

No. 70514-8-I

IN THE COURT OF APPEALS  
OF THE STATE OF WASHINGTON  
DIVISION I

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U.S. BANK, Personal Representative of the Estate of ELAINE B.  
GREEN-ELDRIDGE,

Respondent,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Appellant.

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**BRIEF OF RESPONDENT**

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## I. INTRODUCTION

This case is about the Washington Department of Revenue's ("DOR") attempt to reach back and tax an irrevocable trust created 28 years ago by the estate of Joshua Green, Jr. ("Joshua").

Before his death, Joshua executed a will directing the creation of a marital trust ("Joshua's Trust"), also referred to as a qualified terminable interest property ("QTIP") trust. Joshua died in 1985. The terms of Joshua's Trust were fixed at his death and could not thereafter be changed—his wife Elaine ("Elaine") would receive trust income during her life, but when her income interest terminated at her death, Joshua's Trust would go to the beneficiaries Joshua designated in his 1983 will.

Elaine died twenty years later, in 2005. Before her death, the Washington legislature enacted a new stand-alone estate tax. This new tax was imposed on every "transfer of property" of a decedent and applied "prospectively only, not retroactively."<sup>1</sup> Notwithstanding the clear language of the statute, the DOR attempted to impose this new tax not only on the transfer of property in Elaine's estate, but also on the entire amount of Joshua's Trust.

Elaine's Estate filed suit in 2009 to obtain a refund for taxes attributable to Joshua's Trust. At the same time, the DOR was in litigation with several other estates over the inclusion of marital (QTIP) trust property in the taxable estate of the surviving spouse. Because two other

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<sup>1</sup> RCW 83.100.040 (legislative notes).

cases had sought review before the Supreme Court on this very issue, the Estate's case was stayed for over two years.

The Supreme Court ruled unanimously in favor of estate taxpayers in *Clemency v. State (In re Estate of Bracken)* 175 Wn.2d 549, 290 P.3d 99 (2012) ("*Bracken*"), on October 18, 2012, denying reconsideration on January 10, 2013. When the DOR refused to issue the refund due for several months, the Estate was forced to file a motion to compel a refund. In response to the motion, the DOR conceded that the Estate was due a refund under *Bracken*. The trial court granted the Estate's motion and ordered the DOR to refund the tax no later than May 24, 2013. The DOR remained recalcitrant, ignoring the trial court order, instead hoping that the Washington legislature would eventually amend the statute retroactively. On June 13, 2013, the DOR filed a notice of appeal of the very judgment it conceded was correct under *Bracken*. The day *after* the DOR's notice of appeal, Washington enacted amendments to its estate tax. See Engrossed House Bill 2075, 63rd Leg., 2d Sp. Sess. (Laws of 2013, 2d Sp. Sess., ch. 2) (the "2013 Amendments").

The 2013 Amendments do not change the threshold requirement of RCW 83.100.040(1) and *Bracken* that an estate tax can only be imposed on a "transfer of property" of the decedent. As is explained below, any interest Elaine had in Joshua's Trust terminated as of her death. She did not, and could not, transfer Joshua's Trust. And no court has ever held that termination of a lifetime interest in a QTIP trust is a "transfer."

The DOR nevertheless argues in this case that the 2013 Amendments allow the DOR to impose a tax on Joshua's Trust. To the extent that the 2013 Amendments would do so, they are unconstitutional and in violation of the Separation of Powers doctrine, the federal and state Due Process Clause, and the federal and state Impairment Clause. In addition, the 2013 Amendments violate the Uniformity Clause of the Washington Constitution, art. VII, § 1. Finally, this Court should not condone the DOR's use of delay and violation of a court order to deprive Elaine's Estate of a refund.

## II. STATEMENT OF ISSUES

1. Should the trial court's final judgment be upheld because the expiration of Elaine's lifetime income interest in Joshua's Trust is not a "transfer" under Washington Supreme Court precedent (including *Bracken* and *McGrath*), U.S. Supreme Court precedent and RCW 83.100.040(1)?

2. If the 2013 Amendments are read to tax Joshua's Trust in Elaine's Estate, then are the 2013 Amendments unconstitutional under: (a) the Separation of Powers doctrine; (b) the federal and state Due Process Clause; (c) the federal and state Impairment Clause; and (d) the Uniformity Clause of the Washington Constitution?

3. Should the Court deny the DOR's collection of a retroactive estate tax where the DOR: (a) improperly used delay to deprive Elaine's Estate of a tax refund; and (b) filed an appeal with no legal basis?

### III. STATEMENT OF THE CASE

#### 1. Joshua Green, Jr. Created an Irrevocable Marital Trust 28 Years Ago.

Joshua Green, Jr. died in Washington on October 18, 1985. *See* CP 5; CP 23. His Last Will and Testament included provisions for the creation and funding of a marital trust at death. *See* AR 199-200 (Joshua's Last Will and Testament); CP 113, Nos. 4-5 (DOR's admissions regarding same). Accordingly, at Joshua's death, his estate created an irrevocable marital trust in 1988. *See* CP 5; CP 23; AR 199-208. Joshua's Trusts provided a lifetime income interest for Elaine terminating at her death and designated beneficiaries thereafter. *Id.* His federal estate tax return was prepared and his estate made an irrevocable federal election under IRC § 2056(b)(7).<sup>2</sup> *See* CP 6; CP 23; CP 116 (No. 16); AR 210-43. Joshua's Estate also filed a Washington state estate tax return in full compliance with state law, but no state QTIP election was available. *See* CP 6; CP 23. His estate paid all taxes due, and it received both federal and state final tax clearance. *See* CP 6; CP 24 ¶.

#### 2. Washington Enacts a New Stand-Alone Tax on

May 17, 2005. From 1981 through December 31, 2004, Washington's estate tax was referred to as a "pickup tax." *See Bracken*, at 556-77. This

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<sup>2</sup> The effect of a federal QTIP election is described in *Bracken*, at 555-56. While the creation of a marital trust is a transfer, and therefore taxable on the federal return, a taxpayer may elect under IRC § 2056(b)(7) to treat the trust as a QTIP. *Id.* A QTIP transfer is not taxed on the federal return; however, the statutory quid pro quo is that the property is included in, and therefore taxed in, the surviving spouse's *federal* estate under IRC § 2044. *Id.* Logically, QTIP property in the surviving spouse's estate is not a transfer--if it were, the fiction of Section 2044 would be unnecessary.

tax was calculated by simply picking up the maximum allowed federal credit for state death taxes. *Id.* All state estate taxes were thus fully reimbursed as a federal credit. *Id.* In essence, Washington shared estate tax revenues with the federal government. *Id.* However, in *Estate of Hemphill v. Department of Revenue*, the Court held that Washington's estate tax was phased out from 2001 to 2004 following the elimination of the federal state death tax credit. *See* 153 Wn.2d 544, 105 P.3d 391 (2005).<sup>3</sup>

From January 1, 2005 to May 16, 2005, Washington had no estate tax. Then, effective May 17, 2005, the legislature passed a new stand-alone estate tax. Laws of 2005, ch. 516, § 1, *codified as* ch. 83.100 RCW (the "2005 Act" or "Act"). The Act provides that the estate tax is "imposed on every transfer of property located in Washington." RCW 83.100.040(1). Provisions of the Act apply "prospectively only and not retroactively" and "only to estates of decedents dying on or after [May 17, 2005]." Laws of 2005, ch. 516, § 20. The new stand-alone tax also authorized a state QTIP election as a companion to the federal QTIP election under IRC § 2056(b)(7). *See* 83.100.047.

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<sup>3</sup> In *Hemphill*, the Court stated that "[u]ntil or unless the legislature revises [former] RCW 83.100.030 ... to specifically and expressly create a stand-alone estate or inheritance tax, [former] RCW 83.100.030 remains as a 'pickup' tax, in which all state estate tax due must be fully reimbursed as a current federal credit." *Hemphill*, 153 Wn.2d at 551.

### **3. DOR Taxes Joshua's Trust in Elaine's Estate.**

Elaine Green-Eldridge died on December 23, 2005, twenty years after Joshua's death. *See* CP 6; CP 24. U.S. Bank, as personal representative of Elaine's Estate, deposited \$10,650,000 (the "Tax Deposit") with the DOR on September 25, 2006 in advance of filing a Washington estate tax return. *See* CP 7; CP 24; CP 124 (no. 37). Subsequently, the Estate filed both state and federal estate tax returns on an extended due date. CP 129-30; AR 147-80. The Tax Deposit was made in good faith and with the expectation that the DOR would promptly refund any excess portion if it were determined later that the estate had overpaid.

After preparation of the federal and state estate tax returns, it became apparent to Elaine's Estate that it had overpaid Washington estate tax. *See* CP 5; CP 23; 206-07. Elaine's Estate's "Washington State Estate and Transfer Tax Return (for deaths occurring on or after May 17, 2005)" was filed on or about March 21, 2007. *See* CP 7; CP 24; CP 206-07. In the Washington return, the Estate calculated the net Washington estate tax to be \$1,851,380.00, because it did not include Joshua's Trust. *See* CP 112 No. 1, Ex. A (Washington state estate tax return). The same return showed a refund due Elaine's Estate in the amount of \$8,798,620.00. *Id.* Rather than refund the amount shown on the return, the DOR chose to refund only \$169,456.00. No state estate tax attributable to Joshua's Trust was refunded.

The Estate received a final IRS Estate Tax Closing Letter, which it forwarded to the DOR on April 2, 2009. CP 8; CP 25; CP 114 (No. 8, Ex. G). Together with a Tax Refund Application, this triggered a final determination of taxes by the DOR. *See* CP 114 (No. 7). In response, the DOR denied the refund request and issued a “Final Washington State Closing Letter” on April 17, 2009. *See* CP 8; CP 25.

**4. The *Bracken* Court Rules Unanimously in Favor of Estate Taxpayers That Section 2044 QTIP Property is Not a Transfer in Surviving Spouse’s Estate.**

U.S. Bank, as duly authorized Personal Representative of the Estate, then filed a tax refund lawsuit on May 15, 2009. Elaine’s Estate and the DOR jointly moved to stay the proceedings, however, until the Supreme Court’s resolution of two other cases with identical legal issues: *In re Estate of Sharon Bracken* and *In re Estate of Barbara J. Nelson* (consolidated in the Washington Supreme Court as case no. 84114-4). The parties then awaited the Supreme Court’s decision, which they expected would be binding and dispositive of the issue in Elaine’s Estate.

The Washington Supreme Court ruled in favor of the taxpayers in *Bracken* and *Nelson* on October 12, 2012, holding that the DOR improperly imposed a tax on QTIP property on the death of the surviving spouse without a present transfer. *Bracken*, at 575-76 (“the statute and regulations are not ambiguous”). The court then denied reconsideration on January 10, 2013. The issue in this case was identical to the issue in *Bracken*, and as a result, *Bracken* became controlling law, binding upon

the DOR in Elaine's Estate. As of January 10, 2013 the Estate was entitled to an immediate refund.

**5. The DOR Refuses to Issue Elaine's Estate a Refund, Solely for Purposes of Delay.**

For over five months, the DOR refused to issue a refund to which Elaine's Estate was entitled under *Bracken*. Thus, the Estate was forced to file a summary judgment motion based upon the holding in *Bracken*. Notably, in a Memorandum in Opposition to the motion, the DOR stated that "*there is no dispute that the Estate is entitled to a refund of Washington estate tax and interest.*" CP 144 (emphasis added). On May 14, 2013, the trial judge specifically ordered the Director of the DOR to pay the refund within 10 days—May 24, 2013.<sup>4</sup> CP 188.

The DOR ignored even this trial court order. As of, and after, that date, no refund was paid and the DOR said nothing about when it might be paid. At 4:00 p.m. on June 13—the last day for filing a notice of appeal of the trial court's order—the DOR filed a notice of appeal. CP 190-96. However, as of June 13, *Bracken* was binding on the DOR and the DOR offered no explanation regarding why the trial court's order was wrong as of the date of the appeal.

The day *after* the notice of appeal was filed, the state enacted the 2013 Amendments. The Amendments include a proviso that it "does not affect any final judgment, no longer subject to appeal, entered by a court

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<sup>4</sup> The DOR's counsel agreed that "The parties stipulate . . . that there is no genuine issue of material fact and that Petitioner is entitled to judgment as a matter of law." CP 188.

of competent jurisdiction.” 2013 Amendments, § 10. According to the DOR, this provision means that the 2013 Amendments are applicable to all estates except the Estate of Bracken and Estate of Nelson.

The 2013 Amendments retained the operative taxing provision that an estate tax is “imposed on a transfer of property by a decedent” in RCW 83.100.040 but modified the definitions contained in the Act in two respects. The legislature updated the definition of “transfer” to include a quote from *Fernandez v. Wiener*, 326 U.S. 340, 352, 66 S. Ct. 178, 90 L. Ed. 116 (1945) that “transfer” “includes any shifting upon death of the economic benefit in property or any power or legal privilege incidental to the ownership or enjoyment of property.” See 2013 Amendments, § 1(3). The 2013 Amendments also provide that the “Washington taxable estate” is the “federal taxable estate, and includes, but is not limited to,” a number of adjustments, including the addition of IRC § 2044 property.<sup>5</sup> *Id.*, § 2(14).

In the Brief of Appellant, the DOR contends that *Bracken* no longer controls and that the 2013 Amendments impose a present tax on Joshua’s Trust in Elaine’s Estate.

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<sup>5</sup> Where a state QTIP election is made, IRC § 2044 property is added to, and QTIP property is deducted from, the surviving spouse’s estate. See RCW 83.100.047(3).

#### IV. ARGUMENT

##### A. **The Expiration of Elaine’s Terminable Life Interest is Not Taxable Because It is Still Not a Present “Transfer” Under Washington Supreme Court Precedent, U.S. Supreme Court Precedent, Federal Law and the 2013 Amendments.**

A “transfer of property” is the *sine qua non* for any estate tax. On this point, the DOR, the legislature, and the Estate all agree. “The requirement for a transfer is constitutionally grounded and long standing.” *Bracken*, 175 Wn.2d at 564. This undisputed principle stems from the U.S. Constitution’s requirement that any direct tax must be apportioned between the states. U.S. CONST. art. I § 9, cl. 4.<sup>6</sup> *See id.*<sup>7</sup> Our Supreme Court has held that this transfer requirement “appl[ies] equally to any Washington estate tax.” *Id.* (citing *In re McGrath's Estate*, 191 Wash. 496, 503, 71, P.2d 39 (1937), cert denied, 303 U.S. 651, 58 S.Ct. 749, 82 L.Ed. 1111 (1938)); *see also* 2013 Amendments, § 4 (“A tax ... is imposed on every transfer of property located in Washington.”). Notably, the legislature’s ill-conceived attempt to expand the definition of a “transfer” in the 2013 Amendments still acknowledges this inherent constitutional limit on the State’s ability to tax, stating: “the term ‘transfer’

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<sup>6</sup> To comport with the Constitution, Congress has long relied on excise taxes, which do not directly tax the property itself, but the “use or transfer of property.” *United States v. Wells Fargo Bank*, 485 U.S. 351, 355, 108 S. Ct. 1179, 99 L. Ed. 2d 368 (1988). Thus, it is crystal clear that “[i]f estate taxation cannot be tied to a transfer, it fails as an unapportioned (and therefore unconstitutional) direct tax.” *Bracken*, 175 Wn.2d at 565 (citing *Levy v. Wardell*, 258 U.S. 542, 42 S. Ct. 395, 66 L. Ed. 758 (1922)).

<sup>7</sup> Section E of Respondent’s Brief (“The Retroactive 2013 Amendments Violate the Provisions of Article VII, Section 1 of the Washington Constitution Requiring Uniformity in Property Taxation”), *infra*, discusses a related restriction under the Washington Constitution.

is to be given its broadest possible meaning *consistent with established United States Supreme Court precedent.*” *Id.* § 1 (emphasis added).

As explained below, the DOR’s attempt to tax the termination of Elaine’s lifetime receipt of trust income as a “transfer” remains wholly inconsistent with established U.S. Supreme Court precedent, including the Washington Supreme Court’s interpretation of that precedent in *Bracken*, which is itself consistent with previous precedent in *Estate of McGrath*. The 2013 Amendments thus fail as unconstitutional.

**1. *Bracken’s Reasoning Controls and is Binding on this Court.***

The Washington Supreme Court’s reasoning in *Bracken* is still applicable even to the 2013 Amendments, and *Bracken* therefore controls. In *Bracken*, our Supreme Court said “If estate taxation cannot be tied to a transfer, it fails as an unapportioned (and therefore unconstitutional) direct tax.” 175 Wn.2d at 565. The Court then reaffirmed its precedent in *In re Estate of McGrath*—decided 75 years earlier—which held that “in neither case can there be any tax unless there is a transfer.” 191 Wash. at 505. The Court then held that Washington’s attempt to tax the expiration of a terminable trust interests could not be tied to a transfer—therefore strongly pointing to the logical conclusion that such a tax is unconstitutional. *Id.* at 563. The Court found that the statute unambiguously excludes Section 2044 property because it was not a present transfer. *Id.*

*Bracken* did not distinguish between a “transfer” in the constitutional sense and a “transfer” as used in the statute. *See id.* More

importantly, the estate tax statute—both the version construed by *Bracken* and after the 2013 Amendments—limits the term “transfer” to “established United States supreme court precedent” (as it is constitutionally required to do). 2013 Amendments, § 1(5). Thus, since both versions are limited by the same U.S. Supreme Court precedent, the Washington Supreme Court’s decisive application of that precedent in *Bracken* applies with equal force to the 2013 Amendments. There is still no transfer, and the tax is still unconstitutional as applied to pre-2005 QTIP trusts.

**2. For Estate Tax to Apply, U.S. Supreme Court Precedent Requires a Present Transfer.**

The death of a lifetime interest holder in an irrevocable trust is simply not a true transfer under U.S. Supreme Court precedent.

*Coolidge v. Long* alone is dispositive of this issue. 282 U.S. 582 51 S. Ct. 306, 75 L. Ed. 562 (1931). The facts are remarkably similar to this case, and the DOR can point to no other authority so closely on point. In *Coolidge*, a husband and wife conveyed a large amount of real and personal property to trust by deed. *Id.* at 593-94. Like Joshua’s Trust, the trust in *Coolidge* was irrevocable and provided income to a lifetime beneficiary.<sup>8</sup> *Id.* Also like Joshua’s Trust, the trust in *Coolidge* created remainder beneficiaries to divide the principal at the end of the lifetime interest. *Id.* When the trust was executed, no statute in the state of Massachusetts taxed such property. *Id.* However, before the husband and

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<sup>8</sup> In *Coolidge*, the husband and wife were joint income beneficiaries. 282 U.S. at 583.

wife died, the state enacted a tax on all property passing by “deed, grant or gift” where the property passed or accrued upon the “death of persons dying on or after” May 4, 1920. *Id.* at 595. The husband and wife both died after this date, and the state attempted to tax on the trust property at their deaths. *Id.* at 594-595.

The U.S. Supreme Court held, unequivocally, that the state could not impose a tax at the end of the lifetime interest because the “overwhelming weight of authority sustains the conclusion that the succession in the present case was complete when the deed took effect.” *Id.* at 602. The Court reasoned,

The situation would have been precisely the same if the possibility of divestment had been made to cease upon the death of a third person instead of upon the death of the survivor of the settlors. . . . Succession is effected as completely by a transfer of a life estate to one and remainder over to another as by a transfer in fee.

*Id.* at 597-98 (internal citations omitted). *Coolidge* makes it perfectly clear that the *only transfer* in this case occurred when the trust is created.

The DOR’s attacks on *Coolidge* are baseless. The DOR primarily relies on *Wiener*, a case referenced in the 2013 Amendments to clarify the meaning “transfer,” and claims that *Wiener* “effectively overruled” *Coolidge*. Br. Appellant at 31 n.13 (“expressly limiting the holding in *Coolidge*”). *Id.* As explained below, the DOR’s description of *Weiner* is not only incorrect, but flat-out misleading.

*First, Wiener* did, indeed, “expressly limit” *Coolidge* with the following statement:

So far as *Coolidge v. Long* . . . is inconsistent . . . , the application of the reasoning of the *Coolidge* case to the taxation of *joint or community interests* must be taken to have been limited . . . .

326 U.S. at 357. By specifically limiting *Coolidge* in situations *other than* trusts, *Wiener* left *Coolidge*'s application otherwise and to this case fully intact. The DOR has attempted to misdirect this Court and rewrite federal precedent.<sup>9</sup>

Moreover, *Wiener* did not change the law because *Wiener* relies on cases that *Coolidge* addressed or distinguished.<sup>10</sup> Thus, the cases share a common legal foundation and coexist because they reach different holdings on different fact situations. *Wiener* does not affect the application of *Coolidge* to this case.

The State seems to believe that *Wiener*'s general language—taken out of context and apart from all facts—constitutes the core of federal law regarding transfer taxation. But that is not precedent. The DOR mistakenly relies on the out-of-context language in *Wiener*, even though *Coolidge* offered a clear ruling on facts nearly identical to this case, and *Wiener* clearly does not overrule or distinguish *Coolidge* on those facts.

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<sup>9</sup> A closer look at *Wiener*'s facts confirm that it did not overrule *Coolidge*. The issue was the inclusion of all community property as part of a husband's estate in a community-property state where the wife's rights were restricted until the husband's death. 326 U.S. at 353.

<sup>10</sup> See, e.g., *Tyler v. United States*, 281 U.S. 497, 50 S. Ct. 356, 74 L. Ed. 991 (1930) (approving taxation of tenancies by the entirety, which *Wiener* compares but *Coolidge* distinguishes); see also *Reinecke v. Northern Trust Co.*, 278 U.S. 339, 49 S. Ct. 123, 73 L. Ed. 410 (1929) (cited favorably by *Wiener* and *Coolidge*); *Clapp v. Mason*, 94 U.S. 589, 24 S. Ct. 671, 24 L. Ed. 212 (1876) (*Wiener* compares and *Coolidge* distinguishes.).

Two other Supreme Court cases cited by the DOR, *Klein v. United States* and *Helvering v. Hallock*, do not support the State's conclusion.<sup>11</sup> *Hallock* expressly overruled two prior inconsistent cases on similar issues; neither case was *Coolidge*, which still stands.

### 3. The Expiration of a Terminable Trust Interest Has Never Been Held to Be A "Transfer."

It is universally recognized that there is no transfer by the lifetime beneficiary at the death of a lifetime beneficiary of a trust that also contains a remainder interest.<sup>12</sup> The nature of a "terminable interest" is that the second spouse has no interest in the property.<sup>13</sup> Thus, the DOR's claim that there are two taxable transfers finds no support in the law.

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<sup>11</sup> DOR incorrectly relies on *Klein v. United States*, 283 U.S. 231, 51 S. Ct. 398, 75 L. Ed. 996 (1931) and *Helvering v. Hallock*, 309 U.S. 106, 60 S. Ct. 44, 84 L. Ed. 604 (1940) for the proposition that the federal estate tax code "taxes not merely those interests which are deemed to pass at death according to refined technicalities of the law of property [but] also taxes inter vivos transfers that are too much akin to testamentary dispositions to not be subjected to the same excise [tax]." *Id.* at 112; Br. Appellant at 30. Conveniently, however, the DOR ignores the very next line in *Hallock*, where the court said: "By bringing into the gross estate at his death that which the settlor gave contingently upon it [*i.e.*, the settlor's death], this Court [in *Klein*] fastened on the vital factor [*i.e.*, the contingency]." *Hallock*, 309 U.S. at 112 (emphasis added). The remainder interest in Joshua's Trust was not contingent, but vested and irrevocable.

<sup>12</sup> See R. Stephens, G. Maxfield, S. Lind, D. Calfee & R. Smith, FEDERAL ESTATE AND GIFT TAXATION ¶ 4.05[5][b], at 4-157 (8th ed. 2002) (where A grants B a life estate in Blackacre or lifetime beneficiary interest in a trust, subject to a remainder interest, "B has no interest that B can transmit to others at B's death"); 1 J. Mertens, THE LAW OF FEDERAL GIFT AND ESTATE TAXATION § 1.04, at 11 (1959) ("a basic element is that the decedent must have an interest in property which is capable of transfer."); see also, *U.S. v. Field*, 255 U.S. 257, 41 S. Ct. 256, 65 L. Ed. 617 (1921); *Helvering v. Safe Deposit & Trust Co.*, 316 U.S. 56, 62 S. Ct. 444, 86 L. Ed. 1266 (1942) (cases that construe the termination of such trusts to not be transfers of an interest in property when the surviving spouse dies).

<sup>13</sup> "Indeed, this principle is so deeply entrenched in the structure of the federal estate tax that formal judicial and administrative pronouncements to this effect are unnecessary and hard to find." 5 B. Bittker & L. Lokken, FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS ¶ 125.5, at 125-11 (1993).

The history of the marital deduction shows that Congress has always known that it cannot impose a second transfer tax on such a terminable interest. In *Clayton v. Comm'r*, 976 F.2d 1486 (5th Cir. 1992), the Fifth Circuit notes that, when the Marital Deduction was first enacted, Congress was concerned that “[i]f a terminable interest in property were deductible in the first estate, such property would escape tax in the estates of both spouses.” *Id.* at 1491. Clearly, if the death of the beneficiary of a terminable interest trust were an independently taxable transfer, then Congress would have simply applied the marital deduction to such interests from the start; there would be no need for concern about the inability to tax the trust property as part of the second estate.

But Congress knew it lacked the constitutional authority for such a tax, and this reality defeats the DOR’s extreme reliance on the “shifting of economic benefits” standard. Br. Appellant at 31. The “shifting of economic benefits” standard was established through case law, such as *Wiener*, before the enactment of the marital deduction in 1948. *See Wiener*, 326 U.S. at 358. Yet, armed with this allegedly liberal standard, Congress still realized that it could not reach trust property at the death of the beneficiary of a terminable lifetime interest. *See Clayton*, 976 F.2d at 1491. No case law supports that the “shifting of economic benefits” standard—or any other standard—would allow such a tax.

In 1981, Congress enacted IRC § 2056(b)(7) (the QTIP provision) to extend the marital deduction to terminable interests, *id.*, but only with

the creation of IRC § 2044 as a necessary counterpart for IRC § 2056(b)(7) to provide that property deducted from the first estate would be “treated as” part of the second estate. If the termination of a surviving spouse’s life estate were a taxable event *on its own*, it would have been unnecessary for Congress to enact IRC § 2044. Congress would have simply taxed the property as part of the second estate instead of relying on the fiction that such property “shall be *treated as* property passing from the decedent.” IRC § 2044(c) (emphasis added). Thus, Congress again acknowledged that there is no independent second (taxable) transfer at the death of a surviving spouse who held only a terminable lifetime interest.<sup>14</sup>

**B. The 2013 Amendments Violate the Separation of Powers Doctrine.**

If the 2013 Amendments are read to overrule *Bracken* and impose a tax on Joshua’s Trust, then they violate “the bedrock principle that the legislature cannot contravene an existing judicial construction of a statute.” *State v. Maples*, 171 Wn. App. 44, 50, 286 P.3d 386 (2012).

The DOR argues that the legislature has done all it needs to do to respect the integrity of the judiciary by preserving the final judgments of the Estates of Bracken and Nelson from the retroactive effect of the 2013 Amendments via Section 10 of the Amendments. *See Br. Appellant* at 26.

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<sup>14</sup> It is imperative to remember that “QTIP” trusts are trusts under state trust law. Settlers do not create “QTIP” or create a “QTIP trust”; they create trusts for which certain *federal* tax treatment is elected. The legislature has no authority to reach back and impose wholly new taxes on an irrevocable trust by forcing property into Elaine’s Estate as a result of a *federal* tax election made through her husband’s Will and by his estate.

This provision, says the DOR, responds to the statement in *Haberman v. Wash. Pub. Power Supply Sys.*, 109 Wn.2d 107, 144, 744 P.2d 1032 (1987), that retroactive legislation is permitted if it “does not dictate how the court should decide a factual issue” and does not “affect a final judgment.” Having preserved the final judgment in *Bracken*, the DOR argues, the legislature was free to “retroactively amend a statute to *affirmatively change* the law.” Br. Appellant at 28 (emphasis added).

This analysis is wrong. The legislature sought to reassert a now-claimed intention of the original 2005 Act and “clarify” the language to conform to that intent. In other words, the legislature sought to construe what the prior statute meant rather than to change it affirmatively.

(5) . . . [T]he legislature finds it necessary to *reinstate* the legislature’s intended meaning when it enacted the estate tax, . . . , and prevent the adverse fiscal impacts of the *Bracken* decision by *reaffirming its intent* that the term “transfer” as used in the Washington estate and transfer tax is to be given its broadest possible meaning consistent with established United States supreme court precedents, subject only to the limits and exceptions expressly provided by the legislature.

(6) As curative, *clarifying*, and remedial, the legislature intends for this act to apply both prospectively and retroactively to estates of decedents dying on or after May 17, 2005.

2013 Amendments § 1 (emphasis added). Given that the DOR’s predicate about the legislature’s intent is wrong (*i.e.*, the legislature did *not* intend to change the law affirmatively, but rather to clarify its 2005 intent), its analysis of the law is wrong for the reasons stated below.

Before reaching those reasons, however, the Court should know that the DOR itself, *in this very case*, has previously characterized the impact of the 2013 Amendments as “clarifying.”<sup>15</sup>

This Court, in all Divisions, has repeatedly held that “legislative clarifications construing or interpreting existing statutes are unconstitutional when they contravene prior judicial interpretations of a statute.” *State v. Elmore*, 154 Wn. App. 885, 905, 228 P.3d 760 (2010) (citing *Marine Power & Equip. Co. v. Human Rights Comm’n Hearing Tribunal*, 39 Wn. App. 609, 615 n.2, 694 P.2d 697 (1985)). *See also State v. Maples*, 171 Wn. App. 44, 49, 286 P.3d 387, 292 P.3d 125 (2012) (citing cases for the proposition that a “clarifying enactment cannot apply retrospectively when it contravenes a judicial construction of the statute,” but presuming that the act in question was not a clarification) (citations omitted); *State v. Mann*, 146 Wn. App. 349, 358, 189 P.3d 843 (2008)

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<sup>15</sup> In response to the Estate’s motion for summary judgment, the DOR asked the trial court to delay its ruling while the legislature considers a bill to clarify the original 2005 intent:

With respect to the Estate’s refund claim, the Court should defer ruling on the motion in order to permit the Washington Legislature to consider a pending bill (Engrossed House Bill 1920) *that would retroactively clarify the intent of the Legislature to tax QTIP*. Simply put, the Washington Legislature should be permitted the opportunity to consider pending legislation that would apply to the Estate. *If that clarifying legislation passes*, the Estate’s motion for summary judgment should be denied.

CP 135 (emphasis added). The cited bill, EHB 1920, contained an intent provision identical to the 2013 Amendments as passed. *See* CP 164-65. The contemporaneous understanding of the Attorney General’s Office, as representative of the Executive Branch, of the bill’s intent while the bill was pending, let alone the bill’s own language, should trump the argument of convenience now placed before this Court. *See also* Br. Appellant App. B at 2 (DOR’s Fiscal Note stating, “This legislation clarifies the meaning of the terms ‘transfer’ and ‘Washington taxable estate’ . . .”).

(citing *Marine Power*, 39 Wn. App. at 615 (“A separation of powers conflict is avoided, however, if the legislative enactment amends, rather than clarifies, an existing statute.”) (citing *Johnson v. Morris*, 87 Wn.2d 922, 926, 557 P.2d 1299 (1976)). In *In re Pers. Restraint of Stewart*, 115 Wn. App. 319, 75 P.3d 521 (2003), the Court said:

When an amendment clarifies existing law and where that amendment does not contravene *previous constructions of the law*, the amendment may be deemed curative, remedial and retroactive.

*Id.* at 331 (quoting *Tomlinson v. Clarke*, 118 Wn.2d 498, 510-11, 825 P.2d 706 (1992) and adding emphasis).

The DOR relies primarily on two Supreme Court decisions, *Hale v Wellpinit Sch. Dist.*, 165 Wn.2d 494, 198 P.3d 1021 (2009), and *Lummi Indian Nation v. State*, 170 Wn.2d 247, 241 P.3d 1220 (2010). These decisions represent, per the DOR, the proposition that “the separation of powers doctrine is not violated when the Legislature affirmatively amends a previously construed statute.” Br. Appellant at 27 (citing *Lummi*, 170 Wn.2d at 262; *Hale*, 165 Wn.2d at 509-10). While this proposition is not relevant to this case, the factual contexts and statutory changes involved in *Lummi* and *Hale* are also far afield from the simple, retroactive tax increase at issue here.<sup>16</sup>

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<sup>16</sup> The DOR also cites convenient dictum in *Plaut v. Spendthrift Farms, Inc.*, 514 U.S. 211, 226-27, 115 S. Ct. 1447, 131 L. Ed. 2d 328 (1995), to the effect that retroactive legislation does not violate separation of powers limits when applied to a case not yet finally decided. Br. Appellant at 26. The *Plaut* case was squarely about Congressional action that explicitly re-opened fully adjudicated cases, which the Supreme Court held to be unconstitutional, and the words of Justice Scalia concerning what the case was *not* about do not undermine Washington’s many subsequent decisions that prohibit retroactive “clarifying” statutes in contravention of a judicial construction.

In *Lummi*, the Supreme Court rejected a separation of powers challenge to several 2003 amendments to Washington’s water laws. The Court had previously held in 1998 that, under then-existing law, new *private* water rights did not fully vest until the water was put to a beneficial use. *Dep’t of Ecology v. Theodoratus*, 135 Wn.2d 582, 586, 957 P.2d 1241 (1998). In *Theodoratus*, the Court cautioned that it was not addressing the vesting of *municipal* water rights in that case. *Id.* at 594.

The *Lummi* Court noted that the 2003 legislature responded not only to the *Theodoratus* decision but also to additional uncertainty created by the Department of Ecology by “significantly amending the water law act.” *Lummi*, 170 Wn.2d at 256. Among other things, the amendments created new definitions concerning “municipal” water use and declared that water rights certificates issued for municipal purposes before the 2003 act’s effective date based on system capacity (rather than actual use) were rights in good standing. “The legislation essentially put the legislature’s imprimatur on our holding in *Theodoratus* prospectively while confirming the good standing of water certificates issued under the former system.” *Id.* at 257 (citing secondary authority).

The Court held that the retroactive affirmation of water rights obtained under the prior system did not violate separation of powers because the “legislature approached its legislative task . . . with deference to this court’s construction in *Theodoratus*.” *Id.* at 263. The Court cited the legislature’s adoption of the *Theodoratus* interpretation for prospective

application and the legislature's reliance on the limitations of the *Theodoratus* analysis (which avoided construction of the term "municipal" water users) "as an opportunity to secure the rights of some existing water certificate holders." *Id.* In effect, the amendments were "remedial" in that they expanded rights rather than increased burdens. Nothing in the opinion or the act, Laws of 2003, ch. 5, suggests a legislative intent to "clarify" the prior statutes. *Lummi* is simply not relevant precedent.

In *Hale*, the Court held that the retroactive amendment of the Washington Law Against Discrimination ("WLAD") did not violate the separation of powers doctrine. The amendments were adopted in 2007 in response to the Supreme Court's decision in *McClarty v. Totem Elec.*, 157 Wn.2d 214, 137 P.3d 844 (2006). The *McClarty* Court addressed the undefined term "disability" in the WLAD and decided that the legislative intent best matched the definition in the federal Americans with Disabilities Act ("ADA"). In doing so, the Court overturned its own decision of six years earlier in *Pulcino v. Fed. Express Corp.*, 171 Wn.2d 629, 9 P.3d 787 (2000). *Hale*, 165 Wn.2d at 500-01. As the *Hale* Court emphasized, a "[c]losely divided court" in *McClarty* adopted the ADA definition "in a five to four opinion." *Id.*, 165 Wn.2d at 501, 510.

The amendments included a new definition of "disability" and applied the definition retroactively to claims arising before the date of the *McClarty* decision but *not* to claims arising between the date of the *McClarty* decision and the effective date of the act. *Id.* at 502.

The effect of this provision was to carefully carve out a window of time during which claims would still be controlled by the definition of “disability” we announced in *McClarty*.

*Id.* The Court also quoted the legislative purpose section reflecting the intention that “[t]his act is *remedial*.” *Id.* (quoting Laws of 2007, ch. 317, § 3) (emphasis added). The legislature indicated no intention to “clarify” the meaning of the term “disability,” nor could such an intention have been logical, since the legislature did not apply the definition to all prior periods. (The act was indeed “remedial,” since it expanded the basis for discrimination claims beyond the ADA protections. *See id.*)<sup>17</sup>

In holding that the retroactive amendment did not violate separation of powers, the Court expressly relied on the legislature’s own express intent that the amendment be “remedial and retroactive.” *Id.* at 508. The Court also found the “legislature was careful not to reverse our decision in *McClarty*.” *Id.* at 510. And, as the DOR claims, the Court saw that the amendment “change[d] the definition of ‘disability’.” *Id.*

The present case represents something entirely different. In *Hale*, the legislature had added a new definition to the law that “had not previously existed.” *Marine Power*, 39 Wn. App. at 615. Here the 2005 Act modified the definition of “transfer” – which under the 2013 Amendments is still based on the Internal Revenue Code definition. In *Hale*, the legislature claimed that its action was “remedial,” whereas the

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<sup>17</sup> The Court of Appeals has previously rejected the State’s claim that *Hale* overruled *In re Pers. Restraint of Stewart*, *supra*, noting that both *Hale* and *Lummi* had discussed *Stewart* and left it intact. “Notably, the *Hale* decision did not overrule *Stewart*, nor could it, as *Stewart* rested on the bedrock principle that the legislature cannot contravene an existing judicial construction of a statute.” *Maples*, 171 Wn. App. at 50 ¶ 10.

2013 Amendments were expressly “clarifying.” 2013 Amendments § 1(6). In contrast to both *Hale* and *Lummi*, in this case the legislature left no period open when the Court’s decision in *Bracken* would control. Finally, also unlike both *Hale* and *Lummi*, the 2013 Amendments expanded no one’s rights or remedies but instead substantially increased individual tax burdens.

In short, the 2013 Amendments “reversed” the decision in *Bracken* in just the way that violates separation of powers – as a clarifying interpretation that contravenes a prior, final judicial interpretation.

**C. The Retroactive Application of the 2013 Amendments Violates Due Process.**

The DOR’s argument that the 2013 Amendments meet the Due Process requirements for retroactive tax increases, Br. Appellant at 19-24, does not accurately reflect the controlling precedent. The Estate will debunk the relevance of the DOR’s authorities in the second subsection below, after first showing how the legislature violated Due Process in this case, both on the face of the 2013 Amendments and as applied.

**1. Federal and Washington Cases Show That Retroactivity Violates Due Process in This Case.**

The retroactive 2013 amendments were arbitrary and irrational and therefore unconstitutional under the Due Process protections of both Washington and federal law.

Due Process protects private persons from “arbitrary and irrational legislation.” *United States v. Carlton*, 512 U.S. 26, 30, 114 S. Ct. 2018,

129 L. Ed. 2d 22 (1994) (quoting *Pension Benefit Guar. Corp. v. R.A. Gray & Co.*, 467 U.S. 717, 733, 104 S. Ct. 2709, 81 L. Ed. 2d 60 (1984)). A retroactive tax statute will be upheld against a Due Process challenge if it “is supported by a legitimate legislative purpose furthered by rational means.” *Id.* at 30-31 (quoting *Pension Benefit*, 467 U.S. at 730). But, as the Supreme Court’s opinion illustrated, an otherwise legitimate purpose may be tainted by an illegitimate purpose, such as targeting a specific taxpayer’s claims. *Id.* at 32. Also, the rationality of the chosen means is always contingent on circumstances, such that a retroactive period that is more than “modest” in length, given the practicalities of the legislative process, is not rational. *Id.*

The Estate will first show that the retroactive application of the 2013 Amendments was not a rational means of achieving the legislature’s stated objectives. Second, the Estate will show that those objectives were not themselves a legitimate basis for a retroactive tax increase.

**a. The Eight-Year Retroactivity Period on the Face of the Amendments and the 28-Year Period as Applied in this Case Are Not a Rational Means of Enhancing State Revenues.**

The Supreme Court in *Carlton* said that a “modest period of retroactivity” may be a reasonable response to unintended consequences of a tax enactment. *See* 512 U.S. at 32. The periods in this case are wholly unreasonable.

*First*, the Court in *Bracken* already noticed the infirmity of the DOR position on an as-applied basis. The Court asserted that DOR’s argument in that case (subsequently adopted in the 2013 Amendments) would have the “state reaching into the grave and taxing a transfer 25 years after the fact.” 175 Wn.2d at 572. The Estate endorses the Court’s view of the legislature’s action, given that the retroactive amendments rely on only fictional transfers said to have occurred in the 2005-13 period. As applied, the retroactive period in this case is 28 years – back to the date of Joshua’s death in 1985. This is obviously unreasonable and violates Due Process. *See Tesoro I*, 159 Wn. App. at 119 (“There is no colorable argument to suggest a legislative act creating a 24-year retroactive tax period is ‘prompt [ ]’ or establishes a ‘modest period of retroactivity’.”) (quoting *Carlton*, 512 U.S. at 32-33).

*Second*, the eight-year period on the face of the 2013 Amendments exceeds the *Carlton* threshold because the issue had already come to the State’s notice at least by March 2007, when the Estate filed its refund claim of over \$8,000,000. CP 7 ¶ III.C.4; CP 24 ¶ III.C.4. Numerous other refund claims and assessments, including those in *Bracken*, were well known to the State in the same period. Yet the legislature took no action to remedy its now-claimed oversight. The delay in the legislature’s response until after final, definitive action by the Supreme Court in *Bracken* does not meet the standard in *Carlton*.<sup>18</sup>

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<sup>18</sup> That the legislature acted promptly after *Bracken*, as claimed at page 22 of the DOR’s brief, is a red herring that masks the legislature’s actual response time. The DOR’s claim

The Supreme Court’s decision in *Carlton* shows that a claim of “unintended consequences” will support a retroactive change or clarification only when the difference between legislative goals and actual results are readily apparent to roughly the same body of legislators that enacted the original statute. *Carlton* emphasized how the IRS informed Congress of the mistake in the statute in question within three months of enactment, 512 U.S. at 33, and how the “curative measure,” *id.* at 31, was then promptly introduced one month later. *Id.* at 33. The amendment was passed less than 14 months after the original tax act. *Id.* at 32. This process, in which taxpayers and the administrative agency test the consequences of a new tax statute, provides an appropriate context for prompt legislative review and correction within a “modest period.”

The legislature’s action in this case, by contrast, is an abuse of this balance. To allow the legislature license to “correct” asserted “unintended consequences” in this case after many years of very high profile litigation between taxpayers and the DOR is not rationally related to *Carlton*’s standard of a legislature surprised by the effect of new tax legislation.

Moreover, there is no precedent in Washington for a retroactive tax increase of more than two months. *See Tesoro Ref. & Mktg. Co. v. Dep’t of Revenue*, 159 Wn. App. 104, 120 ¶ 29, 246 P.3d 211 (2010) (“*Tesoro I*”), *rev’d on other grounds*, 173 Wn.2d 551, 269 P.3d 1013 (2012) (24-year retroactive clarification of B&O exemption invalid as “well beyond

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could support a retroactive application back to the date the *Bracken* decision was final, not further.

the limit of permissible retroactivity and retroactive enforcement of the amendment would violate due process”) (citing *State v. Pac. Tel. & Tel. Co.*, 9 Wn.2d 11, 17, 113 P.2d 542 (1941)); *Japan Line, Ltd. v. McCaffree*, 88 Wn.2d 93, 94-95, 97-98, 558 P.2d 211 (1977) (upholding retroactive (two months) leasehold excise tax as substitution for prior property taxation of leasehold interests in public property); *Bates v. McLeod*, 11 Wn.2d 648, 655, 120 P.2d 472 (1941) (retroactive (2.5 months) imposition of new tax to support unemployment compensation invalid); *Pac. Tel. & Tel.*, 9 Wn.2d at 16-17 (invalidating retroactive (four years) expansion of use tax to cover storage of property in Washington prior to use).<sup>19</sup>

If the legislature wishes to increase or expand a tax retroactively, Due Process requires that the period of retroactivity reflect the practical circumstances associated with promptly addressing the particular problems in the prior statute. *See Carlton*, 512 U.S. at 31-32. This did not occur in this case. “Clarifying” the meaning of “transfer” after many years of high-profile litigation does not rationally correct an “unintended consequence” and is instead an arbitrary means of raising taxes.

**b. The Legislature’s Objectives Do Not Legitimately Justify a Retroactive Tax Increase.**

The DOR attempts to clothe the 2013 Amendments with a legislative purpose akin to that endorsed in *Carlton* – Congress’s action to

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<sup>19</sup> *Cf. Pac. Tel. & Tel. Co. v. Henneford*, 19 Wash. 553, 562-63, 81 P.2d 786 (1938) (Court’s prior holding – parallel to *Bracken* in this case – that original 1935 use tax did not apply to acts of storage).

correct what Congress “reasonably viewed as a mistake” that had produced “a significant and *unanticipated* revenue loss.” *Carlton*, 512 U.S. at 32 (emphasis added), *cited in* Br. Appellant at 21. The 2013 Amendments were motivated, says, the DOR by the concern for “an *unexpected* loss of revenue to public school funding brought about by the Supreme Court’s holding in *Bracken*.” *Id.* at 21 (emphasis added). Close examination of the facts shows that this is the DOR’s spin and not the actual purpose of the legislation. It is not rational to characterize the revenue impact of *Bracken* as “unexpected.”

In the 2013 Amendments, the legislature first identified the reason for the 2005 Act in the first place: “an unexpected significant loss of tax revenue resulting from the *Estate of Hemphill* decision.” 2013 Amendments § 1(1). The legislature did not, however, describe the revenue impact of *Bracken* as “unexpected,” “unanticipated,” or even “significant.” Instead, it merely stated that the *Bracken* decision would have “adverse fiscal impacts.” *Id.* § 1(5). This is true of every case where a taxpayer wins a refund. “Adverse fiscal impacts” do not by themselves provide a legitimate purpose for adopting a retroactive tax increase.

It could not be rational in this case to claim that the “adverse fiscal impacts” of *Bracken* were “unanticipated.” For virtually the entire period after enactment of the Estate Tax in 2005, the DOR was in conflict with taxpayers about the meaning of the 2005 Act. The DOR could have and maybe did alert the legislature to these disputes about QTIP, but the

legislature made no change to the statute to protect the DOR's position. Contrast this situation to that of *Tesoro I* during the same period, where the DOR informed the legislature of Tesoro's refund suit in 2009 and the legislature promptly amended the statute on the eve of Tesoro's trial. See *Tesoro I*, 159 Wn. App. at 110 ¶ 6.

In light of this history, no one could reasonably have understood that the DOR's position on QTIP was settled law before the decision in *Bracken*. And the legislature did *not* make that claim in the 2013 Amendments. The State simply could not have had "settled expectations" concerning tax payments on QTIP after the 2005 Act.

Consequently, the DOR's attempt to sustain legitimacy under *Carlton* is without foundation. The circumstances in *Carlton* were different in two critical respects.

*First*, in *Carlton*, there was legislative history showing that the new 1986 estate tax deduction in question was expressly intended to incentivize business owners to sell their company stock to employees "who helped them build the company, rather than liquidate [or] sell to outsiders'." 512 U.S. at 31 (quoting report of the Joint Committee on Taxation). Congress's error was writing the deduction without any requirement of prior ownership and thus extending it far beyond the intended incentive. *Id.* at 32. There is no analogous legislative history in this case—only the legislature's bare assertion that it reads the federal tax code and case law better than Washington's Supreme Court and that the

2013 legislature knew, eight years later, what the 2005 legislature's interpretation of federal law was. *See* 2013 Amendments § 1(1), (3).

*Second*, the *Carlton* Court demonstrated the “unexpectedness” of the statutory mistake by comparing Congress’s estimated revenue loss for the original 1986 deduction (\$300 million) to its estimate of the consequences of the broader interpretation (\$7 billion). 512 U.S. at 31-32. In this case, by contrast, the legislature considered only the cost of the *Bracken* interpretation, not any comparison to original forecasts. *See* Br. Appellant App. B (DOR Fiscal Note).

Consequently it is clear that the legislature was really concerned with maintaining or expanding state revenues. As the DOR’s Fiscal Note put it, “This legislation increases revenues . . . .” *Id.* App. B at 3. This objective does not justify imposing retroactive burdens on taxpayers.

In the most recent Due Process retroactivity decision around the country, the New York Court of Appeals (the state’s highest court) held that a retroactive revocation of tax credits for a period of 16 or 32 months (depending on the effect of a first amendment) violated the taxpayers’ Due Process rights. *See James Square Assocs. LP v. Mullen*, 21 N.Y.3d 233, 248-50, 993 N.E.2d 374 (2013). The court held that “the State fails to set forth a valid public purpose for the retroactive application of the 2009 Amendments.” *Id.* at 249.

*James Square* addressed a change in the eligibility criteria for job-creation credits in the “Empire Zones Program” for designated regions of

the state. The legislature’s purposes “were to stem abuses in the Empire Zones Program (increasing the benefits to the public relative to the cost of the credits) and *to increase tax receipts.*” *Id.* at 250 (emphasis added). The first purpose was not rationally related to the retroactive application, because no change in taxpayer behavior could be incentivized for completed periods. As to the second purpose:

[R]aising money for the state budget is not a particularly compelling justification. Absent an *unexpected* loss of revenue, such a legislative purpose is insufficient to warrant retroactivity in a case where the other factors militate against it, as is the situation here. Raising funds is the underlying purpose of taxation, and such a rationale would justify every retroactive tax law, obviating the balancing test itself.

*Id.* (emphasis added) (referring to New York’s three-factor Due Process balancing test under *Matter of Replan Dev. v. Dep’t of Hous. Preserv. & Dev. of N.Y.*, 70 N.Y.2d 451 (1987)).

As in *James Square*, in this case, the legislature’s primary objective of maintaining or increasing revenues in the face of a difficult school funding situation certainly supports a prospective change in law but does not justify a major retroactive tax increase.<sup>20</sup>

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<sup>20</sup> The DOR’s brief makes no effort to rely on the other objectives recited by the legislature in Section 1 of the 2013 Amendments. The legislature said it also sought to “restore parity between married couples and unmarried individuals [and] restore parity between QTIP property and other property eligible for the marital deduction.” 2013 Amendments § 1(5). There are no sound legislative findings to support these objectives. First, the 2013 Amendments did not eliminate the marital deduction, so it is apparent that some forms of disparity existed before the amendments and continue after 2013. There is no record to show what the 2013 Amendments did to “restore parity” in fact. Second, under the *Bracken* decision, the exclusion of QTIP from the surviving spouse’s estate, where the first spouse to die passed away before 2005, meant that the federal estate tax for such estates was higher (given that the federal deduction for state estate taxes was

**2. The DOR's Authorities Do Not Support the Retroactive Application of the 2013 Amendments Under Due Process Standards.**

In addition to the DOR's failure to identify a legitimate government purpose for the retroactive expansion in the Estate Tax, and its error in claiming that the legislature acted promptly to correct unintended consequences, there are two additional reasons why the DOR's Due Process authorities fail to justify the retroactive expansion of the Estate Tax in this case.

*First*, the Department's single Due Process precedent from Washington, *W.R. Grace & Co. v. Dep't of Revenue*, 137 Wn.2d 580, 973 P.2d 1011 (1999), arose out of an irrelevant context – the correction of a technical violation of the Commerce Clause nondiscrimination principle. Washington cases on the retroactive expansion of tax liability do not authorize the legislature's action in this case.

*Second*, the cases listed by the Department that upheld retroactive tax changes all involved situations dissimilar to this case, or the Estate Tax Amendments, in critical ways and so do not govern this case.

**a. Commerce Clause Discrimination Cases Such as *W.R. Grace* Have Their Own Rationale on Retroactivity and Do Not Control Cases Where the Legislature Expands Tax Liabilities Retroactively.**

The DOR naturally wants to rely on *W.R. Grace*. It is the only Washington decision that approved a retroactive change in tax law of

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less). The legislature had no basis to know whether, taking everything into consideration, it was doing anything to "restore parity."

more than two months. However, its context is not relevant here and it can provide no persuasive authority. The most relevant Washington case, *Pac. Tel. & Tel.*, 9 Wn.2d at 16-17, held that expanding a state tax retroactively for four years in the face of a contrary state Supreme Court interpretation of the prior statute is unconstitutional. *See supra* at 28.

*W.R. Grace* involved a challenge to the retroactive B&O taxpayer *remedy* (a credit) adopted by the legislature after the U.S. Supreme Court invalidated the former multiple-activities exemption in *Tyler Pipe Indus., Inc. v. Washington State Dep't of Revenue*, 483 U.S. 232, 107 S. Ct. 2810, 97 L. Ed. 2d 199 (1987). *See also* Br. Appellant at 20-21.<sup>21</sup>

The Supreme Court found in *Tyler Pipe* that the multiple-activities exemption worked a discrimination against interstate commerce, even though the same provision had been *validated* by the Court previously in *General Motors Corp. v. Washington*, 377 U.S. 436, 84 S. Ct. 1564, 12 L. Ed. 2d 430 (1964). The Supreme Court even offered Washington a simple fix for the constitutional defect: “[A]n expansion of the multiple activities exemption to provide out-of-state manufacturers with a *credit* for manufacturing taxes paid to other States would presumably *cure* the discrimination.” *Tyler Pipe*, 483 U.S. at 249 (emphasis added).

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<sup>21</sup> *Tyler Pipe* was one of a series of Commerce Clause cases in the 1980s in which the Supreme Court was working out the logic of the new “internal consistency” test developed in *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 163, 103 S. Ct. 2933, 77 L. Ed. 2d 545 (1983). *See Am. Trucking Ass'ns v. Scheiner*, 483 U.S. 266, 283 n.14, 107 S. Ct. 2829, 97 L. Ed. 2d 226 (1987) (citing *Tyler Pipe*, 483 U.S. at 247); *Armco Inc. v. Hardesty*, 467 U.S. 638, 644-45, 104 S. Ct. 2620, 81 L. Ed. 2d 540 (1984); and *Container*, 463 U.S. at 163.

The taxpayers in *W.R. Grace* argued that the constitutional violation rendered the B&O tax a nullity for all periods open to refund claims. *W.R. Grace*, 137 Wn.2d at 594. However, the state Supreme Court framed its entire decision on the U.S. Supreme Court's specific doctrine that discriminatory taxes may be corrected rather than tossed out entirely. That is, if the discrimination in the state tax scheme is fixed so that it is valid under the Commerce Clause, the state may retain the taxes collected *to the extent* they comply with the reformulated scheme. The Washington Court quoted the U.S. Supreme Court as follows:

[A] State found to have imposed an impermissibly discriminatory tax retains flexibility in responding to this determination. Florida may reformulate and enforce the Liquor Tax during the contested tax period in any way that treats petitioner and its competitors in a manner consistent with the dictates of the Commerce Clause. Having done so, *the State may retain the tax appropriately levied upon petitioner* pursuant to this reformulated scheme because this retention would deprive petitioner of its property *pursuant to a tax scheme that is valid under the Commerce Clause*.

*W.R. Grace*, 137 Wn.2d at 595 (emphasis added) (quoting *McKesson Corp. v. Div. of Alcoholic Beverages & Tobacco*, 496 U.S. 18, 39-40, 110 S. Ct. 2238, 110 L. Ed. 2d 17 (1990)).

The specific Commerce Clause context for consideration of retroactive tax amendments, as framed by the *McKesson* decision, was helpfully elaborated in *City of Modesto v. Nat'l Med, Inc.*, 128 Cal. App. 4<sup>th</sup> 518, 27 Cal. Rptr. 3d 215 (2005). In *Modesto*, the California Court of Appeals invalidated an eight-year retroactive adoption of apportionment provisions in a city business tax. This action was designed to comply with

California's implied constitutional limitations on city tax jurisdiction, which are analogous to the federal Commerce Clause. *See id.* at 525. Analyzing Modesto's originally unapportioned tax, the court reiterated *McKesson's* distinction between taxes that are a nullity under Commerce Clause analysis and taxes that operate in a discriminatory manner:

If a city collects a business tax on activity carried on outside of its boundaries, i.e., the tax is not apportioned, that extraterritorial tax is beyond the city's power to impose. In such a situation, no corrective action by the city can cure the invalidity of the tax. Rather, the city has no choice but to "undo" the unlawful deprivation by refunding the tax previously paid by the business on its extraterritorial activities. . . .

In contrast, if the tax is invalid because it operates in a discriminatory manner, i.e., similarly situated taxpayers are assessed at different tax rates, a city has several corrective options. To equalize the tax rate, the city can issue a partial refund to the disfavored parties, assess and collect back taxes from the favored parties, or combine a partial refund with a partial retroactive assessment.

*Id.* (citing *McKesson*, 496 U.S. at 39-41).

In this legal context, in *W.R. Grace*, given that the legislature adopted exactly the credit remedy specifically suggested by the U.S. Supreme Court in *Tyler Pipe*, *see W.R. Grace*, 137 Wn.2d at 599, 601, the state Supreme Court saw no need to analyze either of the "legitimate purpose" or the "rational means" prongs of the *Carlton* analysis in detail. Because taxpayers were not required to pay more under the new multiple activities credit than they had under prior law, the Court rejected the idea that the retroactive credit mechanism had unreasonably disappointed taxpayer expectations: "[I]t cannot reasonably be said . . . retroactive

application of the 1987 curative credit, *designed to benefit taxpayers*, has made their tax liability more burdensome.” *W.R. Grace*, 137 Wn.2d at 602 (emphasis added).

The dispute in *W.R. Grace* – the retroactive *enhancement* of taxpayer protections against multiple taxation – has nothing in common with the context of this case, which is the retroactive expansion of the Estate Tax base.

**b. All of the Department’s Cases Are Distinguishable.**

The DOR identifies a number of decisions upholding a retroactive change in tax statutes for periods longer than four years against Due Process challenges. *See* Br. Appellant at 23. All arose in circumstances significantly different from this case and the DOR relies on *none* of them on their facts.

As noted above, *W.R. Grace* was a Commerce Clause discrimination case in which the Legislature enhanced taxpayer remedies rather than increased taxpayer burdens. The New York case cited by the Department, *Moran Towing Corp. v. Urback*, 1 A.D.3d 722, 768 N.Y.S. 2d 33 (2003), had the same context. *See id.* at 723.

Two cases involved retroactive amendment of statutes that the court held were previously *ambiguous* and which had not been judicially construed. *See Montana Rail Link Inc. v. United States*, 76 F.3d 991, 994 (9<sup>th</sup> Cir. 1996); *Enterprise Leasing Co. v. Ariz. Dep’t of Revenue*, 211 P.3d 1 (Ariz. App. 2008). The Alabama case, *Maples v. McDonald*, 668 So. 2d

790, 792 (Ala. Civ. App. 1995), similarly involved an express legislative declaration of intent to clarify the statute in question, which had *not* been judicially construed.

*Miller v. Johnson Controls, Inc.*, 296 S.W.2d 392, 394, 400 (Ky. 2009), involved retroactive amendment of a statute that had been judicially construed, but the basis of the prior decision was only that the Kentucky Revenue Cabinet was bound to its prior, contemporaneous construction of an *ambiguous* statute. *See GTE v. Revenue Cabinet*, 889 S.W.2d 788, 792 (Ky. 1994). Moreover, unlike the Estate in this case, the taxpayer in *Johnson Controls* had *never* sought the lower-tax benefit allowed by the decision in *GTE* until after the *GTE* decision was issued. 296 S.W.3d at 394.

As in *Johnson Controls*, the three other tax cases all involved ongoing business taxes (not one-time tax events) and claims for refund by taxpayers that were *never* filed until after a judicial decision or legislative amendment pointed out the potential for a lower tax. *See King v. Campbell County*, 217 S.W.3d 862, 866 (Ky. App. 2006); *General Motors Corp. v. Dep't of Treasury*, 290 Mich. App. 355, 365, 376, 803 N.W.2d 698 (2010); *Atlantic Richfield Co. v. Dep't of Revenue*, 14 Or. Tax 212, 213 (1997).

The DOR also cites a non-tax case with a six-year retroactive period concerning coordination of workers' compensation benefits, *General Motors Corp. v. Romein*, 503 U.S. 181, 112 S. Ct. 1105, 117 L.

Ed. 2d 328 (1992). *Romein's* quick two-paragraph Due Process discussion, 503 U.S. at 191-92, is not relevant to a dispute about the permissible period for retroactive tax increases after *Carlton* (1994). Neither the majority in *Carlton* nor Justice O'Connor, who wrote a concurrence in *Carlton* as well as the *Romein* opinion, cited *Romein* as relevant to a tax-increase context.

Due Process requires that a retroactive imposition of *additional* taxes have a legitimate governmental purpose furthered by rational means. *Carlton*, 512 U.S. at 30-31. The DOR's arguments fail this test, and its reliance on *W.R. Grace* has the context wrong. The legislature's action egregiously fails to meet the standards in *Carlton* because of the delay in its response to the issue in dispute and the absence of any "unexpected" loss of revenues. *Carlton* and the other law and arguments stated here call on the Court to reject the DOR's position and affirm the court below.

**D. The Retroactive Application of the 2013 Amendments Violates the Impairment Clause of the Federal and State Constitutions.**

Joshua's Trust was an irrevocable trust created in 1985. Taxing Joshua's Trust in Elaine's Estate violates the federal and state Impairment Clauses. At Joshua's death in 1985, Joshua's beneficiaries held a future but vested interest in Joshua's Trust. This is the textbook example of a vested remainder. *See Edwards v. Edwards*, 1 Wn. App. 67, 70-72, 459 P.2d 422 (1969) ("[W]e hold that testatrix created a life estate and a future interest denominated a vested remainder, both interests of which

came into being at the time of [the creator's] death.”) (quoting *In re Estate of Gochmour*, 192 Wash. 92, 93, 72 P.2d 1027 (1937)). Thus, rights under Joshua's Trust became irrevocable and clearly vested 28 years ago. The 2013 Amendments purport to substantially impair these rights almost three decades later.

Article I, § 10 of the U.S. Constitution provides that “[n]o state shall . . . pass any bill of attainder, ex post facto law, or law impairing the obligations of contracts.” Article I, § 23 of the Washington Constitution provides that “[n]o bill of attainder, ex post facto law, or law impairing the obligations of contracts shall ever be passed.” These constitutional provisions are coextensive. *Tyrpak v. Daniels*, 124 Wn.2d 146, 151, 874 P.2d 1374 (1994).

The threshold inquiry under the Impairment Clauses is whether the law has, in fact, “operated as a substantial impairment of a contractual relationship.” *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, 459 U.S. 400, 411, 103 S.Ct. 697, 74 L. Ed. 2d 569 (quoting *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 244, 98 S.Ct. 2716, 57 L. Ed. 2d 727 (1978)). The Court then must weigh the nature of the state interest at stake against the severity of the impairment. *Allied*, 438 U.S. at 247-250. The essential purpose of the Impairment Clauses is to protect settled contractual expectations. *Id.* at 245.

*First*, the Impairment Clauses apply to trusts like any other contractual relationship. As the U.S. Supreme Court explained in

*Coolidge v. Long*, “trust deeds are contracts within the meaning of the contract clause of the Federal Constitution.” 282 U.S. at 595. As discussed earlier, *Coolidge* has never been overruled.<sup>22</sup> The DOR can point to no case holding that a trust is not an Impairment Clause contract, while *Coolidge* holds expressly that it is.<sup>23</sup>

As the Washington and U.S. Impairment Clauses are coextensive, the Court should follow this uncontroverted U.S. Supreme Court precedent. *See Tyrpak*, 124 Wn.2d at 151; *Farrell v. Mentzer*, 102 Wash. 629, 174 P. 482 (1918) (“express trusts are created by contract of the parties”); *In re Estate of Bodger*, 130 Cal. App. 2d 416, 279 P.2d 61 (1955) (the act of trust creation “is nothing more than a third party beneficiary contract”). Trusts have long been held to be within the protection of these constitutional provisions. *See Adams v. Plunkett*, 274 Mass. 453, 175 N.E. 60 (1931); *Maine Edu. Assoc. Benefits Trust v. Cioppa*, 842 F. Supp. 2d 373, 384-85 (D. Me. 2012) (analyzing trust agreement as if it were a contract for Impairment Clause purposes but concluding there had been no substantial impairment).

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<sup>22</sup> And *Wiener* did not address the Impairment Clause. *See Wiener*, 326 U.S. at 342-43.

<sup>23</sup> The DOR may claim that trusts are not contracts “in the usual sense of [that] word,” meaning “an agreement of two or more minds, upon sufficient consideration, to do or not to do certain acts.” *Caritas Services, Inc. v. Dep’t of Soc. And Health Services*, 123 Wn.2d 391, 403, 896 P.2d 28 (1994) (quoting *Crane v. Hahlo*, 258 U.S. 142, 146, 42 S. Ct. 214, 66 L. Ed. 514 (1922)). Significantly, however, this oft-repeated quote originated with the U.S. Supreme Court a decade *before* the Court’s opinion in *Coolidge*, which held a trust deed to be a contract even through the transaction was not a “bona fide purchase for full consideration. . . .” *Coolidge*, 282 U.S. at 593.

The impairment of vested rights here is substantial. A contract is “impaired by a statute which alters its terms, imposes new conditions or lessens its value.” *Caritas Servs., Inc. v. Dep’t of Social & Health Servs.*, 123 Wn.2d 391, 404, 869 P.2d 28 (1994). The impairment is “substantial if the complaining party relied on the supplanted part of the contract, and contracting parties are generally deemed to have relied on existing state law pertaining to interpretation and enforcement.” *Margola Assocs. v. City of Seattle*, 121 Wn.2d 625, 653, 854 P.2d 23 (1993).

Here, Joshua and his Estate “relied on existing law” and relied on the fundamental nature of the trust that the legislature has now “supplanted.” See *Margola*, 121 Wn.2d at 653. The trust was created, and the property subject to the trust vested in the remainder beneficiaries, in 1985, years before Washington enacted its estate tax. Two decades later, the legislature has attempted to change the very nature of the trust by forcing its life-time beneficiary to include the trust property in her estate. The fact that Joshua’s Estate elected the trust property to be treated as if it were part of Elaine’s estate under *federal* law does not give the State of Washington authority to reach back in time and rewrite history by imposing a then-nonexistent *state* tax on the trust. To be clear, Joshua’s federal QTIP election did nothing to change the nature of the trust. If Joshua had intended to *actually* allow the trust property to become part of Elaine’s estate (for any purpose other than *federal* estate tax law), then he would have simply given her the property without creating a trust. But

Joshua instead executed a trust—a legal contract—which created vested contractual rights in the trust’s remainder beneficiaries and kept the property out of Elaine’s control, *i.e.*, out of her actual estate. The new legislation fundamentally dismantles and readjusts these key terms of the trust, which is no small impairment.<sup>24</sup> *United States Trust Co. of N.Y. v. New Jersey*, 431 U.S. 1, 19 n.17, 97 S. Ct. 1505, 52 L. Ed. 2d 92 (1977) (A mere change of law “is much less likely to upset expectations than a law *adjusting the express terms of an agreement.*”) (emphasis added).

Moreover, under both state and federal law, a retroactive estate tax applied to preexisting contracts creates a substantial impairment. In *Coolidge*, the U.S. Supreme Court held that an estate tax created after the execution of a trust deed but before the death of the lifetime beneficiaries substantially impaired contractual rights. 282 U.S. at 595. Neither the size of the tax nor the size of the estate was relevant to the Court’s conclusion that the impairment would be unacceptably substantial. *See id.*

The Washington Supreme Court followed *Coolidge* in *In re McGrath’s Estate*, concerning two life insurance policies purchased before

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<sup>24</sup> Moreover, at the time Joshua created the trust, Washington only collected estate taxes by sharing federally collected estate taxes through a credit. *See Bracken*, 175 Wn.2d at 557. By electing to defer *federal* taxation under IRC § 2056, Joshua’s Estate took a risk that *federal* estate taxes may increase or decrease by the time of Elaine’s death. But because Washington had no separate estate tax or QTIP election, Joshua’s settled expectation was that the trust’s tax liability to the State would correlate with the trust’s federal tax liability—his trusts would incur no greater tax burden because of the “revenue-sharing” feature of the former pickup tax. Thus, it was a fundamental assumption of the trust that any tax benefit or detriment resulting from the trust’s *federal* tax deferral could not be undone through a separate state tax, which did not exist at the time. Washington’s attempt to collect tax on federal QTIP property reaches into the past and attempts to unwind this settled expectation.

the legislature subjected life insurance proceeds to inheritance tax. *McGrath*, 191 Wn. at 497-98. The Court held that taxing the insurance proceeds was an unconstitutional impairment of the insurance contracts, finding that the right to the proceeds of the life insurance arose and vested when the purchaser executed the contracts. *Id.* Any later statute that attempted to tax the insurance proceeds would, if enforced, substantially impair the purchaser's contractual rights because it would receive less than it was entitled to receive under the contract's term. *Id.* at 508-09.<sup>25</sup>

Finally, the State's attempts to justify the law do not outweigh the severity of the impairment.<sup>26</sup> The facially absolute language of the Impairment Clauses is limited only to accommodate the "inherent police power of the State," but the severity of the impairment "increases the level of scrutiny to which the legislation will be subjected." *Birkenwald Distributing Co. v. Heublein, Inc.*, 55 Wn. App. 1, 9, 776 P.2d 721 (1989) (citing *Energy Reserves*, 459 U.S. at 411).

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<sup>25</sup> The DOR cannot cite to a case overruling *McGrath* or *Coolidge* because none exists. The Washington Supreme Court in *Bracken* also relied on *McGrath*. See 175 Wn.2d at 565-66. Despite the DOR's and the legislature's attempts to subvert the judiciary system, both arms of the State must admit that they lack the authority to decide what is or is not "good law." That determination is for the courts, and the Washington Supreme Court has affirmed that *McGrath* is still alive and well. See *Id.*

<sup>26</sup> The State's only justification for the substantial contractual impairment in the 2013 Amendments is funding the "Education Legacy Trust Account," which is simply, naked government fundraising; that is, there is no policy change or health and safety rationale to the State's attempt to grab and tax federal QTIP property—it's all about money. And, specifically, "[f]inancial necessity, though superficially compelling, has *never been sufficient of itself to permit states to abrogate contracts.*" *Carlstrom v. State*, 103 Wn.2d 391, 396, 694 P.2d 1 (1985) (emphasis added); see also *United States Trust Co.*, 431 U.S. at 25-26.

The 2013 Amendments unconstitutionally impair the QTIP trust beneficiaries' contractual rights because they would receive less—far less—than they would have received under the pickup tax regime at the trust's inception. *McGrath*, 191 Wash. at 508-09.

**E. The Retroactive 2013 Amendments Violate the Provisions of Article VII, Section 1 of the Washington Constitution Requiring Uniformity in Property Taxation.**

It is a given that the Washington Estate Tax is not *intended* to be a “property tax.” *Bracken*, 175 Wn.2d at 559 (citing WAC 458-57-105(2)); *see also In re McGrath's Estate*, 191 Wn.2d 496, 502, 71 P.2d 395 (1937) (former inheritance tax was not imposed on the “corpus” of citizens’ “property”). Both the new Estate Tax and the old inheritance tax are intended to be imposed on “transfers.”<sup>27</sup>

However, the 2013 Amendments break faith with this intention. Instead of taxing *transfers* of trust property, they impose retroactive tax on the *property* of QTIP trusts itself. For this reason, given that the Estate Tax would be imposed unequally on QTIP trusts (given the exclusion amounts, deductions, and graduated rates of the Estate Tax), the retroactive provisions provide for unconstitutional, non-uniform taxation of QTIP.

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<sup>27</sup> Under the pre-1981 inheritance tax, the tax was clearly not applicable to the termination of a life beneficiary's interest, but could apply in the beneficiary's estate if the Washington beneficiary also had a power of appointment that she exercised in her Last Will. *See In re Simond's Estate*, 188 Wash. 211, 215, 61 P.2d 1302 (1936) (citing *Chanler v. Kelsey*, 205 U.S. 466, 27 S. Ct. 550, 51 L. Ed. 882 (1907)).

It is undisputed that: (i) the “transfer” of the QTIP in this case occurred upon Joshua’s death, (*Bracken*, 175 Wn.2d at 567, where (Department agreed that QTIP is property of the first spouse to die and is transferred to the QTIP trust); and (ii) the QTIP at issue in this case was not part of the estate of Elaine under *Bracken’s* interpretation of the 2005 Act. *See* CP 135 (for DOR’s concession that the refund is due under *Bracken* if “clarifying” legislation does not pass). The *only* reason that the QTIP in this case would be taxable today is via the retroactive incorporation of IRC § 2044’s provisions into the definition of “Washington taxable estate” in amended RCW 83.100.020(14). That is, IRC § 2056(b)(7), which provides that QTIP “*shall be treated as*” passing to the surviving spouse and no other person.

Consequently, the tax in question relates to property that *did, in fact*, transfer to *both* Elaine **and** the remainder interests of the QTIP Trust in 1985 (when there was only a pickup tax) and the tax application is based solely on a fiction. And, the Supreme Court in *Bracken* already held that, because of the nature of the estate tax, the legislature does not have power to “*substitute*” a fictional transfer for an actual transfer. *See* 175 Wn.2d at 566. Consequently, the retroactive imposition of tax on fictional transfers has to be interpreted as a *change* in the nature of the tax, so that it functions as a property tax with respect to a limited range of property that “escaped” taxation because the otherwise taxable transfer occurred before the 2005 Act was adopted.

The legislature's own statement of intent shows that taxing *property* was key to its motivation, *i.e.*, as needed "to restore parity between QTIP property and other property eligible for the marital deduction." 2013 Amendments §1(5). The DOR specifically explained to the trial court that 2013 Amendments would "retroactively clarify the intent of the Legislature *to tax QTIP*." CP 135 (emphasis added).

Section 1 of Article VII of the Washington Constitution provides:

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

The Estate Tax is shot through with mechanisms that differentiate how the value of estates is taxed.<sup>28</sup> These differences are sufficient so that any part of the Estate Tax deemed to be a property tax will violate the uniformity requirement with regard to the relevant "class" of property.

The Estate does not argue that the Estate Tax as amended is a property tax in its entirety. However, the legislature's targeted, retroactive amendment to capture tax on property that was *in fact* "transferred" before the 2005 Act is not a valid excise tax. It is not a tax on any privilege, or

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<sup>28</sup> For example, and this is not a complete list of the non-uniform aspects of the Estate Tax, various "exclusion amounts" are defined in RCW 83.100.020(1)(a) and given effect in the definition of "Washington taxable estate" in RCW 83.100.020(14); a deduction is granted for certain family-owned business assets in 2013 Amendments § 3; and graduated tax rates are established in RCW 83.100.040.

transfer right, but only a retroactive tax on property. The retroactive amendments violate the Washington constitution and should be rejected.

**F. The Court Should Not Allow the DOR to Intentionally Delay the Estate's Right to an Undisputed Right.**

The State of Washington has egregiously ignored its laws and regulations to be in position to enforce retroactive legislation against the Estate. After the decision terminating review in *Bracken*, the DOR brazenly admitted that it sought to delay the Estate's refund and the trial court's ruling solely to give time to have the law changed. Then, after the trial court finally ordered the Director of the DOR to issue the refund, the DOR ignored that order. Finally, in contravention of Rule 11, DOR attorneys filed a baseless appeal to avoid the final judgment that would have made moot the Legislature's subsequent corrective bill. Our government should not be permitted to flout the law with one hand to deprive the Estate of its right to a refund with the other.

This case was pending in the trial court long before the Supreme Court accepted review in *Bracken*. In 2010, the Estate accepted a proposal to stay the trial court proceedings and patiently awaited the outcome of *Bracken*, which the parties understood would be binding on the DOR as well as the Estate. *Bracken* became a final decision on January 10, 2013, after which the Estate's refund was immediately due and payable.

There is no dispute that as of January 11, 2013, the DOR had an immediate obligation to pay the Estate a refund. *See* CP 144 ("there is no dispute that the Estate is entitled to a refund of Washington estate tax and

interest”). The Estate had filed a timely application for refund nearly four years earlier. Once the final order denying reconsideration in *Bracken* was entered, there were no other issues precluding issuance of a refund.

Under RCW 83.100.130(1), once “the examination of the returns or records of [the] taxpayer” is concluded, and an estate has made application for refund within the statute of limitations described in RCW 83.100.095, “the department shall refund the amount of the overpayment together with interest . . . .” Elaine’s Estate had already received final state and federal tax clearance in 2009. Thus, as of January 11, 2013, the Supreme Court of Washington effectively determined that Elaine’s Estate was entitled to a refund. The Estate had a right to a refund under 83.100.130(1). Nevertheless, the DOR delayed for nearly five months, refusing to issue any refund.

This action forced the Estate to file a motion to compel payment of the refund. In response, the DOR openly admitted that it was filing its pleading solely for the purpose of delay—in the hope that the legislature would, eventually, retroactively amend the statute. The DOR then disregarded a clear court order and refused to issue the refund. The Estate has also been deprived of its clear and settled right to a refund as a result of the DOR’s use of delay to gain an advantage.<sup>29</sup>

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<sup>29</sup> See *Mission Springs v. City of Spokane*, 134 Wn.2d 947, 954 P.2d 250 (1998) (City’s intentional delay of permit issuance for tactical purposes supported a claim under 42 U.S.C. § 1983 for the deprivation of a constitutional or state property right. )

Despite its admission that *Bracken* was conclusive, DOR also filed the current appeal for the sole and impermissible basis of artificially delaying final judgment until the legislature passed a bill that expressly attempted to overrule *Bracken* as to this case and others that had already received a favorable trial court ruling. On the date of the DOR's appeal, no legal basis existed for the appeal.<sup>30</sup>

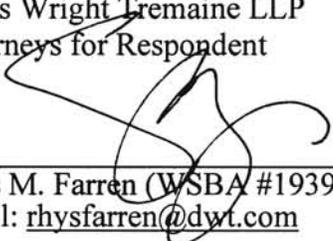
Both CR 11 and RAP 18.9(a) provide that a Court may sanction a party for signing and filing pleadings solely for the purpose of delay, as DOR unquestionably did here. The sanction should take the form of a denial of a defense to the Estate's refund application. For the same reason, the Court should award the Estate its attorneys' fees incurred in connection with the DOR's appeal under RAP 18.1, RAP 18.9 and CR 11.

## V. CONCLUSION

The trial court order should be affirmed.

RESPECTFULLY SUBMITTED this 14<sup>th</sup> day of November, 2013.

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Attorneys for Respondent



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<sup>30</sup> By definition, the 2013 Amendments do not apply to "any final judgment, no longer subject to appeal, entered by a court of competent jurisdiction," as of the June 14, 2013 effective date. Laws of 2013, 2d Sp. Sess., ch. 2 § 10. The statute cannot seriously be read to suggest that "appeal" means still subject to a "frivolous appeal."

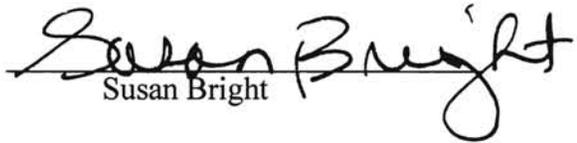
PROOF OF SERVICE

I, Susan Bright, the undersigned, hereby certify and declare under penalty of perjury under the laws of the State of Washington that the following statements are true and correct:

On this date, I caused to be delivered a true copy of the foregoing document to be sent by First Class U.S. Mail and electronic mail on the following:

Washington State Department of Revenue  
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Executed at Bellevue, Washington this 14<sup>th</sup> day of November, 2013.

  
Susan Bright