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

SCOTT B. OSBORNE, Personal
Representative of the Estate of Barbara Hagyard Mesdag,

Appellant,

v.

THE DEPARTMENT OF REVENUE OF
THE STATE OF WASHINGTON,

Respondent.

BRIEF OF RESPONDENT

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I. INTRODUCTION

The estate of Barbara Mesdag (Estate) litigated and lost its claim for refund of estate tax it paid in 2010. *Osborne v. Dep't of Revenue*, 189 Wn. App. 1029, 2015 WL 4760567 (2015) (unpublished). Although the Estate now concedes that it owed the tax that it previously sought to have refunded, it contends that the interest it paid with respect to that tax should be refunded, and contends that it is entitled to the payment of accrued interest on the tax from the date of payment until the date in June 2013 when the Legislature retroactively amended the estate tax code in response to *In re Estate of Bracken*, 175 Wn.2d 549, 290 P.3d 99 (2012). The Estate's claim for interest is supported by no relevant authority and overlooks key statutory provisions dictating when payment of the estate tax is due and when interest begins to accrue on unpaid tax.

The Estate owed the tax it paid in 2010, as this Court has previously held. And under the plain terms of RCW 83.100.070(1) (imposing interest on the late payment of tax) and RCW 83.100.060(1) (establishing the date tax must be paid), interest on that tax began to accrue from the date the estate tax return was due. Because the Estate did not pay the tax until approximately twenty-two months after its estate tax return was due, it owed the interest it paid in 2010 under the plain language of the Washington estate tax code. Additionally, no authority

authorizes the Department to pay interest on tax the Estate undeniably owes. The Department did not err when it rejected the Estate's claims to the contrary, and its decision should be affirmed.

II. STATEMENT OF THE ISSUES

1. Did the Department correctly reject the Estate's claim for refund of assessed interest it paid in 2010 along with assessed estate tax when there is no dispute that the estate tax was properly due and owing, and the statute imposing interest on the late payment of tax plainly states that interest accrues from the date the decedent's return is due?

2. Did the Department correctly reject the Estate's claim for payment of accrued interest on the estate tax that the Estate paid in 2010 when there is no dispute that the estate tax is properly due and owing and no statute authorizes the Department to pay interest when there has been no overpayment of tax?

III. STATEMENT OF THE CASE

A. **The Estate Claimed a QTIP Deduction in 2008, Which the Department Denied.**

Barbara Mesdag died on July 4, 2007. AR 138. At the time of her death, Ms. Mesdag was a Washington resident with an estate large enough to trigger an obligation to file a Washington estate tax return. That return was initially due on April 4, 2008, nine months after Ms. Mesdag's death. However, the Estate sought and received a six-month extension of time to

file. AR 2. The Estate made an estimated tax payment of \$320,589.14 with its request for extension of time to file its Washington return. *Id.*; *see also* AR 5 (copy of check).

On October 6, 2008, the Estate filed its Washington estate tax return. AR 138; AR 9. On that return, the Estate claimed a deduction for qualified terminable interest property (QTIP) included in its federal taxable estate. AR 138; *see also* AR 9 at Part 2, line 2b (deduction of “§ 2044 Property” totaling \$16,417,504.74).¹ The Washington estate tax due after claiming the deduction, subtracting the prior estimated tax payment, and adding accrued interest was \$49,961.66. AR 8. The Estate remitted payment of that amount with the return. *Id.*; *see also* AR 11 (copy of check).²

The Department reviewed the Estate’s Washington estate tax return and denied the QTIP deduction. AR 138; AR 19. It sent notice to the Estate assessing additional tax and interest in the amount of \$3,103,161.82. AR 19.

¹ QTIP is a life estate set up to take advantage of the marital deduction allowed under federal estate tax law. When a spouse dies, his or her estate can create a QTIP trust that provides income to the surviving spouse for life. The assets contributed to the QTIP trust are deducted from the taxable estate of the spouse who made the election. I.R.C. § 2056(b)(7). However, upon the surviving spouse’s death, the assets remaining in the QTIP trust are included in that spouse’s taxable estate. I.R.C. § 2044.

² Interest in the amount of \$3,268.52 was remitted with the return because the Estate had been granted a six month extension of time to file and the estimated tax payment remitted with its application for extension was less than the tax due per the return. *See* AR 2-3 (application for extension); AR 9 at Part 2, line 12 (interest added on return). That interest payment had nothing to do with the Estate’s 2010 payment of tax and interest on QTIP and, therefore, is not part of the assessed interest the Estate is asking the Department to refund in this appeal.

However, a few months after notifying the Estate of the assessment of unpaid tax and interest, the Department informed the Estate that it would not take any enforcement or collection action “until the Department resolved pending lawsuits against other estates where the same or similar [QTIP] issues were being disputed.” AR 29.

The Estate was dissatisfied with the Department’s decision to refrain from taking enforcement action with respect to the unpaid tax and interest. In order to push the matter forward, the Estate first filed a lawsuit against the Department under the Trust and Estate Dispute Resolution Act (TEDRA) seeking a declaration that it owed no Washington estate tax on the QTIP included in its federal taxable estate. CP 10; *see also* AR 38 (TEDRA petition). The trial court dismissed the Estate’s TEDRA lawsuit in February 2010 for lack of subject matter jurisdiction. CP 10. Shortly thereafter, on February 25, 2010, the Estate paid the assessed tax and interest. AR 54-56. Approximately one month later it filed an amended Washington estate tax return claiming the same QTIP deduction that the Department had previously denied. AR 66.

The Department again denied the deduction and notified the Estate of its agency action. AR 139; AR 87.³ Thereafter the Estate filed a petition for judicial review under the Administrative Procedure Act. AR 139.

B. The Estate Unsuccessfully Litigates the QTIP Issue.

The APA proceedings were stayed pending final resolution of *In re Estate of Bracken*, which involved the same QTIP issue. AR 139. *Bracken* was decided in October 2012. The Supreme Court held that the Legislature did not intend to impose estate tax on QTIP passing at the death of the second spouse. *Bracken*, 175 Wn.2d at 574. After *Bracken* was decided, the Estate moved for judgment on the pleadings, asserting that it was entitled as a matter of law to the tax refund it was seeking. AR 139. The trial court granted the Estate's motion, and the Department appealed. *Id.*

In June 2013, while the appeal was pending, the Legislature amended the estate tax code in response to *Bracken*. AR 140. Several estates, including the Mesdag Estate, challenged the 2013 Act. The Supreme Court consolidated for argument two of those appeals. *See In re Estate of Hambleton*, 181 Wn.2d 802, 815-16, 335 P.3d 398 (2014), *cert. denied* 136 S. Ct. 318 (2015). The Supreme Court rejected all of the estates' arguments and held that the 2013 Act was a constitutionally valid

³ The Department granted the Estate's request for refund on an issue unrelated to the deduction of QTIP passing at the death of Ms. Mesdag. AR 87. However, it denied the Estate's refund claim with respect to the QTIP issue.

exercise of the Legislature’s authority to enact and amend the tax laws of this state. *Id.* at 836.

After *Hambleton* was decided, the Estate filed a supplemental brief with this Court arguing that *Hambleton* did not fully resolve its appeal.

AR 95. The Estate claimed that it was entitled to the estate tax refund it was seeking because “the Estate’s judgment was final” at the time it was entered by the trial court and not subject to appeal, and that even if it owed the underlying estate tax in dispute it was entitled to a refund of interest.

AR 107. The Court rejected the Estate’s claim that the trial court’s order was final at the time it was entered, holding that the Department filed a proper appeal and observing that the Estate cited no persuasive authority supporting its claim to the contrary. AR 141-44. By contrast, the Court did not address the merits of the Estate’s “interest” argument. Instead, it ordered that the issue be remanded to the Department for determination pursuant to RCW 34.05.554(2). AR 146.

C. The Department Rejects the Estate’s Claim for Refund of Interest, and the Trial Court Affirms.

On remand to the Department, the Estate argued that the Department had illegally collected an “interest penalty” from the Estate in 2010 when the Estate paid the disputed tax assessment, and “illegally took” and retained that payment during the period in which the

Department “was obligated under *Bracken* to refund the contested amounts paid by the Estate.” AR 134. The Department denied the Estate’s interest refund claim by letter decision issued July 13, 2016. AR 169. The Department explained that interest imposed under the estate tax code was not a penalty, and that the estate tax refund statute, RCW 83.100.130, permitted a refund of interest only in connection with the refund of an overpayment of tax. AR 169-71. “Since there was no overpayment of tax by the Estate, no interest is due.” AR 171.

The Estate timely appealed the Department’s letter decision, seeking judicial review under the APA. CP 4. The trial court, after considering arguments from the parties, rejected the Estate’s refund claim and affirmed the Department’s letter decision. CP 85. This appeal followed. CP 87.

IV. ARGUMENT

A. Standard of Review.

This is an appeal of final agency action under the Administrative Procedure Act. The agency action at issue is the Department’s denial of the Estate’s refund claim. “On review of an agency decision, this court ‘sits in the same position as the superior court’ and applies the standards of the APA to the record before the agency.” *Purse Seine Vessel Owners Ass’n v. State*, 92 Wn. App. 381, 388, 966 P.2d 928 (1998) (quoting *Tapper v.*

Employment Sec. Dep't, 122 Wn.2d 397, 402, 858 P.2d 494 (1993)). The Estate, as the party challenging the Department's action, bears the burden of demonstrating that the action is invalid. RCW 34.05.570(1)(a); *Hillis v. Dep't of Ecology*, 131 Wn.2d 373, 381, 932 P.2d 139 (1997).

Because this appeal involves "other agency action," judicial review is governed by RCW 34.05.570(4). In the context of other agency action, the Court may grant relief only if it determines the action was unconstitutional, outside the agency's statutory authority, arbitrary or capricious, or taken by a person who was not lawfully entitled to take the action. RCW 34.05.570(4)(c). The Estate asserts only that the Department's decision was contrary to law and, therefore, outside its statutory authority. The Court reviews an agency's legal conclusions under the error of law standard. *Beatty v. Fish & Wildlife Comm'n*, 185 Wn. App. 426, 443, 341 P.3d 291, *review denied*, 183 Wn.2d 1004 (2015). Under the error of law standard, a court may substitute its own judgment for that of the agency, although it must give "substantial weight to the agency's view of the law it administers." *Id.*

B. The Department Correctly Rejected the Estate's Claim for Refund of Assessed Interest.

The first issue the Estate raises involves interest that it paid in 2010 prior to filing its amended Washington estate tax return. That interest

(hereinafter the “assessed interest”) totaled \$307,668.63.⁴ The Estate contends that the Department lacked statutory authority to “collect” the assessed interest. App. Br. at 6-9. It makes this argument even though it is undisputed that the Estate owed Washington estate tax on the QTIP and did not pay that tax until February 2010, twenty-two months after payment was due.

1. The Estate owed the assessed interest under the plain language of the Washington estate tax code.

Interest is imposed under the Washington estate tax code pursuant to RCW 83.100.070. That code section mandates that “any tax due under this chapter which is not paid by the due date under RCW 83.100.060(1) shall bear interest . . . from the date the tax is due until the date of payment.” RCW 83.100.070(1). Tax due under the estate tax code “shall be paid by the person required to file a Washington return on or before the date the Washington return is required to be filed . . . , not including any extension-of time for filing.” RCW 83.100.060(1). A Washington estate tax return is required to be filed nine months after the date of the decedent’s death. WAC 458-57-135(3)(a).

⁴ The “assessed interest” paid in 2010 is computed as follows:

• Total interest paid by the Estate (<i>see</i> AR 90)	\$310,937.15
• Less interest paid in 2008 unrelated to QTIP (<i>see</i> AR 9)	<u>\$(3,268.52)</u>
• Interest paid in 2010 with respect to QTIP deduction	<u>\$307,668.63</u>

Applying the plain language of RCW 83.100.070(1), RCW 83.100.060(1), and WAC 458-57-135(3)(a), the Estate clearly owed interest on its late payment of estate tax. This Court has already held in its prior unpublished opinion that estate tax is due on QTIP passing at Ms. Mesdag's death. AR 145 (Slip op., p. 9). And that tax was not paid by April 4, 2008—the date the Estate's Washington return was required to be filed without regarding any extension.⁵ Because tax due under the estate tax code was not paid by the due date under RCW 83.100.060(1), that tax “shall bear interest” from the due date until it is paid. The Legislature has provided no exception for tax due resulting from a retroactive change to the estate tax code or any other unusual circumstance. Thus, the Estate's claim for interest in this “unusual case” fails. *See* App. Br. at 16 (referring to this appeal as “an unusual case”); *cf.*, *Rufer v. Abbott Labs*, 154 W.2d 530, 553, 114 P.3d 1182 (2005) (statute awarding postjudgment interest mandates that interest accrues from the date of entry of the judgement and “provides no exception for delays, unreasonable or otherwise”).

⁵ The Estate incorrectly asserts that the due date for payment of the Washington tax was October 4, 2008. App. Br. at 8. The Estate confuses the date it filed its return with the due date for payment of the tax. Under RCW 83.100.050(2)(a), a person required to file a Washington return can obtain an extension of time to file. The Estate sought and received a six-month extension of time to file, extending the due date for its return from April 4, 2008, to October 4, 2008. AR 2-3. However, under RCW 83.100.060(1), payment of the tax is due when the return is due “not including any extension of time for filing.” Consequently, the Estate's six-month extension of time to file its Washington return did not extend the time for payment of the tax. That is why the Estate included payment of interest with its Washington return. *See* footnote 2, *supra*.

The statutes imposing interest and establishing the due date for payment of the tax are not ambiguous and demonstrate the Legislature's intent to impose interest whenever estate tax is not paid by the statutory due date. Because there is no ambiguity in the language used by the Legislature, that plain language controls. *Cerrillo v. Esparza*, 158 Wn.2d 194, 205-06, 142 P.3d 155 (2006); *Rozner v. City of Bellevue*, 116 Wn.2d 342, 347, 804 P.2d 24 (1991).

The Estate contends, however, that no tax was actually "due" on QTIP until June 2013 as a result of the *Bracken* decision. App. Br. at 9. There are two flaws with the Estate's argument. First, *Bracken* did not involve RCW 83.100.070(1) or RCW 83.100.060(1). Thus, that decision did not modify the statute's plain requirement that interest is computed from the date the Washington return is required to be filed without regard to any extension of time for filing. Consequently, it does not matter precisely when the tax on QTIP became "due" under the Washington estate tax chapter. The fact that it is due and was not paid by the required due date triggers the imposition of interest. Accordingly, the Estate's refund claim should be rejected because it is inconsistent with the plain language of the statutes imposing interest on the late payment of estate tax. *See generally, Priess v. United States*, 42 F. Supp. 89, 91 (E.D. Wash. 1941) (court declined to "disregard the provisions of" interest imposing

statute that did not make an exception for the taxpayer's specific and unusual circumstances).

Second, as discussed in greater detail below, the Estate's reliance on *Bracken* is misplaced. That decision was the controlling law in this state for only a few short months before it was repudiated and replaced by retroactive legislation enacted in 2013. Under that retroactive legislation, the Estate was not entitled to deduct QTIP on its Washington return and should have paid the tax when it was due in order to avoid interest on the underpayment.

2. The short-lived retroactive effect of *Bracken* does not control over the 2013 legislation repudiating *Bracken*.

Bracken involved a challenge to the measure of the Washington "stand-alone" estate tax. That tax was enacted in 2005 in response to a dramatic change in the federal estate tax code that seriously eroded the effectiveness of the state's prior "pick-up" estate tax system. Laws of 2005, ch. 516; see generally *In re Estate of Ackerley*, 187 Wn.2d 906, 910, 389 P.3d 583 (2017) (discussing the history of Washington's stand-alone estate tax). The stand-alone tax was measured by an estate's "Washington taxable estate," which was defined as the "federal taxable estate" less certain adjustments. Laws of 2005, ch. 516, § 2(13). By using the federal taxable estate as the starting point for computing the Washington tax, the

state “avoided having to duplicate congressional effort involved in explaining all the possible inclusions, exemptions, and deductions necessary to reach the taxable estate, and also helped to avoid the complication and confusion that a different set of state rules might create.” *Bracken*, 175 Wn.2d at 583 (Madsen, C.J., concurring and dissenting).

Shortly after the Legislature enacted the stand-alone estate tax, the estates of Sharon Bracken and Barbara Nelson filed TEDRA lawsuits in King County seeking to exclude from their respective Washington taxable estates the value of QTIP included in their federal taxable estates under I.R.C. § 2044. After the lawsuits were consolidated, the trial court entered summary judgment in favor of the Department, rejecting the estates’ claim. *Bracken*, 175 Wn.2d at 562.

The Supreme Court reversed. It held that no actual “transfer” of QTIP occurs within the meaning Washington’s estate tax code when the spouse who received the terminable interest property died and the QTIP assets passed to the remainder beneficiaries. *Id.* at 575-76.⁶ The Court reasoned that I.R.C. § 2044—the federal statute requiring QTIP to be

⁶ The stand-alone estate tax applies to the “transfer” of property located in Washington at death. RCW 83.100.040(1). When initially enacted, the tax code defined a “transfer” as a “transfer” as used in section 2001 of the Internal Revenue Code.” RCW 83.100.020(11) (2006). There was no dispute in *Bracken* that the death of the second spouse resulted in a “transfer” of QTIP under section 2001 of the federal estate tax code. Rather, the issue in *Bracken* was whether there was a “transfer” within the meaning of the Washington estate tax code.

included in the taxable estate of the spouse who received the terminable interest property—created only a “deemed” transfer and was insufficient to sanction the Washington tax, which only applied to “real” transfers. *Id.* at 570-71, 573; *see also Hambleton*, 181 Wn.2d at 812 (summarizing the holding in *Bracken*). From this initial premise, the Court concluded that “the federal definition of ‘taxable estate’ cannot be used” as the starting point for computing the Washington tax “without a modification necessary to conform to the [Washington estate tax code]: the definition must be read to exclude items that are not [real] transfers.” *Bracken*, 175 Wn.2d at 570-71. As a result of that modification, QTIP included in computing the federal estate tax of a decedent was entirely excluded from the measure of the Washington tax.

The Supreme Court’s narrow interpretation of the Washington estate tax code, distinguishing between “deemed” and “real” transfers of property at death, applied retroactively. *See McDevitt v. Harbor View Medical Center*, 179 Wn.2d 59, 75, 316 P.3d 469 (2013) (“in Washington, a new decision of law generally applies retroactively”); *cf., Harper v. Virginia Dep’t of Taxation*, 509 U.S. 86, 97, 113 S. Ct. 2510, 125 L. Ed. 2d 74 (1993) (federal court decisions always operate retroactively).⁷ It

⁷ Our Supreme Court has not yet abolished the concept of “purely prospective” application of its decisions as the U.S. Supreme Court did in *Harper* with respect to federal court decisions. *See Lunsford v. Saberhagen Holdings, Inc.*, 166 Wn.2d 264, 278,

thus allowed estates of decedents dying on or after May 17, 2005 (the date the stand-alone estate tax was enacted), to exclude from the Washington tax the “deemed” transfer of QTIP occurring when the second spouse died and the QTIP assets passed to the remainder beneficiaries.

Within months, the Legislature closed this unexpected tax loophole by amending the Washington estate tax to make clear that the tax *does* apply to QTIP passing at the death of the second spouse. *See* Laws of 2013, 2d Spec. Sess., ch. 2. The intended purpose of the legislation was “to reinstate the legislature’s intended meaning when it enacted the estate tax, restore parity between married couples and unmarried individuals, restore parity between QTIP property and other property eligible for the marital deduction, and prevent the adverse fiscal impacts of the *Bracken* decision.” *Id.* at § 1(5). The 2013 amendment applied retroactively to “all estates of decedents dying on or after May 17, 2005.” *Id.* at § 9.

It is true that for a short period of time, between the date *Bracken* was issued in late 2012 and the date the 2013 amendment was signed into law, the Estate owed no Washington estate tax on QTIP. But the Estate is not seeking a refund of interest for that short period when *Bracken* was the

208 P.3d 1092 (2009). Nevertheless, retroactive application is “overwhelmingly the norm.” *Id.* at 270 (quoting *Robinson v. City of Seattle*, 119 Wn.2d 34, 74, 830 P.2d 318 (1992)). Washington court decisions operate retroactively “unless we expressly limit our decision to purely prospective application.” *Id.* at 285. *Bracken* was not expressly limited to a purely prospective application and, therefore, applied retroactively.

controlling law.⁸ Instead, by seeking a refund of interest assessed from April 4, 2008 through February 25, 2010, the Estate seeks to retain the benefit of retroactive application of *Bracken* while rejecting retroactive application of the 2013 amendment repudiating *Bracken*. But *Bracken* does not have “super” retroactive effect that cannot be overcome by subsequent retroactive legislation.

Moreover, our Supreme Court in *Hambleton* expressly rejected the notion that *Bracken* was immune from subsequent retroactive legislation. *See Hambleton*, 181 Wn.2d at 817 (“We hold that the legislature did not intrude on judicial power when it retroactively amended the Estate and Transfer Tax Act”). Thus, retroactive application of *Bracken* is no longer controlling with respect to *whether* estate tax is due under the Washington estate tax chapter. And *Bracken* has never been controlling with respect to *when* that tax is due. Rather, under the controlling law, the Estate unquestionably owed Washington estate tax on QTIP included in its federal taxable estate and was required under RCW 83.100.060(1) to pay that tax on or before April 4, 2008. Having failed to pay the tax until February 25, 2010, it owed the assessed interest that it paid with that tax and has no legal right to a refund. Accordingly, the Department’s decision

⁸ No interest has been assessed for that short period of time because the Estate had already paid the tax before *Bracken* was decided.

denying the Estate's refund claim was correct as a matter of law and should be affirmed.

3. The Department's decision denying the Estate's refund claim is consistent with persuasive federal authority.

Although not necessary to decide this appeal, it is worth pointing out that persuasive federal authority supports the Department's decision to reject the Estate's refund claim. That authority addresses liability for interest resulting from a retroactive amendment to the tax code regarding both refunds to taxpayers and assessments of additional tax owed.

Federal courts have long taken the position that interest is owed on a retroactive change to the tax code absent express legislation to the contrary. In *Siegel v. United States*, 84 Ct. Cl. 551, 18 F. Supp. 771 (Ct. Cl. 1937), the federal Court of Claims explained that where retroactive tax statutes are enacted that result in an overpayment of tax, but are silent as to interest, the government must pay statutory interest on the refund from the date of payment of the tax even though it was not required to refund the tax until much later. 18 F. Supp. at 775-76. The same general rule of law applies to tax assessments. See *Morton-Norwich Products, Inc. v. United States*, 221 Ct. Cl. 83, 602 F.2d 270, 272 (Ct. Cl. 1979) (taxpayer owed interest "from the time the original return was due" even though pertinent Treasury regulations were applied retroactively for the first three

years of the audit period); *Priess*, 42 F. Supp. at 91 (taxpayer owed interest on assessed tax resulting from federal taxing agency's newly adopted interpretation of federal tax statute). When a retroactive change to a law results in an overpayment or underpayment of tax, the "principal" tax amount is either held by the government prior to refund to the taxpayer or held by the taxpayer prior to payment to the government. In either circumstance, it is appropriate to impose interest on the party that had the use of the tax amount prior to its lawful refund or payment. *See generally*, *Brown & Williamson, Ltd. v. United States*, 231 Ct. Cl. 413, 688 F.2d 747, 750 (Ct. Cl. 1982) (noting that the U.S. Supreme Court "has stressed the importance of symmetry in the payment of interest") (citing *United States v. Koppers Co.*, 348 U.S. 254, 267, 75 S. Ct. 268, 99 L. Ed. 302 (1955) and *Manning v. Seeley Tube & Box Co.*, 338 U.S. 561, 568, 70 S. Ct. 386, 94 L. Ed. 346 (1950)).

The general rule that interest is owed on a retroactive change to the tax code is rooted in well-established constitutional law. In 1902 the United States Supreme Court held that there is no due process prohibition against imposing interest that arises as a result of a retroactive amendment to the procedures pertaining to the collection of delinquent taxes. *League v. State of Texas*, 184 U.S. 156, 161, 22 S. Ct. 475, 46 L. Ed. 478 (1902).

League involved a retroactive Texas law permitting the collection of property tax through judicial proceedings. *Id.* at 157. In rejecting the taxpayer's claim that interest could not be imposed under the retroactive law, the Court explained that "there exists a general power in the state governments to enact retrospective or retroactive laws" so long as the state law is not "technically *ex post facto*, or such as [to] impair the obligation of contracts." *Id.* at 161. The due process guarantee provided under the 14th Amendment "contains no prohibition of retrospective legislation as such." Thus, a state may, consistent with due process principles, enact retroactive legislation providing that "taxes which have already become delinquent shall bear interest from the time the delinquency commenced. This is adding no novel or extraordinary penalty, for interest is the ordinary incident of the nonpayment of obligations." *Id.* at 162.

League involved a retroactive amendment to the procedures for collecting delinquent taxes. This appeal involves a retroactive amendment to a substantive tax statute in order to reinstate the Legislature's original intent to tax QTIP at the death of the second spouse. But this distinction between a procedural tax statute and a substantive tax statute is of no constitutional significance. In either case, the general rule applied by federal courts is that interest is owed on the resulting tax deficiency unless there is clear evidence of a different legislative intent. This federal

authority is added support for the Department's decision to deny the Estate's refund claim.

4. Application of the plain language of the estate tax code does not raise "constitutional problems."

In its opening brief, the Estate suggests that the Court should construe "the statutes at issue" in its favor in order to avoid "manifest constitutional problems." App. Br. at 11. The Estate tosses out two constitutional arguments. First, it asserts that "[u]nder procedural due process principles, taxpayers must be provided a 'clear and certain' remedy for the illegal imposition of taxes." *Id.* (citing *Reich v. Collins*, 513 U.S. 106, 115 S. Ct. 547, 130 L. Ed. 2d 454 (1994) and *Newsweek, Inc. v. Florida Dep't of Revenue*, 522 U.S. 442, 118 S. Ct. 904, 139 L. Ed. 2d 888 (1998)). Next, it asserts that "[i]t is a violation of a person's due process rights to have to pay an illegal tax." *Id.* (citing *Sintra v. City of Seattle*, 119 Wn.2d 1, 829 P.2d 765 (1992) and *Patel v. City of San Bernadino*, 310 F.3d 1138 (9th Cir. 2002)). Both arguments are premised on the Estate's erroneous contention that the tax it paid on QTIP was "illegal." But this Court has already held that the tax was lawfully owed. AR 145. Additionally, our Supreme Court in *Hambleton* held that the Legislature acted within its proper sphere of authority when it retroactively amended the estate tax code in response to the unexpected

fiscal and tax policy impact of *Bracken*. Finally, there was certainly nothing “illegal” about the Department accepting the Estate’s payment of tax and interest in February 2010 as a precondition to the Estate filing suit under the APA to challenge the tax. Thus, there is no merit to the Estate’s premise that it was forced to pay an “illegal” tax.

Additionally, the Estate’s concern over “manifest constitutional problems” is unsupported by the cases it cites. *Sintra* and *Patel* involved claims for damages stemming from alleged violations of the plaintiffs’ civil rights. *Sintra*, 119 Wn.2d at 10; *Patel*, 310 F.3d at 1140. In this appeal, the Estate has not alleged a violation of a substantive due process right. *See* CP 87 (Notice of Appeal). Thus, its citations to *Sintra* and *Patel* are meaningless. There is no legal or logical reason to construe the estate tax code in favor of one party or the other based on constitutional claims that have not been alleged and are not in dispute.

The Estate’s citation to *Reich* and *Newsweek* are also unhelpful to its statutory construction argument. *Reich* and *Newsweek* stand for the proposition that the Due Process Clause of the United States Constitution prevents a state from offering a clear remedy to contest a tax obligation and then “reconfiguring” the remedial provision in a manner to thwart a meritorious challenge to the tax. Our Supreme Court discusses both cases in some detail in *W.R. Grace & Co. v. Department of Revenue*, 137 Wn.2d

580, 973 P.2d 1011 (1999). *See* 137 Wn.2d at 598-99. Neither case has any impact on this APA appeal.

In *Reich*, a Georgia statute offered the taxpayer a clear and certain post-deprivation remedy (i.e., a refund) if it prevailed in its constitutional challenge to a Georgia tax. After the taxpayers relied on the availability of the post-deprivation remedy, paid the tax, and prevailed on the merits, the state nonetheless denied the refund because the taxpayer had an available pre-deprivation remedy that it chose not to use. *Reich*, 513 U.S. at 110. The Supreme Court reversed, holding that the state's offer of a clear post-deprivation remedy could not be rescinded once a taxpayer has relied on the availability of that procedure. *Id.* at 111. The Court first noted that the States were free to establish and reconfigure the "remedial scheme" by which they permitted a taxpayer to challenge a state tax. "Such choices are generally a matter only of state law." *Id.* "But what a State may not do, and what Georgia did here, is to reconfigure its scheme, unfairly, in midcourse—to 'bait and switch,' as some have described it." *Id.*

Newsweek involved facts similar to *Reich* and echoes the holding in that case. Because Florida offered the taxpayer a clear and certain post-deprivation process "to adjudicate the merits of its claim," the state could not later deny the right to a refund where the taxpayer prevailed on the merits. *Newsweek*, 522 U.S. at 455.

The procedural due process issue addressed in *Reich* and *Newsweek*—the availability of a “clear and certain” remedial scheme by which to challenge a tax—is not an issue in this case. Washington offers a clear and certain post-deprivation remedy for estates to challenge the legality of the estate tax. Specifically, RCW 83.100.130(1) permits an estate that has paid estate tax that it believes is not lawfully owed to seek a refund of the tax through an application filed with the Department. If an estate is dissatisfied with the Department’s decision pertaining to its application for refund, it can seek judicial review under the Administrative Procedure Act. That is precisely what the Mesdag Estate has done here. The state did not “bait” the Estate into seeking a post-deprivation remedy only to cut off the right by “reconfiguring” its remedial scheme.

Additionally, procedural due process does not require the taxing authority to grant an otherwise unmeritorious refund claim. *See Montana Rail Link, Inc. v. United States*, 76 F.3d 991, 994-95 (9th Cir. 1996) (rejecting argument that *Reich* required a finding that retroactive tax statute violates due process). It requires only a meaningful opportunity to contest the validity of the tax and the right to a refund or other appropriate relief should the challenge succeed. *W.R. Grace*, 137 Wn.2d at 599. Had the tax the Estate paid on the value of QTIP been “illegal,” the Estate would have been entitled to a refund of that tax plus statutory interest

under the established refund mechanism provided in the estate tax code. The fact that the estate tax code allows for a refund of taxes that are not legally owed provides a “clear and certain” remedy under established due process principles. *Id.*

Fairly applying the unambiguous language of RCW 83.100.070(1), which imposes interest on unpaid estate tax due under the estate tax code, and RCW 83.100.060(1), which establishes the date interest begins to accrue, does not raise “constitutional problems.” The Estate’s claim to the contrary is supported by no cogent legal analysis and, in light of *Montana Rail Link* and *W.R. Grace*, is plainly wrong.

5. The interest imposed under the estate tax code is not a penalty.

The Estate contends that the assessed interest it paid on QTIP passing at the death of Ms. Mesdag “is a retroactive penalty.” App. Br. at 13. But it provides no meaningful analysis supporting its claim. Instead, the Estate argues that the issue has already been decided in prior cases, namely *Department of Revenue v. Estate of Pohelmann*, 63 Wn. App. 263, 818 P.2d 616 (1991), and *In re Elvigen’s Estate*, 191 Wash. 614, 71 P.2d 672 (1937). App. Br. at 14. However, neither case supports the Estate’s claim. Furthermore, the interest imposed under RCW 83.100.070(1) is not a penalty under established criteria that the Estate neglects to discuss.

a. The Estate's reliance on *Pohelmann* and *Elvigen's Estate* is misplaced.

Pohelmann did not involve RCW 83.100.070(1) and contains no analysis suggesting that interest imposed under that provision is, in fact, a civil penalty. Rather, *Pohelmann* involved a statute imposing a five percent per month penalty on the late filing of an estate tax return. *See* 63 Wn. App. at 264 (quoting former RCW 83.100.070(2)) (now codified at RCW 83.100.070(3)(b)). At the time *Pohelmann* was decided, the statute contained no provision permitting the penalty to be waived. *Id.* The issue the Court addressed was whether the late-filing penalty assessed against the *Pohelmann* estate was actually due in light of the fact that a similar federal penalty had been waived by the IRS. *Id.* The Court rejected the estate's claim that the Washington penalty was not owed, explaining that the unambiguous language of the state statute did not support the claim. *Id.* at 265.⁹ The Court never addressed RCW 83.100.070(1) or whether interest imposed under that statute is a penalty. The Estate has simply misread the case.

Elvigen's Estate is also unhelpful. That case involved a statute imposing interest on the underpayment of inheritance tax. *Elvigen's Estate*, 191 Wash. at 621 (quoting Rem. Rev. Stat. § 11210). For reasons

⁹ The statute was amended in 1997 to permit the Department to waive the penalty in certain circumstances. *See* Laws of 1997, ch. 136, § 1; RCW 83.100.070(3)(c).

that are not clear from the decision, the Court used the ambiguous phrase “interest penalty” to refer to the amount imposed under the statute. *Id.* at 622.¹⁰ The Court made no effort to distinguish whether the charge was interest or, instead, was a penalty. That distinction made no difference to the issue being litigated. If it had made a difference, based on the language of the statute quoted in the decision, the charge appears to be interest. The statute provided in relevant part that if the inheritance tax was not paid within fifteen months from the date it was due, “interest shall be charged and collected at the rate of eight per centum per annum unless by reason of necessary litigation such tax cannot be determined and paid as herein provided, in which case interest” begins to run from the date the “cause of such delay is removed.” *Id.* at 621. The charge was referred to as interest in the statute, and there is nothing about the statutory language to suggest that it was actually a penalty.

In any event, the ambiguous term “interest penalty” as used in *Elvigen’s Estate* does not establish that the charge imposed under the current Washington estate tax code is a penalty. The Estate simply asserts a proposition that is unsupported by *Elvigen’s Estate* or any other authority.

¹⁰ The Supreme Court never referred to the charge strictly as a “penalty.” It either referred to the charge as interest or as an “interest penalty.” *Elvigen’s Estate*, 191 Wash. at 621-24.

b. Under established criteria, RCW 83.100.070(1) imposes *interest* on the late payment of tax, not a penalty.

Whether interest imposed under a tax statute is, in fact, a penalty is primarily a question of legislative intent. *United States v. Childs*, 266 U.S. 304, 309, 45 S. Ct. 110, 69 L. Ed. 299 (1924). “A penalty is a means of punishment; interest a means of compensation.” *Id.* at 307. In addressing whether a charge is interest intended as a means of compensation or a penalty designed to punish, courts start from the proposition that when the legislative branch declares a charge to be “interest,” that designation controls absent evidence to the contrary. *See, e.g., In re Beardsley & Wolcott Mfg. Co.*, 82 F.2d 239, 240 (2d Cir. 1936) (“The items claimed as ‘interest’ are sought to be recovered under a statute which denominates them interest. While nomenclature is not conclusive, it is [of] probative force, particularly when the rate . . . is below the statutory [usury] limitation”).

The Estate makes no effort to establish that interest imposed under RCW 83.100.070(1) is, in fact, a civil penalty designed to punish those who fail to timely pay their taxes. It relies instead on its assertion that the issue has already been decided by our Supreme Court, which is not true. As a result, the Estate has not overcome the presumption that the “interest” charge imposed under RCW 83.100.070(1) is interest. The

Estate's claim can be denied for this reason alone. *See Cook v. Brateng*, 158 Wn. App. 777, 794, 262 P.3d 1228 (2010) (“Appellate courts need not consider arguments that are unsupported by pertinent authority, references to the record, or meaningful analysis”).

In any event, there is no justification from the plain language of the estate tax code for treating the amount charged under RCW 83.100.070(1) as anything other than interest. The charge is designated as “interest” in the statute, which is a strong indication of legislative intent. *In re Beardsley*, 82 F.2d at 240. In addition, the amount payable depends on the lapse of time between the date the tax payment was due and the date it was paid, and is computed based on the same rate used to compute interest under the state's excise tax laws. *See* RCW 83.100.070(2) (incorporating by reference RCW 82.32.050(2), which establishes the rate of interest for late payment of excise taxes). Thus, the charge imposed under RCW 83.100.070(1) is time-based and rate-based, which are hallmarks of interest. *Unemployment Reserves Comm'n of California v. Meilink*, 116 F.2d 330, 335 (9th Cir. 1940), *aff'd* 314 U.S. 564 (1942).

As noted above, interest is imposed under the estate tax code at the same rate that applies to excise taxes. RCW 83.100.070(2). That rate is determined annually from “an average of the federal short-term rate as defined in 26 U.S.C. § 1274(d) plus two percentage points.” RCW

82.32.050(2). As relevant here, the interest rate computed under RCW 82.32.050(2) fell from seven percent per annum in 2008 to three percent in 2010. See <https://dor.wa.gov/sites/default/files/legacy/Docs/Reports/InterstRatesExciseTx.pdf> (Department Research Report # 2017-3 listing historical interest rates computed under RCW 82.32.050(2)). Thus, the rate used to compute interest on delinquent tax payments is not excessive and is another indication that the charge is intended to compensate the State at a fair rate of return, not to punish recalcitrant taxpayers.

Finally, the estate tax code already contains an express “penalty” provision, RCW 83.100.070(3)(b). Thus, the Legislature understands how to enact a civil penalty pertaining to the late payment of estate taxes. The fact that the Legislature has created both an “interest” charge and a distinct “penalty” charge is further evidence of its intent to impose interest under the provision it labeled as “interest.” See *Childs*, 266 U.S. at 309-10 (fact that income tax code included both an interest charge and a penalty charge established that interest was “clearly intended to compensate the delay in payment of the tax” and not to punish); *Meilink v. Unemployment Reserves Comm’n of California*, 314 U.S. 564, 570, 62 S. Ct. 389, 86 L. Ed. 458 (1942) (same with respect to state unemployment tax statute, citing *Childs*); *Priess*, 42 F. Supp. at 90 (fact that Congress included penalty provisions “apart from the interest on deficiency section” of the

tax code established “[t]he legislative intent to distinguish between penalty and interest”).

Applying established criteria for distinguishing between interest and penalty, the amount charged under RCW 83.100.070(1) is clearly interest. For this additional reason, the Estate’s claim for a refund of interest it paid in 2010 should be denied.

C. The Department Correctly Rejected the Estate’s Claim for Payment of Accrued Interest.

In addition to seeking a refund of the interest the Estate paid in 2010 when it paid the assessed estate tax, the Estate also claims that the Department should be ordered to pay interest on the assessed estate tax from the date of payment until the date the Legislature retroactively amended the estate tax code to close the *Bracken* loophole. App. Br. at 15. That interest (hereinafter the “accrued interest”), if it were lawfully owed, would total roughly \$249,119.¹¹ However, the Department correctly rejected the Estate’s claim because no statute authorizes the payment the Estate is seeking.

¹¹ The “accrued interest” is computed as follows:

- 2010: $(\$2,953,186.56 \times .03) \times 308/365 = \$74,760.12$
- 2011: $(\$2,953,186.56 \times .03) \times 365/365 = \$88,595.60$
- 2012: $(\$2,953,186.56 \times .02) \times 366/366 = \$59,063.73$
- 2013: $(\$2,953,186.56 \times .02) \times 165/365 = \underline{\$26,700.04}$
- Total \$249,119.49

“As a general principle, under the doctrine of sovereign immunity, the State is not liable for interest on its obligations unless it has placed itself expressly, or by reasonable construction of a contract or statute, in a position of attendant liability.” *Union Elevator & Warehouse Co. v. State ex rel. Dep’t of Transp.*, 171 Wn.2d 54, 59, 248 P.3d 83 (2011); *see also Architectural Woods, Inc. v. State*, 92 Wn.2d 521, 526, 598 P.2d 1372 (1979) (the state without its consent cannot be held to interest on its debts). Consequently, the Estate is entitled to the accrued interest only if there is clear statutory authority for the award of interest.

The Estate relies on RCW 83.100.130(1), which is the statute allowing the Department to refund an overpayment of estate tax “together with interest.” App. Br. at 15. But the Estate has not overpaid its estate tax, as this Court has already held. Consequently, the estate is not entitled to interest.¹²

Moreover, the plain language of the tax refund statute when read as a whole and in context does not support the Estate’s claim that interest must be paid even when there is no established overpayment of tax. RCW 83.100.130(1) provides in relevant part:

¹² To the extent the Estate’s claim for accrued interest is based on *Bracken*, the Department had no obligation to issue a refund of taxes that it was properly disputing through judicial proceedings. Until litigation pertaining to a challenged tax becomes final, there is no established overpayment. Here, the final result of the prior litigation is that the Estate did not overpay its taxes.

If, upon receipt of an application by a taxpayer for a refund, or upon examination of the returns or records of any taxpayer, the department determines that within the statutory period for assessment of taxes, penalties, or interest prescribed by RCW 83.100.095 a person required to file the Washington return under RCW 83.100.050 has overpaid the tax due under this chapter, the department shall refund the amount of the overpayment, together with interest as provided in subsection (2) of this section.

Id. (emphasis added). The statute provides a classic “if-then” statement. If an estate has “overpaid the tax due under this chapter,” the Department is then obligated to refund that tax “together with interest.” Where, as here, there has been no overpayment of the tax, the “if” clause is not met and no refund is owed.

The Department did not err in strictly applying the refund statute. See AR 171. As our Supreme Court has explained, tax statutes “conferring credits, *refunds*, or deductions” are strictly construed. *Lacey Nursing Center, Inc. v. Dep’t of Revenue*, 128 Wn.2d 40, 49, 905 P.2d 338 (1995) (emphasis added). More importantly, under general principles of state sovereign immunity, the tax refund statute cannot be read as implicitly obligating the state to pay interest on taxes that are undeniably owed. The Legislature does not waive state sovereign immunity by implication. The waiver must be expressly set out by the statute. *Linville v. State*, 137 Wn. App. 201, 208, 151 P.3d 1073 (2007). And there is no express requirement

under the estate tax code for the payment of interest where, as here, there is no overpayment of tax.

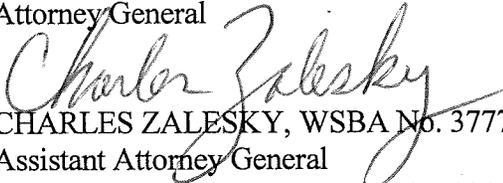
The Estate has no legal basis to an award of accrued interest under the circumstances of this case. Consequently, the Department did not err when it rejected the Estate's claim. AR 171. This Court should affirm.

V. CONCLUSION

The Department correctly denied the Estate's claim for interest on tax that the Estate clearly owes. That decision should be affirmed in this APA appeal.

RESPECTFULLY SUBMITTED this 12th day of January, 2018.

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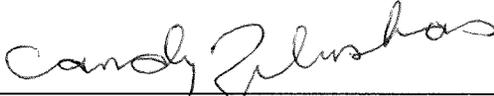
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I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED this 12th day of January, 2018, at Tumwater, WA.



Candy Zilinskas, Legal Assistant

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