No. 102223-9

SUPREME COURT OF THE STATE OF WASHINGTON

ANTIO, LLC, AZUREA, LLC, BACK BOWL I, LLC, CANDICA, LLC, CERASTES-WTB, LLC, GCG EXCALIBUR, LLC, LINDIA, LLC, OAK HARBOR CAPITAL, LLC, OAK HARBOR CAPITAL II, LLC, OAK HARBOR CAPITAL III, LLC, OAK HARBOR CAPITAL IV, LLC, OAK HARBOR CAPITAL VI, LLC, OAK HARBOR CAPITAL VII, LLC, OAK HARBOR CAPITAL X, LLC , OAK HARBOR CAPITAL XI, LLC, and VANDA, LLC,

Petitioners,

v.

WASHINGTON STATE DEPARTMENT OF REVENUE,

Respondent.

MEMORANDUM OF *AMICI CURIAE* SIMPSON TASK FORCE MEMBERS IN SUPPORT OF PETITION FOR REVIEW

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I. IDENTITY AND INTEREST OF AMICUS CURIAE

Amici curiae are state and local tax practitioners in Washington State, Garry G. Fujita and Michael W. Roben. Each served on the task force with the Department of Revenue ("Department") and other business community members in 2001 and 2002 to provide a clarification of the deduction for investment income under RCW 82.04.4281 after this Court's decision in *Simpson Investment Co. v. State*, 141 Wash.2d 139, 3 P.3d 741 (2000). Such task force is referred to as the "Simpson Task Force" and *amici* as amici or "Members."

The Members were directly involved in raising concerns for impacted taxpayers and the economy of the State and working with Department officials on draft legislation to facilitate a fix.

Members join this brief solely as individuals, not as representatives of the firms with which they are affiliated. Each Member is currently in private practice. Member Fujita was previously Assistant Director of the Department of Revenue for

Interpretation and Appeals and, in 2001-02, was a partner at Davis Wright Tremaine LLP. Member Roben practiced at Arthur Andersen at the time of the Simpson Task Force and later founded KOM Consulting, PLLC, a consulting firm focused specifically on state and local taxation.

Members have not been paid by any client to submit this *amicus curiae* memorandum. They submit this memorandum out of a strong interest in ensuring that this Court is aware of the importance of the issues in this case for a very broad cross-section of Washington businesses and residents. They have a further strong interest in seeing that the collaboration of the Department and the business community in the Simpson Task Force is not undone for lack of awareness of this context.

II. ISSUES OF CONCERN TO AMICI

Amici are concerned that the Court of Appeals' decision, if left uncorrected by this Court, will lead to taxing the investment income of the very collective investment vehicles that were supposed to be protected by the 2002 legislation,

which was developed on initiation by the Department as directed by the Governor.

Amici are also concerned that the parties have not accurately informed the Court of either the meaning of its original decision on the prior statute, *John H. Sellen Constr. Co. v. State*, 87 Wash.2d 878, 558 P.2d 1342 (1976), or a pertinent Department regulation, WAC 458-20-19402, that has long represented the policy of the amendment of RCW 82.04.4281.

III. STATEMENT OF THE CASE

The Members adopt the Petitioners' Statement of the Case. *See* Pet. for Review at 6-7.

IV. ARGUMENT

A. The Court of Appeals' Interpretation of RCW 82.04.4281 Raises an Issue of Substantial Public Interest that Should Be Determined by This Court.

This Court should grant review because the scope of the investment income deduction impacts a broad cross-section of

Washington economic activity beyond the facts of Petitioners' case. Review is warranted under RAP 13.4(b)(4).

In the 2002 session law in question, the legislature stated expressly that the statute's interpretation is of the utmost importance to Washington's economy. The legislature wanted to pivot away from this Court's interpretation of the prior statute and avoid a narrow interpretation of the deduction, stating:

> The legislature further finds that the decision of the state supreme court in *Simpson Investment Co. v. Department of Revenue* could lead to *a restrictive, narrow interpretation* of the deductibility of investment income for business and occupation tax purposes.

Laws of 2002, ch. 150, § 1 (emphasis added). Further, the legislature wanted to create a stable legal framework for the deduction that took into account the work of the Simpson Task Force:

> [T]he legislature directed the department of revenue to work with affected businesses to develop a revision of the statute that would provide certainty and stability for taxpayers and the state.

Id. And what policy was to be embodied in this stable legal framework?

> The legislature intends, by adopting this recommended revision of the statute, *to provide a positive environment for capital investment in this state*, while continuing to treat similarly situated taxpayers fairly.

Id. (emphasis added).

In *Antio, LLC v. Washington State Dep't of Revenue*, 26 Wash. App. 2d 129, 527 P.3d 164 (2023), the court acknowledged that a "plain language" reading of the statute supports Petitioners' position. *Id.* at 137. But the court gave priority to a "narrow" interpretation, *see id.* at 135, upholding the Department's theory that the legislature actually intended to preserve an interpretation of the prior statute by this Court in *O'Leary v. Dep't of Revenue*, 105 Wash.2d 679, 717 P.2d 273 (1986). *Id.* at 140.

When the legislature amends a statute expressly because of its dissatisfaction with the trend in this Court's interpretation, it is of utmost public interest that this Court make the

determination whether to reaffirm its pre-amendment cases. *Cf. In re Estate of Hambleton*, 181 Wash.2d 802, 819, 335 P.3d 398 (2014) ("Although it is the court's obligation to determine and carry out the intent of the legislature, the legislature is occasionally disappointed with the court's interpretation.") (citing *Hale v. Wellpinit Sch. Dist. No. 49*, 165 Wash.2d 494, 509, 198 P.3d 1021 (2009)).

The legislature's goal of providing a "positive environment for capital investment in this state" meant assuring that there be a *competitive* environment for capital investment, because of the mobility of intermediary investment vehicles. Collective investment vehicles, as well as charitable trusts and foundations, represent jobs and other economic and social contributions to the community.[1]

[1] The legislature's policy in support of a robust capital investment climate in the state as expressed in RCW 82.04.4281, covering all types of investment income – whether ordinary income items like interest and dividends, and short-term capital gains as well as long-term capital gains – is distinct from and perhaps even complementary to the economic and social policies underlying the more recent Washington capital gains tax, which taxes Washington individual residents' sales of long-term capital assets (with a $250,000 annual deduction).

The Members are feeling a kind of whiplash from the lower court's decision. Their informal discussions *today* with clients, the tax-advisor community, and staff at the Department of Revenue are just like the same discussions *in 2000-02*. Member Fujita testified at a committee hearing on H.B. 1853, a bill filed in the 2001 legislative session on behalf of business interests to clarify the deduction. He identified as "chaotic panic" the sense of uncertainty that *Simpson* generated. House Finance - TVW (https://tvw.org/video/house-finance-38/) (H. Fin. Comm. Hr'g (Feb. 20, 2001), audio recording at 2:43). Mutual fund advisors, for example, realized that a B&O tax of 1.5% on mutual funds total investment returns would have tended to push funds out of Washington to preserve a competitive position with funds in other states.[2]

The Department's Director in 2001, Fred Kiga, testified in response that "[t]he department understands the potential

[2] *See also* Testimony of G. Barton (California income tax laws made the location of a fund neutral in California's taxation of venture capital investors), *id.* at 2:55.

chaos that the uncertainty occasioned by Simpson Investment may cause." *Id.* (beginning at 2:58:56).[3] He, however, sought to allay concerns, saying, "Furthermore, we have recently circulated a draft that stipulates those collected investment vehicles, which by the way includes venture capital funds, that are not subject to taxation under the department's current reading of the exemption." Importantly, this statement logically rests on the assumption that the income of collective investment vehicles was from "investments."

Although H.B. 1853 was not enacted in 2001, the legislature did pass H.B. 1361 (Laws of 2001, ch. 320). It required the Department to report to the legislature "on the progress made in working with affected businesses on potential amendments to RCW 82.04.4281 . . . ." *Id.,* § 20. Governor Locke's veto message on section 19 of the act stated that he had directed the Department to adhere to its prior policies and interpretations, unaffected by *Simpson*, and that "[t]he Director

[3] Unofficial transcriptions by counsel.

[of Revenue] has formed a task force" to reach consensus on tax policy and administrative changes in response to *Simpson,* including representatives from many companies as well as Arthur Andersen (Member Roben) and Davis Wright Tremaine (Member Fujita). Governor's Partial Veto, H.B. 1361 (May 15, 2001).

The Members and the Washington business and taxpayer community understood from this act and the work of the Simpson Task Force that the consensus draft of the 2002 amendment – called "this recommended version" in Laws of 2002, ch. 150, § 1 – resolved this chaos by establishing a "plain language" deduction for investment income limited only by the express exclusions in current RCW 82.04.4281(2). *See* H. Bill Report, H.B. 2641, 57th Wash. Legis. (2002).

The lower court's decision has revived the old uncertainty – perhaps even made it worse. Individuals are wondering whether to withdraw from Washington-based collective investment funds due to uncertainty and potential

impact on investment returns. The Members are also aware that some non-Washington investment funds have already decided to close their funds to investors from Washington out of concern that their income would be attributed to Washington in proportion to their investor base here.

In sum, the decision below has renewed the uncertainty of 2000-02 at a level of substantial public interest. This Court's review is fully warranted.

B. Review is Warranted under RAP 13.4(b)(1): the Decision Below is Inconsistent with This Court's Decision in *Sellen*.

The Members disagree with statements by either Petitioners or the Department that *O'Leary* simply drew on the meaning of "investments" inherited from *Sellen.* *E.g.*, Department's Answer at 12. *Sellen* did not define "investments." Instead, it *assumed* a plain meaning for the term and framed the legal question thus:

> The investment incomes [of all taxpayers in the case] clearly are "(a)mounts derived by persons . . . from investments or the use of money as such." Thus, respondents' incomes are deductible unless

> respondents are "engaging in banking, loan, security, or other financial businesses."

Sellen, 87 Wash.2d at 882. The Court applied the term "investments" to the specified items in which the taxpayers placed their capital: time certificates, commercial paper, repurchase agreements, commercial discount notes, corporate bonds, savings deposits, stocks, bonds, and real estate notes and mortgages. *Id.* at 879-80.

The Court did *not*, in *Sellen*, say that a deductible "investment" is limited to the employment of surplus capital by a business otherwise engaged in some other activity. This was instead a tool for distinguishing the taxpayers – other than Acacia Memorial Park Permanent Care Fund (AMPPCF) – from "other financial businesses." *Id.* at 883. However, AMPPCF had *only* investment income and was held entitled to the deduction. Therefore, "incidental investments of surplus funds" cannot logically have been the touchstone of *Sellen*'s rule of decision.

When the legislature has expressly called this Court's jurisprudence into question, the issue merits a full, nuanced review and recapitulation of its precedents. *See, e.g., Quinn v. State*, 1 Wash.3d 453, 472-77, 526 P.3d 1 (2023) (parsing the precedents on excise versus property taxation). Just as the Court can acknowledge the flaws of its opinion in *Apartment Operators Ass'n of Seattle, Inc. v. Schumacher*, 56 Wash.2d 46, 351 P.2d 124 (1960), in historical context, *see Quinn*, 1 Wash.3d at 476, the Court should question whether the terse opinion in *O'Leary* was a reasonable reinterpretation of *Sellen.* It was not.

In *O'Leary*, the Court said:

> As we stated in *John H. Sellen Constr. Co. v. Department of Rev.*, 87 Wash.2d 878, 883, 558 P.2d 1342 (1976), an interpretation of an "investment" *should be* limited to the plain and ordinary meaning of the word.

105 Wash.2d at 682 (emphasis added). *Nothing* on page 883 of the *Sellen* opinion says anything like that. Then the Court said,

> Whether an investment is "incidental to the main purpose of a business" *is an appropriate means* of

> distinguishing those investments whose income *should be exempted* from the B & O tax of RCW 82.04.4281.

Id. (emphasis added). This sentence, too, does not fairly paraphrase anything the Court said in *Sellen*, and it introduced policy judgments without a clear source in legislative text.

Instead, *Sellen* had endorsed the Department's by-then withdrawn Excise Tax Bulletin 368.04.224 (June 12, 1970), which had stated:

> Where the activities involved are essentially *in competition with* financial businesses and this is a regular part of the taxpayer's normal business practice, the department believes that the activities constitute financial business and are subject to tax.

87 Wash.2d at 884 (emphasis added). This statement is 100% aligned with amended RCW 82.04.4281, as argued by Petitioners. It is also aligned with the legislature's intention to "continu[e] to treat similarly situated taxpayers fairly," Laws of 2002, ch. 150, § 1, because businesses "in competition with" banks, lenders, and securities businesses are excluded from the deduction through RCW 82.04.4281(2)(a). Subsection (2), it

should be noted, preserved the result in *O'Leary* independent of the deduction-granting clause in subsection (1).

The Court should read the history carefully and acknowledge that RCW 82.04.4281, as amended, actually restored *Sellen's* approach. Notwithstanding the Court of Appeals' reliance on *O'Leary*, the decision below conflicts with *Sellen.*

C. A Legislative Acquiescence Context in This Case Merits Review

The parties have not alerted the Courts to a Department regulation adopted more than 10 years ago that belies the Department's changed position on the investment deduction. The regulation implies legislative acquiescence in and validation of Petitioners' interpretation of RCW 82.04.4281.

WAC 458-20-19402 was promulgated by the Department in 2012 to provide methods for apportioning income from interstate activities for B&O tax purposes. The statute requires attributing receipts based on where the taxpayer's customers receive the benefit of the taxpayer's services. RCW

82.04.462(3)(b)(i). The Department identified several different categories of service activities for purposes of implementing this standard, among them services provided to a customer "not engaged in business" or unrelated to the customer's business. WAC 458-20-19402(303)(d).

Of relevance are examples identified by the Department of customers "not engaged in business." These include an "Arizona resident" who receives stockbroker services from a Washington business and a "***mutual fund***" that is managed by an "Investment Manager." WAC 458-20-19402(304)(d)(Examples 31, 32) (emphasis added).

Although RCW 82.04.140 defines "business" broadly as including "all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or to another person or class, directly or indirectly," the Department formally adopted a regulation saying both individual investors and mutual funds are *not* "engaged in business." Why? The reason is, both have

been entitled to the investment income deduction pursuant to the plain language of amended RCW 82.04.4281.

Legislative acquiescence comes into play when statutory language is ambiguous and the agency has a longstanding regulation in place. *See, e.g.*, *First Student, Inc. v. Dep't of Revenue*, 194 Wash.2d 707, 717, 451 P.3d 1094 (2019) (quoting *Pringle v. State*, 77 Wash.2d 569, 573, 464 P.2d 425 (1970)). If amended RCW 82.04.4281 is considered ambiguous, the Department's regulation impeaches its new argument that the legislature enshrined *O'Leary's* supposed definition of "investment" for periods after 2002.

V. CONCLUSION

For these reasons, we respectfully request that the Court accept review of the Court of Appeals' decision and reverse.

I certify that this document, excluding the parts exempted from the word count by RAP 18.17, contains 2,499 words.

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Respectfully submitted September 25, 2023,

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CERTIFICATE OF SERVICE

I certify under penalty of perjury under the laws of the State of Washington that on September 25, 2023, I caused the foregoing Memorandum of *Amici Curiae* to be filed and caused a true and correct copy of same to be served upon the following parties as indicated below:

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