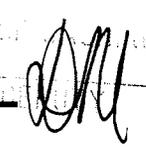


NO. 42159-3-II

COURT OF APPEALS
DIVISION II
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STATE OF WASHINGTON
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**COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON**

DONALD R. WATTS, DONALD L. ODEGARD, and STEPHEN D.
BANNWORTH,

Appellants,

v.

WASHINGTON STATE DEPARTMENT OF REVENUE,

Respondent.

BRIEF OF RESPONDENT

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ORIGINAL

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I. INTRODUCTION

For many years Washington has imposed a real estate excise tax on the sale of real property located in this state. In 1993, to prevent easy avoidance, the Legislature amended the tax so that it also applied to the sale of a controlling interest in an entity with an interest in real property located in this state. When the tax is triggered by the sale of a “controlling interest,” the selling price upon which the tax is measured is the fair market value of the real property owned by the entity. *McFreeze Corp. v. Dep’t of Revenue*, 102 Wn. App. 196, 201, 6 P.3d 1187 (2000).

In 2008, appellants Donald R. Watts, Donald L. Odegard, and Stephen Bannworth (hereinafter “sellers”) paid real estate excise tax arising from their indirect sale of 50.01 percent of a limited liability company that owned farm land in Washington. The sellers do not dispute that the transaction was a taxable sale of a controlling interest in an entity with an interest in Washington real property under the tax statute. Instead, the sellers attack the constitutionality of the statute with respect to a *portion* of the tax they paid. They argue that 49.99 percent of the tax represents a nonuniform property tax in violation of article VII, section 1 of the Washington Constitution. The sellers also assert an equal protection claim.

The sellers' constitutional arguments are unfounded. Under the well-established analysis for distinguishing an excise tax from a property tax, the real estate excise tax as applied to the sale of a controlling interest is an excise tax. Consequently, the tax does not violate article VII, section 1 of the Washington Constitution. That provision applies only to property taxes. Furthermore, the sellers offer no analysis and no relevant authority supporting their assertion that the tax violates equal protection.

The sellers have not met their burden of showing that any portion of the tax they paid is unconstitutional. Accordingly, this Court should affirm the superior court's order granting summary judgment in favor of the Department of Revenue.

II. RESTATEMENT OF THE ISSUE

Statutes enacted by the Legislature are presumed to be constitutional and a party seeking to invalidate a statute on constitutional grounds must establish that the provision is unconstitutional beyond a reasonable doubt. *Washington State Grange v. Locke*, 153 Wn.2d 475, 486, 105 P.3d 9 (2005). In light of this presumption of constitutionality, this refund action presents the following two issues:

1. Does the real estate excise tax imposed on a sale of a controlling interest in an LLC that owns Washington real property violate

the uniformity requirement of article VII, section 1 of the Washington Constitution?

2. Does the real estate excise tax imposed on a sale of a controlling interest in an LLC that owns Washington real property violate the equal protection clause of the United States Constitution or the privileges and immunities clause of the Washington Constitution?

III. STATEMENT OF THE CASE

A. Sale Of Watts Brothers Farms, Resulting In Indirect Sale Of 100 Circle Farms.

Prior to February 25, 2008, the sellers were the owners of Watts Brothers Farms, LLC (“Watts Brothers Farms”). CP 111 (Stip., ¶ 1). Watts Brothers Farms was a Washington limited liability company that owned 50.01 percent of 100 Circles Farms, LLC (“100 Circles Farms”). CP 112 (Stip., ¶ 2). 100 Circles Farms was a Washington limited liability company that owned approximately 19,400 acres of farm land in Benton County, Washington. CP 112 (Stip., ¶ 3). ConAgra Lamb Weston, Inc. (“ConAgra”) owned the remaining 49.99 percent of 100 Circles Farms was owned by. CP 112 (Stip., ¶ 2).

On February 25, 2008, the sellers sold Watts Brothers Farms to ConAgra. CP 112 (Stip., ¶ 4). As a result of this sale, the sellers’ 50.01 percent interest in 100 Circle Farms was transferred to ConAgra, causing ConAgra’s interest in 100 Circles Farms to increase from 49.99 percent to

100 percent. The transaction qualified as a sale of a controlling interest in an entity with an interest in Washington real property.

B. Controlling Interest Transfer Return And Payment Of The Tax.

In March 2008, the sellers filed a controlling interest transfer return with the Department of Revenue to report the sale of Watts Brothers Farms. CP 113 (Stip., ¶ 6); CP 148. The return showed total real estate excise tax due of \$1,320,643.60. CP 113 (Stip., ¶ 7); CP 148. The sellers paid the real estate excise tax shown due on the return with two checks. CP 113 (Stip., ¶ 8). The first check, in the amount of \$841,649.95, represented the tax computed on 50.01 percent of the value of the Washington real property owned by 100 Circle Farms plus the tax owed on other real property owned by Watts Brothers Farms at the time of the sale. CP 113 (Stip., ¶ 8). The sellers do not dispute that this amount was properly due under RCW 82.45. CP 113 (Stip., ¶ 8).

The second check, in the amount of \$478,993.65, represented the real estate excise tax computed on 49.99 percent of the value of the Washington real property owned by 100 Circle Farms. CP 114 (Stip., ¶ 9). The sellers assert that the \$478,993.65 payment was not properly due.

C. Refund Claim And Administrative Appeal.

In January 2009, the sellers filed an application for refund of real estate excise tax with the Department of Revenue. CP 114 (Stip., ¶ 10);

CP 152. In that application, the sellers sought return of the \$478,993.65 disputed tax. The Department reviewed and denied the refund application. CP 114 (Stip., ¶ 13); CP 163.

D. Proceedings Below.

The sellers filed a timely action in Thurston County Superior Court under RCW 82.32.180, seeking a refund of the tax computed on 49.99 percent of the value of the Washington real property owned by 100 Circle Farms. CP 114 (Stip., ¶ 14); CP 10. The parties filed cross-motions for summary judgment on stipulated facts. The superior court granted the Department's motion and denied the sellers' cross-motion. CP 241. This appeal followed.

IV. ARGUMENT

A. Standard Of Review.

This appeal stems from the grant of summary judgment in favor of the Department of Revenue. The Court of Appeals reviews a grant of summary judgment de novo, applying the same standard used by the lower court in ruling on the motion. *Seiber v. Poulsbo Marine Ctr., Inc.*, 136 Wn. App. 731, 736, 150 P.3d 633 (2007).

Summary judgment is appropriate when no genuine issue of material fact exists and the moving party is entitled to judgment as a matter of law. CR 56. The material facts supporting the Department's

motion for summary judgment were not disputed. When the material facts in an excise tax refund action are undisputed, the appellate court reviews the superior court's legal conclusions de novo. *Simpson Inv. Co. v. Dep't of Revenue*, 141 Wn.2d 139, 148, 3 P.3d 741 (2000).

B. The Real Estate Excise Tax Imposed On The Sellers' Sale Of A Controlling Interest In An LLC That Owned Washington Real Property Did Not Violate Article VII, Section 1 Of The Washington Constitution.

1. The Legislature amended the real estate excise tax in 1993 to apply the tax to the sale of a controlling interest.

A brief history of the real estate excise tax provides context in addressing the legal issues before the Court. The Washington Legislature enacted the real estate excise tax in 1951. Laws of 1951, 1st Ex. Sess., ch. 11. Initially, the statute allowed counties to impose a 1 percent transfer tax on each sale of real property located within the county for the support of common schools. In 1980, the Legislature amended the tax so that it was levied by the State. Laws of 1980, ch. 154.

In a series of decisions in the 1950s and 1960s, the Washington Supreme Court held that the real estate excise tax did not apply to the transfer of real property that occurred when a corporation owning Washington real property was dissolved and the property was distributed to the shareholders. *See, e.g., Deer Park Pine Indus., Inc. v. Stevens Cy.*, 46 Wn.2d 852, 286 P.2d 98 (1955); *Ban-Mac, Inc. v. King Cy.*, 69 Wn.2d

49, 416 P.2d 694 (1966). This created a “sizable loophole” in the tax by effectively removing from its reach real property transfers occurring “when a person buys the stock of an existing corporation and then dissolves the corporation to obtain the land.” *Ban-Mac*, 69 Wn.2d at 51 (quoting *Christensen v. Skagit Cy.*, 66 Wn.2d 95, 100, 401 P.2d 335 (1965) (Finley, J., dissenting)). Over time, it became commonplace to avoid the tax by placing real property into a corporation or partnership and then transferring ownership of the entity. *See* Final Legislative Report, 53d Leg., at 325 (Wash. 1993).¹ Because the tax could be avoided with relatively simple advanced planning, it lost much of its effectiveness as a revenue source for the State.

The Legislature first attempted to close this “sizable loophole” in 1991 by imposing an excise tax “on each ownership transfer of a corporation[.]” Laws of 1991, 1st Spec. Sess., ch. 22, § 1(1).² The 1991 act did not amend the real estate excise tax in RCW 82.45, but imposed a separate tax codified as RCW 82.45A.

¹ Relevant portions of the 1993 Final Legislative Report are attached as Appendix A. That Report confirms that the real estate excise tax was easy to avoid prior to the 1993 amendment: “If real estate is owned by a partnership or corporation, a sale of a controlling interest in the partnership or corporation can effectively transfer control of real estate without creating tax liability. Many transactions are structured in this manner to avoid real estate excise taxes.” *Id.*

² The stated intent of the 1991 act was “to apply an excise tax to transfers of corporate ownership when the transfer of ownership is comparable to a sale of real property.” Laws of 1991, 1st Spec. Sess., ch. 22, § 1(2).

The Legislature soon concluded that the 1991 act was ineffective. After just two years, the Legislature repealed the 1991 act in its entirety, Laws of 1993, 1st Spec. Sess., ch. 25, § 512, and amended the real estate excise tax statutes in RCW 82.45 with the intent to apply the tax to “transfers of entity ownership when the transfer of entity ownership is comparable to the sale of real property.” Laws of 1993, 1st Spec. Sess., ch. 25, § 501(2).

The real estate excise tax is imposed “upon each sale of real property.” RCW 82.45.060. As amended in 1993, “real property” is defined as “any interest, estate, or beneficial interest in land . . ., *including the ownership interest or beneficial interest in any entity which itself owns land* or anything affixed to land.” RCW 82.45.032(1) (emphasis added). The term “sale” is defined to include both its ordinary meaning and “the transfer or acquisition within any twelve-month period of a controlling interest in any entity with an interest in real property located in this state for a valuable consideration.” RCW 82.45.010(1), (2)(a).

As explained above, the Legislature extended the real estate excise tax to the sale of a controlling interest to prevent continued avoidance of the tax through relatively simply tax planning measures. Redefining “sale” and “real property” to include a transfer or acquisition of a

controlling interest in an entity with an interest in Washington real property closed the “sizable loophole.”

2. The measure of the tax, which is not prorated when less than 100 percent of a controlling interest in an entity is sold, is constitutional.

The real estate excise tax is imposed on the seller, RCW 82.45.080, and is payable at the time of sale. RCW 82.45.100(1). When the tax is triggered by the sale of a controlling interest in an entity with an interest in Washington real property, the “selling price” upon which the tax is computed is the fair market value of the real property owned by the entity. RCW 82.45.030(2); *see McFreeze Corp. v. Dep’t of Revenue*, 102 Wn. App. 196, 201, 6 P.3d 1187 (2000) (the measure of the real estate excise tax as it applies to the sale of a controlling interest is not ambiguous and “the value taxed is not the consideration paid, but the value of the real estate owned by the entity”). The statute does not allow the tax to be prorated based on the percentage of the entity that is sold. This is because the tax, as it relates to the sale of a controlling interest, is designed to apply when control of the entity has passed from the seller to the purchaser. It is immaterial whether that transfer of control results from the sale of 100 percent of the entity, 50 percent of the entity, or some percentage in between. In short, the triggering event is a binary operation.

If the sale results in control of an entity with an interest in Washington real property being transferred, the tax applies.

The sellers, at least implicitly, assert that prorating the tax based on the ownership percentage of the entity sold is constitutionally required. This is evident from the fact that the sellers (1) concede that tax was properly imposed on 50.01 percent of the value of the Washington real property owned by 100 Circle Farms, and (2) assert that the tax was “invalid” or unconstitutional as imposed on the other 49.99 percent of the value of the Washington real property owned by 100 Circle Farms. Br. of App. at 5. By attacking only the “disputed” tax computed on what the sellers refer to as the “ConAgra Portion” of the Washington real property owned by 100 Circle Farms, the sellers suggest that the tax must be prorated in order to be constitutional. *See also* Br. of App. at 40-41 (suggesting that the omission of a proration mechanism in the tax statute results in “improperly imposing the REET on the ConAgra Portion”).

The sellers cite no authority supporting their assertion that prorating the tax is required, and the Department is aware of no legal or logical reason why the federal or Washington Constitutions would mandate such a mechanism. Moreover, there is nothing inherently unfair about the manner in which the Washington Legislature has designed the tax. Before the sale, the *seller* had control over the entity and, indirectly,

all the Washington real property owned by the entity. After the sale, the *purchaser* has control over the entity and, indirectly, all the Washington real property owned by the entity. Actual transfer of title to the real property is not required in order to transfer control over the real property owned by the entity.

As amended in 1993, the real estate excise tax is specifically designed to impose an excise tax on the sale of a “controlling interest” and is specifically designed to measure the tax on a non-prorated basis. There is nothing unconstitutional about the method the Washington Legislature has chosen to tax these transactions.

3. The real estate excise tax is not an unconstitutional nonuniform property tax under article VII, section 1 of the Washington Constitution.

The sellers argue that the real estate excise tax as applied to the sale of a controlling interest is “an unconstitutional, nonuniform property tax under Washington Constitution art. VII § 1.” Br. of App. at 15. *See also, id.* at 34-41. They are mistaken.

a. Article VII, section 1 of the Washington Constitution applies only to property taxes.

Article VII, section 1 of the Washington Constitution provides in relevant part that “[a]ll 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.” It is well-

established that this provision applies only to property taxes. *See, e.g., Black v. State*, 67 Wn.2d 97, 100, 406 P.2d 761 (1965); *Cosro, Inc. v. Liquor Control Bd.*, 107 Wn.2d 754, 761, 733 P.2d 539 (1987).

b. The real estate excise tax is an excise tax, not a property tax.

The Washington Supreme Court has described a property tax as a tax on ownership and involves “an absolute and unavoidable demand against property or the ownership of property.” *Samis Land Co. v. City of Soap Lake*, 143 Wn.2d 798, 814, 23 P.3d 477 (2001) (quoting *Covell v. City of Seattle*, 127 Wn.2d 874, 890, 905 P.2d 324 (1995)). By contrast, an excise tax is a tax upon the use or transfer of property. *High Tide Seafoods v. State*, 106 Wn.2d 695, 699, 725 P.2d 411 (1986).

The real estate excise tax as applied to the sale of a controlling interest has none of the characteristics of a property tax. The tax is not imposed on mere ownership and does not involve “an absolute and unavoidable demand against property or the ownership of property.” *Samis Land*, 143 Wn.2d at 814. Instead, the tax is an excise tax imposed on the voluntary act of selling real property, which includes a transfer of a controlling interest in an entity with an interest in Washington real property. *See* RCW 82.45.010(2)(a) (defining “sale” to include “the transfer or acquisition . . . of a controlling interest in any entity with an

interest in real property located in this state for a valuable consideration”); RCW 82.45.032(1) (defining “real property” as “any interest, estate, or beneficial interest in land . . . including the ownership interest or beneficial interest in any entity which itself owns land”). It is the act of selling the land or the controlling interest that gives rise to the tax obligation. RCW 82.45.060. If the owner of the land or the controlling interest does not sell the property, no tax is owed.

In *Mahler v. Tremper*, 40 Wn.2d 405, 243 P.2d 627 (1952), the Washington Supreme Court held that the real estate excise tax is an excise tax. While the Court decided *Mahler* before the 1993 amendment to RCW 82.45 that extended the tax to sales of a “controlling interest,” the tax as applied to the sale of a controlling interest is not materially different than the tax as applied to the sale of land. In either case, it is the act of selling the property (the land or the controlling interest) that gives rise to the tax obligation. RCW 82.45.060.

The only aspect of the real estate excise tax that even remotely resembles a property tax is that the tax is measured by the value of the Washington real property owned by the entity. *See* RCW 82.45.030(2). But the measure of the tax, without more, does not make it a property tax. *See Sheehan v. Cent. Puget Sound Reg'l Transit Auth.*, 155 Wn.2d 790, 806-07, 123 P.3d 88 (2005) (motor vehicle excise tax is not a property tax

even though measure of the tax is the value of motor vehicle being licensed for use on public roadways); *High Tide Seafoods v. State*, 106 Wn.2d 695, 700, 725 P.2d 411 (1986) (tax on enhanced food fish is an excise tax even though measure of the tax is the value of the food fish possessed). Moreover, the Legislature has broad discretion in choosing the measure of an excise tax. In short, an excise tax may be measured by the value of property so long as there is a rational connection between the activity being taxed and the property used to measure the tax. *Sheehan*, 155 Wn.2d at 801.

The measure of the real estate excise tax as applied to the sale of a controlling interest is entirely rational. Before the sale, the *seller* had control over the entity and therefore had effective control over the Washington real property owned by the entity. After the sale, the *purchaser* has effective control over the Washington real property owned by the entity. Actual transfer of title to real property from the seller to the purchaser is not constitutionally required. When control or other economic benefit over property is transferred, the Legislature may exercise its plenary power of taxation by imposing an excise tax measured by the value of the associated property. *Cf. In re McGrath's Estate*, 191 Wash. 496, 504, 71 P.2d 395 (1937) (estate tax measured by value of property not formally transferred by the decedent was properly included in

measure of the tax where there was a “shifting of economic benefit” caused by the decedent’s death).

The sellers rely heavily on *Harbour Village Apartments v. City of Mukilteo*, 139 Wn.2d 604, 989 P.2d 542 (1999), to support their argument that the real estate excise tax is a property tax. Br. of App. at 30-34. But the tax in *Harbour Village* bears no resemblance to the tax at issue here.

In *Harbour Village*, the Court concluded that an annual “residential dwelling unit fee” imposed by the City of Mukilteo was a property tax that violated article VII, section 1 of the state Constitution. *Harbour Village*, 139 Wn.2d at 608-09. Before reaching the constitutional validity of the fee, the Court first concluded that the fee was actually a property tax on each dwelling unit within the city that was rented or offered for rent. *Id.* at 607. The dwelling unit fee applied to “the mere ownership of that subclass of real property defined by its rental use. *Each rental unit is directly taxed* at \$80.60 regardless of whether it is actually rented, the number of rental transactions associated with the property, or any other factors normally associated with ongoing business activity” *Id.* (emphasis added). Based on this description of the incidence and measure of the dwelling unit fee, the Court concluded that it was a tax “on rental property as such—and a tax on rental property is no less a tax on property.” *Id.* at 607.

The residential dwelling unit fee at issue in *Harbour Village* is vastly different from the real estate excise tax imposed on the sale of a controlling interest in an entity with an interest in Washington real property. Specifically, the residential dwelling unit fee imposed an annual tax per rental unit, applied regardless of whether the unit was actually rented, and applied without regard to “any other factors normally associated with ongoing business activity.” *Id.* at 607. The real estate excise tax as applied to the sale of a controlling interest has none of those features. Rather, the tax applies once to the voluntary sale of a controlling interest in an entity with an interest in Washington real property, is imposed on the seller of the controlling interest, and is measured by the value of the real property owned by the entity at the time the taxable sale was made. In short, the real estate excise tax—unlike the tax at issue in *Harbour Village*—is not imposed on the mere ownership of real property.

Because the real estate excise tax is an excise tax, not a property tax, there is no merit to the sellers’ assertion that the tax is unconstitutional under article VII, section 1 of the Washington Constitution.

4. The real estate excise tax is not “invalid” under article VII, section 1 of the Washington Constitution.

The sellers also argue that the real estate excise tax as applied to the sale of a controlling interest is “(1) an *invalid* excise tax not directly

imposed on the extent to which Taxpayers enjoyed the privilege of transferring property,” and “(2) an *invalid* excise tax imposed on the right to own or hold property.” Br. of App. at 15 (emphasis added). However, statutes enacted by the Legislature are not “invalid” unless they are found to be unconstitutional by the courts. This is so because “[t]he legislature’s power to enact a statute is unrestrained except where, either expressly or by fair inference, it is prohibited by the state and federal constitutions.” *Wash. State Farm Bureau Fed’n v. Gregoire*, 162 Wn.2d 284, 300-01, 174 P.3d 1142 (2007) (quoting *State ex rel. Citizens Against Tolls (CAT) v. Murphy*, 151 Wn.2d 226, 248, 88 P.3d 375 (2004)). Moreover, the power to tax is one of the “essential and basic attribute[s] of sovereignty.” *Commercial Waterway Dist. 1 v. King Cy.*, 197 Wash. 441, 444, 85 P.2d 1067 (1938). As such, “the legislature possesses inherently a plenary power in the matter of taxation, except as limited by the constitution.” *State ex rel. Mason Cy. Logging Co. v. Wiley*, 177 Wash. 65, 73, 31 P.2d 539 (1934).

The sellers do not clearly identify the constitutional provision they rely on to support their claim that the real estate excise tax is “invalid.” Presumably they are relying on the uniformity requirement of article VII, section 1 of the Washington Constitution. This is the only constitutional

provision they cite. *See* Br. of App. at iii (table of authorities).³ Thus, their claim that the tax is “invalid” is simply the flip-side of their “nonuniform property tax” argument starting at page 34 of their brief.

a. The analysis in *Sheehan* is merely a variation on the general analysis used to distinguish a property tax from other kinds of taxes.

The sellers assert that the real estate excise tax as applied to their sale of a controlling interest in 100 Circle Farms was “invalid” under the analysis described in *Sheehan v. Cent. Puget Sound Reg'l Transit Auth.*, 155 Wn.2d 790, 123 P.3d 88 (2005). Br. of App. at 16. This is incorrect.

In *Sheehan*, the Washington Supreme Court rejected the claim that two local motor vehicle excise taxes were “unconstitutional because they [did] not qualify as valid excise taxes.” *Sheehan*, 155 Wn.2d at 799. In rejecting the constitutional attack, the Court explained:

We have previously noted that excise taxes require two conditions: First, excise taxes are imposed upon a voluntary act of the taxpayer, which affords the taxpayer the benefits of the occupation, business, or activity that triggers the taxable event. Second, excise taxes are directly imposed based upon the extent to which the taxpayer enjoys the taxable privilege.

³ If the sellers are relying on some other constitutional provision to support their “REET is invalid” argument, their claim should be summarily rejected. *See N.W. Motorcycle Ass'n v. Interagency Comm. For Outdoor Recreation*, 127 Wn. App. 408, 413, 110 P.3d 1196 (2005) (courts will not invalidate a statute unless it is found to be in conflict with a specific or definite provision of the state or federal constitution).

Id. at 799-800 (citing *Harbour Village*, Talmadge, J., dissenting).⁴ With respect to the second factor, the Court noted that a “precise” fit between the activity being taxed and the measure of the tax is not required. *Id.* at 801. Thus, “the relationship between the legitimate decision to tax the privilege of relicensing a motor vehicle for use on public roadways and the method of using the value of a vehicle as the measure of that privilege is sufficient to avoid any constitutional infirmity.” *Id.*

The real estate excise tax as applied to the sale of a controlling interest is an excise tax according to the analysis described in *Sheehan*. First, the tax is imposed on the seller of the controlling interest, RCW 82.45.080(1), and applies only if a sale takes place. RCW 82.45.060. Thus, the tax is imposed on the voluntary act of the taxpayer. Second, the relationship between the decision to tax the sale of a controlling interest and the measure of the tax “is sufficient to avoid any constitutional infirmity.” *Sheehan*, 155 Wn.2d at 801. Prior to the sale, the sellers owned Watts Brothers Farm, which owned the controlling interest in 100 Circles Farms, which in turn owned approximately 19,400 acres of real property located in Benton County, Washington. CP 111-12. The sale of

⁴ The Court in *Harbour Village* did not discuss or apply the analysis generally employed to distinguish a property tax from other kinds of taxes, as the dissent pointed out. *Id.* at 609 (Talmadge, J., dissenting) (“The majority pays scant attention to our recent cases differentiating between an excise tax and a property tax.”). This may explain why the Court in *Sheehan* cited the dissenting opinion in *Harbour Village*, not the majority opinion, when discussing this issue.

Watts Brothers Farms to ConAgra gave ConAgra control of 100 Circles Farms and the Washington real property owned by 100 Circles Farms. This is the type of transaction the Legislature intended to tax as “essentially equivalent to the sale of real property held by the entity.” Laws of 1993, 1st Spec. Sess., ch. 25, § 501(1).

The Washington Supreme Court’s analysis in *Sheehan* does not support the sellers’ argument that the real estate excise tax is unconstitutional as applied to their sale of a controlling interest. The real estate excise tax—like the motor vehicle excise taxes at issue in *Sheehan*—is an excise tax, not a property tax. Consequently, the tax does not violate the uniformity requirement of article VII, section 1.

b. The real estate excise tax is not imposed on the right to own and hold property.

The sellers also argue that the real estate excise tax is an “invalid” excise tax on the “right to own and hold property.” Br. of App. at 28-34. The sellers imply that this portion of their brief addresses a separate constitutional requirement or separate analysis from their “nonuniform property tax” argument. However, a review of the cases cited by the sellers reveals that they are simply rehashing the same arguments.

The sellers cite four cases in support of their “right to own or hold property” argument: *Dawson v. Kentucky Distilleries & Warehouse Co.*,

255 U.S. 288, 41 S. Ct. 272, 65 L. Ed. 638 (1921), *Harbour Village*, 139 Wn.2d 604, *Jensen v. Henneford*, 185 Wash. 209, 53 P.2d 607 (1936), and *Apartment Operators Ass'n of Seattle, Inc. v. Schumacher*, 56 Wn.2d 46, 351 P.2d 124 (1960). Br. of App. at 28. Each of these cases involved whether the tax at issue was a nonuniform property tax. More specifically, *Dawson* involved whether a Kentucky “annual license tax” on the business of owning and storing whiskey in bonded warehouses was a property tax subject to the uniformity requirement of the Kentucky constitution. *Dawson*, 255 U.S. at 294. *Harbour Village* (as discussed above) involved whether a city “residential dwelling unit fee” was a property tax subject to the uniformity requirement of article VII, section 1 of the Washington Constitution. *Jensen* involved whether the 1935 personal net income tax was a property tax subject to the uniformity requirement of article VII, section 1. *Jensen*, 185 Wash. at 216. Finally, *Apartment Operators* involved whether a tax on “the renting or leasing of real property” was a property tax subject to the uniformity requirement of article VII, section 1. *Apartment Operators*, 56 Wn.2d at 47.

As explained at pages 12 to 16 above, the real estate excise tax is not a property tax imposed on the “right to own and hold property.” It is an excise tax imposed on the voluntary act of selling “real property,” including a controlling interest in an entity with an interest in Washington

real property. The sellers' assertions to the contrary are not supported by the language of the statute or the facts of this case. As a result, their claim that the superior court erred in granting summary judgment to the Department should be rejected.

C. The Real Estate Excise Tax Imposed On The Sellers' Sale Of A Controlling Interest In An LLC That Owned Washington Real Property Did Not Violate Equal Protection.

The sellers also assert that the measure of the tax as applied to their sale of a controlling interest violates equal protection. Br. of App. at 42. However, they provide virtually no analysis and cite no authority supporting that assertion. As a result, the Court should refuse to consider the issue. *State v. Lord*, 117 Wn.2d 829, 853, 822 P.2d 177 (1991). Courts "generally do not address constitutional arguments that are not supported with adequate briefing." *Margola Associates v. Seattle*, 121 Wn.2d 625, 649-50, 854 P.2d 23 (1993). "Naked castings into the constitutional sea" do not warrant judicial consideration or discussion. *State v. Johnson*, 119 Wn.2d 167, 171, 829 P.2d 1082 (1992).

In any event, the sellers' equal protection challenge has no merit. The Fourteenth Amendment of the United States Constitution provides that "[n]o state shall . . . deny to any person within its jurisdiction the equal protection of the laws." Article I, §section 12 of the Washington Constitution similarly provides that "[n]o law shall be passed granting to

any citizen, class of citizens, or corporation other than municipal, privileges or immunities which upon the same terms shall not equally belong to all citizens, or corporations.” Until recently, it was generally understood that the state privileges and immunities clause provides no broader protection against legislative classification than does the federal equal protection clause. *Gossett v. Farmers Ins. Co. of Washington*, 133 Wn.2d 954, 979, 948 P.2d 1264 (1997). However, in *Grant County Fire Prot. Dist. No. 5 v. City of Moses Lake*, 150 Wn.2d 791, 83 P.3d 419 (2004) (*Grant County II*), the Washington Supreme Court held that in some circumstances the state privileges and immunities clause provides broader protection than the federal equal protection clause. *Id.* at 805-811. Therefore, both provisions require separate analysis.

1. The real estate excise tax does not violate the equal protection clause of the Fourteenth Amendment.

Under the federal equal protection clause, legislation is subject to rational basis review unless the person bringing the challenge is a member of a suspect class or a fundamental right is at stake. *F.C.C. v. Beach Communications, Inc.*, 508 U.S. 307, 313, 113 S. Ct. 2096, 124 L. Ed. 2d 211 (1993); *Gossett*, 133 Wn.2d at 979. Neither circumstance permitting heightened scrutiny is present here. Therefore, the sellers’ equal protection challenge must be analyzed under the rational basis standard.

Under rational basis review, the sellers must prove that the classification drawn by the law is not rationally related to any legitimate state interest. *F.C.C.*, 508 U.S. at 314-15; *DeYoung v. Providence Med. Ctr.*, 136 Wn.2d 136, 144, 960 P.2d 919 (1998). Moreover, the statute is presumed constitutional and the reviewing court “may assume the existence of any conceivable state of facts that could provide a rational basis for the classification.” *Andersen v. King County*, 158 Wn.2d 1, 31, 138 P.3d 963 (2006). Production of empirical evidence is not required. *Id.* Instead, “the rational basis standard may be satisfied where the ‘legislative choice ... [is] based on rational speculation unsupported by evidence or empirical data.’” *DeYoung*, 136 Wn.2d at 148 (quoting *F.C.C.*, 508 U.S. at 315).

A legislative classification will be upheld unless “the varying treatment of different groups or persons is so unrelated to the achievement of any combination of legitimate purposes” that the Court “can only conclude that the [legislature’s] actions were irrational.” *Gregory v. Ashcroft*, 501 U.S. 452, 472, 111 S. Ct. 2395, 115 L. Ed. 2d 410 (1991). Applying this rational basis standard, the real estate excise tax easily survives minimal scrutiny under the equal protection clause.

The 1993 act expanding the real estate excise tax to include the sale of a controlling interest in an entity with an interest in Washington

real property was primarily designed to close the “sizable loophole” that existed in the statute prior to 1993 when real property could easily be transferred untaxed though the use of corporations or partnerships. *See* Final Legislative Report, 53d Leg., at 325 (Wash. 1993) (“If real estate is owned by a partnership or corporation, a sale of a controlling interest . . . can effectively transfer control of real estate without creating tax liability. Many transactions are structured in this manner to avoid real estate taxes.”). Imposing the tax on the sale of a controlling interest was a rational response to the loophole the Legislature sought to close. Measuring the tax based on the value of the Washington real property owned by the entity was a rational response to the problem because it equated the sale of the controlling interest with the sale of the real property owned by the entity. Before the sale, the seller controlled the entity (and indirectly the Washington real property owned by the entity). After the sale, the purchaser controlled the entity (and indirectly the Washington real property owned by the entity). This transfer of control in the entity was equivalent in substance to the transfer of the real property owned by the entity. Thus, measuring the tax based on the value of the Washington real property owned by the entity rationally achieved the legitimate legislative goal of raising revenue through an excise tax on the sale or transfer of real property located in this state.

State legislatures have broad leeway in “making classifications and drawing lines which in their judgment produce reasonable systems of taxation.” *Lehnhausen v. Lake Shore Auto Parts Co.*, 410 U.S. 356, 359, 93 S. Ct. 1001, 35 L. Ed. 2d 351 (1973). “Indeed, in taxation, even more than in other fields, legislatures possess the greatest freedom in classification.” *General Motors Corp. v. Tracy*, 519 U.S. 278, 311, 117 S. Ct. 811, 136 L. Ed. 2d 761 (1997) (internal quotations and citation omitted). The Legislature acted rationally when it chose to impose the real estate excise tax on the sale of a controlling interest in an entity with an interest in Washington real property and when it chose to measure the tax by the value of the Washington real property owned by the entity. These tax policy decisions were rational in light of the “sizable loophole” that existed in the statute prior to 1993 and in light of the express legislative findings that “transfers of ownership of entities may be essentially equivalent to the sale of real property held by the entity” and “should be subject to the same excise tax burdens.” Laws of 1993, 1st Spec. Sess., ch. 25, § 501(1).

In sum, the sellers’ equal protection challenge has no merit under the equal protection clause of the Fourteenth Amendment.

2. The real estate excise tax does not violate the privileges and immunities clause of article I, section 12 of the Washington Constitution.

Analysis under the privileges and immunities clause of article I, section 12 of the Washington Constitution departs from the federal equal protection clause only when the challenged law confers preferential treatment to a minority class to the detriment of the majority. *See Andersen v. King County*, 158 Wn.2d 1, 18, 138 P.3d 963 (2006) (plurality opinion) (an independent analysis applies under article I, section 12 “only where the challenged law grants a privilege or immunity to a minority class”). In those cases where the challenged law does not favor a minority class, the courts “apply the same constitutional analysis that applies under the equal protection clause of the United States Constitution.” *Id.*

Moreover, “it must be remembered that not every statute authorizing a particular class to do or obtain something involves a ‘privilege’ subject to article I, section 12.” *Grant County II*, 150 Wn.2d at 812. Rather, a “privilege” or “immunity” under article I, section 12 pertains to “those fundamental rights which belong to the citizens of the state by reason of such citizenship.” *Id.* at 813 (quoting *State v. Vance*, 29 Wash. 435, 458, 70 P. 34 (1902)).

The sellers contend that the real estate excise tax as applied to the sale of a controlling interest “creates a separate category” of land owners

who are “penalize[d]” by choosing to hold real property “within a business enterprise.” Br. of App. at 42. However, the sellers cite no authority suggesting that there is a “fundamental right” to use a business enterprise such as an LLC to own or hold property. Nor do they explain how the classification in the real estate excise tax statute favors a minority class of land owners. Without presenting cogent analysis relating to these essential preconditions, the sellers’ separate privileges and immunities clause argument fails. *See Madison v. State*, 161 Wn.2d 85, 96-98, 163 P.3d 757 (2007) (separate analysis under the state privileges and immunities clause was not warranted where the challengers made no persuasive showing of favoritism to a minority class); *Des Moines Marina Ass’n v. City of Des Moines*, 124 Wn. App. 282, 296, 100 P.3d 310 (2004) (privileges and immunities claim rejected for lack of analysis addressing the issue), *review denied*, 154 Wn.2d 1018 (2005).

But even if the sellers had met the prerequisites of identifying a “fundamental right” and a statutory classification favoring a minority class, their separate privileges and immunities argument would still fail. In general, a legislative classification will be upheld under article I, section 12 unless there are no reasonable grounds “for distinguishing between those who fall within the class and those who do not.” *Grant County Fire Prot. Dist. No. 5 v. City of Moses Lake*, 145 Wn.2d 702, 731,

42 P.3d 394 (2002) (*Grant County I*). “[T]he level of scrutiny applied when determining whether a ‘reasonable ground’ exists . . . differ[s] depending on the issue involved.” *Id.* at 731-32. In matters involving taxation, the Legislature has broad discretion in making classifications. *Id.* at 732; *see also id.* at 738 (Madsen, J., concurring/dissenting) (same). Thus, “a revenue statute will not be invalidated under article I, section 12 if ‘any state of facts can reasonably be conceived that would sustain the classification.’” *Id.* at 732 (quoting *United Parcel Serv. v. Dep’t of Revenue*, 102 Wn.2d 355, 369, 687 P.2d 186 (1984)). Moreover, the “challenger bears the burden of showing there is no reasonable basis for the questioned classification in a revenue statute,” and “[t]he test is merely whether any state of facts can reasonably be conceived that would sustain the classification.” *United Parcel*, 102 Wn.2d at 369.

In the present case, the sellers seem to suggest that there is no reasonable basis for the distinction in RCW 82.45.030(1) and (2) between the “selling price” used to measure the tax on a conventional sale of Washington real property (i.e., the fair market value of the real property conveyed) and the “selling price” used to measure the tax on the sale of a controlling interest in an entity owning Washington real property (i.e., the fair market value of the Washington real property owned by the entity). But the statute as it pertains to the measure of the real estate excise tax is

entirely reasonable. A transfer of control in an entity that owns Washington real property is equivalent in substance to a transfer of control over the real property owned by the entity. *See* Laws of 1993, 1st Spec. Sess., ch. 25, § 501(1) (legislative finding that “transfers of ownership of entities may be essentially equivalent to the sale of real property held by the entity” and “should be subject to the same excise tax burdens”). Therefore, it is rational that the measure of the tax is essentially the same.

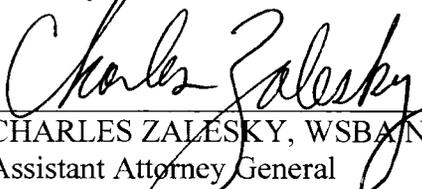
The sellers may object to the real estate excise tax and may believe that the measure of the tax is unfair as applied to them. But the “controlling interest” provisions are rational and do not violate article I, section 12 of the Washington Constitution.

V. CONCLUSION

For the reasons set forth, the Department respectfully requests that the Court affirm the superior court’s order granting the Department’s motion for summary judgment.

RESPECTFULLY SUBMITTED this 19th day of August, 2011.

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I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED this 19th day of August, 2011, at Tumwater, WA.

Carrie A. Parker
Carrie A. Parker, Legal Assistant

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Fifty-Third
Washington State Legislature
1993 Regular Session, First Special Session

ESSB 5966

Protection of the state's investment is perpetuated by using lowest life cycle costing, which is an important factor for determining investment priorities.

The Transportation Commission shall work with affected local jurisdictions to designate a freight and goods system. This statewide system shall include state highways, county roads, and city streets. The commission shall review and make recommendations to the Legislature regarding policies governing weight restrictions and road closures which affect the transportation of freight and goods. The first report is due by December 15, 1993 and biennially thereafter.

Major projects addressing capacity deficiencies which prioritize allowing for preliminary engineering shall be reprioritized during the succeeding biennium, based on updated project data. Reprioritizing projects may be delayed or cancelled by the commission if higher priority projects are awaiting funding.

Major project approvals which significantly increase a project's scope or cost from original prioritization estimates shall include a review of the project's estimated revised priority rank and the level of funding provided. Projects may be delayed or cancelled by the Transportation Commission if higher priority projects are awaiting funding.

Votes on Final Passage:

Senate	48	0	
House	96	0	(House amended)
Senate	47	0	(Senate concurred)

Effective: July 25, 1993

ESSB 5966

C 3 L 93 E1

Concerning the state veterans' homes.

By Senate Committee on Ways & Means (originally sponsored by Senators Rinehart, Haugen and M. Rasmussen; by request of Department of Veterans Affairs)

Senate Committee on Ways & Means

Background: The Department of Veterans Affairs operates two state facilities which provide long-term care for veterans and their spouses: the Soldier's Home at Orting, which has approximately 175 residents; and the Veterans' Home at Retsil, which has 325 residents. Both homes are presently funded with a combination of state general funds, payments from the federal Department of Veterans Affairs, and contributions from the residents' incomes.

Approximately two-thirds of the residents of these homes would be eligible for Medicaid payments if the homes were certified as nursing homes. Both Governor Lowry's budget proposal, and the 1993-95 budget passed by the Senate, assume that parts of both homes will be Medicaid certified by July 1, 1993. This will save about

\$6.5 million of state general funds in 1993-95, through replacement with federal Medicaid payments.

Residents of the two homes are able to retain about \$180 of their monthly income for personal use. All income in excess of \$180 is deposited into a revolving fund, for use on purposes the home's superintendent and resident council determine will benefit the residents.

Under state and federal Medicaid rules, all of a nursing home resident's income in excess of a defined personal needs allowance must be used to offset the cost of his or her nursing home care. Under state and federal regulations, the personal needs allowance is \$90 per month for veterans and about \$43 per month for all other residents in private nursing homes. The Department of Social and Health Services and the Department of Veterans Affairs are attempting to obtain clarification from the federal government regarding which amount would apply for a veteran in a state-operated veterans' facility.

Summary: The Department of Veterans Affairs is authorized to operate nursing care units at the two veterans' homes as Medicaid nursing homes, under contract with the Department of Social and Health Services. Statutory language regarding eligibility for residence in the homes is clarified.

The Department of Social and Health Services and the Department of Veterans Affairs are to seek federal approval to set the personal needs allowance for nursing care residents at \$160 per month. If approval is not granted, the allowance for nursing care residents is \$90.

There is to be an elected residents council at each home to advise the director of Veterans Affairs on all aspects of the home's operation. The council must approve expenditures from the home's benefit fund.

Votes on Final Passage:

Senate	36	9	
House	94	0	(House amended)
Senate			(Senate refused to concur)
House	98	0	(House amended)

First Special Session

Senate	38	8
House	96	1

Effective: July 1, 1993

2ESSB 5967

PARTIAL VETO

C 25 L 93 E1

Increasing state revenues.

By Senate Committee on Ways & Means (originally sponsored by Senator Rinehart; by request of Governor Lowry)

Senate Committee on Ways & Means
House Committee on Revenue

Background: SALES AND USE TAX

The state retail sales tax is imposed on each retail sale of tangible personal property and some services. Taxable services include construction, repair, telephone, and some recreation and amusement services. The tax rate is 6.5 percent and is applied to the selling price of the article or service. The use tax is imposed on the use of tangible personal property when the sale of the property has not been subject to the sales tax. The tax rate is 6.5 percent and is applied to the value of the article used (generally the selling price). The use tax generally applies to purchases made outside the state. In addition, local sales and use taxes also apply.

SALES TAX EXEMPTIONS

Currently sales of feed, seed, seedlings, fertilizer, and spray materials to farmers are exempt from the sales and use tax when the products are used to grow any agricultural product for sale at wholesale.

The sales and use tax does not apply to sales of prescription drugs.

Residents of a state, possession, or Canadian province that does not impose a sales tax of 3 percent or more are exempt from Washington sales tax on purchases in this state of tangible personal property for use outside this state.

SALES TAX DEFERRAL

Current law authorizes the deferral of sales and use tax on plant and equipment investments by manufacturing and research and development firms in distressed counties and by new manufacturers and aluminum firms statewide. These firms are allowed to defer sales and use tax for three years after completion of the project followed by repayment over five years. Sales tax on labor in distressed areas is not repaid. A \$1,000 business and occupation tax credit is available for each new job created above a 15 percent growth rate by manufacturing and research and development firms in distressed areas as an alternative to the deferral program. These programs are due to expire July 1, 1994.

BUSINESS AND OCCUPATION TAX

The business and occupation tax is imposed on the gross receipts of all business activities (other than public utilities) conducted within the state. There are no deductions for the costs of doing business. Although there are 10 separate rates, the three principal rates are:

Manufacturing, wholesaling, & extracting	0.484%
Retailing activities	0.471%
Service activities	1.50%

Magazine and periodical publishing is taxed at a business and occupation tax rate of 0.484.

REAL ESTATE EXCISE TAX

The real estate excise tax applies to sales of real property and is collected when the sale document is recorded with the county. The tax rate is 1.28 percent of the selling price. Most local governments impose an additional rate of 0.25 percent. Additional local options are available.

If real estate is owned by a partnership or corporation, a sale of a controlling interest in the partnership or corpora-

tion can effectively transfer control of real estate without creating tax liability. Many transactions are structured in this manner to avoid real estate excise taxes.

INSURANCE PREPAYMENTS TAXES

Health maintenance organizations, with their own employee medical staff, and health care service contractors without medical staff are subject to the business and occupation tax on their gross income at a rate of 1.5 percent. The health care reform legislation exempts health maintenance organizations and health care service contractors from the business and occupation tax and subjects them to a 2 percent tax on prepayments similar to the insurance premiums tax, effective January 1, 1996.

INSURANCE PREMIUMS TAX CREDIT

The Washington Insurance Guaranty Association Act and the Washington Life and Disability Insurance Guaranty Association Act each created an insurance guaranty association that provides for the payment of claims under policies and contracts of insolvent insurers. Insurance companies that contribute to one of these associations may offset the amount of their contributions against their insurance premium taxes owed to the state over a five-year period.

RESALE CERTIFICATES

Sales for resale are exempt from sales tax if the buyer has a resale certificate. A significant cause of sales tax avoidance is the abuse of resale certificates by persons in business who purchase items for their own use free of tax.

CONTRIBUTIONS IN AID OF CONSTRUCTION

The state subsidizes the capital costs of public entities by allowing a deduction from the business and occupation tax and the public utility tax for income from charges to customers for capital purposes.

Summary: SALES AND USE TAX

State and local retail sales taxes are extended to the sale of selected personal services. Services subject to tax include the use of coin operated laundry facilities in apartment houses, hotels, trailer camps, and tourist camps, landscape maintenance and horticultural services other than horticultural services provided to farmers, service charges associated with tickets to professional sporting events, guided tours and guided charters, physical fitness services, tanning salon services, tattoo parlor services, massage services, steam bath services, turkish bath services, escort services, and dating services. In addition, the rental of equipment with an operator is also subject to sales tax. Because these services are subject to sales tax, the service provider's business and occupation tax will decrease from the services rate of 1.50 percent to the retailer's rate of 0.471 percent.

SALES TAX EXEMPTIONS

The sales tax exemption for sales of feed, seed, seedlings, fertilizer, and spray materials to farmers is expanded to include enhanced pollination agents (bees) and applies whether or not the products are used to grow agricultural products for sale at wholesale.

The sales and use tax exemption for prescription drugs is expanded to include contraceptives.

The nonresident sales tax exemption is limited to residents of a state, possession, or Canadian province that is contiguous to the state of Washington.

SALES TAX DEFERRAL

The state sales tax deferral and business and occupation tax credit programs are extended until July 1, 1998.

Neighborhood reinvestment areas are added to the areas in which sales and use tax deferrals are available under the distressed county deferral program and the business and occupation tax credit program. Neighborhood reinvestment areas are defined as areas that are designated to receive federal, state, or local assistance to increase economic activity, have high unemployment rates, and have a preponderance of low-income households.

Eligibility under the statewide deferral program is expanded to include pulp and paper plants that were in operation before 1960 and located in a county with a population between 40,000 and 70,000.

Eligibility under the business and occupation tax credit program is also expanded to include subcounty areas that are timber distressed areas.

BUSINESS AND OCCUPATION TAX

The business and occupation tax rate on selected business services is increased from 1.5 percent to 2.5 percent, the business and occupation tax rate on banking, loan, security, investment management, investment advisory, or other financial businesses is increased from 1.5 percent to 1.7 percent, and the business and occupation tax rate on all other services is increased from 1.5 percent to 2.0 percent. Services subject to the tax on selected business services include the following:

- Stenographic, secretarial, and clerical services
- Computer services, including computer programming, custom software modification, custom software installation, custom software maintenance, custom software repair, training in the use of custom software, computer systems design, and custom software update services
- Data processing and information services, but excluding information services to the media through an information network
- Legal, arbitration, and mediation services, including paralegal services, legal research services, and court reporting services
- Accounting, auditing, actuarial, bookkeeping, tax preparation, and similar services
- Design services whether or not performed by persons licensed or certified, including engineering services and architectural services
- Business consulting services, including administrative management consulting, general management consulting, human resource consulting or training, management engineering consulting, management information systems consulting, manufacturing management con-

sulting, marketing consulting, operations research consulting, personnel management consulting, physical distribution consulting, site location consulting, economic consulting, motel, hotel, and resort consulting, restaurant consulting, government affairs consulting, and lobbying

- Business management services, including administrative management, business management, and office management, but excluding property management or property leasing, motel, hotel, and resort management, or automobile parking management
- Protective services, including detective agency services and private investigating services, armored car services, guard or protective services, lie detection or polygraph services, and security system, burglar, or fire alarm monitoring and maintenance services
- Public relations or advertising services, including layout, art direction, graphic design, copy writing, mechanical preparation, opinion research, marketing research, marketing, or production supervision, but excluding services provided as part of broadcast or print advertising
- Aerial and land surveying, geological consulting, and real estate appraising

In addition to the permanent tax increases, a 6.5 percent surtax is imposed for four years on all business and occupation tax classifications except selected business services, financial services, and retailing.

The special business and occupation tax rate of 0.484 on magazine and periodical publishers is eliminated.

REAL ESTATE EXCISE TAX

The real estate excise tax is extended to the transfer or acquisition within any twelve-month period of a controlling interest in any entity with an interest in real property in this state. The tax is imposed on the value of the real property transferred.

INSURANCE PREPAYMENTS TAXES

Health maintenance organizations and health care service contractors are exempt from the business and occupation tax and subject to a 2 percent tax on prepayments similar to the insurance premiums tax, effective January 1, 1994, instead of January 1, 1996, and the revenues are deposited into the state general fund for this period.

INSURANCE PREMIUMS TAX CREDIT

Insurers will not be able to claim the insurance premium tax offset for any assessments made by state guaranty associations after April 1, 1993.

RESALE CERTIFICATES

Resale certificates are limited to specific items and are valid for only four years. The abuse of a resale certificate is subject to a penalty of 50 percent of the amount of tax due.

CONTRIBUTIONS IN AID OF CONSTRUCTION

The deduction from the business and occupation tax and the public utility tax for income from charges to customers for capital purposes is eliminated.

MISCELLANEOUS

The State Treasurer, based on information provided by the Department of Revenue, is required to transfer revenues generated under this act during the biennium that exceed the amounts projected to be generated.

Votes on Final Passage:

Senate 25 24
House 50 48 (House amended)

First Special Session

Senate 26 19
House 52 39 (House amended)
Senate (Senate refused to concur)

Conference Committee

House 50 48
Senate 26 22
Effective: May 28, 1993 (Sections 901 & 902)
July 1, 1993
January 1, 1994 (Sections 601-603)

Partial Veto Summary: The following provisions were vetoed: (1) The limit of the nonresident sales tax exemption to residents of a state, possession, or Canadian province that is contiguous to the state of Washington; (2) the expansion of eligibility under the statewide sales tax deferral program to include pulp and paper plants that were in operation before 1960 and that are located in a county with a population between 40,000 and 70,000; and (3) the requirement that the State Treasurer transfer to the budget stabilization account the revenues generated under the act during the biennium that exceed the amounts projected to be generated.

VETO MESSAGE ON 2ESSB 5967

May 28, 1993

To the Honorable President and Members,
The Senate of the State of Washington
Ladies and Gentlemen:

I am returning herewith, without my approval as to sections 306, 405, 406, 407, and 1001, Second Engrossed Substitute Senate Bill No. 5967 entitled:

"AN ACT Relating to taxation;"

Section 306 amends current law which provides a sales tax exemption for property purchased for use outside this state by nonresidents of Washington who live in a state or Canadian province with a sales tax rate of less than three percent by adding the requirement that the beneficiary state be "contiguous to the state of Washington." This would effectively limit the exemption to only Oregon residents.

This amendment presents a constitutional problem, since there does not appear to be a rational basis for distinguishing between residents of noncontiguous states and residents of contiguous states. If a successful class action lawsuit was brought on behalf of all affected parties, the state's costs for administering any payout to members of the class could be substantial.

While I agree that amending current law is necessary, I have vetoed this section because I am concerned with the possible unconstitutionality of this amendment and the consequences of potential lawsuits. Therefore, I will ask the Department of Revenue to develop legislation which addresses the proponents con-

cerns and avoids the constitutional problems for consideration during the 1994 Legislative Session.

Sections 405, 406, and 407 extend the sales and use tax deferral program of chapter 82.61 RCW to include any pulp and paper products plant in operation prior to 1960 and located in a county with a population between 40,000 and 70,000. It was the intent of the sales tax deferral program to encourage new business locations in the state, not to provide a tax break for existing businesses. These sections were not intended to benefit the pulp and paper products industry generally; rather, these criteria were very carefully drawn in order to limit availability of the deferral program to a single taxpayer.

However, the impact could be significantly greater because several taxpayers potentially qualify for the program. Counties that are eligible based on the population range of 40,000 to 70,000 are Chelan, Clallam, Grant, Grays Harbor, Island, Lewis, and Walla Walla. At least four pulp and paper products companies located in these counties were in operation prior to 1960. In addition, there are 21 other pulp and paper products companies that were established prior to 1960; but which are headquartered in non-eligible counties. If any of these 21 other companies also have a plant in an eligible county, they could potentially qualify.

For these reasons, I have vetoed section 405, 406, and 407.

Section 1001 requires the Department of Revenue to determine the amount of revenue generated in excess of projections during the biennium as a result of this act. The State Treasurer would transfer the excess revenue from the general fund to the budget stabilization account. If actual revenue collections exceed the forecast, the Legislature can always choose to make transfers to the budget stabilization account. Therefore, it is not clear why this section is needed.

In addition, this section would require costly and burdensome accounting procedures for the Department of Revenue and would require the department to make unreasonable, and in some cases impossible requests for information from taxpayers. The Department of Revenue already has the capability to measure these and other revenues by other means which are less costly to administer and do not place unreasonable burdens on taxpayers.

For these reasons, I have vetoed section 1001. However, in line with the intent of this section, I am directing the Department of Revenue to report quarterly how well estimates for all of these revenue sources are tracking.

With the exception of sections 306, 405, 406, 407, and 1001, Second Engrossed Substitute Senate Bill No. 5967 is approved.

Respectfully Submitted,

Mike Lowry

Mike Lowry
Governor

SSB 5968

PARTIAL VETO

C 24 L 93 E1

Making appropriations.

By Senate Committee on Ways & Means (originally sponsored by Senators Rinehart and Gaspard; by request of Office of Financial Management)

Senate Committee on Ways & Means
House Committee on Appropriations