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## **Washington: The Budget That Never Happened**

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### **Abstract**

The crafting of the Washington state 2017–2019 biennial budget during the 2017 legislative session coincided with the looming deadline set by the Washington Supreme Court in the *McCleary* decision requiring a sustainable system to achieve “ample provision” for equitable K-12 support. Washington’s improving urban economy lessened some of the budget challenges, eviscerated by divided government and the Supreme Court’s *McCleary* and *Hirst* decisions. In what is become common place, the legislature required multiple special sessions to, on the last day prior to the mandated budget shutdown, pass the *McCleary* fulfilling operating budget. Three special sessions, however, weren’t enough for the legislature to negotiate a solution to the *Hirst* decision. This standoff between rural water rights and development resulted in the state capital budget being held as a pawn in the negotiations and is indicative of the greater challenges facing Washington State and its divided population, economy and territory.

### **Introduction**

Washington State’s longest legislative session on record, where the 2015–2017 operating budget was signed just 20 minutes prior to midnight heading off a mandated government shutdown, foreshadowed the 2017 legislative session and the day of reckoning. The 2017–2019 biennial budget in the 2017 session coincided with the looming deadline set by the Washington Supreme Court in the *McCleary* decision. This ruling required a sustainable system for “ample provision” for equitable K-12 support throughout the state by the end of the 2017 session (Washington State Supreme Court 2015).

To comply with the funding level requirements specified in the Washington State Supreme Court’s 2012 *McCleary* decision, legislators ramped up biennial funding for basic education since 2013 and will now need to increase the commitment of state funds another \$3.3–\$4.5 billion in the 2017–2019 biennial budget. The Supreme Court, previously disappointed with the legislature’s pace of enhancement of K-12 funding, currently holds the legislature in contempt and has levied a \$100,000/day fine being held in escrow for when an acceptable plan is approved

by the Court. The Washington State Supreme Court is not the only one disappointed by the pace of recent legislatures. During the 2016 “short” legislative session, Governor Inslee’s reaction to the slow pace of negotiations over a budget led him to execute 27 vetoes of popular bipartisan policy bills (Reading 2012, Washington State Courts 2012, Justice et al. 2013, O’Sullivan and Brunner 2015, Washington State Supreme Court 2015).

In 2016, the Economic and Revenue Forecast Council lowered the upcoming four-year revenue forecasts by over \$500 million but in 2017 provided the legislature a bit of reprieve by revising revenue forecasts higher. The more favorable forecasts, however, still pointed to soft economic areas nationally and globally. Against this backdrop, the 2017 legislature gathered for a 105-day “long” session on January 9 to draft the 2017–2019 biennial budget, which fully funded basic education, but many were doubtful whether they would accomplish their work within the time period of the regular session.

## **Washington State Budget Process**

The state of Washington is one of 15 states that follows a biennial budget process with annual legislative sessions. The two-year budget is adopted during odd-numbered years, leaving the even-numbered legislative session years to adjust the budget with a supplemental budget. The supplemental budget provides adjustments driven principally by unanticipated changes in revenue forecasts and/or deviations in anticipated spending due to either changing caseload levels or natural disaster expenditures. The operating, transportation, and capital budgets make up Washington’s three distinct budgets. Of the three, the operating budget far exceeds the other two budgets and is used to fund the day-to-day state government expenditures as well as the bulk of many of agencies and programs. The transportation budget follows next in size and provides funding for multimodal transportation infrastructure both on land and water. The smallest budget is the capital budget, which focuses on the state’s built infrastructure (Legislative Evaluation & Accountability Program Committee 2016a, Snell 2011).

Traditionally, influenced by the governors’ public policy priorities and founded on expected revenue forecasts, the governor starts off the budget process by proposing a balanced biennial budget to the legislature in December of the even-numbered years prior to the legislative session. In tandem, the supplemental budget of the existing biennial budget is proposed. The supplemental budget normally doesn’t reflect new allocations for additional projects, but instead provides necessary mid-course biennial budget corrections based on economic changes and adjusted program spending directions or requirements. .

When developing an operating budget, funding is necessary to provide for:

- K-12 Education—for more than 1,050,000 students
- Early Learning—for more than 10,000 students
- Higher Education—for over 230,000 students
- Health Care—for about 1,900,000 children and low-income adults
- Social Services—for children, adults, and families in need of assistance
- Public Safety—for more than 17,600 inmates and 17,300 parole/probation under community supervision

(Sources: Legislative Evaluation & Accountability Program Committee 2016a, Legislative Evaluation & Accountability Program Committee 2017a, Washington State Office of Financial Management 2016a, Washington State Office of Financial Management 2017b)

The legislature takes the governor's proposed budget under consideration as each chamber independently develops its own budgets. The two legislative budgets, after considerable deliberation and ensuing compromise, are merged into a single budget bill that must be passed by both chambers. This budget bill is then sent to the governor for his or her signature. The governor, even at this juncture, has the option to sign the budget bill, not sign the bill and have it automatically take effect, or use line-item veto authority to invalidate individual spending provisions, commonly referred to as "provisos." The governor's authority is limited such that the governor may use a veto to reject funding for specific activities, but the governor cannot transfer funds from one appropriation to another, nor is she or he permitted to add funding for an activity for which the legislature provided no authorized funding (Washington State Legislature 2016a).

### **Political Composition of State Government**

Political party support for Democrats and Republicans in Washington State is predominantly split geographically by the Cascade mountain range (LeLoup and Herzog 2004, 189–206). The west side of the state, which includes the Seattle-Tacoma-Bellevue-Everett Metropolitan Region, is highly urbanized and more densely populated than the eastern portion of the state; it is disproportionately supportive of Democratic Party candidates in most statewide and local elections alike. In contrast, the eastern side of the state is considerably more rural, less densely populated, and is very heavily supportive of Republican Party candidates in statewide and local elections. This geographical dispersion and the state's west side accelerated population growth has affected current and future prospects for all Republican Party candidates standing for statewide elected office and accounts for the fact that the governor's mansion has been filled by a Democrat for over 30 years (see Table 1). The re-election of Governor Inslee in 2016, due to the support of west-side voters, ensures that Democratic control will extend to at least 35 straight years (Clayton and Lovrich 2011, Washington State Legislative Information Center 2016).

The Democrats control of the west-side population centers and many urban areas of Washington State have allowed them to direct the political scene of the Evergreen State. The only major political "bump in the road" that the Democrats have experienced in the recent past came in 2012, and that setback was not the consequence of the election process. Instead, it took place during the regular legislative session when three senators from the Democratic majority crossed over and supported the Republican minority's budget and formed a "majority coalition." Five years later, the coalition—now with one lone Democratic senator—continues this majority coalition rule. Interestingly enough, there was a period during the majority coalition's tenure where without the cross-over senator the Republican Party would have had the majority, but the Senate majority caucus instead preferred to maintain the majority coalition. Preceding the coalition's formation, the state's Democrats maintained a nine-year period of control of the upper chamber. The Democratic Party has maintained unbroken control of the House of Representatives for 19 years, and the governor's office for 32 years (Benjamin and Lovrich 2011, 209–12).

Governor Inslee is currently in his first year of his second four-year term. He became the 23rd governor of state of Washington in 2013 after first serving two terms in the Washington State House of Representatives, and six terms in the U.S. House of Representatives. Governor Inslee is recognized as a champion for environmental protection, sustainability, and the promotion of clean energy issues. His ardent support for renewable energy alternatives and carbon penalties hasn't wavered despite strong opposition from the Senate Majority Coalition and mixed

**Table 1. Historical Party Control of Governor and Legislature**

<b>Position</b>	<b>Majority</b>	<b>Dem Split</b>	<b>Rep Split</b>	<b>Length of Control</b>	<b>When the Current Minority Party was Last in Power</b>
Governor	Democrat			32 years	1985 John Spellman –R
House	Democrat	50	48	19 years*	1998 Republican majority
Senate	Coalition**	24	25	5 years	2003 Rep & 2012 Dem majority

\* 1999–2001: The House was evenly split 49 Democrats and 49 Republicans

\*\* 2013–2015: Two Democrats joined the Republicans to form a coalition majority in the Senate, 2015–2017: One Democrat joined the Republicans to form a coalition majority in the Senate

Sources: Benjamin and Lovrich 2011, 209–12, Washington State Legislature 2016b.

support from the Democratic caucuses (Project Vote Smart 2014, Washington State Office of the Governor 2016).

### **Governor’s Proposed Budget**

Governor Inslee’s 2017 supplemental budget proposal included only modest adjustments to the 2015–17 budget currently in place to cover spending increases necessary to maintain the delivery of state services at current levels and to cover unexpected caseload and enrollment changes. His focus instead was on the 2017–2019 biennial budget. His proposal for 2017–2019 included an increase of \$4.4 billion in new tax revenue to:

- Fully fund K-12 basic education
- Overhaul the mental health system
- Reduce homelessness
- Advance clean energy and environmental issues
- Preserve safety net for vital services

His proposed budget first focused on meeting the state supreme court’s order to fully fund basic education and then on increasing teacher compensation, shrinking class sizes, increasing teacher mentoring, and addressing opportunity gaps. In related education areas, his proposed budget also froze college tuition, increased student financial aid, and provided more funding for early childhood education. Overhauling mental health included expanding and improving services, increasing behavioral health hospital capacity, and increasing staff. His budgetary approach to homelessness included increasing stock of affordable housing, private-sector partnerships, and housing for those discharged from psychiatric hospitals. Clean energy and environmental protection has for years been Governor Inslee’s mantra, and he continued this focus within his budget.

As part of the proposed 2017–2019 budget was the discussion that the current revenue system is no longer sustainable and the necessity for the state to change its funding mechanism. Over the past 30 years, state revenue collections have increased, but as a share of the economy have fallen by nearly 30 percent. Governor Inslee’s budget proposed over \$4.4 billion in new tax revenue with \$2.3 billion coming from Business & Operation (B&O) tax increases, \$821 million from capital gains tax, \$2 billion from a carbon pollution tax, and \$200–\$300 million from clos-

ing tax loopholes related to bottled water sales, nonresident sales tax exemptions, extracted fuel, trade-ins, and Real Estate Excise Tax (REET) (Washington State Office of the Governor).

## **State of the Economy**

The Washington State Economic and Revenue Forecast Council, Washington State’s official independent forecast agency, June forecast increased projected revenues through 2019 by an additional \$159 million. With this increase, revenues for the 2017–2019 state budget are projected to reach \$41.7 billion. This is good news as Washington continues to recover from the 2007–2009 Great Recession. Washington’s unemployment rate declined from 5.6 percent in May 2016 to 4.5 percent in May 2017. The May 2017 unemployment rate was the lowest in the series which extends back to 1976. Washington’s employment is expected to grow 2.4 percent in 2017 and then decelerate to an average of 1.4 percent per year in 2018–2021. Between April 2016 and April 2017 employment grew in the areas of information and retail, but declined in manufacturing. The greatest employment increases involved personnel in education and health services, construction, and electronic shopping and mail-order houses. The greatest employment decline involved the aerospace industry. While the revenue projection is positive, there are significant potential weaknesses at the global and national level. First quarter 2017 Washington exports were down 5.5 percent from the same period in 2016 due to a 14.7 percent decline in aircraft, Boeing planes, exports (Economic and Revenue Forecast Council 2016, Economic and Revenue Forecast Council 2017, Sappenfield 2016).

In the export market, Washington slipped a bit in its total percentage of the U.S. export market. Disappointedly, the total export in dollars that had been on an increasing trend through 2014 continued the slide started in 2015 and dropped by over \$6 billion dollars (see Table 2). Even with a drop of over \$3 billion dollars in export to China, that nation continues to be Washington’s primary export market. Countries to watch due to increasing export sales include Japan, UAE, UK, and Saudi Arabia (U.S. Census Bureau 2017).

In the export market, Washington’s top export—with nearly 60 percent of the total U.S. market—is civilian aircraft-related exports (see Table 3). The separation between Washington’s #1 and #2 export by dollar amount is so great that the aircraft dollar export is more than 11 times that of #2 soybeans. This comparison clearly highlights how critical the Boeing Corporation is to the Washington economy. Agriculture, with six of the top seven export items, is also a major industry in Washington (U.S. Census Bureau 2017).

## **Budget Drivers**

As Washington’s state legislators work to craft a budget, they are constrained not only by mandatory funding obligations, but they are also strongly affected by a number of “budget drivers.” The budget areas with little or no funding discretion include K-12 basic education, debt service, pension contractual obligations, Medicaid obligations, and the safety and health care costs of confined prisoners and juveniles and foster children. These budget drivers (see Figures 1-3) influence costs associated with many programs within the operating budget, and include K-12 enrollment increases, increased basic education funding requirements, increased Medicaid enrollments, decreased higher education enrollments, increased incarceration levels, increased

**Table 2. Top 10 Export Markets (\$ in Millions)**

<b>Market</b>	<b>2013</b>	<b>2014</b>	<b>2015 Rank</b>	<b>2015</b>	<b>2016</b>	<b>2016 Rank</b>	<b>2016 percent Share</b>	<b>percent Change 2015-2016</b>
China	16,711	20,693	1	19,485	16,130	1	20.3	-17.2
Japan	7,037	7,362	3	5,998	7,134	2	9.0	18.9
Canada	8,993	9,298	2	8,019	7,035	3	8.8	-12.3
UAE	3,870	3,272	5	3,211	4,158	4	5.2	29.5
Korea	2,712	2,753	4	4,287	4,155	5	5.2	-3.1
United Kingdom	2,702	2,951	8	2,541	3,566	6	4.5	40.3
Taiwan	1,443	2,474	7	2,758	3,103	7	3.9	12.5
Saudi Arabia	1,661	811	11	1,876	2,666	8	3.4	42.1
Netherlands	831	890	15	1,679	2,173	9	2.7	29.4
Turkey	548	1,340	10	1,922	2,168	10	2.7	12.8
Total	81,630	90,554		86,377	79,559			-7.9
WA Exports								
Percent Share of U.S. Total	5.2	5.6		5.7	5.5			

Source: United States Census Bureau.

per person incarceration costs, increased juvenile caseloads, and increased treatment caseloads (Washington State Office of Financial Management).

Figure 1 highlights the decreasing trend of higher education enrollment since Washington emerged from the recession and employment become more prevalent (Legislative Evaluation & Accountability Program Committee 2016b).

The projected changes in budget driver populations from 2015–2019 are: Juvenile Rehabilitation (ages 12–17)—4.4 percent, Corrections (males ages 18–39) – 6.8 percent, Medical Assistance (general population)—6.4 percent, Long-term care (ages 85+)—5.9 percent, TANF (ages 0–17)—5.2 percent, Higher Education (ages 17–29)—5.2 percent, and K-12 Education (ages 5–17)—4.9 percent (Washington State Office of Financial Management 2017a).

## **Budget Issues**

### ***McCleary Decision***

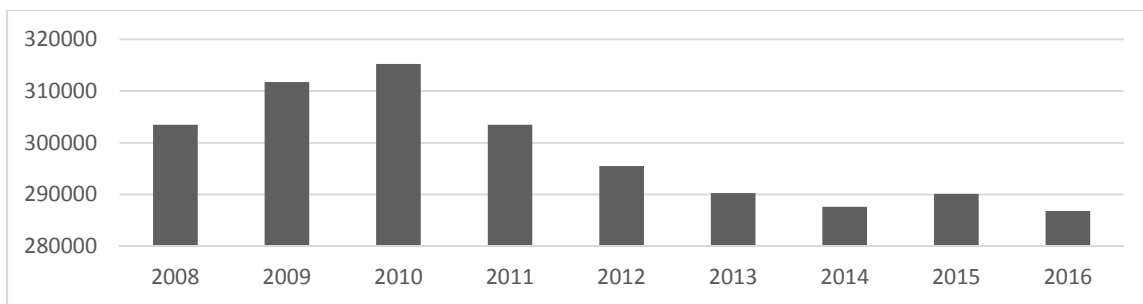
Article IX, Section 1 of the Washington State constitution states “It is the paramount duty of the state to make ample provision for the education of all children residing within its borders, without distinction or preference on account of race, color, caste, or sex.” This language led to a lawsuit filed in 2007 and decided by the Washington State Supreme Court in January 2012 in which the court concluded that the state was not upholding its paramount constitutional duty to amply fund basic K-12 education in Washington State. The court gave the state until the end of

**Table 3. Top 10 Exports (\$ in Millions)**

<b>Export</b>	<b>2013</b>	<b>2014</b>	<b>2015 Rank</b>	<b>2015</b>	<b>2016</b>	<b>2016 Rank</b>	<b>2016 percent Share</b>	<b>percent Change 2015-2016</b>
Civilian Aircraft Parts	42,572	47,786	1	51,149	46,465	1	58.4	-9.2
Soybeans	4,638	5,382	2	3,776	4,050	2	5.1	7.3
Corn (Maize)	835	1,751	5	1,418	2,103	3	2.6	48.3
Wheat	2,456	1,940	3	1,838	1,636	4	2.1	-11.0
Petrol Oil	3,262	2,848	4	1,530	1,237	5	1.6	-19.1
Bitum Mineral								
Potatoes	764	729	8	721	782	6	1.0	8.5
Apples	845	838	7	797	718	7	.9	-9.8
Ultrasonic Scanning	666	744	11	703	697	8	.9	-0.9
Coniferous Wood (Rough)	1,074	1,022	8	681	693	9	.9	1.7
LT Oils	1,092	1,079	12	474	540	10	.7	13.9
<b>Total WA Exports</b>	<b>81,630</b>	<b>90,554</b>		<b>86,377</b>	<b>79,559</b>			<b>-7.9</b>
<b>Percent Share of U.S. Total</b>	<b>5.2</b>	<b>5.6</b>		<b>5.7</b>	<b>5.5</b>			

Source: United States Census Bureau.

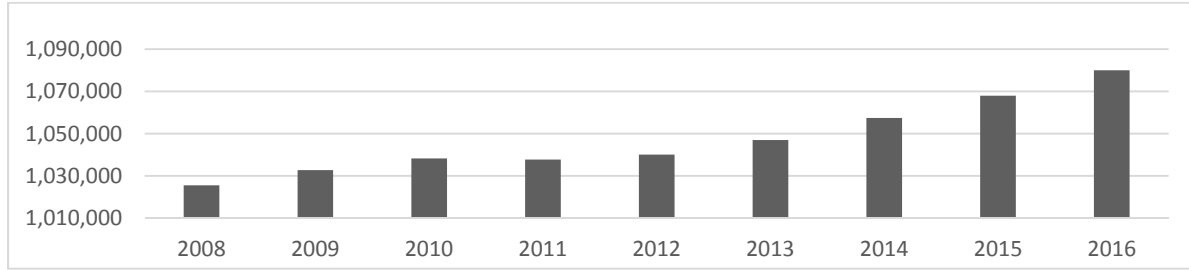
**Figure 1. Public Higher Education: Enrollment**



Source: Washington State Office of Financial Management.

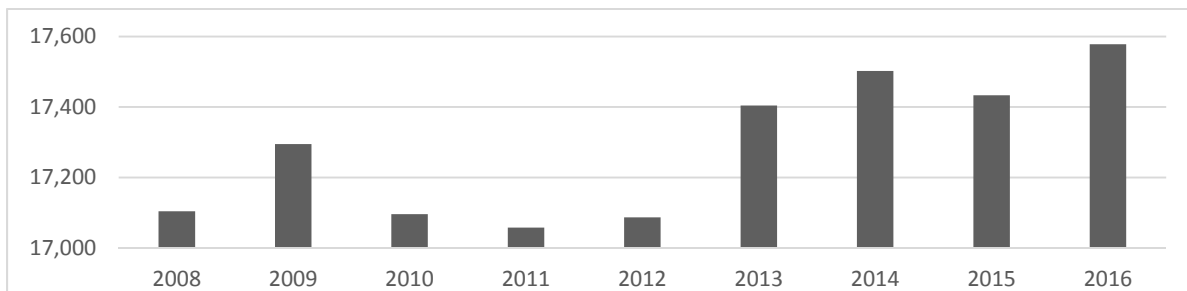


**Figure 2. FTE Enrollment at K-12 Public Schools**



Source: Washington State Office of Financial Management.

**Figure 3. Corrections: Prison Inmate Population**



Source: Washington State Office of Financial Management.

legislative session, beginning in 2013, the legislature give a report to the Supreme Court documenting its progress.

After the legislature filed its first report in 2012 the court determined that the state fell short of the requirements given to document progress in improving education funding. In January 2014, the court required the legislature to present a complete plan for fully implementing funding for basic education by April of that year. The legislature failed to come up with a full plan, leading the court in September 2014 to rule that the legislature was in contempt for failing to comply with the January order. However, the court decided not to implement sanctions until after the 2015 session and gave the legislature two extensions on sanctions in special sessions. In August 2015, the court decided to not give any further extensions and fully implemented sanctions. The legislature was ordered to pay \$100,000 per day it was out of compliance with the court's ruling in the *McCleary* decision, which which the legislature ignored. Further complicating this decision was the fact that several justices who decided *McCleary* were funded in their last reelection campaign by the Washington Education Association (WEA), which was part of the initial *McCleary* lawsuit. The perception was that the decision coming from the nine-member Supreme Court—all of whom are elected by the people of Washington State for six year terms—was a political decision rather than a decision based on the facts of the case (Finne 2014, Washington Policy Center 2017).

At the heart of the debate over amply funding basic K-12 education is the reliance by many school districts on local levies, which the court suggested meant the state was shifting the burden of amply funding K-12 education from the state to local school districts also leading to discrepancies in the quality of education being provided across the state—in direct violation of the constitution’s statement that education must be provided “without distinction or preference.” The court also ruled that “local levies are not a regular and dependable funding source since levies are temporary, subject to approval by the voters, and highly variable” (Washington State Legislature 2017a).

As the legislature was coming to the end of its time to fully fund basic K-12 education per the court’s order in 2012, what constituted basic education and how to fund that education was an overriding issue for the entirety of the 2017 legislative session as the legislature needed to find several million dollars in order to fully comply with the court’s order, in addition to addressing school districts’ reliance on local levies. Democrats proposed increasing revenue through new taxes on business and expanding the on-line sales tax, while republicans proposed addressing the levy issue by increasing the state property tax to \$1.55 per \$1000 while eliminating local school district levies beginning in 2019 (Santos 2017a). This would comply with the court order in McCleary that the state assume a greater percentage of the burden of funding schools also known as a “levy swap” and would decrease property taxes in approximately two-thirds of Washington’s 295 school districts (Santos 2017b).

The levy swap ultimately passed and was signed into law by the governor, and funding for K-12 education increased by \$7.3 billion over the next four years (O’Sullivan 2017b). The levy swap will mean an increase in property taxes primarily for wealthy school districts located in King, Snohomish, and Pierce counties while the rest of the state will see property tax relief assuming that the agreement supported by both Republicans and Democrats at the last minute during the second special session holds as there have been rumors that should a democrat win a special election in the 45th legislative district, effectively giving control of the state Senate to democrats, the governor hopes to undo the property tax increase (Santos 2017c). Of course, this is all assuming that the court approves the funding plan agreed to by the legislature and rules it in compliance with the 2012 ruling.

### **Budget Stabilization Account**

About 43 percent of Washington State’s revenue comes from taxes, 50.6 percent of which is from the statewide sales tax (Washington State Office of Financial Management 2017a). This heavy reliance on sales tax means that Washington can see severe declines in revenue to fund state operations during recessions like the great recession of the late 2000s. In response, in 2007, the legislature created a Budget Stabilization Account, or Rainy Day Fund, intended to provide resources to ensure essential public structures can be maintained during economic recession, natural disasters, and the like. The establishing legislation requires that the legislature deposit an amount equal to at least one percent of general fund revenues into the fund and those deposits cannot be suspended although they can be reappropriated under certain conditions. Furthermore, a three-fifths supermajority vote is required to access funds unless the governor declares an emergency or employment is predicted to grow by less than one percent in the current or coming fiscal year. In these two instances, a simple 51 percent vote is sufficient to access the funds (Nicholas & Pfingst; Washington State Office of Financial Management 2016b).

## **Balanced Budget Requirement**

Like most states, Washington requires that the state balance its budget. This provision, adopted in 2012 for the 2013–15 biennium requires that the state adopt an operating budget that leaves a positive balance in the general fund account at the end of the budget cycle. The project maintenance cost of the budget must not exceed available fiscal resources in the next biennium (Washington State Office of Financial Management 2016a, Washington State Legislature 2107b).

## **2016 Statewide Initiatives**

Washington provides citizens the opportunity to propose, submit evidence of public interest in and support for particular laws to the secretary of state, and subsequently take a statewide vote on citizen initiatives. In recent years, the initiative process has become increasingly used for a variety of issues. In addition to citizen initiatives, legislators can send legislation passed during session to the voters in the form of either a referendum or an advisory vote. In 2016 six initiatives were on the ballot, of which four referendums passed and two advisory votes failed passage. Two of the proposed initiatives, I-1433 and I-732, had the potential for considerable impact on the state budget (Washington State Office of Financial Management 2016b, Washington State Office of the Secretary of State 2016); of the two, only I-1433 concerning the labor standards, and specifically the minimum wage, passed. However, a vote taken in several counties surrounding the Seattle metropolitan area took up much of the legislature's time and energy and impacted discussions regarding additional sources of revenue.

## **2016 ST3 Vote**

In 2015, the legislature gave authorization for Sound Transit to bring to a vote of the people a proposed motor-vehicle excise increase of .5 percent and the imposition of a new property tax of 25 cents per \$1,000 of assessed value to fund an enhancement to the Sound Transit system. The measure, known as ST3, brought to voters in November 2016, actually asked voters to approve three new taxes: a 0.8 percent motor-vehicle excise increase, a .5 percent increase in the sales tax as well as the increase in property taxes initially authorized by the legislature. The anticipated \$53.8 billion will fund the addition of 62 more miles of light rail to complete a 116-mile regional system, making the system five times larger than it is today (McNamara 2017).

ST3 is in response to the Seattle region's rising population and the enhanced system will connect Everett, Tacoma, Seattle, Ballard, Redmond, Kirkland, Bellevue, and Issaquah. In the last six years, congestion on the region's highways has increased by an estimated 95 percent, with the average 2014 peak hour commuter in the Seattle area spending 63 hours stuck in traffic over the course of the year. ST3 is projected to reduce the annual vehicle miles driven in the region over 300 million miles by 2040 and reduce annual greenhouse gas emissions by almost 800,000 metric tons. In 2016, the ballot measure entitled "Regional Transportation Authority Proposition No. 1 Light-Rail, Commuter-Rail, and Bus Service Expansion" (also known as ST3) was passed with 54 percent voter approval (Lindblom 2014, Sound Transit 2016, Washington State Secretary of State 2016).

While ST3 passed, the tax increases triggered by the measure quickly became unpopular as voters in the affected counties saw the real impacts of the increases leading to a call for the legislature to do something about the fees associated with registering vehicles. In some cases, vehicle owners saw up to a 300 percent increase in the cost of licensing their vehicle for one year (Gut-

man 2017a). The argument centered on the vehicle value on which the department of licensing based car tab fees so voters in these three counties looked to the legislature to remedy what was seen by some as intentional misleading on the part of Sound Transit to encourage voters to vote on a measure they did not fully understand (Gutman 2017b).

While a remedy for ST3 was not ultimately addressed by the legislature, the impact of the ST3 tax increases did have an impact on legislator willingness to seriously consider new statewide revenue streams as the perception was that the three most populous counties in the state were tapped out and resistant to new taxes.

### ***Hirst* Decision**

On July 20, 2017, the Washington State Legislature adjourned its third special session without passing a capital budget. This failure was due to the inability of house Democrats and senate Republicans to come to a compromise on the issue of rural water rights and development resulting from a 2016 Supreme Court decision known as the *Hirst* decision in which the court ruled that Whatcom County, located in the state's northwest corner, failed to comply with the Growth Management Act's (GMA) requirements to protect water resources. The ruling stated that a county planning under the GMA cannot issue building permits for wells that would rely on exempt wells unless it can show that the well will not have a negative impact on rivers and senior water rights. The decision also shifted the burden from the Department of Ecology to counties to show that there is sufficient water before new wells can be drilled, and until that proof is attained, new building permits cannot be issued effectively bringing construction and growth in many rural counties to a halt as rural counties do not have the resources to pay the high costs associated with the necessary hydrological studies to prove there is sufficient water to drill a new well (Washington State Supreme Court 2016).

Senate Republicans proposed a fix to the *Hirst* decision; House Democrats replied that the implementation of the decision should be put off for 24 months. Republicans replied that proverbially "kicking the can down the road" was unacceptable as it would provide no certainty to those rural counties impacted by this decision, and any permit issued that was still in active status 24 months from now would be subject to being revoked regardless of project status or previous approvals. This standoff is reflective of a bigger political fight in Washington State between urban areas—primarily King, Snohomish and Pierce counties—represented by Democrats, and the rural areas of the state, primarily represented by Republicans. Most of the state's population lives in the three-county Seattle metropolitan area allowing Democrats control of the house and the governor's mansion, and, as a result, the perception is that often rural concerns are required to play second fiddle to the interests of the liberal Seattle area population.

Ultimately, tribes in the state, many of which made campaign contributions to democratic members of the house and to the governor, demanded that the *Hirst* decision be implemented and that no compromise be reached. Thus, even though Senate Republicans proposed a fix, house Democrats refused to bring it to the floor for a vote, and the third special session ended in a stalemate with the state capital budget held as hostage.

## **Revenues**

As part of the 2017–19 biennial budget agreement, the state of Washington plans to raise \$44,476,000,000 in total revenue from personal and business taxes as well as through various

other, more minor, revenue streams. The beginning balance for this particular budget is \$781 million. The new revenue for this budget includes the cultivation of new sources of revenue including:

- \$1.614 billion through changing the property tax rate per thousand dollars to \$2.70 as opposed to the current rate of \$1.88 per every \$1,000 of assessed value (O’Sullivan 2017a, WashingtonVotes.org 2017). This increase is an attempt to address the *McCleary* decision’s ruling on K-12 education funding. The impact of this increase will obviously vary based on the cost of property in local communities throughout the state. However, the effect of this increase is counteracted by the cap on education levies (\$1.50 per every \$1,000 of assessed value or \$2,500 per student—the state will use the lower or the two).
- The application of the state sales tax to bottled water. The tax went into effect on August 1, 2017 and requires that sellers collect sales tax on bottled water with the exclusion of purchases being made under the Supplemental Nutrition Assistance Program (SNAP) (Washington State Department of Revenue 2017b).
- The elimination of a use tax exemption on fuel used in the process of extracting fuel. This creates parity between oil producers and other industries that are taxed on products that they themselves use during the manufacturing process. The end of this exemption is expected to raise approximately \$52 million for the state.
- The extension of “economic nexus” which determines a company’s jurisdiction, for tax purposes, on its market as opposed to its physical location. This is an attempt to generate revenue from companies that sell their products in the state of Washington without incurring state taxes—particularly with respect to online sales (Hanson 2017). The state may have to deal with legal issues as the Supreme Court ruled in 1992 in the case of *Quill Corp. v. North Dakota* that state governments could only collect taxes on businesses that were physically located within their borders. The state, in part, justified their approach based on a similar law in Colorado that had already been upheld by the Tenth Circuit Court.
- Eliminating payments to local areas working within the 2007 Streamlined Sales and Use Tax Agreement. This agreement was an attempt by 44 states to create parity in the way that sales taxes were enforced and administered by individual states. For businesses with operations in multiple states, this was an attempt to reduce their overhead costs associated with maintaining compliance in numerous states with varied regulations. Likewise, the legislation was an attempt to make it easier for states to collect taxes from online retailers. In accordance with this mission, the state asked local retailers to switch to a “destination-based” approach to collecting taxes (collecting from the location of the purchaser—not the origin of the business or warehouse) (Washington State Department of Revenue 2017a).
- Changing the date of distribution for public utility tax privileges. These taxes are designed to assist businesses working as part of some public service and are used in place of the business and occupation tax. The distribution of funds raised from this tax is now delayed from June until July starting in 2018.

(Legislative Evaluation & Accountability Program Committee 2017a, Legislative Evaluation & Accountability Program Committee 2017b)

In a separate act, the legislature passed SSB 5977, which included tax breaks for motion picture producers and various manufacturers. The expectation was initially that this would reduce

state revenues by a total of \$15.7 million during the 2017–2019 period. However, after Governor Inslee vetoed lowering the Business and Operating tax rate for all manufactures it is now anticipated that the state will lose \$12.8 million in revenue as a result of SSB 5977 during the course of the recently passed biennial budget (Makings 2017).

A more detailed discussion of the revenue is not currently available given the last-minute negotiations, agreement on the operating and transportation budgets as well as the ongoing dispute over the capital budget.

To fund the activities approved in 2017–19 biennial budget, the state anticipates taxing its citizens and businesses \$41.4 billion, procuring federal and other grants of \$25.7 billion, collecting fees and assessing license and permit charges of \$22 billion, and borrowing \$4.6 billion (see Figure 4 & Table 4). Minor sources, including transfers, account for about \$3.3 billion.

Washington State’s shifts in revenue collection during recent biennia have ranged widely, from a low of 1.7 percent to a high of 15.8 percent. Removing federal grants causes the collection range to become even more dramatic, ranging from a low of .6 percent to a high of 19.5 percent. Table 5 highlights how important the federal stimulus was in getting Washington State through the deepest part of the recession.

Most of the funds the state uses to pay for services come from taxes collected within Washington State. Major tax sources include the sales tax, the property tax, and a business and occupation (B&O) tax (see Figure 5 and Table 6). Washington’s B&O tax is unusual when compared to other states in that it is a tax on gross receipts rather than on either profit or income. Washington is also atypical in that it is one of only seven states that do not levy a personal income tax, although some state-to-state tax burden comparisons include B&O taxes paid by solo proprietor businesses in the personal income tax column. These comparisons justify this inclusion based on the interpretation that taxes paid by a solo proprietor business are substantially the same as taxes paid by an individual.

## **Supplemental budget**

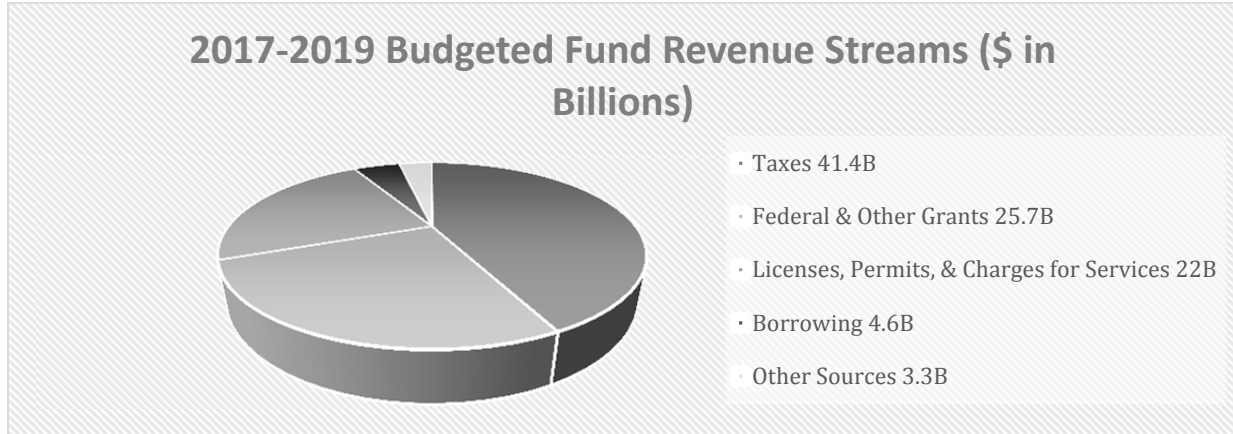
As part of the 2015–17 Omnibus Operating Budget, the state legislature passed a supplemental budget for 2017. The supplemental operating budget passed on June 30, the supplemental transportation budget passed on April 21, and the supplemental capital budget passed on July 1.

Most significantly, the supplemental budget includes \$477 million in cuts to the transportation budget (the largest amount—a total of \$458 million—coming from the capital budget). The area most affected by the cuts is the Department of Transportation, which will lose \$397,924,000 in the 2017 supplemental budget.

In addition, the human services portion of the budget experienced a cut of \$107 million as part of the 2017 supplemental budget agreement. Most of these cuts come from a \$78 million decrease in the budget of the Department of Social and Health Services. There were also marginal increases in spending for some services including the Department of Health, the Department of Veterans’ Affairs, and the Department of Corrections.

The largest increase in state spending went to the public school system that will receive \$71 million in the supplemental budget.

**Figure 4. 2017–2019 Budgeted Fund Revenue Streams**



Source: Washington State Fiscal Information.

**Table 4. 2017–2019 Biennium—Sources of State Revenue**

Category	Dollars in Billions	percent of Revenues
Taxes	41.4	42.7
Federal Grants	25.7	26.5
Licenses, Permits, Fees	22.0	22.7
Borrowing	4.6	4.7
Other Sources (including Transfers)	3.3	3.4
Total	97.0	

Source: Washington State Fiscal Information.

## Expenditures

Governor Inslee signed a 2017–19 biennial budget allocating \$43.7 billion for services in the state of Washington. Significant spending increases include (these values represent the increase in money allocated for these particular areas over the baseline amount from the previous budget) (Legislative Evaluation & Accountability Program Committee 2017a, Legislative Evaluation & Accountability Program Committee 2017b):

- An additional \$1.8 billion in public school spending and \$7.3 billion over the course of the next four years. This includes approximately \$5.2 billion in additional funds for K-12 salaries. This aligns with the legislature’s new minimum starting salary for K-12 educators of \$40,000 (La Corte 2017).
- A \$618 million expenditure for state employees as per collective bargaining agreements.

**Table 5. All Revenue and Other Sources (Uses) By Major Fund (\$ in billions)**

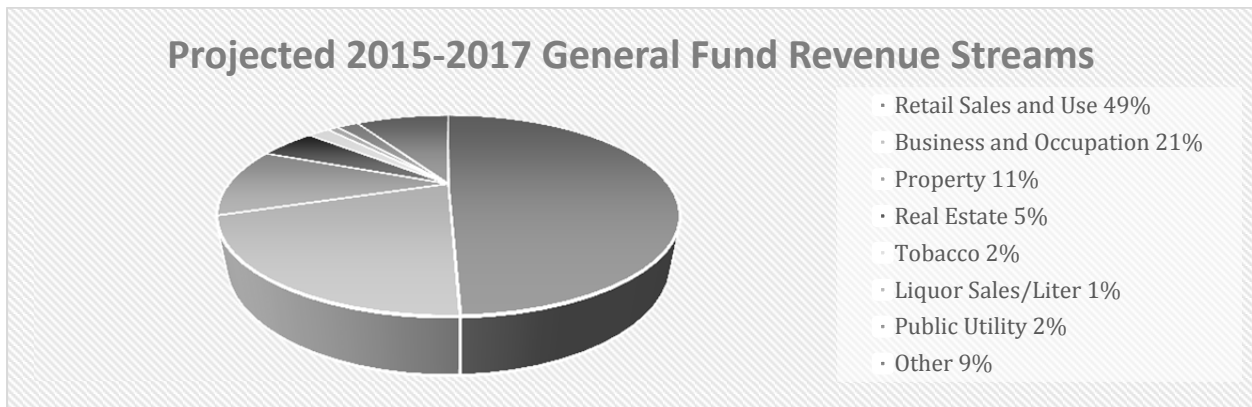
Category	2005- 2007	2007- 2009	2009- 2011	2011- 2013	2013- 2015	2015- 2017*	2017- 2019**
Taxes	32.4	32.5	31.3	33.3	36.8	40.2	41.4
Federal Grants	14.3	16.8	20.4	18.5	23.3	28.5	25.7
Licenses, Fees	2.1	2.3	2.6	2.9	3.3	18.0	22.0
Misc	15.7	15.7	17.2	18.2	17.6	7.1	7.9
Total	64.5	67.3	71.5	72.9	81.0	93.8	97
Total% Change	15.3%	4.3%	6.5%	1.7%	11.1%	15.8%	3.4%
(Total – Federal Grants)% Change	19.5%	0.6%	1.6%	6%	6%	13.1%	9.2%

Sources: State of Washington Office of Financial Management 2015 Data Book (OFM), Washington State Legislative Evaluation & Accountability Program (LEAP), and Washington State Fiscal Information.

\*Note: 2015–2017 data are from LEAP.

\*\*Note: 2017–2019 data are from Washington State Fiscal Information.

**Figure 5. Projected 2017–2019 General Fund Revenue Streams**



Source: Washington State Fiscal Information.

- \$116.1 million for mental health services in the state of Washington. While this represents a significant increase in spending, it is far short of Governor Inslee’s request of \$300 million. The largest share of the allocated funds will be spent on issues related to Eastern State Hospital and Western State Hospital—the psychiatric hospitals in Washington (Bellisle 2017).
- \$75 million is added to the budget for higher education (\$143 million over the next four years). However, it is important to view these funds in the light of the approximately 2 percent increase in tuition costs for students attending state four-year and community col-

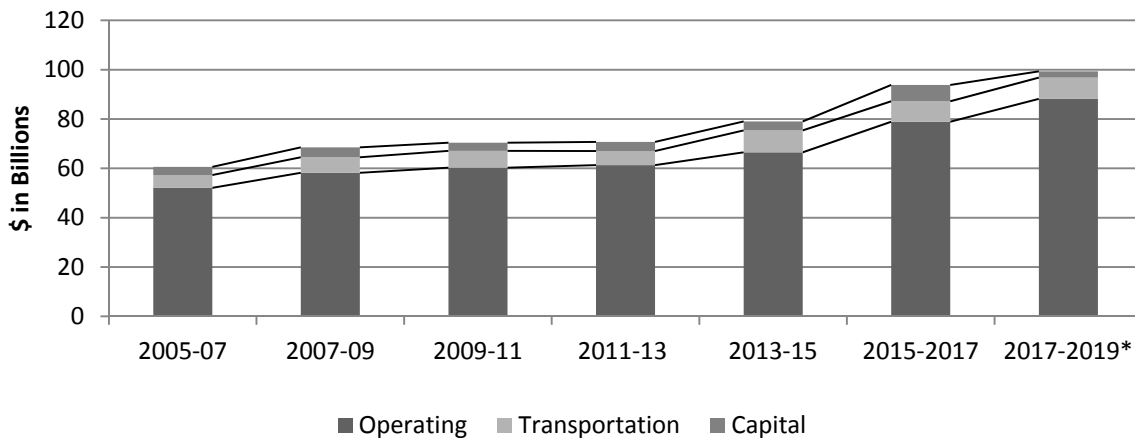


**Table 6. Top General Fund—State (GF-S) Revenue Streams (\$ in Millions)  
Sources of General Fund—State Revenue: 2017–19 Biennium Estimates**

Category	Dollars in Millions	Percent (%)
Retail Sales & Use Tax	\$18,404	49.4
Business & Occupation Tax	\$7,641	20.5
Property Tax	\$4,161	11.2
Real Estate Excise Tax	\$1,893	5.1
Other*	\$5,144	13.8
<b>Total</b>	<b>\$37,243</b>	

\*The Other category includes revenue from liquor sales, tobacco taxes, insurance premiums, etc.  
Source: Washington State Fiscal Information

**Figure 6. Washington State Spending History**



\* Capital Budget: New Appropriations have yet to be passed by the legislature.

Sources: Washington State Legislative Evaluation & Accountability Program and Washington State Fiscal Information.

leges. This is a break from the last several years during which tuition rates have been frozen. To offset the impact of this increase, \$50 million will be allocated to the State Need Grant (Orenstein 2017).

- \$73 million will be used for Long-Term Care and Developmental Disabilities (\$147 over the course of the next four years). In terms of the overall budget for this area, the majority of funds (\$126.7 million) will be spent on meeting the collective-bargaining agreements between the state and employees in this field.

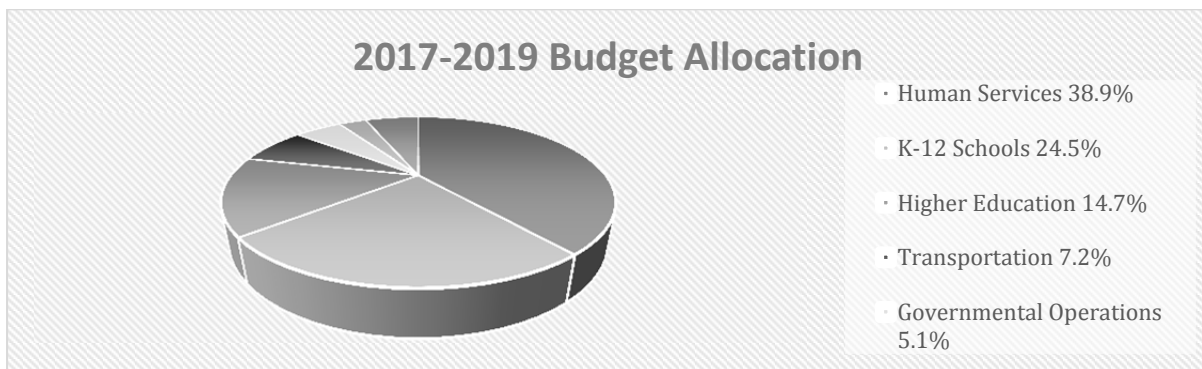
**Table 7. Biennial Budget Totals, Washington State (\$ in Billions)**

<b>Budget</b>	<b>2005- 2007</b>	<b>2007- 2009</b>	<b>2009- 2011</b>	<b>2011- 2013</b>	<b>2013- 2015</b>	<b>2015- 2017</b>	<b>2017- 2019</b>
Operating	52.1	58.2	60.3	61.3	66.5	78.9	88.3
Transportation	5.2	6.3	6.8	5.7	8.9	8.3	8.6
Capital	3.3	4	3.3	3.7	3.6	6.6	2.5*
<b>Total</b>	<b>60.6</b>	<b>68.5</b>	<b>70.4</b>	<b>70.7</b>	<b>79.0</b>	<b>93.7</b>	<b>99.4*</b>
percent Growth	13%	13%	2.7%	0.4%	11.7%	18.7%	*

\* Capital Budget: New Appropriations have yet to be passed by the legislature.

Sources: Washington State Legislative Evaluation & Accountability Program and Washington State Fiscal Information.

**Figure 7. 2017–2019 Budget Allocation by Agency**



Source: Washington State Fiscal Information.

The 2013–2015 biennial budget witnessed a return to the prerecession level of growth in the budget, and the 2017–2019 biennial budget continues this trend (see Figure 6 and Table 7).

Budget allocations displayed by agency illustrate that the top three funded agencies combined receive over three-fourths of the total budget; these three agencies are Human Services, Public Schools (K-12), and Higher Education (see Figure 7 and Table 8). While Human Services is essentially an umbrella organization that provides social, income, and medical assistance to citizens in need, the largest single state program is that of the public schools, which provides state support for K-12 education allocations to the state’s 295 local school districts.

Agency budgets, as a whole, follow the same biennial trends as the overall budgets (see Table 9). From 2003 to 2009 agency budgets grew on average by over 11 percent, and then from 2009 to 2013 on average by less than two percent. Starting again with 2013 the overall biennial budgets through 2017 brought a degree of growth to almost every category. Transportation is an

**Table 8. 2017–2019 Biennium Budgeted Expenditure**

<b>Category</b>	<b>Dollars in Billions</b>	<b>Percent of Budget</b>
Human Services	38.9	39.2
K-12 Schools	24.5	24.7
Higher Education	14.7	14.8
Transportation	7.2	7.2
General Government	5.1	5.1
Natural Resources	3.0	3.0
Other	5.9	5.9

Source: Washington State Fiscal Information.

**Table 9. Expenditure History of Total Budgeted (\$ in Billions)**

<b>Agency</b>	<b>2005- 2007</b>	<b>2007- 2009</b>	<b>2009- 2011</b>	<b>2011- 2013</b>	<b>2013- 2015</b>	<b>2015- 2017</b>	<b>2017- 2019*</b>
Human Services	21.4	24.7	25.6	25.8	28.8	35.5	38.9
K-12 Schools	13.7	15.9	16.1	16.4	17.7	21.3	24.5
Higher Education	10.3	11.7	12.4	11.7	12.8	14.9	14.7
Natural Resources	2.0	2.3	2.1	2.7	3.0	4.1	3.0
Transportation	5.0	5.9	6.1	5.9	7.8	6.9	7.2
General Government	4.1	4.8	4.7	4.7	4.4	5.9	5.1
Other	4.0	3.3	3.6	3.5	4.6	5.1	5.9
Total	60.5	68.5	70.7	70.7	79.0	93.7	

Sources: Washington State Legislative Evaluation & Accountability Program and Washington State Fiscal Information.

\*Note: 2017–2019 data are from Washington State Fiscal Information.

outlier during this time due to the one-time federal stimulus funds. The 2017–2019 budget’s focus on K-12 education resulted in inconsistent growth over the various categories.

### **Summary/Conclusion**

It was known going into the 2017 session that there would be many challenges in adopting a budget due to the impact of the Supreme Court’s *McCleary* decision and the consequences that decision had for prioritizing funding for K-12 education. It was also known that the two chambers controlled by two parties would have different ideas about how to fund the operations of government. In other words, no one went in assuming that this would be a short or easy legislative session. What was not known was the impact that other Supreme Court decisions—namely

the *Hirst* decision—would ultimately play on the legislature’s ability to pass all three of the state’s budgets. Since the operating and transportation budgets are critical for the day-to-day operations of the state of Washington, it should be no surprise that the less critical of the three budgets—the capital budget—was ultimately the budget held as the pawn in the negotiations between the democratically controlled house and governor’s mansion and the republican/majority coalition caucus controlled senate.

However, this standoff between rural water rights and development and the state capital budget is truly indicative of the greater challenges facing Washington State and its divided population, economy, and territory. The perception among many rural Washingtonians is that their health and well-being are being sacrificed for the good of the liberal, metropolitan areas, and they are placing pressure on their elected officials to stand up for the concerns of rural and agricultural Washington. It is likely that Washington will continue to need several special sessions as long as the state is governed under divided government and competing interests that are associated with that divided government.

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