No. 23-171

IN THE

Supreme Court of the United States

CHRIS QUINN, *et al.*,
Petitioners,

v.

STATE OF WASHINGTON, *et al.*,
Respondents.

On Petition for Writ of Certiorari to the Supreme Court of Washington

BRIEF OF THE CITIZEN ACTION DEFENSE FUND, THE ASSOCIATION OF WASHINGTON BUSINESS, THE NATIONAL FEDERATION OF INDEPENDENT BUSINESS SMALL BUSINESS LEGAL CENTER, INC., THE WASHINGTON TRUCKING ASSOCIATIONS, AND THE ETHNIC CHAMBER OF COMMERCE COALITION AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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INTEREST OF THE *AMICI CURIAE*

This *amicus* brief is jointly submitted by the Citizen Action Defense Fund, the Association of Washington Business, the National Federation of Independent Business Small Business Legal Center, Inc., the Washington Trucking Associations, and the Ethnic Chamber of Commerce Coalition.[1] These groups represent individual and small-business taxpayers in the State of Washington and beyond who are negatively affected by Washington's novel capital gains excise tax.

The Citizen Action Defense Fund (CADF) is an independent, nonprofit organization based in Washington State that supports and pursues strategic, high-impact litigation in cases to advance free markets, restrain government overreach, or defend constitutional rights. As a government watchdog, CADF files lawsuits, represents affected parties, intervenes in cases, and files *amicus* briefs when the state enacts laws that violate the state or federal constitutions, when government officials take actions that infringe upon the First Amendment or other constitutional rights, and when agencies promulgate rules in violation of state law.

The Association of Washington Business (AWB) is the principal representative of Washington State's business community. AWB is the state's oldest and

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[1] Pursuant to Rule 37.6, no counsel for a party authored this brief in whole or in part. In addition to the *amici*, their members, and their counsel, the Opportunity for All Coalition made a monetary contribution intended to fund the preparation or submission of this brief. Counsel of record for all parties received notice of *amici*'s intention to file an *amicus* brief more than 10 days prior to the due date for this brief.

largest general business membership federation, representing the interests of approximately 7,000 Washington companies that, in turn, employ over 700,000 employees—around one quarter of the state's workforce. AWB serves both as the state's chamber of commerce and as a manufacturing and technology association. AWB members are located throughout Washington, represent a broad array of industries, and range from sole proprietors to large Washington-based corporations that do business across the country and around the world. Although AWB's membership includes major employers, 90 percent of its members employ fewer than 100 people, and more than half employ fewer than 10. AWB's members include all types of employers that conduct business within and outside Washington.

The National Federation of Independent Business Small Business Legal Center, Inc. (NFIB Legal Center), is a nonprofit, public interest law firm established to provide legal resources to and be the voice for small businesses in the Nation's courts, through representation on issues of public interest affecting small businesses. It is an affiliate of the National Federation of Independent Business, Inc. (NFIB), which is the nation's leading small business association. NFIB's mission is to promote and protect the right of its members to own, operate, and grow their businesses. To fulfill its role as the voice for small business, NFIB Legal Center frequently files *amicus* briefs in cases that will affect small businesses.

The Washington Trucking Associations (WTA) has served as the unified voice for the trucking industry in Washington State since 1922. Member-supported, WTA is dedicated to advocating sound

public policies, providing excellence in education, training, and information, and promoting a safe, dependable, and efficient trucking industry in Washington State.

The Ethnic Chamber of Commerce Coalition (ECCC) was formed in 2016 by 7 ethnic chambers of commerce in the Greater Seattle area to provide a unified voice and increase cooperation on issues affecting small business owners in their communities. The ECCC came together because separately these chambers' voices, despite representing the interests of an estimated 39,000 small businesses in the Seattle area, were not being heard. Among those interests are tax and regulatory stability, as the ECCC's members are directly and negatively affected by increased taxes—including taxes on their owners—and by higher regulatory burdens. The capital gains tax will make it harder and more expensive for small businesses to operate in Washington State.

The *amici* have a strong interest in the outcome of this case. Investment by individual entrepreneurs in Washington is critical to a vibrant economy. The organizations' members have invested their personal resources in developing businesses that provide jobs to hundreds of thousands of individuals throughout the state. Without these investments, the state and local economies will suffer. The challenged law undermines this core investment by allowing for the duplicative taxation of capital gains by different states, and by significantly complicating the system of state taxation of capital gains—thus leading to lower investment in, and migration away from, Washington State.

INTRODUCTION AND SUMMARY OF ARGUMENT

As petitioners explain, review in this case is warranted because Engrossed Senate Substitute Bill (ESSB) 5096 violates the United States Constitution. No state may impose a tax on transactions that occur entirely outside of that state—but that is precisely what ESSB 5096 authorizes. The law is so far afield of the appropriate "horizontal separation of powers," *Nat'l Pork Producers Council* v. *Ross*, 598 U.S. 356, 376 (2023), and the rule that it is "beyond the power of the state" to impose a tax when "the taxable event is outside its boundaries," *Memphis Nat'l Gas Co.* v. *Stone*, 335 U.S. 80, 95 (1948), that review would be warranted even ignoring the real-world consequences of the Washington Supreme Court's decision upholding the law. See Pet. 14-19. But the effects of the law on taxpayers in Washington and beyond, and on the nation's system of state taxation, further demonstrate the need for review.

It is critical not to lose sight of the very premise of ESSB 5096, as defined by the State and as conclusively interpreted by the Washington Supreme Court: The law does *not* tax Washington taxpayer *income* derived from the sale of long-term capital assets. Instead, the law taxes the *actual transactions* in which those assets are sold—and does so in large measure irrespective of where those sales occur. See Pet. App. 25-26; Pet. 18. To be sure, the dollar amount of the tax owed is based on the taxpayer's profits from long-term-capital transactions—but nothing about the Washington Supreme Court's decision upholding the tax depends on that fact. See Pet. App. 27 ("The tax is not *levied* on capital gains; rather, it is *measured* by capital gains.") (emphasis added). The State of

Washington could, under the Washington Supreme Court's analysis, equally calculate the tax as a percentage of the gross revenue from such transactions (*e.g.*, 7 percent of gross proceeds[2]), or at a flat rate unlinked to either gross or net revenue ($1 per share of stock sold[3])—neither of which would depend at all on a Washington taxpayer's Washington income.

Petitioners have demonstrated that this is indefensible, and that ESSB 5096 runs roughshod over our constitutional system's division of sovereignty among the states. See Pet. 15-25. There are also at least two practical, real-world consequences of this novel tax—to taxpayers in Washington and elsewhere—that we write to highlight. These further demonstrate the importance of this Court's review.

First, the fact that Washington has chosen to tax *transactions* rather than *income* leads to the very real chance of duplicative or double taxation. This is true both for intangible and for tangible assets. See Part A, *infra*.

Second, the inconsistent treatment of capital gains between Washington, on the one hand, and every other state and the federal government, on the

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[2] See *Comptroller of Treasury of Md.* v. *Wynne,* 575 U.S. 542, 552 (2015) ("[W]e have … squarely rejected the argument that the Commerce Clause distinguishes between taxes on net and gross income.").

[3] See Jared Walczak, *Why Washington State Can't Claim Its Capital Gains Tax Is an Excise Tax*, Tax Foundation, Dec. 16, 2021, *available at* https://taxfoundation.org/blog/washington-state-capital-gains-tax/ ("If Washington had chosen to levy a tax on sales of stocks or bonds, such a stock transfer tax would be an excise tax, because it's based on the transaction or activity.").

other, will significantly complicate tax compliance, causing no shortage of problems for Washington taxpayers—and especially taxpayers with multiple residences or who move between states. See Part B, *infra*.

REASONS FOR GRANTING THE PETITION

The Washington Supreme Court's Decision Has Grave Implications For Washington Taxpayers And The Nation's System Of State Taxation.

Petitioners have demonstrated that ESSB 5096 is unconstitutional, and that this Court's review is warranted to undo the grave threat the lower court's decision poses to our federalist system. Review is also warranted because of the consequences for individual taxpayers in Washington. The law creates a significant risk of double taxation, see Part A, *infra*; and will damage the Washington State business environment and significantly complicate tax compliance, see Part B, *infra*.

A. ESSB 5096 creates a significant risk of double taxation.

The federal government, as well as *every* state that taxes capital gains except Washington, imposes capital gains taxes directly on the income the taxpayer receives from the sale of capital assets. See Pet. App. 57 (McCloud, J., dissenting). There are rules for allocating that income among the states, thus ensuring that the same income is not taxed multiple times. See *Wynne*, 575 U.S. at 561 ("[T]he near-universal state practice is to provide credits against personal income taxes for such taxes paid to other States."); *Goldberg* v. *Sweet*, 488 U.S. 252, 260-61 (1989) ("[T]he central purpose behind the apportionment requirement [of *Complete Auto*

Transit, Inc. v. *Brady*, 430 U.S. 274 (1977)] is to ensure that each State taxes only its fair share of an interstate transaction."); see also, *e.g.*, FTB Pub. 1100, *Taxation of Nonresidents and Individuals Who Change Residency* (May 2020), *available at* https://www.ftb.ca.gov/forms/misc/1100.html (California rules). Of course, states at times seek to extract more of the overall tax burden than is appropriate—but the courts are well-versed in blocking such schemes. See, *e.g.*, *Wynne*, 575 U.S. at 561 ("[A]s our Commerce Clause jurisprudence developed, the States have almost entirely abandoned [protectionist regimes that favored the local economy over interstate commerce], perhaps in recognition of their doubtful constitutionality.").

But Washington State has not proceeded down this well-trodden income-tax path, choosing instead to directly tax *transactions* that occur in other states. This is plainly unconstitutional—"The principle that a State may not tax value earned outside its borders rests on the fundamental requirement of both the De Process and Commerce Clauses that there be some definite link, some minimum connection, between a state and the person, property, or transaction it seeks to tax." *Allied-Signal, Inc.* v. *Dir., Div. of Tax'n*, 504 U.S. 768, 777 (1992) (cleaned up). But this choice also leads to a very real chance of duplicative or double taxation, which this Court has also held unconstitutional. *Wynne*, 575 U.S. at 551 (noting the numerous times the Court has invalidated laws "that might have resulted in the double taxation of income earned out of the State").

As in *Wynne*, "[t]he effect of" Washington State's novel "scheme is that some of the income earned by [Washington] residents outside the State is taxed

twice," and the "scheme creates an incentive for taxpayers to opt for intrastate rather than interstate economic activity." *Id.* at 545. This significant risk of duplicative taxation occurs in at least two distinct ways—one for intangible assets, and one for tangible assets.

1. Double taxation of intangible assets.

The risk of double taxation is most obvious with respect to "intangible" assets. Under RCW 82.87.100(1)(b), Washington taxes the full value of "[l]ong-term capital gains … derived from intangible personal property … if the taxpayer was domiciled in [Washington] state at the time the sale … occurred." *Ibid.* Unlike with respect to tangible assets, see RCW 82.87.100(2)(a), Washington provides *no* credit to taxpayers against the capital gains tax on intangible assets for any capital gains tax levied by another state. But while it may be definitional that intangible assets do not exist in a specific physical place, there are many instances in which another state might reasonably impose a capital gains tax on the sale of those assets even if owned by a Washington domiciliary.

Imagine, for example, a Washington domiciliary who is a part-owner of a business, organized as an LLC or an S corporation, that is physically located solely in Montana. See RCW 82.87.040(b)(1) (taxing individual owner for capital gains earned by such corporate pass-through entities); *Wynne*, 575 U.S. at 546 n.1. If the owners sell that business, the tangible assets will be located in Montana and (assuming those assets have not been in Washington in the past two years, see RCW 82.87.100(1)(a)(i)) will be taxed only by Montana. But Washington will nonetheless tax any amount obtained for the sale of the goodwill and brand

recognition of that business, see RCW 84.36.070(2)(c) (defining "brand names, … reputation, … prestige, [and] good name" as intangible personal property)—and will give no credit for any tax that Montana reasonably assigns to the sale of those intangible assets.

This is problematic because Montana would be well within its rights to tax the capital gains on these intangible assets. As this Court explained in *Mobil Oil Corp.* v. *Commissioner of Taxes*, 445 U.S. 425 (1980), "[a]lthough a fictionalized situs for intangible property sometimes has been invoked to avoid multiple taxation of ownership, there is nothing talismanic about the concepts of 'business situs' or 'commercial domicile' that automatically renders those concepts applicable when taxation of income from intangibles is at issue." *Id.* at 445. The Court specifically noted in *Mobil Oil* that "'the reason for a single place of taxation no longer obtains' when the taxpayer's activities with respect to the intangible property involve relations with more than one jurisdiction." *Ibid.* (quoting *Curry* v. *McCanless*, 307 U.S. 357, 367 (1939)); see also Pet. 20.

But one does not need to posit an out-of-state business for double taxation to be possible. A second example of potential double taxation of intangible assets occurs with respect to a Washington resident's ownership of corporate stocks or securities. Washington, like most states, defines the "stocks, or shares of private corporations" as intangible personal property. See RCW 84.36.070(2)(a). And most states attribute the income from the sale of stock to the domicile of the seller. See, *e.g.*, New York State, *IT-203-I: Instructions for Form IT-203*, *available at* https://www.tax.ny.gov/forms/html-instructions/2022/

it/it203i-2022.htm#nonres-ny-income ("New York source income *does not include* … gains from the sale or exchange of intangible personal property"). Recall, however, that Washington is *not* taxing the income from the sale of those shares of stock—it is taxing the actual act of selling those shares. And *that sale* happens in a physical location—for example, the location of the New York Stock Exchange. If the Washington law is constitutional, and the physical sale of intangible stock in New York State can be taxed by Washington State, New York State too could choose to tax the sale of these shares (based on the location at which the sale occurred), despite the seller's Washington domicile. And indeed, New York has recently considered just such a tax. See Reuters, *NYSE chief warns it may exit New York if stock transfer tax is imposed*, Feb. 9, 2021, *available at* https://www.reuters.com/article/us-nyse-new-york-tax/nyse-chief-warns-it-may-exit-new-york-if-stock-transfer-tax-is-imposed-idUSKBN2A92UL. Unlawful double taxation could thus occur. See *Wynne*, 575 U.S. at 562; *Goldberg*, 488 U.S. at 261-62.

2. Double taxation of tangible assets.

There is also a real risk of double taxation with respect to tangible assets. Although ESSB 5096 provides for a credit in certain circumstances for the capital gains tax imposed by another state on the sale of tangible assets, see RCW 82.87.100(1)(a)(3), 82.87.100(2)(a), that credit is incomplete and does not eliminate the risk of double taxation. In particular, the Washington law creates a significant risk of double taxation for residents of *other* states (including individuals with dual residences, in Washington State and elsewhere).

Washington imposes its excise tax on the capital gains derived from tangible property located in Washington, irrespective of the domicile or residency of the owner of that property. See RCW 82.87.100(1). And Washington offers no credit against that tax for taxes paid to another state. See RCW 82.87.100(2)(a) (credit allowed for taxes "derived from capital assets *within the other taxing jurisdiction*") (emphasis added). But many other states—including Oregon, Washington's southern neighbor—afford residents credits against those states' capital gains taxes only for *income taxes* paid to another jurisdiction, not for excise taxes. See, *e.g.*, ORS 316.082(1) ("A resident individual shall be allowed a credit against the tax otherwise due under this chapter for the amount of any *income* tax imposed on the individual … by another state on *income derived from sources therein*.") (emphasis added). Thus, as one Oregon analyst has noted, "[i]f [an Oregon] farmer … sells … [an] asset in Washington, they may be subject to the new excise capital gains tax.… [T]he farmer could end up paying both taxes on the same source of income." Jeff Newgard, *Washington's Capital Gains Could Present Tax Challenges for Some Oregonians*, Peak Policy, Apr. 14, 2023, *available at* https://peakpolicy.com/washingtons-new-capital-gains-tax-could-present-tax-challenges-for-some-oregonians/.

This risk is by no means limited to Oregon residents. In Idaho, too, "[a] resident individual shall be allowed a credit against the tax otherwise due under this chapter for the amount of any *income tax* imposed on the individual … for the taxable year by another state on income derived from sources therein while domiciled in Idaho and that is also subject to tax under this chapter." Idaho Stat. § 63-3029(1) (emphasis added). And the same is also true in

Arizona, a state where many Washington part-year residents also reside. See Ariz. Rev. Stat. § 43-1071(A) ("residents are allowed a credit against the taxes imposed by this chapter for *net income taxes* imposed by and paid to another state or country on income taxable under this chapter") (emphasis added).

* * * * *

Washington's contrived scheme to avoid the Washington State Constitution's limits on *income* taxes, by constructing a novel capital gains *excise* tax, trenches on the rights of other states to obtain their reasonable share of tax revenue—and on the rights of taxpayers not to be taxed multiple times—in contravention of the Constitution.

B. Washington's novel approach of taxing capital gains via excise tax will damage the Washington State business environment and significantly complicate tax compliance.

Review of ESSB 5096 is also warranted because of the negative effects the law will have on businesses and individual business owners in Washington State.

For starters, the law amounts to an immense tax on Washington business owners. Indeed, initial collections for the 2022 tax year were almost $850 million—more than *triple* what the state had projected the tax would raise ($248 million). See Jerry Cornfield, *State rakes in nearly $850M from capital gains tax*, WASHINGTON STATE STANDARD, May 25, 2023, *available at* https://washingtonstatestandard.com/2023/05/25/washington-collects-nearly-850-million-in-capital-gains/.[4] While a state generally may set

[4] This $850 million figure includes some estimated capital gains tax payments for the 2022 tax year. Analysts expect that, once

tax rates as it sees fit without violating the Constitution, the size of this tax burden—and the state's woefully inaccurate modeling of that burden—support further review of the constitutional questions presented.

In addition, the law will impose massive compliance burdens on taxpayers. For example, although the law purports to exclude small businesses, RCW 82.87.070, it will actually affect 95 percent of all businesses because under RCW 82.87.040(4)(b) the law applies to so-called "disregarded entities"—all pass-through businesses, including sole proprietorships, partnerships and S-corporations, as well as single-member LLCs. See Victor Menaldo, *WA's capital gains tax will have unintended consequences,* SEATTLE TIMES, Apr. 11, 2023, *available at* https://www.seattletimes.com/opinion/was-capital-gains-tax-will-have-unintended-consequences/. The net effect will be far more complicated tax compliance and a significant reduction in business investment and R&D. *Ibid.*

The law will also greatly complicate the tax situation for anyone with multiple residences or who moves between states. As discussed above, ESSB 5096 differentiates taxes based on residence and domicile, but gives little guidance for how to *determine* a taxpayer's residence or domicile. The law defines a resident as:

> an individual: (i) Who is domiciled in this state during the taxable year, unless the individual (A) maintained no permanent place of abode in this state during the entire taxable year,

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all taxpayers finalize their 2022 tax filings, the final amount collected may "dip[] a few million dollars." *Ibid.*

> (B) maintained a permanent place of abode outside of this state during the entire taxable year, and (C) spent in the aggregate not more than 30 days of the taxable year in this state; or (ii) Who is not domiciled in this state during the taxable year, but maintained a place of abode and was physically present in this state for more than 183 days during the taxable year.

RCW 82.87.020(10)(a). Despite including various factors for determining residency, the law offers no definition for the terms "domicile," "place of abode," or "permanent place of abode" (and no guidance on whether the latter two terms meaningfully differ), making even the definition of "resident" so opaque that it hardly serves as one.

Far from providing a clear standard for taxpayers to follow, ESSB 5096 thus raises more questions than it answers. Indeed, one law firm published an 8-page, 15-point checklist to assist its clients in determining their domicile for purposes of ESSB 5096. See Lane Powell, *Washington Capital Gains Tax: Checklist of Factors Relevant to a Taxpayer's Domicile*, July 13, 2023, *available at* https://www.lanepowell.com/our-insights/264101/washington-capital-gains-tax-checklist-of-factors-relevant-to-a-taxpayers-domicile.

The law will also add complexity for all taxpayers who need to track transactions that are taxed differently by multiple states, given Washington's unique excise tax system. See page 11, *supra*.

Of course, tax laws generally are complex. But the complexity here derives from the very fact that makes ESSB 5096 unconstitutional—that it imposes an excise tax on transactions that occur outside of the

state, rather than merely taxing income properly attributable to a resident of the state. Before this wholly novel and deeply problematic law is allowed to stand, this Court's review is warranted.

CONCLUSION

For the foregoing reasons and those in the petition for a writ of certiorari, the Court should grant the petition and hold that ESSB 5096 is unconstitutional.

Respectfully submitted.

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