Legal Memorandum

To Citizen Action Defense Fund

From Rob McKenna

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Re SSB 6346-S Is an Unconstitutional Property Tax

Based on nearly a century of Washington Supreme Court precedent and the plain language of the Washington State Constitution, SSB 6346-S is unconstitutional because it imposes a graduated income tax that (1) violates the uniformity requirement of Article VII, Section 1 and (2) exceeds the 1% aggregate property tax limit established by Article VII, Section 2. Under binding Washington precedent going back a century, and reiterated recently by our current Supreme Court, any tax on income must comply with these foundational constitutional requirements applicable to all property taxes.

II. CONSTITUTIONAL FRAMEWORK

In 1930, Washington voters adopted Constitutional Amendment 14, (const. art. VII, sec. 1), the property tax "uniformity" clause, which provides:

> All taxes shall be uniform upon the same class of property within the territorial limits of the authority levying the tax and shall be levied and collected for public purposes only. The word 'property' as used herein shall mean and include *everything, whether tangible or intangible, subject to ownership*.

This definition of "property" is, by design, extraordinarily comprehensive. As the Washington Supreme Court observed in *Culliton v. Chase*: "It would certainly defy the ingenuity of the most profound lexicographer to formulate a more comprehensive definition of 'property.' It is 'everything, whether tangible or intangible, subject to ownership.'" The purpose of Amendment 14 was to expand the reach of property taxes to intangible forms of property, including stocks, bonds, and money, which had previously evaded taxation.

Taxes on income must comply with the constitutional limitations of property taxes. Article VII, Section 2 of the Washington Constitution provides that "the aggregate of all tax levies upon real and personal property by the state and all taxing districts" may not exceed 1% annually. Any property tax must comply with both requirements: (1) uniformity within classes of property under Section 1, and (2) the aggregate 1% rate limit under Section 2.

III. BINDING PRECEDENT: INCOME IS PROPERTY UNDER WASHINGTON LAW

A. *Culliton v. Chase* (1933): The Foundational Decision

The Washington Supreme Court's seminal decision interpreting Amendment 14 came in *Culliton v. Chase*, 174 Wash. 363, 25 P.2d 81 (1933). In *Culliton*, voters had passed a statewide initiative levying a graduated tax on net income. Taxpayers challenged the initiative, arguing the graduated income tax was unconstitutional because it taxed property and therefore violated the uniformity clause in Article VII, Section 1.

The court held that under the Constitution's plain language, income is property, and any tax on income is a tax on property subject to the uniformity requirement:

> Income is either property under our Fourteenth Amendment, or no one owns it… No more positive, precise, and compelling language could have been used than was used in those words of our Fourteenth Amendment. It needs no technical construction to tell what those words mean. The overwhelming weight of judicial authority is that 'income' is property and a tax upon income is a tax upon property."

Critically, *Culliton* rested on the interpretation of the Washington Constitution's own "peculiarly forceful" language. [9] As the court explicitly stated: "None of the decisions from other states have any bearing upon the law before us, because of our peculiarly forceful constitutional definition and the difference in their constitutional authorization or restriction." [10]

The *Culliton* court examined the Washington Constitution's broad constitutional definition of property, distinguished that definition from other states' constitutions, and relied on the plain language of Amendment 14. [12] Contrary to a revisionist history concocted by UW Law Professor Hugh Spitzer in a 1993 law review article that has never been adopted by any court, this interpretation was not based on reliance on a federal case that was later overruled on entirely unrelated equal protection grounds. [10] [11]

B. *Jensen v. Henneford* (1936): Reaffirming *Culliton* Based on Constitutional Text

In 2022, the Legislature enacted an excise tax on Washington capital gains that was upheld by the Supreme Court. The Legislature has not attempted to avoid property tax limitations by characterizing the income tax on millionaires as an “excise tax” for the “privilege” of earning income as a Washington resident. Even if it had, that legislative strategy has been forcefully and forever foreclosed.

Just three years after *Culliton*, the Washington Supreme Court reaffirmed its holding in *Jensen v. Henneford*, 185 Wash. 209, 53 P.2d 607 (1936). [13] In *Jensen*, the State levied a graduated income tax on "every resident of [Washington] for the privilege of receiving income therein while enjoying the protection of its laws." [14] The State argued this constituted an excise tax not subject to the Constitution's uniformity clause. [15] The court rejected this argument. Because *Culliton* established that the broad definition of property in Article VII, Section 1 encompassed income, the purported excise tax was in fact an income tax subject to the uniformity clause. [17] As the *Jensen* court explained:

> The right to receive, the reception, and the right to hold are progressive incidents of ownership and indispensable thereto. To tax any one of these elements is to tax their sum total, namely, ownership, and therefore the property (income) itself.

Justice Millard, who had originally dissented in an earlier case, felt bound to respect stare decisis in *Jensen*:

> We held in [*Aberdeen* and *Culliton*], that, under our Constitution, income is property, and that an income tax is a property tax. From that declaration this court has never departed, and the people have not seen fit to amend the Constitution to permit us to hold otherwise. …Surely, the rule of stare decisis-a rule whereby uniformity, certainty, and stability in the law are obtained-should now apply.

C. Subsequent Decisions Consistently Apply *Culliton*

The Washington Supreme Court has consistently reaffirmed the rule that income is property for nearly a century:

Petroleum Navigation Co. v. Henneford, 185 Wash. 495, 55 P.2d 1056 (1936): Tax on a "corporation's net income" is "a property tax" and "subject to the uniformity clause." [18]

Power, Inc. v. Huntley, 39 Wn.2d 191, 235 P.2d 173 (1951): "It is no longer subject to question in this court that income is property." The court had "no hesitancy" in finding that a tax on "almost any income from almost every source" was "a mere property tax 'masquerading as an excise.'" [19]

Apartment Operators Ass'n of Seattle, Inc. v. Schumacher, 56 Wn.2d 46, 351 P.2d 124 (1960): "Is the tax [on rental income] an excise tax or a property tax? The question is foreclosed by prior decisions of this court."

Harbour Village Apartments v. City of Mukilteo, 139 Wn.2d 604, 989 P.2d 542 (1999): Relying on *Jensen*, the court held a tax on rental income is a tax on property that violates the constitutional prohibition against non-uniform taxation. [20]

Kunath v. City of Seattle, 10 Wn. App. 2d 205, 444 P.3d 1235 (2019): Seattle's graduated tax on residents' income violated Article VII, Section 1.

The rule is firmly established: "Today, *Culliton* stands for the now-axiomatic proposition that 'income [is] 'property' under amendment 14 of the state constitution.'" [21]

D. The Supreme Court is Constrained from Overturning a Century of Precedent It Recently Reaffirmed

Hope that the Washington Supreme Court will overturn nearly a century of precedent to allow an income tax is misplaced, based on the Court's recent decision in *Quinn v. State*, No. 100769-8 (Wash. Mar. 24, 2023). In *Quinn*, the Court did uphold the capital gains tax at issue there, but it went out of its way to distinguish that excise tax on capital asset transactions from the longstanding precedent forbidding graduated income taxes.

The *Quinn* majority relied heavily on its earlier decision in *Power, Inc. v. Huntley* to distinguish an excise tax on capital gains from a property tax on income. In *Power v. Huntley*, the court had "no hesitancy in saying that an analysis of the present act convinces us that the [business income] tax is a mere property tax 'masquerading as an excise.'" The fatal defect in *Power* was that the tax "has no reference to income from the various business activities on which the business and occupation tax, a true excise tax, is based, but taxes almost any income from almost every source." In other words, a broad-based net income tax capturing "almost any income from almost every source" is necessarily a property tax subject to Article VII's uniformity and rate limitations.

The *Quinn* majority distinguished the capital gains tax from the unconstitutional income taxes in *Culliton*, *Jensen*, and *Power* precisely because the capital gains tax was *not* a broad-based income tax:

> This court once remarked there is no "precise line" separating property and excise taxes. *Morrow v. Henneford*, 182 Wash. 625, 628, 47 P.2d 1016 (1935). But over the course of decades, that line has sharpened. A survey of our cases reveals we have articulated and consistently applied certain key principles for distinguishing property taxes from excise taxes. Applying those principles here, the capital gains tax falls squarely on the excise side of the line because it taxes transactions involving capital assets—not the assets themselves or the income they generate.

The Court then cited with approval the line of cases holding income to be property:

> In 1930, this court ruled in *Aberdeen* that a corporate income tax violated federal equal protection guaranties. 157 Wash. at 365. Three years later, the court issued its landmark decision in *Culliton*, addressing the constitutionality of a newly enacted graduated personal income tax passed by voters through popular initiative. Relying in part on *Aberdeen*, the court held that income is "property" within the meaning of our state constitution, so an income tax must comply with the uniformity and levy requirements of article VII, sections 1 and 2 of the Washington Constitution. *Culliton*, 174 Wash. at 376 (invalidating graduated personal income tax for lack of uniformity). Since *Culliton*, Washington appellate courts have reaffirmed that holding, consistently striking down graduated net income taxes as unconstitutional, nonuniform property taxes. *See Jensen v. Henneford*, 185 Wash. 209, 211, 215, 53 P.2d 607 (1936) (plurality decision) (personal net income tax); *Petrol. Navigation Co. v. Henneford*, 185 Wash. 495, 495-96, 55 P.2d 1056 (1936) (corporate net income tax); *Power, Inc. v. Huntley*, 39 Wn.2d 191, 193-95, 235 P.2d 173 (1951) (corporate net income tax); *Kunath*, 10 Wn. App. 2d at 211, 232 (personal net income tax). What all of

> these taxes had in common was that they imposed a broad-based net income tax, capturing “almost any income from almost every source.” *Power, Inc.*, 39 Wn.2d at 197.

The Court’s distinction is obviously fatal to SSB 6346-S. Unlike the narrow excise tax on the privilege of selling capital assets upheld in *Quinn*, SSB 6346-S is precisely the type of broad-based income tax that the *Quinn* court acknowledged remains unconstitutional under *Power v. Huntley* and numerous other binding decisions. SSB 6346-S taxes "Washington taxable income," defined by reference to federal adjusted gross income. It captures income from virtually any source-wages, salaries, business income, investment income, and all other forms of income reported on federal income tax returns. This is the quintessential broad-based net income tax that *Power* declared unconstitutional because it taxes "almost any income from almost every source."

The *Quinn* decision thus provides no shelter for SSB 6346-S-it confirms its unconstitutionality and reaffirms the Court’s reliance on longstanding precedent holding non-uniform income taxes with rates exceeding 1% to be unconstitutional. As Justice Gordon McCloud observed in dissent in *Quinn*: "Deciding whether to retain our regressive tax structure or to replace it with a more equitable one is up to the legislature through legislation and the people through constitutional amendment. The duty of the judiciary when faced with a direct conflict between a statute and the constitution is to uphold the constitution."

IV. APPLICATION TO SSB 6346-S

Article VII, Section 1 requires that "all taxes shall be uniform upon the same class of property." SSB 6346-S violates this requirement in at least two respects. The bill provides a "standard deduction of $1,000,000 per individual," meaning that individuals with Washington taxable income below $1,000,000 owe no tax, while individuals with income above that threshold are taxed at 9.90%. This creates two categories within a single class of property taxed at different rates. As the *Culliton* court explained: "The constitutional amendment speaks of the same class of property. One who pays a tax on a $2,000 taxable income pays a tax on precisely the same class of property as one who pays a tax on a $1,000 taxable income, and to tax the one at a progressively higher rate than the other positively violates the other clause of the amendment, that all taxes shall be uniform upon the same class of property." The Act provides additional deductions and exemptions that further create non-uniform taxation.

Article VII, Section 2 limits aggregate property tax levies to 1% annually. SSB 6346-S imposes an unconstitutional 9.90% property tax on Washington taxable income.

V. THE DEMOCRATIC PROCESS CONFIRMS THIS INTERPRETATION

Since 1934, Washington voters have rejected proposals to amend the Constitution to allow graduated taxes on income on six occasions.

Each time, the proposal was voted down resoundingly, with at least 64% opposition to every proposed amendment since 1940; the most recent was rejected by 77% of voters statewide:

H.R.J. Res. 37 (Wash. 1973): rejected 77%-23%
H.R.J. Res. 42 (Wash. 1970): rejected 68%-32%
H.R.J. Res. 4 (Wash. 1942): rejected 66%-34%
S.J. Res. 5 (Wash. 1938): rejected 67%-33%
S.J. Res. 7 (Wash. 1936): rejected 78%-22%
H.R.J. Res. 11 (Wash. 1934): rejected 57%-43%

On four other occasions, Washington voters overwhelmingly rejected ballot initiatives that would have imposed statewide graduated income taxes, with the most recent 2010 initiative being voted down by a margin of 64% to 36%:

Initiative 158 (Wash. 1944): rejected 70%-30%
Initiative 314 (Wash. 1975): rejected 67%-33%
Initiative 435 (Wash. 1982): rejected 66%-34%
Initiative 1098 (Wash. 2010): rejected 64%-36%

In addition to the case law above, these repeated expressions of the will of the people reaffirming the broad definition of "property" in Article VII resoundingly defeat the misguided notion that, in the face of this legal and legislative history, five justices on the Washington Supreme Court are free to reinterpret Article VII to permit that which has been clearly forbidden for nearly a century.

VI. THE PROPER PATH: CONSTITUTIONAL AMENDMENT

Unless the Legislature and the Courts overturn longstanding precedent to conclude that income is not property, any tax on income is subject to the rules for property taxes: they must be uniform and limited to 1% per year.

The proper avenue for enacting a graduated income tax with a rate in Washington is through constitutional amendment, not judicial reinterpretation of plain constitutional language.