STATE OF WASHINGTON
DOUGLAS COUNTY SUPERIOR COURT

CHRIS QUINN, an individual; CRAIG LEUTHOLD, an individual; SUZIE BURKE, an individual; LEWIS and MARTHA RANDALL, as individuals and the marital community comprised thereof; RICK GLENN, an individual; NEIL MULLER, an individual; LARRY and MARGARET KING, as individuals and the marital community comprised thereof; and KERRY COX, an individual,

Plaintiffs,

v.

STATE OF WASHINGTON; DEPARTMENT OF REVENUE, an agency of the State of Washington; VIKKI SMITH, in her official capacity as Director of the Department of Revenue,

Defendants,

EDMONDS SCHOOL DISTRICT, TAMARA GRUBB, ADRIENNE STUART, MARY CURRY, and WASHINGTON EDUCATION ASSOCIATION,

Intervenors.

APRIL CLAYTON, an individual; KEVIN BOUCHEY, an individual; RENEE BOUCHEY, an individual; JOANNA CABLE, an individual; ROSELLA MOSBY, an individual; BURR MOSBY, an individual; CHRISTOPHER SENSKE, an individual; CATHERINE SENSKE,

NO. 21-2-00075-09
NO. 21-2-00087-09

DEFENDANTS' MEMORANDUM IN OPPOSITION TO PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT

Noted for February 4, 2022
10:00 a.m.

an individual; MATTHEW SONDEREN, an individual; WASHINGTON FARM BUREAU,

Plaintiffs,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE, an agency of the State of Washington; VIKKI SMITH, in her official capacity as Director of the Department of Revenue,

Defendants.

EDMONDS SCHOOL DISTRICT, TAMARA GRUBB, ADRIENNE STUART, MARY CURRY, and WASHINGTON EDUCATION ASSOCIATION,

Intervenors.

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I. INTRODUCTION

Every one of Plaintiffs' arguments challenging ESSB 5096 is demonstrably wrong under Supreme Court precedent. While Plaintiffs incorrectly claim that the State is asking the Court to reject precedent, in fact it is Plaintiffs who need this Court to ignore binding authority to prevail. The Court should faithfully apply the Constitution and precedent and uphold ESSB 5096.

Plaintiffs' primary argument is that ESSB 5096 violates the dormant Commerce Clause, but their own brief refutes this claim. Plaintiffs raise a facial challenge, meaning they are asking the Court to strike down ESSB 5096 entirely, not just as applied to them. But "a facial challenge must be rejected if there are *any circumstances* where the statute can constitutionally be applied." *Wash. State Republican Party v. Pub. Disclosure Comm'n*, 141 Wn.2d 245, 282 n.14, 4 P.3d 808 (2000) (emphasis added). Plaintiffs admit that the capital gains tax can be applied consistent with the Commerce Clause to capital gains from sales of tangible property in Washington. Pls.' Mot. Summ. J. at 8-9, 12. And of course that is right: if a Washington resident sells a yacht or painting in Washington and earns a $1 million capital gain, there is no Commerce Clause problem with Washington taxing that transaction. Because Plaintiffs admit that the tax can be applied without violating the dormant Commerce Clause in some circumstances, their facial challenge fails.

Even if Plaintiffs could overcome this problem, their Commerce Clause argument would still fail. They claim that Washington cannot tax gains earned by Washington residents from the sale of intangible assets, like stocks and bonds, because the sale might technically occur elsewhere. This theory has never been accepted by any court, would invalidate the taxes imposed on capital gains by virtually every state in America, and ignores United States Supreme Court precedent holding that states have authority to tax intangible property sold or transferred by their residents. *Curry v. McCanless*, 307 U.S. 357, 59 S. Ct. 900, 83 L. Ed. 1339 (1939). In reality, the capital gains excise tax—which includes a credit that prevents multiple taxation—is "internally consistent" and meets every other factor under the Court's dormant

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Commerce Clause test. Plaintiffs' Commerce Clause argument fails under established precedent.

Plaintiffs also incorrectly argue that the tax violates article VII of the Washington Constitution. They say that because selling capital assets generates income, any tax on capital gains must be an income tax. That argument has repeatedly been rejected by our Supreme Court. Selling real estate generates income, but the retail sales tax imposed on buyers is an excise tax. Selling goods generates income for store owners, but the sales tax is an excise tax. When plumbers, carpenters, or barbers sell their services and thereby earn income, they pay the business and occupation (B&O) tax, which is, of course, an excise tax. In short, merely because a transaction generates income does not mean that a tax on that transaction is an income tax. What Plaintiffs are asking for is a special rule exempting the wealthy from taxation of voluntary transactions they commonly engage in—like selling stocks, bonds, or valuable art—while transactions that working people engage in are taxed. The Constitution provides no basis for such a rule.

Finally, Plaintiffs misrepresent the law in arguing that ESSB 5096 violates the Privileges and Immunities Clause of Washington's Constitution. They assert our Supreme Court has recognized a fundamental right of Washington residents to receive any tax exemption available to any other resident. That is simply false, and would call into question tax exemptions favoring seniors and veterans, favoring rural areas, or favoring certain industries, like farming or timber. In any event, even if there were such a rule, our Supreme Court has held that the Legislature has exceptionally broad authority to draw distinctions in creating tax policies and has upheld taxes and tax exemptions that apply to some but not others. Plaintiffs' contrary claim is untenable.

In short, binding precedent refutes every one of Plaintiffs' arguments. The Court should grant summary judgment to the State and reject Plaintiffs' facial challenge to ESSB 5096.

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II. STATEMENT OF MATERIAL FACTS

The material facts are discussed in the State's motion for summary judgment. Plaintiffs' motion, by contrast, includes no facts or evidence about how the capital gains tax will affect them. They do not provide a single example of a transaction they have engaged in, refrained from engaging in, or wish to engage in that would be subject to the tax, and none provides evidence that they will actually be subject to the tax. Instead, Plaintiffs focus primarily on arguing that "income taxes" are unpopular in Washington. *See* Pls.' Mot. Summ. J. at 3. But the capital gains tax is not an income tax, and its constitutionality does not depend on whether Plaintiffs personally agree with it. Under the Constitution, what matters is that ESSB 5096 (codified in Chapter 82.87 RCW) was enacted by a majority vote of our elected legislative leaders, signed into law by the Governor, and advances legitimate policy goals, including funding public education and making the state's tax code less regressive. For that reason, the Court may invalidate the tax only if Plaintiffs prove that there is no "reasonable doubt that the statute violates the constitution." *Amalgamated Transit Union Local 587 v. State*, 142 Wn.2d 183, 205, 11 P.3d 762 (2000). "It is not the function of [the courts] . . . to consider the propriety of the tax, or to seek for the motives or to criticize the public policy which may have prompted adoption of the legislation." *State ex rel. Namer Inv. Corp. v. Williams*, 73 Wn.2d 1, 7, 435 P.2d 975 (1968) (citation omitted).

The State has already described in detail the operation of the tax, State's Mot. Summ. J. at 2-4, and will not repeat that description here, except to say that the Legislature created a detailed allocation process to avoid taxing capital gains that are attributable to another state. RCW 82.87.100. In general, the law allocates to Washington long term capital gains from the sale or exchange of tangible property located in Washington and intangible property owned by an individual domiciled in the state. *Id.* Additionally, all taxpayers are allowed a credit "equal to the amount of any legally imposed income or excise tax paid . . . to another taxing jurisdiction on capital gains derived from capital assets within the other taxing jurisdiction . . .

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." RCW 82.87.100(2)(a). These provisions ensure that capital gains will be taxed only when there is a constitutional nexus with Washington and no other state is lawfully taxing the same gains.

III. ARGUMENTS AND AUTHORITY

No Plaintiff has paid the capital gains tax, and none has shown an existing, non-speculative injury. Accordingly, this Court should dismiss Plaintiffs' complaints for lack of standing alone. *See* State's Mot. Summ. J. at 6-8. But even if Plaintiffs could establish standing, their constitutional claims would fail under established precedent. The capital gains tax easily satisfies dormant Commerce Clause requirements, is not a property tax subject to article VII, and does not violate the Privileges and Immunities Clause. Plaintiffs' challenge fails at every turn.

A. The Capital Gains Tax Meets Dormant Commerce Clause Requirements

Plaintiffs begin their quest to invalidate the capital gains tax by invoking the dormant Commerce Clause. A state tax satisfies the dormant Commerce Clause if it (1) applies to an activity with a substantial nexus with the taxing state, (2) is fairly apportioned, (3) does not impermissibly discriminate against interstate commerce, and (4) is fairly related to services provided by the state. *Wash. Bankers Ass'n v. State*, 198 Wn.2d 418, 429, 495 P.3d 808 (2021) (citing *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274, 279, 97 S. Ct. 1076, 51 L. Ed. 2d 326 (1977)). Plaintiffs contend that the capital gains tax fails the first three elements of this test because it "impermissibly allocates the tax to Washington based on the taxpayer's location instead of where the activity of sale or transfer of the asset occurs, imposes a tax that is not fairly apportioned to activities occurring within the state, and discriminates against interstate commerce." Pls.' Mot. Summ. J. at 7-8.

Plaintiffs are wrong on all counts. First, Plaintiffs concede, as they must, that the dormant Commerce Clause does not preclude applying ESSB 5096 to the sale of tangible property located in the state. *Id*. at 8-9, 12. Because they concede that the tax can constitutionally be applied in some circumstances, their facial challenge fails. But even setting

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that aside, Plaintiffs are simply wrong in arguing that Washington lacks nexus to tax sales by Washington residents. Nor can Plaintiffs show any violation of the fair apportionment or discrimination prongs. The Court should reject their dormant Commerce Clause claim.

1. The capital gains tax properly applies to sales of tangible property located in Washington, so Plaintiffs' facial challenge necessarily fails

Plaintiffs do not and cannot argue that Washington is powerless to tax gains derived from the sale of tangible personal property located in the state. *See Okla. Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 184, 115 S. Ct. 1331, 131 L. Ed. 2d 261 (1995) ("It has long been settled that a sale of tangible goods has a sufficient nexus to the State in which the sale is consummated to be treated as a local transaction taxable by that State."). Plaintiffs correctly concede this issue. Pls.' Mot. Summ. J. at 9-10 (conceding that Washington has nexus to tax, quoting *South Dakota v. Wayfair, Inc.*, ___ U.S. ___, 138 S. Ct. 2080, 201 L. Ed. 2d 403 (2018)); *id.* at 12 (conceding that the tax fairly apportions gains from the sale of tangible property located in the state, citing *Jefferson Lines*).

That concession is fatal to Plaintiffs' dormant Commerce Clause claim. Plaintiffs are challenging the law facially, not "as applied." Pls.' Mot. Summ. J. at 1. A facial challenge is "the most difficult challenge to mount successfully, since the challenger must establish that no set of circumstances exits under which the Act would be valid." *United State v. Salerno*, 481 U.S. 739, 754, 107 S. Ct. 2095, 95 L. Ed. 2d 697 (1987); *see also City of Redmond v. Moore*, 151 Wn.2d 664, 669, 91 P.3d 875 (2004) ("a successful facial challenge is one where no set of circumstances exists in which the statute . . . can be constitutionally applied"). Here, Plaintiffs concede that the statute can be applied in some circumstances without violating the dormant Commerce Clause, so their effort to invalidate ESSB 5096 fails.

When a duly enacted law is challenged on its face, the court must, whenever possible, construe it "'so as to uphold its constitutionality.'" *In re Detention of Danforth*, 173 Wn.2d 59, 70, 264 P.3d 783 (2011) (quoting *State v. Reyes*, 104 Wn.2d 35, 41, 700 P.2d 1155 (1985)).

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Plaintiffs advocate for the exact opposite approach, pointing to a limited circumstance where the tax might not constitutionally apply because the owner of tangible assets has removed the property from the state prior to its sale. Pls.' Mot. Summ. J. at 8 (citing *Curry*, 307 U.S. at 363-64, which holds that *tangible property* is taxable by the state where it is physically located). But Plaintiffs do not know, and cannot show in this facial challenge, whether that circumstance will ever arise. This is so because ESSB 5096 expressly excludes from the tax "[a]mounts that the state is prohibited from taxing under the Constitution of the state or the Constitution or laws of the United States." RCW 82.87.060(2). The Legislature modeled this provision after a similar provision in the B&O excise tax code, *see* RCW 82.04.4286, and it provides the Department of Revenue with authority to apply the tax as constitutionally required. Thus, even if the hypothetical scenario comes to pass that a Washington resident removes tangible assets from the state before selling them at a capital gain exceeding $250,000, and even if Plaintiffs are right that under the specific circumstances of that transaction the state could not constitutionally apply its tax, RCW 82.87.060(2) would require the Department not to apply the tax in that specific situation. If the Department ever sought to tax such a transaction, a taxpayer could bring an as-applied challenge at that time. But that hypothetical possibility provides no basis to strike down the entire statute. *See Woods v. Seattle's Union Gospel Mission*, 197 Wn.2d 231, 240, 481 P.3d 1060 (2021) ("When determining whether a law is facially invalid, courts must be careful not to exceed the facial requirements and speculate about hypothetical cases.") (citation omitted).

In sum, Washington is constitutionally permitted to impose the capital gains excise tax on the sale of tangible property located in the state, as Plaintiffs concede. Because ESSB 5096 can constitutionally apply in this circumstance, Plaintiffs' facial challenge fails.

2. The capital gains tax properly applies to sales of intangible property

Even if Plaintiffs could overcome the concession discussed above, their dormant Commerce Clause argument still fails because ESSB 5096 may constitutionally apply to gains

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earned by Washington residents from the sale of intangible assets, like stocks and bonds. Plaintiffs' claim to the contrary misstates the law and is entirely meritless.

a. The capital gains tax satisfies *Complete Auto's* nexus prong

Plaintiffs first claim ESSB 5096 violates the dormant Commerce Clause because it allocates gains to Washington that are not derived from activity with a nexus to the state. Pls.' Mot. Summ. J. at 9. But Plaintiffs' claim is built on the false premise that intangible property owned by persons domiciled in the state is "located" outside the state. Building on this erroneous premise, they contend that Washington is powerless to tax amounts derived from the sale of intangible property by persons domiciled in the state. *Id*. at 9. Under their misguided narrative, the dormant Commerce Clause precludes Washington from taxing the "'sale or exchange' of certain long-term capital assets simply because the assets' owners are residents of or domiciled in Washington . . . ." *Id*. This claim finds no support under established law, which treats the sale of intangibles as occurring at the place where the owner is domiciled.

The Legislature intentionally used the term "domicile" in RCW 82.87.100(1)(b). "Domicile" is not synonymous with "residence." *Sasse v. Sasse*, 41 Wn.2d 363, 365, 249 P.2d 380 (1952). Every natural person has a domicile, and there is a "settled legal relation" between the person and his or her chosen domicile. *Id*. at 366. Once established, a person's domicile "continues until it is superseded by a new domicile." *Id*. Consequently, a person can have only one domicile at a time. *In re Lassin's Estate*, 33 Wn.2d 163, 165, 204 P.2d 1071 (1949). The term "residence" carries a different connotation, as a person "may have more than one residence at the same time, but only one domicile." 28 C.J.S. Domicile § 5 (Nov. 2021) (footnotes omitted).

Domicile is important in the tax context because intangible personal property is treated as "located" in the state of the owner's domicile. *Greenough v. Tax Assessor of City of Newport*, 331 U.S. 486, 492-93, 67 S. Ct. 1400, 91 L. Ed. 1621 (1947); *In re Eilermann's*

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Estate, 179 Wash. 15, 18, 35 P.2d 763 (1934). Consequently, states have broad authority to impose taxes on the sale or transfer of intangible property owned by a person domiciled in the state. *Curry v. McCanless*, 307 U.S. at 366. The power to sell or dispose of intangible property "is the appropriate subject of taxation at the place of domicile of the owner of the power." *Graves v. Elliott*, 307 U.S. 383, 386, 59 S. Ct. 913, 83 L. Ed. 1356 (1939). Thus, to the extent Plaintiffs argue that Washington has no authority to impose a capital gains tax on the sale or transfer of intangible property because the property is "located" elsewhere, they are plainly wrong under binding precedent. *See, e.g.*, *Curry* 307 U.S. at 366 (the sovereign taxing power of the state extends to intangible property of a domiciled resident even though the intangible has "no physical location within its territory"); *In re Grady's Estate*, 79 Wn.2d 41, 43, 483 P.2d 114 (1971) (citing *Curry* for the proposition that intangibles have their "situs at the domicile of the owner"); *In re Plasterer's Estate*, 49 Wn.2d 339, 342, 301 P.2d 539 (1956) (citing *Curry* as support for upholding inheritance tax imposed on intangible property of a Washington domiciliary).

Plaintiffs also theorize that the capital gains tax lacks a nexus to Washington because certain asset sales that could be included in the Washington tax allegedly "occur[] outside its borders." Pls.' Mot. Summ. J. at 8. But as just explained, United States Supreme Court precedent makes clear that any sales of *intangible* property owned by persons domiciled in Washington are treated as occurring in Washington. And Plaintiffs concede that all sales of *tangible* property located in Washington have a sufficient nexus to the State. That leaves only Plaintiffs' hypothetical claim that the tax might be applied to certain sales of tangible property that occur outside of Washington. Plaintiffs offer no evidence that the State has attempted to tax such a transaction, and if the State ever did, a taxpayer could argue a lack of nexus as to that transaction at that time. The theoretical possibility that the State might seek to tax such a transaction provides no basis to invalidate the tax.

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b. The capital gains tax is fairly apportioned

The central purpose of the fair apportionment requirement "is to ensure that each State taxes only its fair share of an interstate transaction." *Goldberg v. Sweet*, 488 U.S. 252, 260-61, 109 S. Ct. 582, 102 L. Ed. 2d 607 (1989). Consistent with that purpose, the Constitution "imposes no single [apportionment] formula on the States" and instead evaluates a state's apportionment method "by examining whether it is internally and externally consistent." *Id*. at 261 (citations omitted). Internal consistency requires a tax to be structured so that if every state imposed it, no multiple taxation would result. *Id*. In contrast, the external consistency test evaluates the "economic justification for the State's claim upon the value taxed." *Jefferson Lines*, 514 U.S. at 185. Here, the capital gains tax meets both requirements. *See* State's Mot. Summ. J. at 22-23.

Plaintiffs admit that the capital gains tax is internally consistent. *See* Pls.' Mot. Summ. J. at 12 n.8, 13.[1] They claim, however, that the tax lacks external consistency based on their view that Washington is reaching beyond the portion of value that is fairly attributed to economic activity within the state. *Id*. at 12. They further claim that the "risk of multiple taxation" is evidence of such overreach. *Id*. at 13. For multiple reasons, these arguments fail.

First, as explained above, Plaintiffs' claim is built on the false premise that intangible property owned by persons domiciled in the state is "located" outside the state. In reality, binding precedent makes clear that intangible personal property is treated as "located" in the state of the owner's domicile. *Greenough*, 331 U.S. at 492-93; *Eilermann's Estate*, 179 Wash. at 18. And our Supreme Court has held that amounts derived from the sale of property located in Washington are "inherently apportioned" to the state without the need for any further

[1] Indeed, Washington's capital gains tax easily satisfies internal consistency because the tax credit in RCW 82.87.100(2)(a) ensures multiple state taxes would not overlap in a hypothetical world where every state has copied Washington's tax system. *See Goldberg*, 488 U.S. at 264 (Illinois excise tax on full value of interstate telecommunication originating in the state satisfied the fair apportionment requirement as "the credit provision" contained in the state's tax "operates to avoid actual multiple taxation").

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division. *Chicago Bridge & Iron Co. v. Dep't of Revenue*, 98 Wn.2d 814, 830, 659 P.2d 463 (1983). That holding is supported by controlling federal authority, most notably *Jefferson Lines*. There, the Supreme Court rejected the taxpayer's claim that Oklahoma could not tax the entire amount earned from the in-state sale of an interstate bus ticket, holding that the dormant Commerce Clause did not require the state to divide the proceeds among all states where the purchaser would travel. *Jefferson Lines*, 514 U.S. at 186. To the contrary, the Court had "consistently approved taxation of sales without any division of the tax base among different States." *Id*. This was proper because a sale of goods is "most readily viewed as a discrete event facilitated by the laws and amenities of the place of sale." *Id*. Consequently, the state where the sale occurs may properly tax the full amount of the transaction. *Id*.; *see also Tyler Pipe Indus. Inc. v. Dep't of Revenue*, 483 U.S. 232, 251, 107 S. Ct. 2810, 97 L. Ed. 2d 199 (1987) (Washington tax imposed on the full value of sales within the state satisfies fair apportionment requirement because the activity is "conducted wholly within Washington"); *Gen. Motors Corp. v. City of Seattle*, 107 Wn. App. 42, 60, 25 P.3d 1022 (2001) (city's B&O tax on full value of sales occurring therein was properly apportioned).[2]

Moreover, our Supreme Court has expressly rejected the claim that Washington's B&O tax imposed on the sale of property within the state must be apportioned by a statutory formula, calling the argument "[m]eritless" and contrary to settled law. *W.R. Grace & Co. v. Dep't of Revenue*, 137 Wn.2d 580, 596, 973 P.2d 1011 (1999). Plaintiffs can cite no authority suggesting that a different rule should apply to the capital gains tax. In sum, it is settled that the

[2] States imposing broad-based corporate net income taxes have long used a system called formulary apportionment to determine how much of a multistate businesses' profits can be attributed to and taxed by a state. *See, e.g.*, *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 103 S. Ct. 2933, 77 L. Ed. 2d 545 (1983) (discussing with approval California's approach to dividing the income of a multinational corporation using a three-factor formula). But states are not constitutionally required to use a formula to apportion amounts derived from the sale of property. This is well-settled law. *Jefferson Lines*, 514 U.S. at 186; *Chicago Bridge*, 98 Wn.2d at 830.

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state may tax the full value of sales or transfers of property, tangible and intangible, located within its borders.

Additionally, no genuine risk of multiple state taxation exists under the capital gains tax statutes because Washington provides a credit for taxes lawfully paid to another state. RCW 82.87.100(2)(a). Consequently, if another state has jurisdiction to tax the sale of property because it has a situs in both Washington and that other state, Washington will give up its tax. *Id.* Providing a credit for taxes paid to another state is a common and accepted method of avoiding dormant Commerce Clause concerns. *D.H. Holmes Co., Ltd. v. McNamara*, 486 U.S. 24, 31, 108, S. Ct. 1619, 100 L. Ed. 2d 21 (1988); *Steiner v. Utah State Tax Comm'n*, 449 P.3d 189, 194 (Ut. 2019), *cert. denied* 140 S. Ct. 1114 (2020). Importantly, Plaintiffs cite no case in which a court has invalidated a state tax imposed on the sale of intangible property by a person domiciled in the state where, as here, the tax includes a credit mechanism that ensures the sale will be taxed by only one state.

Plaintiffs rely heavily on *Comptroller of Treasury of Maryland v. Wynne*, 575 U.S. 542, 135 S. Ct. 1787, 191 L. Ed. 2d 813 (2015). But that case supports the State's position, not Plaintiffs'. To begin with, *Wynne* invalidated Maryland's tax based solely on the tax failing the "internal consistency" test, *id.* at 561-69, a test that Plaintiffs concede is satisfied here, Pls.' Mot. Summ. J. at 12 n.8, 13. The Court never applied the "external consistency" test relied on by Plaintiffs here, but even if it had, the Maryland tax is obviously and crucially different from Washington's capital gains excise tax.

In *Wynne*, Maryland imposed an individual income tax composed of two parts, "a 'state' income tax . . . and a so-called 'county' income tax." *Id*. at 545-46. The "state" tax included a credit for taxes paid to other states, while the "county" tax did not. *Id.* at 546. Characterizing the Maryland tax system as "unusual," *id*. at 545 and 556, the Supreme Court held that it lacked "internal consistency" because, without a credit for both the state tax and the "so-called county tax" (which was imposed by the state and amounted to an additional state-

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level tax), two states could tax a Maryland resident's income from engaging in interstate commerce. *Id*. at 565. The Court did not suggest that state taxes that provide a full credit, like ESSB 5096 does, are constitutionally suspect. Rather, the Court said just the opposite: "To be sure, Maryland could remedy the infirmity in its tax scheme by offering, as most States do, a credit against income taxes paid to other States. If it did, Maryland's tax scheme would survive the internal consistency test and would not be inherently discriminatory." *Id*. at 568.

Plaintiffs conveniently ignore the obvious distinction between the type of tax at issue in *Wynne* (allowing no credit against Maryland's "county" tax) and tax systems that allow a full credit for taxes paid on amounts that another state has taxed. As an example of the latter type of tax, the Utah Supreme Court in *Steiner* upheld a single tax on income earned by Utah residents that provided a credit for income taxes paid to other states on the same income. 449 P.3d at 194, 197. The Court held that "Utah's provision of credits for income taxes already paid to other states satisfies the dormant commerce requirements set forth in controlling precedent." *Id*. at 194 (footnote omitted). Specifically, "[t]his arrangement satisfies *Wynne's* internal consistency test" because the credit mechanism prevents persons earning income outside the state from "shoulder[ing] a higher tax burden." *Id*. (footnote omitted).

The same is true of the credit provided in the Washington capital gains tax because it prevents Washington and another state from imposing taxes on the same capital gains. RCW 82.87.100(2)(a). This arrangement satisfies *Complete Auto*'s fair apportionment requirement under controlling law. *See D.H. Holmes*, 486 U.S. at 31 ("We have no doubt that the second and third elements of the [*Complete Auto*] test are satisfied. The Louisiana tax scheme is fairly apportioned, for it provides a credit against its use tax for sales taxes that have been paid in other States."); *Goldberg*, 488 U.S. at 264 (Illinois excise tax satisfied fair apportionment requirement as "the credit provision" contained in the law "operates to avoid actual multiple taxation").

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In sum, the capital gains tax easily satisfies "principles of apportionment," as demonstrated by *Jefferson Lines*, *Chicago Bridge*, *W.R. Grace*, and the other controlling authorities discussed above. As those authorities confirm, amounts derived from in-state sales are "inherently apportioned" to the state. And both the United States Supreme Court and our Supreme Court have made clear that Washington has full authority to tax sales of intangible property by persons domiciled in Washington. *See, e.g.*, *Curry* 307 U.S. at 366 (the sovereign taxing power of the state extends to intangible property of a domiciled resident even though the intangible has "no physical location within its territory"); *In re Grady's Estate*, 79 Wn.2d 41, 43, 483 P.2d 114 (1971) (citing *Curry* for the proposition that intangibles have their "situs at the domicile of the owner"); *In re Plasterer's Estate*, 49 Wn.2d 339, 342, 301 P.2d 539 (1956) (citing *Curry* as support for upholding inheritance tax imposed on intangible property of a Washington domiciliary). Additionally, the credit provided in RCW 82.87.100(2)(a) ensures no genuine risk of multiple state taxation, consistent with established "principles of apportionment." Thus, the cited cases demonstrate that dividing the tax base with other states is not required.

c. Plaintiffs fail to show impermissible discrimination

Plaintiffs also assert, without argument, that the capital gains tax fails the discrimination prong of the *Complete Auto* test. Pls.' Mot. Summ. J. at 8. Our Supreme Court recently addressed this prong in *Washington Bankers*, explaining that "discrimination" under *Complete Auto* means "'differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter.'" *Wash. Bankers*, 198 W.2d at 430 (quoting *Filo Foods, LLC v. City of SeaTac*, 183 Wn.2d 770, 809, 357 P.3d 1040 (2015)). Plaintiffs offer no cogent argument that the tax discriminates against interstate commerce. Consequently, the claim fails. *See id*. at 439 ("discrimination requires more than mere assertion that it exists").

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In sum, Plaintiffs' facial challenge under the dormant Commerce Clause fails at every turn. Properly analyzed, the capital gains tax satisfies all dormant Commerce Clause constraints and should be upheld.

B. The Capital Gains Tax is a Valid Excise Tax, Not a Tax on Property

Plaintiffs argue that the capital gains tax is a tax on income, which Plaintiffs then assert is a type of property tax subject to the uniformity and levy limit requirements of article VII, sections 1 and 2. Their argument fails under established law.

1. Under established precedent, the capital gains tax is an excise tax, not a property tax

As Plaintiffs concede, article VII, sections 1 and 2 apply only to property taxes. Pls.' Mot. Summ. J. at 22. This is settled law. *In re Estate of Hambleton*, 181 Wn.2d 802, 832, 335 P.3d 398 (2014) (article VII, section 1 "applies only to property tax and not excise tax"); *High Tide Seafoods v. State*, 106 Wn.2d 695, 725 P.2d 411 (1986); *see also St. Paul & Tacoma Lumber Co. v. State*, 40 Wn.2d 347, 354, 243 P.2d 474 (1952) (timber company's contention that tax imposed on its use of wood products was a property tax "is patently specious"). Thus, any challenge to a tax based on article VII involves a key threshold question: is the challenged tax a property tax? If the answer is no, the analysis ends. *Cosro, Inc. v. Liquor Control Bd.*, 107 Wn.2d 754, 761, 733 P.2d 539 (1987).

Plaintiffs cannot meet this threshold requirement because the capital gains tax is not a property tax under binding Washington Supreme Court precedent. For at least 85 years, the Court has defined a property tax as "'a tax which falls upon the owner *merely because he is owner*, regardless of the use or disposition made of his property.'" *Morrow v. Henneford*, 182 Wash. 625, 631, 47 P.2d 1016 (1935) (emphasis added) (quoting *Bromley v. McCaughn*, 280 U.S. 124, 137, 50 S. Ct. 46, 74 L. Ed. 226 (1929)). By contrast, a tax that applies to the sale, transfer, or use of property is an excise tax, not a property tax. *Id.* at 630. Thus, Washington distinguishes between a tax on the mere ownership of property and a tax on selling,

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transferring, or otherwise exercising power over property. Perhaps the most relevant case applying this principle is *Mahler v. Tremper*, 40 Wn.2d 405, 243 P.2d 627 (1952). There, the Court unanimously upheld the constitutionality of the real estate excise tax, which it deemed an excise tax on the sale of real estate. *See id.* at 407. The Court held the tax was not a property tax because "a tax upon the sale of property is not a tax *upon the subject matter of that sale*." *Id*. at 409 (emphasis added). Instead, the real estate excise tax—which applies to sales of real property—applied "upon the act or incidence of transfer. The imposition relates to an exercise of one of several rights in and to property. Imposition is not upon each and every owner merely because he is the owner of the property involved." *Id*. at 410.

Numerous cases have applied this same principle. *See* State's Mot. Summ. J. at 10-15 (discussing cases). In the 1990s, the Court distilled this principle into a simple test: A property tax is an "absolute and unavoidable demand against property or the ownership of property" that arises merely from the taxpayer's "status as property owner[.]" *Covell v. City of Seattle*, 127 Wn.2d 874, 890, 905 P.2d 324 (1995), *abrogated on other grounds by Yim v. City of Seattle*, 194 Wn.2d 682, 451 P.3d 694 (2019). In contrast, an excise tax "'is based upon the voluntary action of the person taxed in performing the act, enjoying the privilege or engaging in the occupation which is the subject of the excise, and the element of absolute and unavoidable demand, as in the case of a property tax, is lacking.'" *Black v. State*, 67 Wn.2d 97, 99, 406 P.2d 761 (1965) (quoting 1 Cooley, *Taxation* § 46, at 132 (4th ed. 1924)).

Under the above test, the capital gains tax is not a property tax. It is neither absolute nor unavoidable as it applies only upon voluntary sales of long-term capital assets. Consequently, the limitations in article VII do not apply.

Plaintiffs make no effort to address the analysis our Supreme Court has applied for the past 85 years. They do not even cite *Morrow*, *Mahler*, *Black*, *Covell*, or other cases in which the Court carefully analyzed whether a challenged tax was an "absolute and unavoidable demand against property." Instead, they primarily rely on fractured decisions in *Culliton v.*

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Chase, 174 Wash. 363, 25 P.2d 81 (1933), and *Jensen v. Henneford*, 185 Wash. 209, 212, 53 P.2d 607 (1936). *See* Pls.' Mot. Summ. J. at 17-18.[3] But these cases involved annual net income taxes that applied broadly to all amounts received during the tax year, and not just amounts derived from sales of property—which the Court has consistently upheld as valid excise taxes. *See Morrow*, 182 Wash. 625 (tax on sales of personal property is an excise tax); *Mahler*, 40 Wn.2d 405 (tax on sales of real property is an excise tax). Neither case held that a tax on the *sale or transfer of property* is a tax on the property itself. In fact, when our Supreme Court decided *Culliton* and *Jensen* in the early 1930s, it had already concluded that a tax on the sale of property is an excise tax, not a tax on the property itself. *See Standard Oil Co. v. Graves*, 94 Wash. 291, 306, 162 P. 558 (1917), *rev. on other grounds*, 249 U.S. 389, 39 S. Ct. 320, 63 L. Ed. 662 (1919) (oil inspection fee imposed "only upon the contingency that the oil is sold or offered for sale" is an excise tax). Neither *Culliton* nor *Jensen* called into question that prior precedent. And numerous cases decided after *Culliton* and *Jensen* followed this uninterrupted principle that a tax on the sale or transfer of property is an excise tax.

Plaintiffs' only other argument is a simplistic and deeply flawed syllogism. They say that capital gains are income, and income taxes are property taxes, therefore capital gains taxes must be property taxes. Pls.' Mot. Summ. J. at 15. But this argument is obviously wrong under Supreme Court precedent. Many types of transactions generate income, from a shopkeeper selling goods to a carpenter selling services to a property owner selling a building. But that does not mean that a tax on these transactions is an income tax. To give an obvious example, nearly every small business owner in the state, from carpenters to plumbers to hairdressers, pays B&O tax on their gross revenue, even though that revenue is undeniably income. Yet the Supreme Court has long held that the B&O tax is an excise tax. *See State ex rel. Stiner v. Yelle*,

[3] The "majority" in *Culliton* consisted of a two-member lead opinion authored by Justice Holcomb, a two-member concurring opinion authored by Justice Mitchell, and a concurring opinion from Justice Steinert. In *Jensen*, Justice Steinart authored a four-justice plurality opinion and Justice Millard concurred solely on *stare decisis* grounds. 185 Wash. at 225.

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174 Wash. 402, 407, 25 P.2d 91 (1933) (in upholding the B&O tax against an article VII challenge, the Court explained that merely because "the amount of the tax is measured by the amount of . . . income [received] in no way affects" its proper classification as an excise tax). Similarly, a property owner may earn significant income from selling a piece of property, yet the real estate excise tax applying to that sale is still an excise tax. *Mahler*, 40 Wn.2d at 409-10. Plaintiffs essentially ask this Court to ignore all of this precedent, with the outcome that rich people who generate significant income from selling stocks and bonds would get a special rule exempting them from being taxed on these voluntary transactions. There is no support for such a ruling.

In short, the capital gains tax is an excise tax under controlling Washington authority and thus is not subject to article VII's limits on property taxes. Plaintiffs' claim to the contrary is "patently specious." *St. Paul & Tacoma Lumber Co.*, 40 Wn.2d at 354.

2. The capital gains tax on the voluntary sale of assets does not become a property tax because other states have elected to tax capital gains differently

Because Plaintiffs cannot possibly prevail under the reasoning and legal principles established by our Supreme Court, they offer a new test. They contend the capital gains tax must be an income tax because that is how the federal government and most states have elected to tax capital gains. Pls.' Mot. Summ. J. at 17, 19-20. This argument fails on two levels.

First, whether the capital gains excise tax is a property tax under Washington's Constitution is a matter of Washington law, not an issue determined by the vagaries of other jurisdictions' tax laws. As explained above, a tax on the voluntary sale of capital assets is an excise tax under controlling Washington law. And the Legislature justifiably followed Washington law when enacting ESSB 5096.

Second, if Plaintiffs were correct that federal law or the law of other states was controlling, they would lose, because case law from those jurisdictions shows that they would uniformly reject Plaintiffs' claim that capital gains taxes are property taxes. Plaintiffs'

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argument, which is based entirely on non-judicial statements, Pls.' Mot. Summ. J. at 20 (citing Mercier Decl.),[4] skips the key question: is the capital gains tax a "tax on property" under article VII? They assert that Washington's capital gains tax cannot be an excise tax because most states treat capital gains taxes as income taxes. What they ignore is that the federal government and the same other states they rely on so fervently *treat income taxes as excise taxes*.

As the United States Supreme Court noted in the late 1930s, the vast majority of states have expressly held that an income tax is a form of excise tax, not a property tax. *Hale v. Iowa State Bd. of Assessment & Revenue*, 302 U.S. 95, 104 n.7, 58 S. Ct. 102, 82 L. Ed. 72 (1937). The Court also explained that "decisions of our own court . . . [support] the classification of a tax upon net income as something different from a property tax." *Id*. at 105-06 (citations omitted). Since the 1930s, even more states have expressly held that an income tax is a form of excise tax, not a property tax. *See Dooley v. City of Detroit*, 121 N.W.2d 724, 728 (Mich. 1963) (citing cases); *see also Thorpe v. Mahin*, 250 N.E.2d 633, 635 (Ill. 1969) ("We have reviewed the many State cases dealing with this question and find the weight of authority to be that an income tax is not a property tax."). If the legal reasoning of our Sister States and the United States Supreme Court is applied, the logical conclusion would be that income taxes are not property taxes. Thus, even if Plaintiffs were correct that the capital gains tax is an income tax under Washington law (which it is not), the capital gains tax still would not be a property tax subject to article VII.[5]

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[4] Plaintiffs generally rely on the Mercier declaration for their statements of out-of-state "authority." But the Mercier declaration consists of collected correspondence with various non-judicial state and federal employees across the country, all of which are inadmissible hearsay. "A court cannot consider inadmissible evidence when ruling on a motion for summary judgment." *Dunlap v. Wayne*, 105 Wn.2d 529, 535, 716 P.2d 842 (1986). Defendants move to strike the Mercier declaration and its exhibits in their entirety.

[4] The overwhelming weight of authority holding that an income tax is a form of excise tax shows how misleading it is to ask other states and the federal government whether a tax on capital gains is an income tax or an excise tax. *See* Pls.' Mot. Summ. J. at 20. There simply is no substantive distinction within those jurisdictions between an income tax and an excise tax. A more telling question would be to ask other states and the federal government whether they consider a tax on capital gains to be a *property tax*. The State is unaware of any federal or state authority supporting the idea that a tax on capital gains is a type of property tax.

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The Court need not follow Plaintiffs down their "other jurisdictions" rabbit hole. What matters here is Washington law, under which the capital gains tax is not a property tax because it is not an "absolute and unavoidable demand against property or the ownership of property" arising from the taxpayer's "status as property owner." *Covell*, 127 Wn.2d at 890. That ends the inquiry. *Cosro*, 107 Wn.2d at 761.

3. The capital gains tax has the "hallmarks" of an excise tax

Plaintiffs next argue that the capital gains tax "bears hallmarks" of an income tax, which they claim overrides the Legislature's characterization of the tax as an excise tax. Pls.' Mot. Summ. J. at 20-22. Plaintiffs' argument misses the mark. Washington courts determine the true nature of a challenged tax based on how it operates in practice, not on whether it may have features in common with some other jurisdiction's tax. Properly analyzed, the capital gains tax operates in practice as an excise tax. It is imposed on the voluntary act of selling non-exempt capital assets, and the "element of absolute and unavoidable demand, as in the case of a property tax, is lacking." *Black*, 67 Wn.2d at 99. The tax is not on *ownership* of the capital asset, which is what makes a property tax unavoidable.

Plaintiffs are wrong when they contend that the capital gains tax is unlike other excise taxes enacted by the state. Pls.' Mot. Summ. J. at 20. Like Washington's retail sales tax upheld in *Morrow* and real estate excise tax upheld in *Mahler*, the capital gains tax is imposed on the voluntary sale of property located in the state. Further, our Supreme Court has long held that excise taxes may be measured by income generated from the activity or transaction being taxed. This principle goes back nearly 90 years, when the Court upheld the state's first B&O tax, which was measured by the gross income generated from in-state business activity. *State ex rel. Stiner v. Yelle*, 174 Wash. 402, 25 P.2d 91 (1933). "[T]hat the amount of the tax is measured by the amount of . . . income in no way affects the purpose of the [tax] or the principle" that the state may tax the privilege of acquiring income from in-state business activity. *Id*. at 407.

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Plaintiffs also go astray when they assert that the capital gains tax must be an invalid property tax simply because it is "geared" or "tethered" to definitions and concepts from the federal income tax code. Pls.' Mot. Summ. J. at 19, 21.

First, the federal income tax is considered a type of excise tax, not a property tax. *See Hale,* 302 U.S. at 104; *see generally Graves v. People of State of N.Y. ex rel. O'Keefe*, 306 U.S. 466, 480, 59 S. Ct. 595, 83 L. Ed. 927 (1939) ("The theory, which once won a qualified approval, that a tax on income is legally or economically a tax on its source, is no longer tenable . . . ."). It is illogical to assert that Washington's capital gains tax is invalid simply because it employs terminology from the federal tax code when that federal tax, under federal law, is a form of excise tax and not a property tax.

Second, our Supreme Court has already held that Washington's estate tax is an excise tax, even though it, too, is tethered to federal law in a variety of ways. *Estate of Ackerley v. Dep't of Revenue*, 187 Wn.2d 906, 912, 389 P.3d 583 586 (2017) (citing *Estate of Hambleton*, 181 Wn.2d at 811). As one noteworthy example, Washington's estate tax uses the "federal taxable estate" as the starting place for computing the tax. *See* RCW 83.100.020(15) (defining "Washington taxable estate" as starting with "federal taxable estate"). In both the capital gains tax and the estate tax, the Legislature had valid reasons for using federal terminology that have nothing to do with whether the tax is a property tax or an excise. As our Supreme Court explained in analyzing Washington's estate tax, by using "federal taxable estate" as the starting point for computing the "Washington taxable estate," the Legislature "avoided having to duplicate congressional effort involved in explaining all the possible inclusions, exemptions, and deductions necessary to reach the taxable estate, and also helped to avoid the complication and confusion that a different set of state rules might create." *In re Estate of Bracken*, 175 Wn.2d 549, 583, 290 P.3d 99 (2012) (Madsen, C.J., concurring/dissenting), superseded by statute as stated in *Estate of Hambleton*, 181 Wn.2d at 809. A similar benefit is achieved under the capital gains tax. Persons subject to the tax are not required to start from scratch; they can start with an amount

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computed and reported on their federal tax return. Additionally, the Legislature avoids duplicating congressional efforts and all the "complication and confusion that a different set of state rules might create." *Id*. This sound tax policy should not be turned into a constitutional liability.

Plaintiffs' additional arguments pertaining to deductions allowed under the capital gains tax code and the distinction between individual taxpayers and corporations are all inconsequential. The Legislature has "very extensive powers to make classifications for purposes" of regulatory laws, *Sonitrol NW, Inc. v. City of Seattle*, 84 Wn.2d 588, 590, 528 P.2d 474 (1974), and those powers are "greater . . . in making classifications for taxation than . . . for regulations." *Texas Co. v. Cohn*, 8 Wn.2d 360, 375, 112 P.2d 522 (1941); *see also Commonwealth Title Ins. Co. v. Tacoma*, 81 Wn.2d 391, 395, 502 P.2d 1024 (1972) ("[T]he legislative power is particularly broad in the area of taxation. It is inherent in the exercise of the power to tax that a state be free to select the objects or subjects of taxation and to grant exemptions. Neither due process nor equal protection imposes upon a state any rigid rule of equality of taxation."). The Legislature acts entirely within its proper sphere of authority when it authorizes deductions and exemptions to excise tax laws.

Moreover, our Supreme Court has already held that there is no constitutional problem with imposing excise taxes on certain activities or transactions while exempting others. *Supply Laundry Co. v. Jenner*, 178 Wash. 72, 34 P.2d 363 (1934). Importantly, *Supply Laundry* involved (among other things) an excise tax measured by wages earned by public employees while exempting wages earned by private employees. *Id*. at 78. Without dissent, the Court upheld that distinction. *Id.* at 80. As *Supply Laundry* confirms, the Legislature did not overstep its authority when it included within the capital gains excise tax a deduction for charitable contributions or when it limited the tax to individuals that have long term capital gains exceeding $250,000.

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In sum, the capital gains tax is exactly what the Legislature says it is, an excise tax on the voluntary sale of capital assets. That the tax may use some federal terms and forms does not transform it into an income tax.

4. Stare decisis supports the State, not Plaintiffs

While Plaintiffs assert this Court must follow controlling Supreme Court authority, they fail to address the pertinent authority that controls here. Applying the proper precedent requires ruling for the State.

Plaintiffs rely on the holdings in *Culliton* and *Jensen*. Pls.' Mot. Summ. J. at 24-25. But, as discussed above, these cases are inapposite as both involved unavoidable taxes on the receipt of income during the taxable year, not taxes on the voluntary sale of property.

The authority that actually controls here, but that Plaintiffs never discuss, is the long line of cases from our Supreme Court upholding taxes on the voluntary sale, transfer or use of property as excise taxes. Plaintiffs' proposed test—that looks to how other jurisdictions elect to tax capital gains—does not and cannot control over the test actually applied by our Supreme Court in *Morrow*, *Mahler*, *High Tide Seafoods*, *Hambleton*, and numerous other cases.

Our Supreme Court has established a clear path for deciding this case. Under controlling Washington law, the capital gains tax is an excise tax because it is not an "absolute and unavoidable demand against property or the ownership of property." Plaintiffs ask this court to ignore applicable precedent, not to apply it. The Court should decline.

C. ESSB 5096 Does Not Violate Article I, Section 12

Plaintiffs' final argument theorizes that ESSB 5096 violates article I, section 12 of the state Constitution by "impermissibly tax[ing] certain persons while exempting others." Pls.' Mot. Summ. J. at 25. Their argument misrepresents the law and is meritless.

Article I, section 12 provides that "[n]o law shall be passed granting to any citizen, class of citizens, or corporation other than municipal, privileges or immunities which upon the same terms shall not equally belong to all citizens, or corporations." The purpose of this

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provision is "to limit the sort of favoritism [towards special interests] that ran rampant during the territorial period." *Martinez-Cuevas v. DeRuyter Bros. Dairy, Inc*., 196 Wn.2d 506, 514, 475 P.3d 164 (2020). As described in the State's opening brief, courts apply a two-step analysis. First, the court asks whether the law grants a "privilege" or "immunity" within the meaning of the constitution. *Schroeder v. Weighall*, 179 Wn.2d 566, 572–73, 316 P.3d 482 (2014). If the answer is yes, then it asks whether there is a "reasonable ground" for granting that privilege or immunity. *Id*.

Here, Plaintiffs' challenge fails at the first step: they identify no "privilege" or "immunity" protected under article I, section 12. It is well settled that "[n]ot every benefit constitutes a 'privilege' or 'immunity' for purposes of the independent article I, section 12 analysis." *Schroeder*, 179 Wn.2d at 573. Rather, "privileges" or "immunities" are only "those fundamental rights which belong to the citizens of [Washington] by reason of such citizenship." *Grant Cnty. Fire Prot. Dist. No. 5 v. City of Moses Lake*, 150 Wn.2d 791, 813, 83 P.3d 419 (2004) (quoting *State v. Vance*, 29 Wash. 435, 458, 70 P. 34 (1902)).

Plaintiffs seriously misrepresent the law when they claim that our Supreme Court has long held that there is a fundamental right to be exempt from taxes that "others in the state are" exempt from. Pls.' Mot. Summ. J. at 26.[6] To support this proposition, Plaintiffs cite *Vance* and *Grant County*, but neither holds anything of the sort. *Vance* was a murder case, not a tax case, and in passing the Court listed as an example of fundamental rights the right to be exempt from taxes that "citizens *of some other state* are exempt from." *Vance*, 29 Wash. at 458 (emphasis added). The right being described restricts taxes that arbitrarily favor out-of-state interests over similarly situated in-state interests, or vice versa.[7] *Grant County* simply quoted the same

[6] It is settled law that there is no fundamental right to be free from taxes. *See City of Seattle v. Rogers Clothing for Men, Inc.*, 114 Wn.2d 213, 234, 787 P.2d 39 (1990) ("Legislative bodies have extensive authority to make classifications for purposes of legislation and even broader discretion in making classifications for taxation than it has for regulation.").

[7] *See generally Allied Stores of Ohio, Inc. v. Bowers*, 358 U.S. 522, 529, 79 S. Ct. 437, 3 L. Ed. 2d 480 (1959) (holding no violation of Equal Protection Clause where a state tax that favored nonresidents was founded on reasonable distinctions and not "palpably arbitrary").

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language in passing. 150 Wn.2d at 813. Neither case holds or suggests that Washington residents have a fundamental right to be exempt from state taxes merely because the Legislature has enacted rational exemptions that apply to other Washington residents. Indeed, taking Plaintiffs' argument to its logical conclusion, any state tax applicable to some residents but not others (such as the estate tax, B&O tax, or the leasehold excise tax) would implicate a "fundamental right" under the Privileges and Immunities Clause. That simply is not the law.

Because Plaintiffs identify no fundamental right of state citizenship implicated by ESSB 5096, their article I, section 12 challenge fails at the first step. *See Ass'n of Wash. Spirits & Wine Distrib. v. Wash. State Liquor Control Bd.*, 182 Wn.2d 342, 363, 340 P.3d 849 (2015) ("Because this case does not involve a constitutional privilege, we need not analyze the second prong of our article I, section 12 test . . .").

Even if ESSB 5096 implicated a recognized "privilege or immunity" of state citizenship (which it does not), Plaintiffs' article I, section 12 challenge would fail because reasonable grounds exist for the distinctions drawn therein. For example, Plaintiffs never argue that it violates article I, section 12 for the Legislature to exempt from the capital gains tax retirement accounts, or gains of less than $250,000 annually, because these exemptions advance legitimate goals, including the Legislature's stated purpose to "mak[e] material progress toward rebalancing the state's tax code" to make it less regressive. *See Cohn*, 8 Wn.2d at 386–87 (listing "the equalization of the burdens of taxation" as a "lawful taxing policy of the state"); *see generally Wash. Bankers*, 198 Wn.2d at 444 (upholding tax law that "asked the wealthy few to contribute more to funding essential services and programs to the benefit of all Washingtonians").

Plaintiffs' sole claim is that the Legislature lacked reasonable grounds to impose the capital gains excise tax on *individuals* but not on corporations or other non-natural persons.

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Pls.' Mot. Summ. J. at 27. But they cite no relevant authority for this claim,[8] nor does the law support it. States have broad leeway in "making classifications and drawing lines which in their judgment produce reasonable systems of taxation." *Lehnhausen v. Lake Shore Auto Parts Co*., 410 U.S. 356, 359, 93 S. Ct. 1001, 35 L. Ed. 2d 351 (1973). "Indeed, in taxation, even more than in other fields, legislatures possess the greatest freedom in classification." *General Motors Corp. v. Tracy*, 519 U.S. 278, 311, 117 S. Ct. 811, 136 L. Ed. 2d 761 (1997) (internal quotations and citation omitted). Consistent with this view, our Supreme Court has held that the Legislature "has the power to make reasonable and natural classifications for purposes of taxation, and that in the exercise of this power the legislature has very broad discretion in making such classifications." *Hemphill v. Wash. State Tax Comm'n*, 65 Wn.2d 889, 891, 400 P.2d 297 (1965). Stated another way, "'[a] legislature is not bound to tax every member of a class or none.'" *Id*. at 892–93 (quoting *Carmichael v. S. Coal & Coke Co*., 301 U.S. 495, 509, 57 S. Ct. 868, 81 L. Ed. 1245 (1937)). The difference between classes "need not be great" and a particular tax classification may "be permissible if it is reasonably related to some lawful taxing policy of the state, such as greater ease or economy in the administration or collection of a tax, the selection of a fruitful source of revenue with the exemption of sources less promising, or the equalization of the burdens of taxation." *Cohn*, 8 Wn.2d at 386–87.

Under this principle, our Supreme Court has repeatedly rejected arguments similar to those Plaintiffs make here, i.e., that excise taxes applicable to some groups but not others violate the Constitution. *See, e.g., United Parcel Serv., Inc. v. Dep't of Revenue*, 102 Wn.2d 355, 367–69, 687 P.2d 186 (1984) (upholding exemption from use tax for vehicles carrying cargo across state lines); *Black*, 67 Wn.2d at 100–01 (upholding retail sales tax on lease of vessel as floating hotel although land-based hotels were not taxed in a similar manner);

[8] Plaintiffs cite *Comptroller of Treasury of Md. v. Wynne*, 575 U.S. 542, but the Supreme Court's discussion of individual versus corporate income there was made in the context of holding that the dormant Commerce Clause does not treat individuals less favorably than corporations. *Id*. at 553–54. *Wynne* did not involve Washington's Privileges and Immunities Clause.

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Hemphill, 65 Wn.2d at 891–94 (upholding exemption of bowling from a sales tax applied to the amusement industry); *Armstrong v. State*, 61 Wn.2d 116, 119–22, 377 P.2d 409 (1962) (upholding the application of a B&O tax to general insurance agents, despite the fact that their counterparts working in insurance company branch offices were not so taxed).

The Legislature in ESSB 5096 addressed a genuine concern that Washington's low and middle income families pay a disproportionate share of their incomes in taxes as compared to its wealthiest residents. Imposing a capital gains tax on those with gains beyond a quarter million dollars annually is a reasonable step toward equalizing the tax burden as between individuals. *See Cohn*, 8 Wn.2d at 386–87. That the Legislature imposed the tax upon individuals and not corporations does not violate article I, section 12. *Cf. Lehnhausen*, 410 U.S. at 362–65 (state constitutional provision subjecting corporations and similar entities, but not individuals, to ad valorem tax on personal property was within state's wide latitude in making classifications that in its judgment produce reasonable taxation systems, and did not violate equal protection). The Court should reject Plaintiffs' misguided claim that it does.

IV. CONCLUSION

Plaintiffs have failed to meet their burden of showing beyond a reasonable doubt that the Legislature's enactment of the capital gains excise tax is unconstitutional, so it should be upheld.

DATED this 7th day of January, 2022.

ROBERT W. FERGUSON
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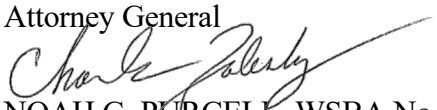

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I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED this 7th day of January, 2022, at Tumwater, WA.

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