Case No: 95295-7

IN THE SUPREME COURT OF THE STATE OF WASHINGTON

S. MICHAEL KUNATH, et al.,

Respondents,

v.

CITY OF SEATTLE,

Appellant.

RESPONSE BRIEF OF SCOTT SHOCK, SALLY OLJAR, STEVE DAVIES, AND JOHN PALMER

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TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page

Cases

State Statutes

Constitutions

Rules

Other Authorities

Seattle Municipal Code

INTRODUCTION

The City of Seattle adopted its so-called "high-earner" income tax ordinance in purposeful violation of a long line of Washington Supreme Court precedent holding that income is property and, therefore, a tax on income is subject to the Uniformity Clause of Article VII, Section 1, of the Washington State Constitution.[1] *See Aberdeen Savings & Loan Ass'n v. Chase*, 157 Wash. 351, 289 P. 536 (1930); *Culliton v. Chase*, 174 Wash. 363, 25 P.2d 81 (1933); *Jensen v. Henneford*, 185 Wash. 209, 53 P.2d 607 (1936); *Petroleum Nav. Co. v. Henneford*, 185 Wash. 495, 55 P.2d 1056 (1936); *Power, Inc. v. Huntley*, 39 Wn.2d 191, 235 P.2d 173 (1951); *Apartment Operators Ass'n of Seattle v. Schumacher*, 56 Wn.2d 46, 351 P.2d 124 (1960); *Harbour Village Apartments v. City of Mukilteo*, 139 Wn.2d 604, 989 P.2d 542 (1999); *Washington Public Ports Ass'n v. Dep't of Revenue*, 148 Wn.2d 637, 62 P.3d 462 (2003). The reason why the City enacted a plainly illegal tax was to set up a "test case" in which to ask this Court to overturn those and other decisions concluding that an individual's wages are personal property. Seattle's goal is to authorize itself to levy a tax on the region's "high-earners" by removing income from the Uniformity

[1] The Economic Opportunity Institute did not intervene in Shock's lawsuit below and did not address any of the unique issues raised in Shock's complaint at summary judgment or on appeal. The Shock respondents, therefore, do not respond to the arguments raised in EOI's appellate brief.

Clause's unique and expansive definition of property as "including everything, whether tangible or intangible, subject to ownership." Wash. Const. art. VII § 1.

This Court should reject the City's "test case" for several reasons. First and foremost, the question whether to expand municipal taxing authority to include a local income tax must be brought before the Legislature. When the government last challenged the Uniformity Clause's application to income in 1960, the Supreme Court directed the government that, if it believed that changed circumstances warrant an income tax not allowed by the Constitution, then the proper course of action is to follow the legislative procedure to amend the Constitution. *Apartment Operators*, 56 Wn.2d at 47–48. Seattle's decision to ignore this direction and instead to try to force such a change through the courts "violate[s] the constitutional blueprint [and] frustrate[s] the mandates of the people of the State as a whole." *1000 Friends of Wash. v. McFarland*, 159 Wn.2d 165, 168, 149 P.3d 616 (2006). The City's desire to change the Constitution must go to the State Legislature, which operates subject to the will of the people of Washington. Only that process guarantees that all voices are heard and all contingencies are vetted. Wash. Const. art. XXIII.

Second, the City's request that this Court strip an individual's wages of their legal character as personal property is baseless and dangerously

shortsighted. The judiciary exists to ensure constitutional protection of settled rights, not to second-guess them. *See* Wash. Const. art. IV, § 28; *Stop the Beach Renourishment v. Fla. Dep't of Envtl. Prot.*, 560 U.S. 702, 735, 130 S. Ct. 2592, 177 L. Ed. 2d 184 (2010) (A court's power does not include the ability "to eliminate or change established property rights."). As such, this Court must uphold the Constitution regardless of the City's changing needs, wants, or policy arguments. Wash. Const. art. I, § 29 ("The provisions of this Constitution are mandatory, unless by express words they are declared to be otherwise."). The fact that decisions from other states exclude earned income from their tax uniformity requirements is of little relevance to this case because those cases are based on the particular language of their constitutions and statutes—none of which define property as "including everything, whether tangible or intangible, subject to ownership." Wash. Const. art. VII § 1.

Third, the City's desire to set up a "test case" is constitutionally infirm because its decision to target one segment of the population based on "total income," rather than actual income, violates the Equal Protection Clauses of the Washington and U.S. Constitutions. Wash. Const. art. I § 12; U.S. Const. amend. 14, § 1. Binding precedent from the U.S. Supreme Court holds that the government cannot rationally rely on "total income" to justify the conclusion that any person within the so-called "high-earner"

classification is more or less capable to pay a tax. *Stewart Dry Goods Co. v. Lewis*, 294 U.S. 550, 558, 55 S. Ct. 525, 79 L. Ed. 1054 (1935). As shown below, Seattle's reliance on a "total income" measure subjects its citizens to unequal treatment, allowing some "high-earners" to avoid the income tax while subjecting many middle earners to the tax based solely on *how* they earn their money, not their actual incomes. Seattle has offered no rational explanation for such unequal treatment. The City's tax is unconstitutional and must be stricken.

For these reasons, and for the reasons set out by the Levine and Burke respondents, Scott Shock, Sally Oljar, Steve Davies, and John Palmer respectfully request that this Court deny the City's appeal.

RESTATEMENT OF THE ISSUES

Issue No. 1. Whether questions of statewide tax policy are subject to the exclusive authority of the legislative branch.

Issue No. 2. Whether the Washington Supreme Court's characterization of income as personal property in *Culliton v. Chase*, 174 Wash. 363, 25 P.2d 81 (1933), should be upheld where the Court has held the same in numerous decisions predating and post-dating *Culliton* in a variety of contexts.

Issue No. 3. Whether Seattle's income tax is an arbitrary and discriminatory tax which violates the Equal Protection Clauses of the State and Federal Constitutions?

STATEMENT OF THE CASE

On July 10, 2017, the Seattle City Council unanimously voted to adopt Council Bill 119002 as part of a strategy to set up a "test case" in which the City could challenge the constitutional requirement that income taxes be uniform.[2] *See* CP 371 (Ordinance 125339, § 1(5)). Four days later, on July 14, 2017, former Seattle Mayor Ed Murray signed into law Ordinance 125339, titled in part, "AN ORDINANCE imposing an income tax on high-income residents." CP 371.

The ordinance imposes an annual "tax on the total income of every resident taxpayer," defining "total income" as

> the amount reported as income before any adjustments, deductions, or credits on a resident taxpayer's United States individual income tax return for the tax year, currently listed as "total income" on line 22 of Internal Revenue Service Form 1040 or "total income" on line 15 of Internal Revenue Service Form 1040A.

SMC §§ 5.65.020, .030. Although the City uses the phrase "total income," SMC § 5.65.020, the ordinance imposes a tax on net income because the

[2] *Seattle passes income tax. Next: lawsuits?* Crosscut.com (July 10, 2017) (http://crosscut.com/2017/07/seattle-passes-an-income-tax-next-court-action/)

income reported on line 22 of IRS Form 1040 or line 15 of IRS Form 1040A is determined after calculating certain deductions, exclusions, and expenses.

Despite stating that the tax is intended to target only "high-earners," the ordinance does not limit the definition of "total income" to salary. Instead, an individual's "total income" can include moneys received from interest income, as well as the sale of a home or business, an inheritance, or other one-time occurrences.

The ordinance does not impose the tax at a uniform rate as required by the Uniformity Clause. Instead, the ordinance states that individuals who receive over $250,000 in total income per year, or married couples earning over $500,000 in total income per year, must pay a 2.25% income tax. SMC § 5.65.030(B). Persons with incomes below those amounts are subject to the tax ordinance but, for the time being, are taxed at a rate of 0%. SMC § 5.65.030(B) ("There is imposed a tax on the total income of every resident taxpayer in the amount of their total income multiplied by the applicable rates as follows.").

The threshold income and tax rates are subject to change. The ordinance states that the City will adjust the threshold total income amounts annually for inflation and based on adjustments to the Consumer Price Index. SMC § 5.65.030(C). Nothing in the ordinance limits the City's authority to adopt new rates or set new income thresholds.

Shortly after the City enacted the tax, several Seattle residents challenged the ordinance in four separately filed complaints in King County Superior Court, alleging that the City lacked authority to levy the income tax and contesting the constitutionality of the tax. CP 1–5, 1608–52, 1629–1658, 1658–98. The trial court consolidated the cases. CP 74–75.

The court ruled in favor of the consolidated plaintiffs on cross-motions for summary judgment, concluding on statutory grounds that the tax was unlawful and unenforceable. CP 1306–08. In addition to the statutory grounds, the parties fully briefed several constitutional claims and agreed that those claims were properly subject to summary judgment. The trial court, however, declined to address those arguments under the doctrine of constitutional avoidance. CP 1317–18. Those undecided claims, which are properly considered on appeal under RAP 2.4, include Shock's arguments that (1) the Takings and Due Process Clauses of the Federal Constitution prohibit courts from declaring that well-recognized rights in property do not exist and (2) that the tax violates the Uniformity Clause of the Washington State Constitution and the Equal Protection Clauses of the State and Federal Constitution.

STANDARD OF REVIEW

Because this case was resolved on cross-motions for summary judgment and all parties agreed that there were no material issues of fact,

the standard of review is de novo, and the appellate court performs the same inquiry as the trial court. *Sheikh v. Choe,* 156 Wn.2d 441, 447, 128 P.3d 574 (2006) (quoting *Jones v. Allstate Ins. Co.,* 146 Wn.2d 291, 300, 45 P.3d 1068 (2002)). Questions pertaining to constitutional limitations on local taxation are also issues of law to be determined de novo. *Id*. (citing *Okeson v. City of Seattle,* 150 Wn.2d 540, 548–49, 78 P.3d 1279 (2003)).

ARGUMENT AND AUTHORITIES

Since 1930, the Washington Supreme Court has consistently held that income is property subject to the protections guaranteed by the Washington and U.S. Constitutions, including the State's Uniformity Clause. *See Aberdeen Savings & Loan*, 157 Wash. 351; *Culliton*, 174 Wash. 363; *Jensen*, 185 Wash. 209; *Petroleum Nav.*, 185 Wash. 495 ; *Power, Inc.*, 39 Wn.2d 191. Seattle cannot challenge the Uniformity Clause's unique and broad definition of property as "including everything, whether tangible or intangible, subject to ownership." Wash. Const. art. VII § 1. Instead, the City contests the premise that income—whether earned as wages or from a wealth-generating investment—constitutes personal property. Seattle's arguments, however, must fail for a number of reasons. First, the judicial branch lacks the authority to extinguish settled property rights—any limitation on those rights must be enacted by the legislative branch. Second, the City's claim that *Aberdeen Savings & Loan* and *Culliton* were

unsupported by any case law recognizing that income is property is baseless. The Washington Supreme Court concluded that earnings are property subject to the Uniformity Clause decades before it decided *Aberdeen Savings & Loan* and *Culliton*. Moreover, Seattle's request that this Court declare that income is not property is dangerously overbroad because courts across the nation characterize income as property in a wide range of legal contexts, including constitutional law, family law, inheritance law, criminal law, and contracts. Fourth, the city's income tax violates the Equal Protection Clauses of the Washington and U.S. Constitutions because its "high-earner" classification is not supported by any rational method for measuring individual wealth and therefore treats similarly situated persons unequally across all income classes.

I

THE QUESTION WHETHER INCOME IS SUBJECT TO THE UNIFORMITY CLAUSE IS PROPERLY BROUGHT TO THE LEGISLATIVE BRANCH

The City's request that this Court reverse nearly a century of case law holding that income is personal property, and therefore subject to the Constitution's tax uniformity requirement, is not appropriate for judicial determination. Seattle's appeal merely reasserts the same arguments that Washington's Supreme Court has rejected on numerous occasions. *Power, Inc.*, 39 Wn.2d at 194 ("It is no longer subject to question in this court that

income is property."). Thus, when the government last challenged the Uniformity Clause's application to income, the High Court directed the government that, if it believed that changed circumstances warrant an income tax not allowed by the Constitution, then the proper course of action is to follow the legislative procedure to amend the Constitution. *Apartment Operators Ass'n*, 56 Wn.2d at 47–48. There has been no change in circumstances since the Court's last pronouncement. The Uniformity Clause's broad definition of property as "including everything, whether tangible or intangible, subject to ownership" remains in force; thus, there is no new constitutional language or legislative history to interpret. *W.G. Clark Const. Co. v. Pac. Nw. Reg'l Council of Carpenters*, 180 Wn.2d 54, 65, 322 P.3d 1207 (2014) (noting that the Court may reconsider settled law in those "relatively rare" occasions where new developments and/or changed circumstances compel a reevaluation).

Instead of showing the type of changed circumstances that may warrant reevaluation of past precedents (*e.g.*, a constitutional or statutory amendment, intervening case law, etc.), the City merely argues that progressive taxation provides a better policy than tax uniformity going forward. That, however, is an inappropriate question for the judiciary: "It is not the function of this court … to criticize the public policy which may have prompted adoption of the [tax] legislation." *State ex rel. Namer Inv.*

Corp. v. Williams, 73 Wn.2d 1, 7, 435 P.2d 975 (1968) (citing *State Board of Tax Comm'rs of Indiana v. Jackson*, 283 U.S. 527, 51 S. Ct. 540, 75 L. Ed. 1248 (1931)); *see also City of Tacoma v. Tax Comm'n*, 177 Wash. 604, 617, 33 P.2d 899 (1934) (Questions of tax policy must be submitted to the Legislature, not to the courts.). And, more to the point, this Court has recognized that the Legislature—not the judiciary—is authorized "to exercise its discretion in classifying personal property" subject to the uniformity requirement. *Belas v. Kiga*, 135 Wn.2d 913, 921, 959 P.2d 1037 (1998) (quoting Alfred Harsch, *The Washington Tax System—How It Grew,* 39 Wash. L. Rev. 944, 956–57 (1965)). Thus, unless and until the Legislature opts to amend the Constitution, tax uniformity will remain the "highest and most important of all requirements applicable to taxation under our system."[3] *Belas*, 135 Wn.2d at 937–38; *Boeing Co. v. King Cty.*, 75 Wn.2d 160, 165, 449 P.2d 404 (1969); *Savage v. Pierce Cty.*, 68 Wash. 623, 625, 123 P. 1088 (1912).

Seattle also fails to acknowledge Washington Supreme Court case law holding that a decision establishing a rule of property law must be followed unless and until the Legislature acts to amend the law. *Eilers*

[3] The chief policy consideration underlying tax uniformity is the principle that citizens should contribute to the support of government in proportion to ability to pay. *Belas,* 135 Wn.2d at 923.

Music House v. Ritner, 88 Wash. 218, 224, 154 P. 787 (1916) (Where the Supreme Court "announced a rule of property, and property rights have become fixed and determined thereunder, … the doctrine of stare decisis demands it be followed, except as otherwise determined [by an act of legislation]."). The U.S. Supreme Court recently confirmed this limitation on the judicial branch, explaining that a court's power does not include the ability "to eliminate or change established property rights." *Stop the Beach Renourishment.*, 560 U.S. at 735 (J. Kennedy, concurring); *see also id.* at 715 ("If a legislature *or a court* declares that what was once an established right of private property no longer exists, it has taken that property, no less than if the State had physically appropriated it or destroyed its value by regulation.") (Scalia, J., lead opinion). This limitation on the judicial branch is consistent with the Constitution's understanding that the judiciary exists to ensure constitutional protection of guaranteed rights and liberties, not to second-guess them. *See* Wash. Const. art. IV, § 28. As such, this Court's role is to uphold the Constitution regardless of the City's changing needs, wants, or policy arguments. Wash. Const. art. I, § 29 ("The provisions of this Constitution are mandatory, unless by express words they are declared to be otherwise."); *see also City of Seattle v. Evans*, 182 Wn. App. 188, 196 n.25, 327 P.3d 1303 (2014), *aff'd on other grounds*, 184 Wn.2d 856, 366 P.3d 906 (2015) (If a settled constitutional guarantee was subject to change

based solely on the shifting needs of local government, it would be no constitutional guarantee at all.).

Judicial restraint is particularly appropriate here where the Legislature has demonstrated its intent to limit local government authority to levy income taxes and the Governor has stated his opposition to an income tax.[4] RCW 36.65.030 (local governments "shall not levy a tax on net income"). Deferring to the Legislature is also warranted here because tax uniformity has broad support among the people of Washington, who have rejected proposals to implement a graduated income tax on ten occasions between 1934 and 2010,[5] and rejected a constitutional amendment to exempt income from the Uniformity Clause in 1934, 1936, 1938, 1942, 1970 and 1973.[6] The policy of protecting income from unequal taxation is also supported and relied upon by government and business. Indeed, the Department of Commerce's website boasts that Washington's lack of a personal income tax is a key competitive advantage when attracting the types of business and talent necessary to grow the State's

[4] "Inslee: Income tax is not right for Washington state" http://mynorthwest.com/621844/inslee-income-tax-not-right/?

[5] https://www.sos.wa.gov/elections/research/income-tax-ballot-measures.aspx

[6] https://www.washingtonpolicy.org/publications/detail/timeless-advice-from-wa-supreme-court-on-income-taxes

economy.[7] Seattle—one city in a state with a wide-ranging population spread across many cities and rural areas—advocates a minority viewpoint on this issue and should not be allowed to drive state tax and constitutional policy through this litigation. *See* Hugh D. Spitzer, *A Washington State Income Tax—Again?*, 16 U. Puget Sound L. Rev. 515, 520 (1993) ("Such a tax may or may not be good policy, but that is a determination for legislators to make, not judges or scholars.").

Even if this Court were disposed to address the City's policy arguments, Seattle's so-called "high-earner" tax provides a poor vehicle in which to consider the merits of progressive taxation because the tax is not progressive. By definition, a progressive system spreads the tax burden across all income brackets and sets graduated rates that progressively increase as an individual's income increases. *See Knowlton v. Moore*, 178 U.S. 41, 69, 20 S. Ct. 747, 44 L. Ed. 969 (1900). Seattle's tax, by contrast, targets only "high-income residents" to pay for a variety of general needs, such as providing green jobs, addressing homelessness, replacing possible lost federal funding, etc. *See* CP 371 (Ordinance 125339, § 1(1)). Unlike a progressive tax in which all persons with an ability to pay bear some responsibility, the City's income tax law states *if you're rich, you pay; if*

[7] http://www.choosewashington.com/why-washington/our-strengths/pro-business/

you're not, you don't. And, unlike past attempts to advance progressive taxation, Seattle did not propose any simultaneous cuts to its regressive taxes alongside the income tax. *See* 1932 tax initiative (proposed to cut property taxes in half). Instead, the City levied its income tax shortly after enacting a regressive tax on soda (City of Seattle Ordinance 125324 (June 6, 2017)), and since then, the City Council has proposed a measure to lift the limit on property taxes in order to raise those regressive tax rates higher than currently allowed by law.[8] The City's arguments in favor of progressive taxation have absolutely no bearing on the case.[9] *Walker v. Munro*, 124 Wn.2d 402, 415, 879 P.2d 920 (1994) (The court will not render judgment on a hypothetical or speculative controversy.).

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[8] Q13 Fox, "A week after controversial head tax passes, Seattle City Council members propose property tax increase." (May 21, 2018) (http://q13fox.com/2018/05/21/a-week-after-controversial-employee-head-tax-passes-seattle-city-council-members-launching-ordinance-in-hopes-of-raising-property-taxes/)

[9] Moreover, the undisputed facts of this case establish that the City targeted a politically unpopular class to bear the entire tax burden, which is a direct affront to the State's well-settled and broadly supported policy of fairness in taxation. The ordinance's co-sponsor, Seattle City Councilmember Kshama Sawant, stated that her proposal to impose a "tax on Seattle's rich" is part of a larger "battle" against wealthy citizens and was motivated by her belief that the "capitalist class" actively works to "undercut" the policies that she supports. *Seattle Answers Trump's War on Workers by Taxing the Rich*, the Real News Network (July 12, 2017) (http://therealnews.com/t2/story:19531:Seattle-Answers-Trump%27s-War-on-Workers-by-Taxing-the-Rich); *see also "Tax the Rich! Town Hall with Kshama Sawant & Trump-Proof Seattle"* (May 19, 2017) (https://www.youtube.com/watch?v=DAqBWiIU-J8).

Enforcing the separation of powers here is essential because "Of all the powers conferred upon the Government that of taxation is most liable to abuse.…This power can as readily be employed against one class of individuals and in favor of another, so as to ruin the one class and give unlimited wealth and prosperity to the other, if there are no implied limitations of the uses for which the power may be exercised." *Loan Association v. Topeka,* 87 U.S. 655, 662–664, 22 L. Ed. 455, 20 Wall. 655 (1874). Seattle's desire to tax personal income must go to the State Legislature, which operates subject to the will of the people. Only that process guarantees that all voices are heard and all contingencies are vetted before radically changing statewide tax and constitutional policy.

II

INCOME IS PROPERTY

The question whether income is property is separate and distinct from the question whether income is subject to the Uniformity Clause. The first question turns on whether a wage earner owns and holds exclusive rights to his or her wages. The second question turns entirely on the Legislature's unique classification of property subject to the uniformity requirement as "including everything, whether tangible or intangible, subject to ownership." Wash. Const. art. VII § 1.

A. Washington Courts Held That Income Is Property Decades Before *Culliton*

1. *Culliton* was a continuation of settled law; not a new beginning

Seattle's argument for stripping income of its character as protected property is predicated on its claim that the Washington Supreme Court was mistaken when it concluded in *Culliton* that settled law had established that income is property. Seattle Op. Br. at 12–29. This claim is baseless. Indeed, to make this claim, the City relies on an incomplete overview of the contemporaneous case law, omitting from its discussion the larger body of precedents establishing that income is property well in advance of this Court's decisions in *Aberdeen Savings & Loan* and *Culliton*. The City's failure to acknowledge this case law is fatal to its appeal, which seeks only reversal of *Aberdeen Savings & Loan* and *Culliton* and its progeny.

In truth, this Court had held that income is property subject to the uniformity requirement a quarter century before deciding *Culliton*. In *State ex rel. Wolfe v. Parmenter,* this Court was asked to determine whether money and intangible property were subject to the State's original Uniformity Clause. 50 Wash. 164, 177, 96 P. 1047 (1908). At issue was a 1907 statute that defined taxable property as excluding "mortgages, notes, accounts, moneys, certificates of deposit, tax certificates, judgments, state, county, municipal and school district bonds and warrants." *Id*. at 171–72.

Aggrieved taxpayers filed writs of mandamus, arguing that money and intangible property constitute property and therefore must be subject to taxation like all other property. *Id*. at 170–71. The Court agreed with the aggrieved taxpayers in regard to money, but disagreed that intangible instruments were presently taxable as property (this latter conclusion set the table for the expansive definition of property adopted by the modern Uniformity Clause). *Id.* at 176.

The Court based its decision on the language of the original Uniformity Clause, which authorized the Legislature to tax "[a]ll property in the state, not exempt under the laws of the United States, or under this Constitution," and required that the tax be "uniform and equal … according to its value in money." *Id.* at 173 (citing Wash. Const. art. VII, §§ 1, 2 (amended 1930)). With that language in mind, the Court distinguished intangible instruments from money on the basis that (1) intangible instruments are a mere expectation with no immediate value to the holder until paid; whereas, (2) income from such investments becomes property immediately upon its receipt and, therefore, the earned money cannot be held exempt from the State's property tax.[10] *Id.* at 176. The Court ultimately

[10] *See also id*. at 180 (Writing in dissent, Justice Fullerton agreed that money is property—a fact known "by all English-speaking people, by all law-writers, and by the entire commercial world. [Money and intangibles] are held by the courts to be protected against spoliation and theft by the statutes

held that the Legislature could not constitutionally exclude money from taxation and invalidated the exclusion. *Id*. This Court thereafter confirmed that income is property for the purpose of taxation on at least two separate occasions prior to *Aberdeen Savings & Loan* and *Culliton*. *See State ex rel. Atwood v. Wooster*, 163 Wash. 659, 662, 2 P.2d 653 (1931) (money is property); *State ex rel. Egbert v. Gifford*, 151 Wash. 43, 44, 275 P. 74 (1929).

2. *Parmenter* and the resulting tax revolt solidified Washington's policy decision to equate income and property

The City's failure to discuss *Parmenter* is critical because that case, which treated real and tangible property (including money) differently from intangible property, sparked the tax revolt that resulted in the constitutional amendment that defined property as "including everything, whether tangible or intangible, subject to ownership." Wash. Const. art. VII § 1. Thus, when the City argues that the Fourteenth Amendment focused primarily on capturing intangible property, which had escaped taxation, it is correct. But its following argument, that income was never considered property, omits the fact that the Court had held income subject to taxation in the decades leading up to the amendment.

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which make it a crime to despoil or steal personal property. The question of ownership and title to them is daily the subject of controversy in the civil courts.") (Fullerton, J., dissenting).

In the wake of *Parmenter*, critics (especially farmers represented by the Grange) argued that the tax structure envisioned by the original Uniformity Clause placed an undue burden on those who owned and relied on real estate for their livelihood, and reformers sought to lower this burden by adding intangible property to the tax base. *Wooster*, 163 Wash. at 661–64. The Legislature heard many proposals calling for a constitutional amendment classifying all property—whether tangible or intangible—as being subject to taxation. *Wooster*, 163 Wash. at 663 (noting the criticism that, under the former tax system, a mortgagee would pay taxes on the property whereas the mortgager would pay no tax on the interest). Reformers reasoned that, if the Constitution set a tax rate that was low enough to remove the incentive to conceal the intangibles from assessment, the state could successfully expand the tax base to include intangible property. *See* Voters Pamphlet for 1928 General Election, at 5–6. Reformers proposed an amendment broadening the definition of property in each biennial legislative session after *Parmenter* (except 1917) until finally, in 1927, the proposal was approved by the Legislature and placed on the 1928 general election ballot. Laws of 1927, ch. 180. This proposal would have allowed the tax classification of any property, real or personal. Opponents feared that this would open the door to legislative favoritism among real estate interests with constant efforts to shift the tax burden back and forth

among the various classes of property. The opponents urged the voters not to give the Legislature unlimited classification powers:

> Granting the Legislature a free hand simply means pushing the tax burden onto the weak. This amendment opens the doors to special interests at each legislative session in which each group will try to "get out from under." There will be more lobbyists than legislators, and a new set of tax laws at each session. You need one guess as to which group will come out on top in the end. What will become of equality and uniformity then?

Voter Pamphlet for 1928 General Election at p. 3. The campaign against the proposed amendment was successful, and voters defeated the measure. *See* Abstract of Votes for 1928 General Election.

At the next legislative session in 1929, proponents again sought an amendment. This time, to calm discrimination concerns, the Legislature inserted a requirement that all property continue to be taxed uniformly as a single class. Continuing to require strict uniformity did not interfere with the fundamental purpose of the amendment which was to authorize the Legislature to separately classify intangible property so that it could be brought into the tax base. As explained to the voters:

> The amendment to be voted on this year [1930] differs in two important particulars from that submitted in 1928. It fixes real estate all in one class, except for lands devoted to reforestation and mineral lands, and it defines property. These two changes met the commonest objections to the 1928 amendment and were largely responsible for the different factions uniting on this amendment in the Legislature.

Voter Pamphlet for November 4, 1930 General Election at p. 29.

Before the Amendment was voted on, the Advisory Tax Commission posed a series of questions to the Office of the Attorney General of Washington, seeking in relevant part the Attorney General's views in regard to the taxation of income. *See* J. Thomas Carrato & Richard W. Hemstad, *Income Taxation in Washington: In a Class by Itself*, 1 U. Puget Sound L. Rev. 255, 267–68 (1978) (citing 29–30 Wash. Op. Att'y Gen. 431 (1930)). The Attorney General Opinion concluded that a tax on income would constitute a tax on property and would, therefore, be subject to the proposed amendments to the Uniformity Clause. *Id*. at 268 (citing 29–30 Wash. Op. Att'y Gen. at 439–41). The conclusions reached by the Attorney General Opinion were communicated to interest groups across the state in December 1929—well in advance of its publication. *Id*. at 269. The amendment, thereafter, received broad legislative support and was approved by the voters as Amendment 14 to the Washington State Constitution.

Not long after the Legislature enacted the Uniformity Clause in 1930, the State sought to increase its revenue by adopting an income tax law which provided: "There shall be ... a tax on all net income ... as is derived from property located or business transacted within the state, except

as hereinafter exempted."[11] *Culliton,* 174 Wash. at 372 (quoting Rem. 1933 Sup., §§ 11200–1). In an attempt to avoid the uniformity requirement, the State argued that the tax was not on property but was rather a tax on the income generated from use of the property and, therefore, was not subject to the Uniformity Clause. *Id*. at 374. The Court rejected this argument, noting that the Uniformity Clause defined property to mean everything subject to ownership, whether tangible or intangible, and therefore income itself was property subject to the uniformity requirement. *Id.* Because the income tax imposed graduated rates, it failed to meet the uniformity requirements and was invalid. *Id.* at 378.

Culliton cited *Aberdeen Savings & Loan* as precedent for the conclusion that income is property. In *Aberdeen*, this Court was asked whether a business tax violated the Equal Protection Clause of the U.S. Constitution. Before proceeding to the merits of the constitutional claim, the Court addressed whether the tax affected a protected property interest.[12]

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[11] At the time, the popular theory for supporting a graduated income tax was that the Legislature could classify each tax group to be a separate class of property—this theory did not challenge character of income as property or the application of the Uniformity Clause. *See* Carrato, 1 U. Puget Sound L. Rev. at 268, 270–71.

[12] "Because the Constitution protects rather than creates property interests, the existence of a property interest is determined by reference to existing rules or understandings that stem from an independent source such as state law." *Phillips v. Washington Legal Foundation*, 524 U.S. 156, 164, 118 S. Ct. 1925, 141 L. Ed. 2d 174 (1998); *see also Board of Regents of State*

On this threshold question, this Court noted that the petitioner had challenged the income tax on the basis that "it purports to impose a tax directly upon property, to wit, upon the net income earned by appellants upon which the amount of tax due is to be computed[.]" 157 Wash. at 361. The Court agreed, holding that a tax "levied directly upon appellant's property … is equivalent to the levy of a tax upon the net income earned by appellants[.]" *Id*. The Court's treatment of this issue was brief because the respondent did not contest that an income tax is a tax on property (which question had recently been decided in *Parmenter*, *Wooster*, and *Gifford*). *Id*. Thus, even though the Court did not ultimately address the Uniformity Clause question, it did in fact address the threshold question whether an income tax is a tax upon property.[13] *Id*.; *see also id.* at 380, 384 (Fullerton,

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Colleges v. Roth, 408 U.S. 564, 577, 92 S. Ct. 2701, 33 L. Ed. 2d 548 (1972) ("Property interests, of course, are not created by the Constitution. Rather, they are created and their dimensions are defined by existing rules or understandings that stem from an independent source such as state law—rules or understandings that secure certain benefits and that support claims of entitlement to those benefits.").

[13] The City's discussion of *Quaker City Cab Co. v. Pennsylvania*, 277 U.S. 389, 48 S. Ct. 553, 72 L. Ed. 927 (1928), is a red herring. Seattle Op. Br. at 18-22. Although *Aberdeen Savings & Loan* followed that decision, *Culliton* did not rely on any of the conclusions relating to the Federal Equal Protection Clause when determining that income is subject to the Uniformity Clause. At most, *Culliton* relied on the threshold determination that a tax on income impacts a federally protected right subject to the protections guaranteed by the Fourteenth Amendment, but that aspect of *Quaker* is not challenged and remains valid to date.

J., dissenting) (criticizing the majority conclusion that the income tax is a tax upon property).

Seattle's claim that the Court did not reach the property question in *Aberdeen Savings & Loan* is put to rest by the Court's decision on rehearing, in which it reaffirmed the conclusion that income is property:

> In order to clarify the situation, the court now states that the opinions above cited were rendered with a view to determining the questions presented by the cases at bar, and those questions only; that the majority of the court was of the opinion that the legislation therein attacked must be held, under the decisions of the Supreme Court of the United States, to attempt to establish a property and not an excise or corporation franchise tax ….

Washington Mut. Sav. Bank v. Chase, 157 Wash. 351, 392, 290 P. 697 (1930). Importantly, *Aberdeen Savings & Loan* had been published well in advance of the public vote on Amendment 14; therefore, the voters were well-aware that income qualified as property when they approved the amendment. *Culliton*, 174 Wash. at 379–80 (Mitchell, J., concurring). There can be no question, therefore, that *Culliton* correctly cited *Aberdeen Savings & Loan* for the proposition that income constitutes property as defined by the Constitution.

Contemporaneous precedent offers even more support for *Culliton*'s conclusion that an income tax is a property tax. On the same day that it issued *Culliton*, this Court also issued its decision in *State ex rel. Stiner v.*

Yelle, 174 Wash. 402, 25 P.2d 91 (1933). There, the Court reviewed a statute imposing an excise tax on business. *Id*. at 407. At the outset, the Court distinguished an excise tax from an income tax, explaining that, "[w]hen acquired, income immediately becomes property in the hands of the acquirer, and it is, of course, taxable with other property of the same class." *Id*. (concluding that a tax on the privilege of engaging in business is not an income tax).

Three years after *Culliton*, the state tried to levy another income tax, passing the Personal Net Income Tax of 1935. This graduated income tax was levied "for the privilege of receiving income." *Jensen v. Henneford,* 185 Wash. 209, 212, 53 P.2d 607 (1936). Income included "gains, profits, and income derived from … dealings in property, whether real or personal, growing out of the ownership, use of, or interest in such property." *Id.* at 212–13. The state advanced a different argument this time, claiming that the tax was not a property tax because it was imposed on the so-called "privilege of receiving" income rather than the income itself. The Court forcefully reminded the State that it "cannot change the real nature and purpose of an act by giving it a different title or by declaring its nature and purpose to be otherwise, any more than a man can transform his character by changing his attire or assuming a different name…." *Id.* at 217.

The Court found that the State was trying to do what it had done earlier in 1932: impose a graduated tax on personal property. *Id.* at 218 ("[T]he various provisions of the act show[] clearly that the legislature was concerned with the property (income) upon which the amount of the tax was to be levied, not with the mere privilege of the individual to receive the income."). It continued, "the mere right to own and hold property cannot be made the subject of an excise tax, because to tax by reason of ownership of property is to tax the property itself." *Id.* In explaining that the right to receive income cannot be disconnected from the income (property) itself, the Court reiterated:

> The right to receive property (income in this instance) is but a necessary element of ownership, and, without such a right to receive, the ownership is but an empty thing and of no value whatever. . . . 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.

Id. at 218–19 (citations omitted); *see also* 1 E. Coke Institutes ch.1, § 1 (1st Am. ed. 1812) ("[W]hat is the land, but the profits thereof?") (quoted in *Lucas v. South Carolina Coastal Council,* 505 U.S. 1003, 1017, 112 S. Ct. 2886, 120 L. Ed. 2d 798 (1992)).

Seattle's claim that *Culliton* was "incorrect and unfounded" is baseless. The case law and legislative history preceding and contemporary

to *Culliton* consistently holds that income is property and, thus, a tax on income is a property tax. The City's omission of this case law is fatal to its argument.

B. Courts Across the Nation Hold That Income Is Property in a Variety of Contexts

The City's argument also conflicts with holdings from many jurisdictions that income is property in a variety of legal contexts. The U.S. Supreme Court, for example, has long held that income is property subject to the protections guaranteed by the Fifth and Fourteenth Amendments to the U.S. Constitution. *See*, *e.g.*, *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1003, 104 S. Ct. 2863, 81 L. Ed. 2d 815 (1984) (finding a common law property right in the fruits of one's labor when considering whether trade secrets constitute property) (citing 2 W. Blackstone, *Commentaries*; J. Locke, *Second Treatise of Civil Government,* ch. 5 (J. Gough ed. 1947)); *Sniadach v. Family Fin. Corp. of Bay View*, 395 U.S. 337, 340–41, 89 S. Ct. 1820, 23 L. Ed. 2d 349 (1969) (wages constitute constitutionally protected property that may not be taken absent procedures mandated by the Due Process Clause); *Blair v. Comm'r of Internal Revenue*, 300 U.S. 5, 12, 57 S. Ct. 330, 81 L. Ed. 465 (1937) (recognizing that income is a present and transferable property interest); *Hoeper v. Tax Comm'n of Wis.*, 284 U.S. 206, 215, 52 S. Ct. 120, 76 L. Ed. 248 (1931) (a tax on income must comply

with due process). Indeed, money—which is what income is comprised of—has been consistently characterized as property. *See Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155, 161–64, 101 S. Ct. 446, 66 L. Ed. 2d 358 (1980) (Finding a property right in money; the government cannot, by *ipse dixit*, declare one's money "public" without compensation); *see also Phillips v. Washington Legal Foundation*, 524 U.S. at 165–67 ("[W]e hold that the interest income generated by funds held in IOLTA accounts is the 'private property' of the owner of the principal.").

State and federal courts throughout the nation also hold that each person has a constitutionally protected property interest in the wages earned through his or her labor. *See Dean v. Lehman*, 143 Wn.2d 12, 35, 18 P.3d 523 (2001) (noting that "interest income 'is sufficiently fundamental that States may not appropriate it without implicating the Takings Clause.'") (quoting *Schneider v. California Department of Corrections,* 151 F.3d 1194, 1201 (9th Cir. 1998)); *United States v. Skowron*, 839 F. Supp. 2d 740, 750 (S.D.N.Y. 2012), *aff'd*, 529 F. App'x 71 (2d Cir. 2013) ("Money paid in salary is property."); *United States v. Thompson,* 647 F.3d 180, 186–87 (5th Cir. 2011) (a person's labor is property); *United States v. Bahel*, 662 F.3d 610, 648–49 (2d Cir. 2011) (A salary is "plainly 'property.'"); *Eguia v. Tompkins*, 756 F.2d 1130, 1138 (5th Cir. 1985) ("There can be no doubt that the plaintiff's interest in his salary … is a property interest protected by

the Constitution."); *Orloff v. Cleland*, 708 F.2d 372, 378 (9th Cir. 1983) ("It is obvious that Orloff had a property interest in his salary."); *Opinion of the Justices*, 95 N.H. 537, 539, 64 A.2d 320 (1949) (income is property for purposes of uniform statute requirement); *Dunbar v. Johnston*, 170 S.C. 160, 169 S.E. 846, 847 (1933) (an individual's interest in her wages or salary is a property right); *Eliasberg Bros. Mercantile Co. v. Grimes*, 204 Ala. 492, 494, 86 So. 56 (1920) ("[W]hile 'income' is a complex conception of elements and units which may be, and usually are, acquired, and used or disposed of at different times, its elements and units are in the most literal sense wealth and property—none the less so because their possession is transient and their identity easily and quickly lost.").

Income is also considered property in family law, estate planning, bankruptcy, and contract. *See*, *e.g.*, *State v. Somerville*, 67 Wash. 638, 641, 122 P. 324 (1912) (ownership of labor allows individuals to enter employment contracts); *see also Blair v. Comm'r of Internal Revenue*, 300 U.S. at 12 (recognizing that income is a present and transferable property interest); *Lindemann v. Lindemann*, 92 Wn. App. 64, 72, 960 P.2d 966 (1998) (marital community has a property interest in the fruits of a spouse's labor).

Washington's criminal code provides additional illumination. The entire criminal code relies on a definition of property that is very similar to

the Uniformity Clause. The code defines property as "anything of value, whether tangible or intangible, real or personal." RCW 9A.04.110(22)). Courts interpreting that broad definition hold that the meaning of "property" is derived from the definition of "owner." *State v. Pike,* 118 Wn.2d 585, 589, 826 P.2d 152 (1992); *State v. Lau,* 174 Wn. App. 857, 868, 300 P.3d 838 (2013). In turn, the definition of "owner" "establishes the level of interest necessary to claim a right to property." *Pike,* 118 Wn.2d at 589; *see also State v. Joy,* 121 Wn.2d 333, 340–41, 851 P.2d 654 (1993); *State v. Jacobson,* 74 Wn. App. 715, 719, 876 P.2d 916 (1994). Here, despite its attempts to distinguish wages from other types of property, Seattle does not contest that an employee has an exclusive and enforceable ownership right to his or her wages. Thus, as *Parmenter* concluded a century ago, income becomes property immediately upon its receipt and is therefore only taxable as a class of property.

There is more. Seattle's broad assertion that wages are not property also threatens to undermine the fundamental right that each person has in his or her labor. *Patton v. City of Bellingham*, 179 Wash. 566, 574, 38 P.2d 364 (1934) ("The right to labor … is a right of property."); *see also S. Bus Lines v. Amalgamated Ass'n of St., Elec. Ry. & Motor Coach Emp. of Am.*, 205 Miss. 354, 379, 38 So. 2d 765, 771 (1949) ("Labor is property."); *Bayonne Textile Corp. v. Am. Fed'n of Silk Workers*, 114 N.J. Eq. 307, 316,

168 A. 799 (1933) ("Labor is property; capital is property; both must be equally safeguarded."); *Branson v. Indus. Workers of the World*, 30 Nev. 270, 95 P. 354, 361 (1908) ("The right to labor is property. It is one of the most valuable and fundamental of rights."). Recall Frederick Douglass's account of walking toward the wharves shortly after he arrived in New Bedford. Mr. Douglass saw a pile of coal in front of the Reverend Peabody's home and asked Mrs. Peabody if he might put the coal away. She agreed and paid Mr. Douglass two silver half dollars for his work. Mr. Douglass recounted the immense pride he felt from his earnings:

> To understand the emotion which swelled my heart as I clasped this money, realizing that I had no master who could take it from me—that it was mine—that my hands were my own, and could earn more of the precious coin, one must have been in some sense himself a slave. . . . I was not only a freeman but a free-working man, and no master Hugh stood ready at the end of the week to seize my hard earnings.

Frederick Douglass, *Life and Times of Frederick Douglass Written by Himself* 259 (Boston: De Wolfe & Fiske Co., 1892). Seattle would tell Mr. Douglass that those coins were not his property after all—that they are not worthy of the same protections provided to Reverend Peabody's coal. That argument is unjust and harmful to the people of Washington.

The City's attempt to distinguish income from other types of property because income is "in motion" is likewise baseless.[14] *See Am. Smelting & Ref. Co. v. Whatcom Cty.*, 13 Wn.2d 295, 302, 124 P.2d 963 (1942) ("The definition of the word 'property'… is as broad and comprehensive as may well be imagined."). The Massachusetts Supreme Court explained that "'[i]ncome,' like most other words, has different meanings dependent upon the connection in which it is used, and the result intended to be accomplished." *Trefry v. Putnam*, 227 Mass. 522, 526–27, 116 N.E. 904 (1917) (concluding that the specialized definition of income in a taxing provision may differ from the common understanding of the term). Thus, the mere fact that income may be characterized as something "in motion" does not, in and of itself, deprive an individual of his or her property interests in earned wages. *Opinion of the Justices*, 95 N.H. at 539 (holding that income is a class of property that "is sometimes called property in motion as distinct from static property"). Indeed, the common law recognizes rights in "a property in motion"—such as an income, rights in inheritance, or the discovery of an innovation subject to patent—even though the property "has no corporeal tangible substance." *See Millar v.*

[14] Seattle's claim that income is never transferable like real property is simply wrong. *Blair*, 300 U.S. at 12 (recognizing that investment income is a present and transferable property interest).

Taylor, 4 Burr. 2303, 98 Eng. Rep. 201 (1769); *see also Jensen*, 185 Wash. at 227 (Income is "an intangible, inchoate right—susceptible, indeed, to ownership, but not susceptible to manual possession."); *Crown Cork & Seal Co. v. State*, 87 Md. 687, 40 A. 1074, 1076 (1898) (a tax on "property in motion" is a property tax). And, directly on point, binding precedents from the Washington and U.S. Supreme Court hold that income constitutes property immediately upon its receipt. *Parmenter*, 50 Wash. at 176; *see also Eisner v. Macomber*, 252 U.S. 189, 207–08, 40 S. Ct. 189, 64 L. Ed. 521 (1920) (defining income as the gain actually received through an individual's investment or labor). Seattle's argument that income does not constitute property must fail.

III

SEATTLE'S TARGETED INCOME TAX VIOLATES EQUAL PROTECTION[15]

Seattle's decision to levy an income tax on so-called "high-earners" violates the Equal Protection Clauses of the Washington and U.S. Constitutions because the tax is applied in a manner that treats similarly situated persons differently without any rational justification for the unequal

[15] The Shock respondents are authorized to argue any grounds in support of the trial court's decision that are supported by the record. RAP 2.4; *McGowan v. State*, 148 Wn.2d 278, 288, 60 P.3d 67 (2002).

treatment.[16] *Cosro, Inc., v. Liquor Control Bd.,* 107 Wn.2d 754, 760, 733 P.2d 539 (1987). The City's "high-earner" classification is subject to rational basis scrutiny. *Forbes v. City of Seattle*, 113 Wn.2d 929, 941, 785 P.2d 431 (1990); *see also KMS Fin. Servs., Inc. v. City of Seattle*, 135 Wash. App. 489, 498, 146 P.3d 1195 (2006). This standard, however, "is not without teeth—'the court's role is to assure that even under this deferential standard of review the challenged legislation is constitutional.'" *Andersen v. King Cty.*, 158 Wn.2d 1, 136, 138 P.3d 963 (2006) (Fairhurst, J. dissenting) (citation omitted), majority opinion *abrogated by Obergefell v. Hodges*, __ U.S. __, 135 S. Ct. 2584, 192 L. Ed. 2d 609 (2015). Thus, rational basis review demands that the Court "insist on knowing the relation

[16] Wash. Const. art. 1, § 12 ("No 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."); U.S. Const. amend. 14, § 1 (No state shall "deny to any person within its jurisdiction the equal protection of the laws."). Several equal protection challenges to taxation have succeeded in Washington courts. *See*, *e.g.*, *Associated Grocers, Inc. v. State*, 114 Wn.2d 182, 787 P.2d 22 (1990) (B&O tax exemption for distributors but not wholesalers was discriminatory as to wholesalers); *Simpson v. State*, 26 Wn. App. 687, 615 P.2d 1297 (1980) (use tax exemption limited to articles purchased in American states discriminated against persons buying articles in foreign nations like Canada without any rational basis); *Power, Inc.*, 39 Wn.2d 191 (credit allowed only to taxpayers accounting on a fiscal year basis discriminated against taxpayers accounting on a calendar year basis); *State v. Inland Empire Refineries*, 3 Wn.2d 651, 101 P.2d 975 (1940) (exemption from tax on petroleum products for vessels in foreign commerce was discriminatory as an attempt to provide a privilege not afforded to rail or train transportation).

between the classification adopted and the object to be attained." *Romer v. Evans*, 517 U.S. 620, 632, 116 S. Ct. 1620, 134 L. Ed. 2d 855 (1996); *Heller v. Doe by Doe*, 509 U.S. 312, 321, 113 S. Ct. 2637, 125 L. Ed. 2d 257 (1993) (basis for a classification must "find some footing in the realities of the subject addressed by the legislation").

The rational basis test focuses on whether the City's "high-earner" classification is irrational or irrelevant to the achievement of the ordinance's objectives of remedying the problems associated with regressive taxation and the City's affordability crisis. *State v. Thorne*, 129 Wn.2d 736, 771, 921 P.2d 514 (1996); *see also* Seattle Op. Br. at 49 (stating the purpose of its tax). The Court must first determine whether the legislation applies alike to all persons within a designated class. *City of Seattle v. Rogers Clothing for Men Inc.,* 114 Wn.2d 213, 234–35, 787 P.2d 39 (1990). If not, the Court must then determine whether the City had reasonable grounds for distinguishing between those who fall within the class and those who do not. *Id*. And, even if the City can rationally distinguish between classes, the Court must also determine whether the disparity is germane to the object of the laws in which it appears. *Id*.

Seattle's "high-earner" tax fails all three requirements because it adopted a classification that bears no relation to actual wealth or an individual's ability to pay more taxes. *Stewart Dry Goods Co.*, 294 U.S. at

558. In fact, the "total income" measure is so unrelated to an individual's actual earnings that it subjects many middle-class residents to the "high-earner" tax based solely on how they earn their money—not how much they actually make. The City's income tax thus fails rational basis and violates the equal protection guarantee.

The City addresses Shock's equal protection challenge in one paragraph of its opening brief, insisting that the "high-earner" classification satisfies rational basis because they are better able to pay increased taxes. Seattle Op. Br. at 49. Not true. Seattle's conclusory argument cannot satisfy the degree of scrutiny required by the Washington and U.S. Supreme Courts. *Ockletree v. Franciscan Health Sys.*, 179 Wn.2d 769, 776, 317 P.3d 1009 (2014) (A classification must rest on "real and substantial differences bearing a natural, reasonable, and just relation to the subject matter of the act.") (quoting *State ex rel. Bacich v. Huse,* 187 Wash. 75, 84, 59 P.2d 1101 (1936), *overruled on other grounds by Puget Sound Gillnetters Ass'n v. Moos,* 92 Wn.2d 939, 603 P.2d 819 (1979)). Moreover, that single conclusory sentence fails to address all three prongs of the equal protection analysis.[17]

[17] The City's decision to ignore the three-part equal protection test in its opening brief is fatal to its appeal because an appellant cannot raise new arguments for the first time in its reply brief. RAP 10.3; *Cowiche Canyon Conservancy v. Bosley*, 118 Wn.2d 801, 809, 828 P.2d 549 (1992).

Seattle does not contest Shock's allegation that the tax ordinance treats similarly situated individuals differently. Indeed, it cannot credibly do so. The tax ordinance imposes an annual "tax on the total income of every resident taxpayer," defining "total income" as "the amount reported as income before any adjustments, deductions, or credits on a resident taxpayer's United States individual income tax return for the tax year, currently listed as 'total income' on line 22 of Internal Revenue Service Form 1040 or 'total income' on line 15 of Internal Revenue Service Form 1040A." SMC §§ 5.65.020, .030.

Notably, IRS Form 1040 allows some individuals to reduce their "total income" income by claiming certain deductions related to investment income (such as business or capital losses)—IRS Form 1040A does not. The "total income" measure does not allow individuals to claim any of the deductions that fall below line 22 of IRS 1040 and below line 15 of IRS 1040A. Those excluded personal deductions include charitable giving and/or professional expenses, both of which reduce an individual's actual take home pay and are fully accounted for by an ordinary income tax. Thus, under Seattle's "total income" measure, an individual who makes $250,000 from investment income can avoid the "high-earner" tax classification by claiming business and investment losses; whereas, a similarly situated wage-earner cannot reduce his taxable salary by business expenses. Put

simply, the City's decision to classify "high-earners" based on their "total income" levies a tax on the *net income* of individuals who earn in excess of $250,000 per year from investments and the *gross income* of those who earn wages.

The City's "total income" measure also exposes many low- and middle-class residents to the "high-earner" classification based solely on *how* they earn their money, rather than classifying each person based on their actual take home pay. For example, many closely held companies, like mom-n-pop restaurants, contractors, etc., may generate large amounts of gross income (qualifying them for the "high-earner" classification), but, after the costs of doing business are deducted (many of which deductions are calculated below line 22 of IRS form 1040 and therefore are not considered when measuring "total income"), the owners often take home only a modest amount.[18] Those business owners will be taxed as "high-earners;" whereas their similarly situated, wage-earning neighbors will not.

The inequity to middle-earners goes further. Many small business owners (and others) do not have traditional retirement accounts. Instead, they work their entire career with the goal of funding their retirement

[18] *See*, *e.g.*, Maureen Farrell, *The Most and Least Profitable Businesses to Start*, Forbes (Jan. 18, 2008) (https://www.forbes.com/2008/01/18/citigroup-sageworks-nyu-ent-fin-cx_mf_0118mostprofitable.html).

through a sale of a business or other property. Such one-time occurrences do not make a person any more "wealthy" than a neighbor who has tucked away an equivalent amount of money for retirement throughout her career. And yet Seattle's "total income" measure classifies the small business owner as a "high-earner" and taxes the full sum of the sale, while the neighbor's retirement account remains untaxed. These patent inequities demonstrate that the City's "high-earner" classification relies entirely on the fallacy that "income" equals "wealth." It does not. *Stewart Dry Goods*, 294 U.S. at 558.

Seattle does not provide any rationale for its unequal treatment. Again, it cannot do so because numerous courts have found that an individual's "total income" bears no relation to their actual earnings; thus, there is no reasonable relationship between its "high-earner" classification and any individual's greater ability to pay the tax. *See*, *e.g.*, *Stewart Dry Goods Co.*, 294 U.S. at 558 ("[G]ross sales of a merchant do not bear a constant relation to his net profits.") (*cited favorably by Power, Inc.*, 39 Wn.2d at 196). Indeed, the Oregon Supreme Court rejected the argument that gross income can be relied on to determine whether a person is more or less capable of bearing increased tax burdens:

> Moreover, a tax upon gross income finds but little support in the economic reasons which sustain income taxes. It is the theory of such taxes that they cast the burden of

> governmental maintenance upon those best able to bear it. But, gross income does not necessarily indicate the possession of available surplus.

Redfield v. Fisher, 135 Or. 180, 195, 292 P. 813 (1930).[19] The Arkansas Supreme Court similarly held that "a tax on gross profits would necessarily operate in a discriminatory manner and be arbitrary" because gross receipts bear no fixed relation to actual profits. *Sims v. Ahrens*, 167 Ark. 557, 584, 271 S.W. 720 (1925).

Seattle's decision to classify individuals as "high-earners" based on their "total income" is indistinguishable from the "gross receipts" classification that the U.S. Supreme Court invalidated as "unjustifiably unequal, whimsical, and arbitrary" in *Stewart Dry Goods*, 294 U.S. at 557. In that case, Court concluded that a statute imposing a higher tax rate on larger businesses than on small ones, as defined by their gross receipts, violated the Equal Protection Clause. *Id*. at 566. In so ruling, the Court rejected as irrational the very justification that the City relies on in this case: "that 'generally speaking' he who sells more is in receipt of a greater profit and hence has larger ability to pay." *Id*. at 558. The Court explained that the government cannot rationally conclude that an individual is more capable

[19] The Oregon court's conclusions regarding Oregon's Uniformity Clause were superseded by constitutional amendment. *Barnard Motors v. City of Portland*, 188 Or. 340, 348, 215 P.2d 667 (1950). That portion of the decision, however, is not at issue here.

to bear a greater tax burden based on her total income because such a measure does not speak to whether she actually banks any of the money. *Id*. at 558. Moreover, the Court concluded that the "gross inequalities" resulting from such an arbitrary tax system "may not be ignored for the sake of ease of collection." *Id*. at 560. Despite ample briefing on summary judgment, the City ignores *Stewart Dry Goods* and provides no rational justification for its decision to classify "high-earners" based on their "total income."

Finally, Seattle offers no reasonable explanation why its disparate treatment of individuals, based largely on how they earn their money, is germane to the objective of the tax ordinance. The sole rationale offered by the City is that it opted to place the entire tax burden on those it presumes to be most capable of paying the additional taxes. Seattle Op. Br. at 49. That explanation, however, fails to provide any justification for its decision to allow some "high-earners" to escape or reduce tax liability by claiming business and capital loss deductions, while all others must pay the tax based on their gross unadjusted income. This disparity in treatment, in fact, runs contrary to the City's objective of targeting wealthier individuals because they tend to enjoy income from both wages and investments. CP 371. The inequality resulting from the City's "total income" measure bears no relation to the City's objectives and therefore denies Seattle residents equal protection of the law.

CONCLUSION

For the foregoing reasons, the Shock respondents respectfully request that this Court deny Seattle's appeal and affirm the trial court's decision. If this Court determines that the City was authorized to levy a tax on the income of "high-earners," it should hold that the tax is invalid and in violation of the state and federal equal protection guarantees.

DATED: July 27, 2018. Respectfully submitted,

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July 27, 2018 - 10:15 AM

Transmittal Information

Filed with Court:	Supreme Court
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Appellate Court Case Title:	S. Michael Kunath, et al. v. City of Seattle
Superior Court Case Number:	17-2-18848-4

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