, must be classified as either apportionable income or non-apportionable income. Apportionable income is assigned to the state using a receipts factor based on in-state versus total receipts. Sales of tangible personal property are sourced to the state when delivered to an in-state purchaser or shipped from an in-state location under certain conditions. The sale, rental, or lease of real or personal property is sourced to the state when the property is located in Washington. Services are sourced to the state if the services are delivered within the state. Intangible property that is sold, rented, leased, or licensed is sourced to the state when it is used in the state under various criteria. Capital gains and losses from sales of real property located in Washington are allocable to the state. Interest and dividends are allocable to the state if the business's commercial domicile is in the state. The bill also addresses the allocation of income to Washington from net rents and royalties from tangible property and patent and copyright royalties.

For nonresident members of a professional athletic team, the portion of compensation attributable to athletic performances in the state must be apportioned to Washington. To determine this amount, a duty-day methodology is used. The portion of the compensation apportioned to Washington for a nonresident athlete is that portion of compensation received for the tax year that bears the same ratio to total compensation received for the tax year as the number of duty days within this state bears to the total number of duty days spent both within and outside the state during the tax year. Duty days is defined as the days during the tax year from the beginning of the official preseason training period of a professional athletic team through the last game in which the professional athletic team competes or is scheduled to compete during the tax year.

For nonresident student athletes, the portion of AGI of a nonresident student athlete derived from the commercial use of the student athlete's name, image, or likeness is allocated to this

state if the publicity services provided by the student athlete related to such commercial use of the student athlete's name, image, or likeness primarily occur in Washington. Payments by an institution of higher education representing a percentage of institutional athletic revenues to an nonresident student athlete will be apportioned to Washington in a form and manner consistent with a duty-day methodology developed by DOR. DOR is required to submit proposed legislation to the Legislature that would implement an apportionment methodology using a duty-day approach by January 1, 2028.

A part-year resident's Washington AGI includes all income earned while a resident plus only Washington-source income earned while a nonresident. Special rules apply to income from a pass-through entity.

Estimated Tax Payments. Individuals subject to the tax must make estimated payments to DOR using rules aligned with federal estimated tax payment requirements. The estimated tax amount is calculated by dividing the annualized tax by the number of months in the reporting period. Estimated tax payments are not required when the annualized tax liability is under $5,000.

Penalties and interest may apply to underpaid estimated taxes unless the estimated tax payments are either at least 90 percent of the tax shown on the tax return or 100 percent of the tax shown on the previous year's tax return.

Administration of the Tax. Taxpayers owing tax must annually file a return on or before the filing date of the taxpayer's federal income tax return. Individuals not owing tax are not required to file a return. Tax returns and all supporting documents, must be filed electronically using DOR's online tax filing service or some other method of electronic reporting allowed by DOR. A taxpayer is required to attach a copy of the taxpayer's federal income tax return and other supporting documentation. Each taxpayer required to file a return must, without assessment, notice, or demand, pay any tax due to DOR on or before the filing date, regardless of any filing extension. If a taxpayer has obtained an extension of time for filing the federal income tax return for the taxable year and the taxpayer provides DOR, on or before the date fixed for the filing of the return, regardless of any filing extension, information satisfactory to DOR confirming the federal extension, the taxpayer is entitled to the same extension of time for filing the return.

If any return due, along with a copy of the federal income tax return, is not filed with DOR by the due date or any extension granted by DOR, a penalty is assessed in the amount of 5 percent of the tax due for the taxable year covered by the return for each month or portion of a month that the return remains unfiled. The total penalty assessed may not exceed 25 percent of the tax due for the taxable year covered by the delinquent return.

If the federal income tax liabilities of both spouses are determined on a joint federal return for the taxable year, they must file a joint return under this chapter. If the federal income tax liability of any individual, including either spouse of a marital community, is determined on

a separate federal return for the taxable year, they must file separate returns under this chapter. State registered domestic partners may file a joint return under this chapter even if they filed separate federal returns for the taxable year. The liability for tax due under this chapter of each spouse or state registered domestic partner is joint and several, except under certain conditions.

A taxpayer's method of accounting for purposes of the tax is the same as the taxpayer's method of accounting for federal income tax purposes. If no method of accounting has been regularly used by a taxpayer for federal income tax purposes or if the method used does not clearly reflect income, tax due must be computed by the cash method of accounting.

Interest and penalties for underpayments and overpayments of tax under current law are applied to such underpayments and overpayments with respect to taxes owed as part of the April tax return. The bill also establishes a 5 percent penalty for substantially underpaid estimated tax payments.

Substantially underpaid means that an individual's total annual estimated tax payments were less than 80 percent of the actual annual tax due, and at least $5,000.

Pass-Through Entity Tax Election. Pass-through entities, such as partnerships and limited liability companies, may elect to pay tax at the entity level. The tax rate is 9.90 percent and the tax amount would be similar to the Washington tax liability of the individual owners. Pass-through entities may opt in annually by filing an election by DOR's deadline, no later than June 15th of the taxable year, and the election is irrevocable for that year. The election must be signed by an authorized person, depending on the entity type. Electing entities must make estimated tax payments similar to individuals, based on reasonable income estimates, though no estimated payments are required before July 1, 2029. Owners receive a credit for their share of tax paid by the entity and must report their distributive income on their own Washington returns. Resident and nonresident owners report income differently based on sourcing rules but both may claim the credit. In calculating individual Washington taxable income, owners must add back any distributive share of the tax expense deduction that is reflected in federal AGI. Electing entities must file an annual return with all required information, and DOR may adopt rules to administer and streamline the process.

Crimes. Any person who knowingly attempts to evade the tax is guilty of a class C felony. Any person who knowingly fails to pay tax, pay estimated tax, make returns, or supply information, as required under the bill, is guilty of a gross misdemeanor.

Tax Relief. The age requirement of the WFTC program eligibility to individuals 18 years of age or older, regardless of the number of qualifying children is extended. This expanded eligibility takes effect on January 1, 2029, for applications submitted beginning in calendar year 2029. In addition, the income threshold for the WFTC is expanded to include the needs standard used for cash assistance programs, which represents the amount of income required by individuals and families to maintain a minimum and adequate standard of

living. The expansion of the WFTC program eligibility is included in the current TPPS for the WFTC program and is exempt from the ten-year expiration date.

Beginning January 1, 2029, diapers, over the counter drugs, and grooming and hygiene products are exempt from the sales and use tax.

Beginning January 1, 2029, for non-service businesses, the small business B&O tax credit amount is increased from $55 per month in the tax reporting period to $125 per month. For service businesses, the small business B&O tax credit amount is increased from $160 per month in the tax reporting period to $375 per month. The B&O tax annual filing threshold is increased to $250,000.

Beginning January 1, 2029, an exemption from the B&O surcharge on high grossing businesses is provided for licensed health care providers, hospitals, and prescription drug resellers.

The sales and use taxes for retail services included under ESSB 5814 (2025), except for advertising services, are repealed effective January 1, 2029.

Beginning July 1, 2026, the following activities do not meet the definition of live presentations that are subject to the retail sales and use tax:

- before and after school care provided in-person and on-site by elementary schools;
- presentations given by a nonprofit organization exempt from federal income tax;
- musical, dramatic, comedic, or similar performances, including any incidental instruction;
- one-on-one instructional activities including tutoring and consulting; and
- music lessons regardless of the number of participants.

Beginning July 1, 2026, short-term staffing services utilized by hospital-based clinical providers to supplement the fulfillment of hospital contacts for professional services are excluded from the retail sales and use tax on temporary staffing services.

Beginning July 1, 2026, public libraries, library districts, library service centers, schools, school districts, and educational service districts are exempt from retail sales and use tax on the following services:

- information technology;
- custom website development;
- live presentations;
- investigation, security, and armored car services;
- temporary staffing; and
- custom software and customization of prewritten software.

Beginning July 1, 2026, any Washington taxable income attributable to wholesale sales of food and food ingredients sold by wholesalers to retailers not under common ownership is

exempt from the B&O 0.5 percent surcharge implemented in ESHB 2081 (2025).

Advisory Group. Beginning July 1, 2026, DOR must regularly consult an advisory group while implementing this act. The advisory group will include:

- the Director of DOR, or their appointee;
- the Director of the Office of Financial Management, or their appointee;
- the Director of the Office of Minority and Women's Business Enterprise, or their appointee;
- two members of the Senate; and
- two members of the House of Representatives.

In addition, the advisory group will include ten members appointed by the Governor from a list of recommendations from the President of the Senate and the Speaker of the House that include members of the following groups:

- two certified public accountants;
- two members of the tax section of the Washington State Bar Association;
- one member from the Office of the Attorney General;
- one member from a small business association that has membership throughout the state;
- one member from a large business organization; and
- one member of a federally recognized tribe recommended by the Governor's Office of Indian Affairs.

The advisory group will make recommendations regarding the implementation and administration of this act including the pass-through entity election, the development of a state schedule K-1, filing requirements, safe harbor provisions, sales taxes on services, and other essential administrative and implementation matters.

An initial report is due to the Legislature by December 15, 2026, with a final report due December 15, 2027.

DOR must report to the Legislature annually beginning January 1, 2028, on the total cost of administering the income tax program. The report must include the number of full-time employees required to administer the program as well as the cost ratio of implementation compared to revenues raised.

Miscellaneous Provisions. Various pension statutes are modified to specify that pension income is not exempt from the new tax.

If a court of final jurisdiction invalidates the new tax, the entire bill is null and void.

Initiative 2111 is amended to specify that it does not apply to the new tax so long as the standard deduction is at least $1,000,000 for a household.

All new tax preferences created in the bill are exempt from the automatic ten year expiration date and JLARC review.

The bill specifies that the new tax is necessary for the support of the state government and its existing public institutions and also specifies that DOR will continue with implementation efforts regardless of litigation.

Votes on Final Passage:

Senate	27	22	
House	51	46	(House amended)
Senate	27	21	(Senate concurred)

Effective: June 11, 2026
July 1, 2026 - Sections 1101 through 1104
January 1, 2029 - Sections 901, 909 through 911, 1001, and 1002