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STATE OF WASHINGTON

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DEPARTMENT OF REVENUE



No. 44809-2-II

COURT OF APPEALS  
STATE OF WASHINGTON  
DIVISION II

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THE DEPARTMENT OF REVENUE OF THE STATE OF  
WASHINGTON, Appellant,

vs.

NANCY G. KISSNER, Executrix of the Estate of Lillian M. Peste and  
MERVYN SETTLE, Executor of the Estate of Lillian M. Peste,  
Respondents.

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BRIEF OF RESPONDENTS

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**ORIGINAL**

## TABLE OF CONTENTS

Table of Contents.....	i
Table of Authorities.....	iii
I. INTRODUCTION.....	1
II. ISSUES PRESENTED.....	2
III. STATEMENT OF THE CASE.....	3
IV. ARGUMENT.....	10
A. DOR’s Refusal to Issue a Refund is Unlawful Under RCW 34.05.05.570(4).....	10
1. DOR’s refusal to issue the refund is un-constitutional. ....	15
2. DOR failed to perform its legal duty to issue a refund thereby acting outside of its legal authority.....	17
3. DOR’s withholding of the refund to the Estate was arbitrary and capricious. ....	19
B. The Trial Court Did Not Err In Granting The Estate’s Motion for Summary Judgment. ....	21
C. This Court Cannot Apply ER 2075 To This Case. ....	22
1. Legislation that directly overrules Supreme Court precedent will not be applied retroactively as a “change in controlling law”. ....	22
2. The April 12, 2013 Order Granting Summary Judgment was final as of that date. ....	25

3.	EHB 2075 does not require the Estate to include in the Estate the impact of a state tax election that could not be.....	26
D.	Application of ER 2075 Is Unconstitutional.....	28
1.	Applying EHB 2075 to the Estate violates the separation of powers.....	29
2.	EHB 2075 violates the constitutional limit upon imposition of an excise tax.....	31
3.	EHB 2075 violates the due process clause.....	34
4.	EHB 2075 violates the prohibition against impairment of contracts in the State and Federal Constitutions.....	39
5.	EHB 2075 violates equal protection. ....	41
E.	Collateral and Equitable Estoppel Requires Judgment in Favor of The Estate .....	43
F.	DOR violated RAP 18.9(c) by filing a meritless, frivolous appeal solely for the purpose of delay the Estate is Entitled to Attorney’s fees and costs.....	45
V.	CONCLUSION.....	45
	CERTIFICATE OF SERVICE .....	46

Appendices:  
Appendix A  
Appendix B

## TABLE OF AUTHORITIES

### Cases

<i>Barstad v. Stewart Title Guaranteed Company Inc.</i> , 145 Wn.2d 528, 537, 39 P.3d 984.....	24, 30
<i>Bates v. McCleod</i> , 11 Wn.2d 648, 657 120 P.2d 472 (1041).....	37
<i>Bellevue John Doe’s 1-11 v. Bellevue School District No. 405</i> , 129 Wn.App. 832, 867-68, 120 P.3d 616 (2005), rev’d in part on other grounds, 164 Wn.2d 199, 189 P.3d 139 (2008).....	21
<i>Brevick v. City of Seattle</i> , 139 Wn.App. 373, 379, 160 P.3d 648 (2007).....	44
<i>Caritas Services Inc. v. Department of Social and Health Services</i> , 123 Wn.2d 391, 413, 869 P.2d 28 (1994).....	34, 35, 40
<i>Carlstrom v. State</i> , 103 Wn.2d 391, 396, 694 P.2d 1 (1985).....	40
<i>Clemency v. State (“In re Estate of Bracken”) (“Bracken”)</i> , 175 Wn.2d 549, 290 P.3d 99 (2012).....	<i>passim</i>
<i>Coolidge v. Long</i> , 282 US 582, 605, 51 S.Ct. 306, 75 L.Ed. 962 (1931).....	32, 39
<i>Dennis Bloch v. State Department of Revenue</i> , No. 44802-5-II .....	13
<i>Estate of Bodger</i> , 130 Cal.App.2d 416, 424, 279 P.2d 61 (1995). .....	39, 40
<i>Estate of Bonner v. United States</i> , 84 Fed.3d 196, 198 5th Cir. (1006).....	32
<i>Estate of Louise G. Lovekin v. State of WA Dept. of Revenue</i> , No. 44867-0 .....	9
<i>Estate of Smith</i> , 40 Wn.App. 790 797 700 P.2d 1181 (1985).....	33, 35

<i>Ford v. Department of Revenue,</i> No. 44917-0-II .....	9
<i>Haberman v. Wash. Pub. Power Supply Sys.,</i> 109 Wn.2d 107, 750 P.2d 254 (1987).....	22
<i>Hale v. Wellpinit School District No. 49,</i> 165 Wn.2d 494, 498, 198 P.3d 1021 (2009).....	29, 30
<i>Hanson v. City of Snohomish,</i> 121 Wn.2d 552, 561, 852 P.2d 295 (1993).....	43
<i>Isla Verde International Holdings Inc. v. City of Camas,</i> 146 Wn.2d 740, 752, 49 P.3d 867 (2002).....	28
<i>Kabbae v. Dep't of Social &amp; Health Servs.,</i> 144 Wn.App. 432, 439, 192 P.3d 903 (2008).....	18
<i>Lambtec Corp. v. Department of Revenue,</i> 170 Wn.2d 838, 842-43, 246 P.3d 788 (2010).....	28
<i>Lucas v. Velikanje,</i> 2 Wn. App. 888, 894, 471 P. 2d 103 (1970).....	43
<i>Lummi Indian Nation v. State,</i> 170 Wn.2d 247, 241 P.3d 1220 (2010).....	30
<i>Marbury v. Madison,</i> 5 U.S. (1 Cranch) 137, 177 S 2 L.Ed. 60 1803 .....	29
<i>McGrath's Estate,</i> 191 Wn. 496, 498 71 P.2d 395 (1937) cert denied 303 US 651 (1938).....	33, 34, 36, 40
<i>Osborne v. The Department of Revenue,</i> No. 44766-5 .....	9
<i>Pierce Restraint of Stewart,</i> 115 Wn.App. 319, 331 75 P.3d 521 (2003).....	29
<i>Plaut v. Spencer Farm Inc.,</i> 514 U.S. 211, 222, 115 S.Ct. 1447 (1995).....	29

<i>Port of Seattle v. Pollution Control Board</i> , 151 Wn.2d 568, 627 90 P.3d 659 (2004).....	23
<i>R/L Associates Inc. v. The City of Seattle</i> , 113 Wn.2d 402, 780 P.2d 838 (1989).....	16
<i>Rains v. State</i> , 100 Wn.2d 660, 665, 674 P.2d 165 (1983).....	43
<i>Rios v. Washington Department of Labor and Industries</i> , 145 Wn.2d 483,491-92, 39 P.3d 961 (2002).....	11, 12, 20
<i>Samson v. City of Bainbridge Island</i> , 149 Wn.App. 33, 202 P.3d 334 (2009).....	11, 18, 24
<i>Schuchman v. Hoehn</i> , 119 Wn. App. 61, 68, 79 P.3d 6 (2003).....	42
<i>Sintra v. The City of Seattle</i> , 119 Wn.2d 1, 23, 829 P.2d 765 (1992).....	15, 16, 17
<i>Snow's Mobile Homes, Inc. v. Morgan</i> , 80 Wn.2d 283, 287, 494 P.2d 216 (1972).....	42
<i>State ex rel. Hood v. Washington State Personnel Bd.</i> , 82 Wn.2d 396, 511 P.2d 52 (1973).....	19
<i>State ex rel. Dawes v. Washington State Highway Commission</i> , 63 Wn.2d 34, 38, 385 P.2d 376(1963).....	28
<i>State v. Coria</i> , 120 Wn.2d 156, 169, 839 P.2d 890 (1992).....	42
<i>State v. Mann</i> , 146 Wn.App. 349, 360 189 P.3d 843 (2008).....	24
<i>State v. Maples</i> , 171 Wn.App. 44, 49 286 P.3d 386 (2012).....	29, 30
<i>State v. Marintorres</i> , 93 Wn. App. 442, 450, 969 P.2d 501 (1999).....	41

<i>State v. PacTel Intelco</i> , 9 Wn.2d 11 17, 113 P.2d 542 (1941).....	37
<i>Tesoro Refining and Marketing Company v. Department of Revenue</i> , 159 Wn.App. 104, 110, 246 P.3d 211 (2010) reversed on other grounds, 173 Wn.2d 551, 559 note 3, 269 P.3d 1013 (2012).....	38
<i>United States v. Carlton</i> , 512 US 26, 30, 114 S.Ct. 2018 (1994).....	34, 36
<i>United v. Wells Fargo Bank</i> , 485 US 351, 355, 108 S.Ct. 1179 99 L.Ed. 368 (1988).....	32
<i>Verchot's Estate</i> , 4 Wn.2d 574, 582, 104 P.2d 490 (1940).....	33, 35
<i>Washington State Department of Revenue v. Bloch</i> , No. 44802-5 .....	9
<i>Washington State Department of Revenue v. Hambleton</i> , No. 44937-4-II .....	9
<i>Washington State Farm Bureau Federation v. Gregoire</i> , 162 Wn.2d 284, 303-4, 174 P.3d 1142 (2007).....	22, 23, 29
<i>Washington State Republican Party v. Pub. Disclosure Comm'n</i> , 141 Wn.2d 245,282, 4 P.3d 808 (2000).....	28
<i>Wasser and Winters Co. v. Jefferson County</i> , 84 Wn.2d 597, 599, 528 P.3d 471 (1974).....	32
<i>Whatcom County Water Dist. No. 4 v. Century Holdings, Ltd.</i> , 29 Wn.App. 207, 210, 627 P.2d 1010 (1981).....	43
<i>WR Grayson Co. v. Department of Revenue</i> , 137 Wn.2d 580, 602, 973 P.2d 1011 (1999).....	37
<i>Yick Wo v. Hopkins</i> , 118 U.S. 356, 370, 6 S.Ct. 1064, 30 L.Ed.2d 220 (1886).....	17
<b>Statutes</b>	
14th Amendment to the U.S. Constitution.....	15

26 U.S.C. §2056(b)(7) .....	4
Administrative Procedure Act, RCW 34.05.570(4)(c) .....	1, 10, 11, 19, 21
CR 56 .....	21
Laws of 2005, Chapter 516, §20 .....	3
RAP 18.1(a) and 18.9(a) .....	45
RAP 18.9(c) .....	3
RCW 34.05.570(4).....	10
RCW 34.05.570(4)(b) .....	11
RCW 34.05.598 .....	45
RCW 4.84.185 .....	45
RCW 49.17.050(4).....	20
RCW 83.100.040 .....	8
RCW 83.100.047 .....	7, 27
RCW 83.100.130 .....	38
RCW 83.100.130(1).....	18, 20
RCW 83.100.20 .....	24
WAC 458-20-229(7).....	6, 18
WAC 458-57-105 (3)(g)(vi) (2007).....	27
WAC 458-57-115 (2)(d)(vi) (2007).....	27
<b>Other Authorities</b>	
EHB 2075.....	passim
HB 1920 .....	6

## I. INTRODUCTION

This case reviews the actions of the Washington State Department of Revenue (“DOR”) under the Administrative Procedure Act, RCW 34.05.570(4)(c) (“APA”) in denying the Estate of Lillian M. Peste (“Estate”) an estate tax refund. This denial deliberately disregards the rule of law, as determined by the Washington Supreme Court in *Clemency v. State* (“*In re Estate of Bracken*”) (“*Bracken*”), 175 Wn.2d 549, 290 P.3d 99 (2012). Under *Bracken* the Estate is entitled to the refund.

DOR lost *Bracken* and then intentionally disregarded it for a five-month period.<sup>1</sup> During that time, DOR sought – and got – legislation<sup>2</sup> that purports to overrule *Bracken*. As explained herein, DOR’s denial of an estate tax refund to the Estate blatantly violates the APA and its actions were an unjustified abuse of the administrative, legislative and judicial processes.

This Court can find that the DOR acted unlawfully under the APA without addressing the constitutionality of the new, DOR-sponsored legislation. However, should the Court choose to do so, it must strike

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<sup>1</sup> Technically, DOR disregarded *Bracken* since the date it was issued, October 18, 2012. The five-month period refers to the time between the denial of DOR’s motion for reconsideration in *Bracken* (January 10, 2013) and the effective date of the new legislation (June 14, 2013).

<sup>2</sup> EHB 2075 was enacted by the Laws of 2013, 2d Spec. Sess., ch. 2. Throughout this brief this law will be referred to as “EHB 2075”.

down this legislation for multiple constitutional violations. Under no circumstance can DOR's denial of the tax refund to the Estate be sustained. This Court should affirm the Order Granting Summary Judgment in favor of the Estate and reject the DOR's arguments on appeal.

## II. ISSUES PRESENTED

1. Is DOR's refusal to issue a tax refund to the Estate unconstitutional or an arbitrary or capricious act or outside of its legal authority?

2. Did the Trial Court correctly grant summary judgment to the Estate under *Bracken*, requiring the DOR to issue an estate tax refund to the Estate within two weeks?

3. Is DOR's assertion that EHB 2075 justifies its refusal to issue a tax refund to the Estate correct under the language of this legislation?

4. Is DOR's assertion that EHB 2075 justifies its refusal to issue and tax refund unconstitutional as applied in this case?

a. Does EHB 2075 violate the separation of powers doctrine?

b. Does EHB 2075 violate the due process clause?

c. Does EHB 2075 violate constitutional requirements for imposing an excise tax?

d. Does EHB 2075 unconstitutionally impair contracts?

5. Is DOR estopped from refusing to follow *Bracken* in this case?

6. Did DOR violate RAP 18.9(c) by filing a meritless, frivolous appeal solely for the purpose of delay so as to entitle the Estate to attorney's fees and costs?

### III. STATEMENT OF THE CASE

#### A. Background.

The DOR wants to tax estates of a small group of decedents who died long before Washington had a standalone estate tax. This tax, effective May 17, 2005 was intended to apply prospectively to citizens dying after that date. Laws of 2005, Chapter 516, §20. Before that date Washington received a share of federal estate tax, known as a “pickup” tax.<sup>3</sup>

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<sup>3</sup> *Bracken* discusses the inter-relationship between state and federal estate taxes at length, 175 Wn.2d at 558-562.

Fred Peste, husband of Lillian (the decedent in this case) died on March 31, 1985. Fred planned his estate based upon federal estate tax law then in effect. 26 U.S.C. §2056(b)(7). This allowed him to set up a “qualified terminable interest property” (“QTIP”) trust for Lillian which transferred to her a life estate in the QTIP trust. At that time there were no comparable state QTIP provisions.<sup>4</sup> Fred designated the beneficiaries to receive the remainder in the federal QTIP trust once Lillian died. At that point, the federal estate taxes owing on Fred’s Estate, which had been deferred during Lillian’s lifetime, would be paid on the remainder of the federal QTIP trust that Fred set up.

Lillian died on July 16, 2008. Her personal representatives paid the federal estate tax on the QTIP trust set up by Fred twenty-three years earlier. They included this QTIP trust in Lillian’s Washington taxable estate under protest and paid Washington estate taxes of \$1,268,138. (CP 17).

That portion of the estate tax paid attributable to the value of the assets in the federal QTIP trust was \$717,239. On June 9, 2010 the Estate filed a request for a refund of \$717,239. (CP 26). This request was denied

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<sup>4</sup> DOR’s brief refers only to “QTIP” and fails to distinguish between state and federal QTIP trusts. The distinction between the two is critical. Federal QTIP trusts have been allowed under federal law since 1981. State QTIP trusts under RCW 83.100.047 only have been possible since 2005.

by DOR on June 15, 2010. (CP 15). Thereafter on July 13, 2010 the Estate timely filed a petition for judicial review and refund for overpayment of state estate taxes. (CP 4-32).

Shortly after the Estate filed its petition for review, the Supreme Court accepted *Bracken* for review. The central issue in *Bracken* was whether a pre-2005 federal QTIP trust was required to be included in the Washington taxable estate of a surviving spouse who died after May 17, 2005. Counsel for the Estate and DOR agreed that *Bracken* would resolve the Estate's petition. They executed a Stipulated Motion for Order Staying This Action Pending Supreme Court Resolution of Dispositive Issue ("Stipulation") because "the central issue in *Bracken* is identical to that in this action." (CP 33). The Estate's counsel understood at the time of signing the stipulated motion that the DOR would agree to apply whatever decision was rendered in *Bracken*, even if adverse to the DOR.<sup>5</sup> This understanding is consistent with the DOR's own rules that state the DOR will grant refunds required by a court decision. WAC 458-20-

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<sup>5</sup> Declaration of Judith A. Endejan in Support of Motion to Dismiss Under RAP 1.2(a); 18-8(a); 18.12 and 18.14, ¶3, filed in this appeal on May 28, 2013. ("Endejan Declaration")

229(7). (emphasis supplied). Otherwise, the Estate's counsel would have pursued the petition to final judgment and consolidation with *Bracken*.<sup>6</sup>

On October 18, 2012 the Washington Supreme Court issued *Bracken*, holding that QTIP trusts created prior to 2005 are not subject to Washington estate tax from the estate of a surviving spouse who died after May 17, 2005.

Shortly thereafter counsel for the Estate contacted DOR about when the now-required refund of \$717,239 with interest would be issued.<sup>7</sup> The DOR refused to act but filed a motion for reconsideration of *Bracken* that was denied on January 10, 2013.

Within a month it became clear the DOR intended to take no action to issue the required refund to the Estate because DOR requested a bill, HB 1920, that was introduced in the Legislature to reverse *Bracken* (CP 83) on February 18, 2013.<sup>8</sup>

The DOR fiscal note to HB 1920 revealed its strategy to refuse to issue refunds required under *Bracken* and manipulate the legislature to pass retroactive legislation to overturn *Bracken*:

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<sup>6</sup> *Id.*

<sup>7</sup> *Id.* at ¶4.

<sup>8</sup> HB 1920 was the first iteration of what became EHB 2075. Other bills (i.e., HB 2064, SB 5939) failed before EBH 2075 passed. The reverse-*Bracken* provisions were the same in all of these bills.

The estimated revenue increase reflects the retroactive clarifications of the definitions of “transfer” and “Washington taxable estate” to conform to the Department’s interpretation, thereby eliminating any refund claims resulting from the recent court decision, other than for the Estate of *Bracken*.” (CP 93) (Emphasis supplied)

This manipulation is evident from the floor debate on EHB 2075<sup>9</sup>, and the statement of legislative intent for that bill.<sup>10</sup> This reflects an apparent belief that the bill would cure an inequity between single and married decedents because the latter pay no state estate taxes. This mis-belief was adopted in the legislative “findings” in EHB 2075. DOR is the source for this mis-belief. In legislative hearings, DOR spokesperson Drew Shirk told a legislative committee, “As a result of this ruling (*Bracken*), Washington estate tax now contains an unintended consequence, where married couples, properly executing their trusts, do not owe an estate tax, where everyone else does.”<sup>11</sup> This reading of *Bracken* could not be further from the truth.

In fact, EHB 2075 does not eliminate the state QTIP election in RCW 83.100.047, which authorizes state estate tax deductions only for

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<sup>9</sup> The floor debate on EHB 2075 appears in the Appendix A.

<sup>10</sup> See Appendix A to DOR Opening Brief, p.2.

<sup>11</sup> See Appendix B, (p.10) which is a partial transcript of a hearing before the Senate Ways and Means Committee on SB 5939, a predecessor to EHB 2075.

couples, not available to singles. There is no question that all Washington decedents remain subject to state estate tax for both couples and singles. RCW 83.100.040.

DOR also promoted a false urgency among legislators, contending that the funds from taxing federal QTIP trusts were critical to funding education and that this legislation was a justifiable “Robin Hood” solution to education revenue problems. When the DOR-sponsored reverse-*Bracken* bills did not pass in the regular and first special 2013 legislative sessions, DOR threatened to “process” refund checks in June of 2013 to deplete funds from the education legacy trust account that DOR claimed would be available if its legislation passed.<sup>12</sup> This prompted EHB 2075 which was first read on June 12 in the second special legislative session, passed by both the House and Senate on June 13. On June 13, during the floor debate Senator Sharon Nelson said,

And ladies and gentlemen, in eight hours and fifteen minutes without this legislation we begin to refund to the wealthiest estates in Washington. We begin to mail out checks for funds that could be used for our kindergarteners, for our third-graders, for everything that we believe in for our kids' future. (AC-9)

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<sup>12</sup> See, [http://seattletimes.com/html/localnews/2021185408\\_newestatetaxxml.html](http://seattletimes.com/html/localnews/2021185408_newestatetaxxml.html).

Thereafter EHB 2075 was signed by Governor Jay Inslee in the early hours of June 14, to take effect immediately.

Meanwhile, in the five month period between the denial of DOR's motion for reconsideration and when EHB 2075 was signed into law, DOR "litigated" with the Estate and other estates entitled to a refund to buy time with the Legislature.<sup>13</sup> Because the DOR would not issue a refund, the Estate filed a motion for order lifting stay and for summary judgment based upon *Bracken*.<sup>14</sup> (CP 36-71). The DOR's opposition conceded "if that clarifying legislation does not pass, the Department agrees that under the holding in *Bracken* the Estate is entitled to the estate tax refund it is claiming." (CP 96).

On April 12, 2013 Thurston County Superior Judge Gary R. Tabor granted the Estate's motion for summary judgment ordering the DOR to issue the refund within two weeks of the date of the order because *Bracken* controlled. (CP 133-35) Again, DOR took no action. The Estate wrote DOR on April 23, 2013 advising DOR that a refund would have to

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<sup>13</sup> See, e.g., *Osborne v. The Department of Revenue*, No. 44766-5; *Washington State Department of Revenue v. Bloch*, No. 44802-5; *Estate of Louise G. Lovekin v. State of WA Dept. of Revenue*, No. 44867-0; *Washington State Department of Revenue v. Hambleton*, No. 44937-4-II and *Ford v. Department of Revenue*, No. 44917-0-II.

<sup>14</sup> DOR later stipulated that the stay could be lifted.

be issued no later than April 26, 2013 or relief would be sought from the Thurston County Superior Court.<sup>15</sup>

On April 26, 2013 the DOR filed a notice of appeal and notice that decision is superseded without bond. (CP 136-44). On May 28, 2013 the Estate filed a motion to dismiss the appeal under RAP 1.2(a)18.8(a); 18.9(c); 18.12 and 18.14, because the Trial Court's decision was controlled by *Bracken*, a decision from Washington's highest court which the Court of Appeals cannot reverse. The motion also claimed that DOR sought review solely for the purpose of delay because it had no legal basis. This Court denied that motion on June 25, 2013.

#### ARGUMENT

**A. DOR's Refusal to Issue a Refund is Unlawful Under RCW 34.05.570(4).**

This is an APA review. The decisions challenged are DOR's refusal to issue a refund required by law under *Bracken* for the five-month period after *Bracken* became final, and its continued refusal to do so due to passage of EHB 2075.

DOR now claims that because the controlling law has changed it is justified in denying the refund. This sidesteps the first question that is central to the appeal; namely, was DOR required to make the refund or

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<sup>15</sup> Endejan Declaration, Exhibit 8.

issue the release before EHB 2075 became law? DOR's refusal to issue a timely refund is "other agency action" reviewable under RCW 34.05.570(4). *Rios v. Washington Department of Labor and Industries*, 145 Wn.2d 483,491-92, 39 P.3d 961 (2002).

RCW 34.05.570(4)(b) authorizes the Estate to seek a court order compelling performance (issuance of a refund) if its "rights are violated by an agency's failure to perform a duty that is required by law to be performed." (Emphasis supplied.)

RCW 34.05.570(4)(c) provides the standard of review for DOR's actions in this case, which must be corrected, and set aside, if this court finds they are:

- i. Unconstitutional;
- ii. Outside the statutory authority of the agency or the authority conferred by a provision of law;
- iii. Arbitrary or capricious.

In reviewing DOR's actions under RCW 34.05.570(4)(c), the Court must apply the law in effect at the time of the agency action - or inaction in this case - is taken. In *Samson v. City of Bainbridge Island*, 149 Wn.App. 33, 202 P.3d 334 (2009) the appellants challenged city ordinances limiting certain dock and pier development. They argued that the Department of Ecology's conduct should be gauged against proposed

departmental guidelines pending but not in effect at the time the ordinance was passed and reviewed by Ecology. The court rejected this argument finding, in effect, that review of agency conduct must be under the law that exists at the time of the conduct. *See, also Rios*, 145 Wn.2d at 505. The legality of DOR's conduct in the five months preceding EHB 2075 cannot be excused by passage of that act. The Court should assess DOR's five-month period of inaction based upon controlling law during this time, which means that DOR was required by *Bracken* to issue the refund during that time.

The following facts show that DOR's deliberate refusal to follow *Bracken* and issue the refund was: unconstitutional, without legal authority and arbitrary or capricious.

DOR simply refused ever to accept *Bracken*<sup>16</sup> or follow it once the decision was issued. It sought immediate reconsideration of the decision, which DOR lost. Then DOR requested legislation immediately to replace the Supreme Court's interpretation of RCW 83.100.020 with the "Department's interpretation" (CP 93). Thereafter, its refund inaction

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<sup>16</sup> The fact that DOR's Opening Brief devotes almost half of its brief to argue for reversal of *Bracken* demonstrates DOR's dogged refusal to accept its loss. The Estate will not respond to these re-arguments because this Court has no authority to reverse *Bracken* so these arguments are not relevant to this appeal. DOR has not sought review of this case under RAP 4.2 and this appeal is not before the Supreme Court.

forced the Estate to incur considerable legal expense to file a motion for summary judgment to force DOR to provide the required refund.

There was never any question that DOR could not issue the refund in a timely manner due to any lack of administrative resources or other potential justifiable bases for delay. Indeed, DOR conceded that a two-week time period was doable when the DOR's attorney approved the form of Judge Tabor's Order in the Estate's favor, which contained a two-week time period. DOR never presented any other reason for failing to issue a refund except its disagreement with *Bracken* and its refusal to follow it while its legislation was pending.

In the pleadings it filed with the trial court, and now on appeal, DOR reargues *Bracken*, insisting *Bracken* should be overruled, while acknowledging that neither a trial court nor the Court of Appeals could do so. Its opposition to the Estate's motion conceded that the Estate was owed the refund under *Bracken*. (CP 93). Its argument that the delay was justified pending passage of reverse-*Bracken* legislation, has no authority. Indeed, when asked to provide such authority in an identical case in Thurston County Superior Court, DOR's attorney failed to do so and was sanctioned by the trial court.<sup>17</sup>

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<sup>17</sup> See, *In re Dennis Bloch v. State Department of Revenue*, No. 44802-5-II pending before this Court. VRP 8 (March 29, 2013 hearing).

Judge Tabor granted the Estate's motion for summary judgment in this case, stating "everybody agrees that the Washington Supreme Court has made a ruling which is binding in this area, unless that's overturned." VRP 5. (emphasis supplied).

The DOR disobeyed this order, which required issuance of the refund in two weeks, even after prompting from the Estate's attorney to pay the refund.

Instead DOR filed a notice of appeal solely for the purpose of delay in a transparent attempt to render Judge Tabor's judgment "non-final" so that EHB 2075, if passed, might apply to this case.<sup>18</sup>

An overarching factor that makes the prejudice to this Estate even more egregious is the Stipulation that stayed the Estate's litigation, pending the outcome in *Bracken*. (CP 33-35). Any reasonable construction of that stipulation means that both parties agreed to have the Supreme Court in *Bracken* resolve "the dispositive issue" in this case as stated in the Stipulation's caption. If that was not the case the Estate could have pursued this case to judgment and consolidation with *Bracken*. Instead the DOR refused to abide by the Stipulation and has engaged in

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<sup>18</sup> The Estate adopts the arguments and evidence submitted to this Court in its motion to dismiss this appeal, filed on May 28, 2013 to explain why this appeal was frivolous and filed solely for the purpose of delay at the time it was filed.

untenable litigation maneuvers to cause the Estate to incur great legal expense to obtain the refund it was entitled to under *Bracken*. In essence, until DOR could get the legislature to do its bidding, it manipulated the judicial process to run down the clock in order to refuse refunds under the shield of EHB 2075. As explained herein DOR cannot do so.

The above pre-EHB 2075 agency conduct however, must be set aside under the APA.

**1. DOR's refusal to issue the refund is un-constitutional.**

Leaving aside the question of whether EHB 2075 passes constitutional muster, DOR's deliberate refusal to issue the refund to the Estate violates the Estate's right to due process under the 14<sup>th</sup> Amendment to the U.S. Constitution. This provides "nor shall any state deprive any person of life, liberty, or property, without due process of law." DOR's conduct deprived the Estate of its property right in the refund due under *Bracken*. DOR's deliberate disregard of the controlling law violates substantive due process. In *Sintra v. The City of Seattle*, 119 Wn.2d 1, 23, 829 P.2d 765 (1992), the Washington Supreme Court said that substantive due process may be violated where:

"there is a substantial infringement of state law prompted by *animas* directed at an individual or a group, or a "deliberate flouting of the law that trammels significant

personal or property rights.” *Silverman v. Barry*, 845 F.2d 1072, 1080 D.C. Cir., cert. denied 488 U.S. 956, 109 S. Ct. 394, 102 L. Ed. 2<sup>nd</sup> 383 (1988). Arbitrary irrational action on the part of regulators is sufficient to sustain a substantive due process claim under Section 1983. *Coniston Corp. v. Hoffman Estates*, 844 F.2d 466, 467, 7<sup>th</sup> Cir. 1988; *Abbis* 712 F.Supp. at 1164.

In *Sintra*, the Supreme Court found the appellants had a colorable claim for a substantive due process due process violation when the City of Seattle ignored a trial court ruling in one case that invalidated the tenant assistance provisions of Seattle’s Housing Preservation Ordinance.<sup>19</sup> The City deliberately continued to enforce this ordinance against others, including *Sintra*, knowing that the ordinance was legally invalid. The City claimed that the trial court’s decision in one case did not apply to others not a party to that case, even though the others were similarly situated. The Supreme Court rejected this argument and found that the City’s conduct could violate *Sintra*’s due process rights:

“Intentional violations of court orders cannot be tolerated. Respect for the rule of law lies at the heart of due process, and disregard of that law by government can only be considered violative of that right.”

119 Wn.2d at 24.

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<sup>19</sup> This decision was upheld in *R/L Associates Inc. v. The City of Seattle*, 113 Wn.2d 402, 780 P.2d 838 (1989). In *R/L Associates*, the Supreme Court held that the City’s continued enforcement of the tenant assistance provisions in the face of the Superior Court order was contempt of court. *Id.* at 411.

Like the City in *Sintra*, DOR intentionally flouted the law to trammel the property right to a refund of the Estate and others similarly situated. DOR consciously ignored two court rulings: *Bracken* and Judge Tabor's order that followed it. DOR's disregard for the law should not be tolerated. We are "a government of laws and not of men." *Yick Wo v. Hopkins*, 118 U.S. 356, 370, 6 S.Ct. 1064, 30 L.Ed.2d 220 (1886).

DOR's actions also targeted<sup>20</sup> only a small group of taxpayers who would benefit from *Bracken*, a decision DOR stubbornly refused to accept.<sup>21</sup> DOR's refusal to issue refunds to those taxpayers constitutes the type of arbitrary, irrational action that violates due process and is unconstitutional.

**2. DOR failed to perform its legal duty to issue a refund thereby acting outside of its legal authority.**

DOR had a legal duty to issue a refund to the Estate. *Bracken* determined that the Estate overpaid, and DOR agreed that the "Estate is entitled to the state tax refund it is claiming." (CP 96).

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<sup>20</sup> DOR's impermissible targeting also violates the Equal Protection Clause as discussed in Sec. D.5.

<sup>21</sup> As one legislator noted EHB 2075 is targeted at only about 70 estates. A-9 (*See, also* [http://seattletimes.com/html/localnews/2021185408\\_newestatetax.xml.html](http://seattletimes.com/html/localnews/2021185408_newestatetax.xml.html)).

RCW 83.100.130(1) states that “the department shall refund the amount of the overpayment.” (Emphasis supplied.) The use of the word “shall” in a statute ordinarily means that the specified action is mandatory. *Kabbae v. Dep't of Social & Health Servs.*, 144 Wn.App. 432, 439, 192 P.3d 903 (2008).

DOR’s regulations promise:

**“Refunds made as a result of a court decision.** The department will grant refunds or credits required by a court or Board of Tax Appeals, if the decision is not under appeal.”

WAC 458-20-229(7).

“It is well settled law in Washington that public agencies must follow their own rules and regulations.” *Samson v. City of Bainbridge Island*, 149, Wn.App. 33, 44, 202 P.3d 334 (2009).

Given these legal commands there is no justifiable excuse for DOR’s failure to issue the required refunds promptly after *Bracken* was decided.<sup>22</sup>

DOR had no legal authority to withhold the Estate’s refund for five months. DOR presented no lawful reason in the record as to why this refund could not have been issued within at least a two-week period,

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<sup>22</sup> Indeed, DOR must pay interest on refunds that are owed under RCW 83.100.130. If DOR is concerned about the loss of state funds for education it should have *minimized* this loss by issuing refunds as soon possible.

according to Judge Tabor's Order. (CP 133-35). DOR's attorney agreed to the "two-week" language in that Order. Thus, there was no question that DOR could have made a timely refund well before passage of EHB 2075.<sup>23</sup>

In sum, DOR's deliberate refusal to issue the refund to the Estate is outside of its statutory authority under RCW 34.05.570(4)(c)(ii).

**3. DOR's withholding of the refund to the Estate was arbitrary and capricious.**

Arbitrary and capricious agency action is unreasoning action in disregard of facts or circumstances, which violates fundamental rights. *State ex rel. Hood v. Washington State Personnel Bd.*, 82 Wn.2d 396, 511 P.2d 52 (1973).

As discussed above, DOR's purposeful refund delay was arbitrary, in that it was directed at only one set of taxpayers entitled to refunds (those who fell under *Bracken*). DOR deliberately disregarded the "facts and circumstances," which include its Stipulation to abide by *Bracken*, and *Bracken* itself.

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<sup>23</sup> This case presents no administrative reason for delay, unlike others e.g., *Hillis v. State Department of Ecology*, 131 Wn.2d 373, 932 P.2d 139 (1997) (delay by an agency action in processing permits when the agency is not funded by the legislature is not unreasonable).

Courts do not shy away from invalidating arbitrary and capricious agency actions which ignore pertinent facts and circumstances. In *Rios*, *supra* the Supreme Court found the information that was available to the Department of Labor and Industries at the time it received a request from agricultural pesticide handlers to promulgate rules to implement cholinesterase monitoring did not justify denial of that request.

Because the Department had already invested its resources in studying cholinesterase-inhibiting pesticides and because the report of its own team of technical experts had, in light of the most current research, deemed a monitoring program both necessary and doable, the Department's 1997 denial of the pesticide handlers' request was "unreasoning and taken without regard to the attending facts or circumstances." *Hillis*, 131 Wash.2d at 383, 932 P.2d 139. Consequently, in failing to act on the request for rulemaking, the Department violated RCW 49.17.050(4), the requirement that the Department "set a standard which most adequately assures, to the extent feasible, on the basis of the best available evidence, that no employee will suffer material impairment of health."

145 Wn.2d at 508.

In this case the DOR knew that once *Bracken* was final that it had a statutory duty under RCW 83.100.130(1) to issue a refund to the Estate. DOR violated that duty, choosing to act in defiance of *Bracken* to deprive the Estate of its lawful refund.

This Court should invalidate the DOR's actions under RCW 34.05.570(4)(c) and remand to the DOR with directions to issue the Estate's refund within two weeks.

**B. The Trial Court Did Not Err In Granting The Estate's Motion for Summary Judgment.**

The Trial Court properly granted the Estate's motion for summary judgment under CR 56 because, as DOR concedes, there were no disputed issue of material fact.<sup>24</sup> The Trial Court also committed no legal error in following binding law, which was *Bracken*.

It is axiomatic that the Superior Court and this Court are bound by decisions of the Supreme Court under the principle of *stare decisis*:

“the principle of *stare decisis* – “to stand by the thing decided” – binds this Court as well as the Trial Court to follow Supreme Court decisions, not to speculate that they will be overruled.”

*Bellevue John Doe's 1-11 v. Bellevue School District No. 405*, 129 Wn.App. 832, 867-68, 120 P.3d 616 (2005), rev'd in part on other grounds, 164 Wn.2d 199, 189 P.3d 139 (2008). Thus, Judge Tabor's order should be upheld.

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<sup>24</sup> DOR Opening Brief, pp. 7-8.

**C. This Court Cannot Apply ER 2075 To This Case.**

DOR contends that ER 2075 should be applied to this Estate because it is a change in controlling law that occurred prior to final disposition of this case. DOR is wrong for several reasons. First, EHB 2075 cannot retroactively overrule *Bracken*. Second, the Estate had a final judgment as of April 12, 2013 and third, the language of EHB 2075 contradicts DOR's claim.

**1. Legislation that directly overrules Supreme Court precedent will not be applied retroactively as a "change in controlling law".**

None of the cases cited by DOR regarding the application of controlling law authorizes this Court to apply EHB 2075 to this case. *Haberman v. Wash. Pub. Power Supply Sys.*, 109 Wn.2d 107, 750 P.2d 254 (1987) did not involve a Washington Supreme Court interpretation of a prior statute that was reversed by retroactive legislation. This legislation was but a "facially neutral law" for a court to apply to the facts before it in pending litigation. *Id.* at 144. The statutory change did not dictate the result, it just changed the standard of liability for bond counsel and agents when issuing securities.

In *Washington State Farm Bureau v. Gregoire*, 162 Wn.2d 284, 174 P.3d 1142 (2007) again, the Legislature did not address or reverse a Washington Supreme Court ruling. This case involved a challenge as to

how the state calculated the 2006 state expenditure limit as limited by Initiative 601. The legislature passed legislation finding that the 2006 spending limit was properly done. If anything, *Gregoire* states the controlling law that the legislature cannot pass the retroactive legislation “if the subsequent enactment contravenes the construction placed on the original statute by this court,” *Id.* at 304.

The Supreme Court reiterated this binding principle in *Port of Seattle v. Pollution Control Board*, 151 Wn.2d 568, 627 90 P.3d 659 (2004). The Court stated that retroactive applications of a new law only can be done to “clarify” the law in response to an administrative adjudication or trial court decision but “the legislature may not retroactively overrule a decision of the state’s highest court.” *Id.* at 627.

This case involves legislation unlike the legislation in *Haberman*, *Gregoire* or *Port of Seattle*. The legislature intended to directly overrule *Bracken* and to substitute DOR’s statutory interpretation of “transfer” for that of the highest court in Washington charged with the duty of statutory interpretation. EHB 2075 was targeted at a specific group of taxpayers seeking an estate tax refund. DOR’s fiscal note to the original reverse-*Bracken* bill clearly states the bill’s purpose as “restoring the estate tax as it existed before that recent court decision.” (*Bracken*). (CP 92) Floor debate on the bill referred to it as an attempt to “fix the result of

“*Bracken*”. (A-15) The very first section of EHB 2075 even blatantly states that its purpose is to un-do the Supreme Court’s interpretation of the term “transfer” in *Bracken*.

The DOR and the Legislature try to justify this retroactive legislation as “curative, clarifying and remedial.” Courts “do not apply statutes retroactively unless they are merely procedural or remedial.” *Samson*, 149 Wn.App. at 45. EHB is nothing but a substantive amendment which should only apply prospectively. *State v. Mann*, 146 Wn.App. 349, 360 189 P.3d 843 (2008). An amendment is only “curative or remedial if it clarifies or technically corrects an ambiguous statute without changing prior case law constructions of the statute.” *Barstad v. Stewart Title Guaranteed Company Inc.*, 145 Wn.2d 528, 537, 39 P.3d 984. EHB 2075 patently changes the Supreme Court’s construction of “transfer” in RCW 83.100.20. Further, a statute can only be considered remedial if it affects merely procedures, “not substantive or vested rights.” *State v. Mann*, 146, Wn.App. at 356. EHB 2075 deprives the Estate of a lawful refund, which certainly is a vested right. In short, EHB 2075 represents no change in controlling law that this Court should apply retroactively.

**2. The April 12, 2013 Order Granting Summary Judgment was final as of that date.**

When Judge Tabor entered judgment on April 12, 2013 the judgment was final because it was not subject to appeal. Neither the trial court nor this Court has any authority to reverse *Bracken*. Thus, an appeal to this Court was pointless and with no legal merit. Yet DOR filed this appeal as a subterfuge intended to keep this case “pending” until final legislative action on EHB 2075 could be passed. EHB 2075 does not apply to “any final judgment, no longer subject to appeal, entered by a court of competent jurisdiction” before June 14, 2013 the effective date of the statute. (emphasis added) A decision is “no longer subject to appeal” when it is entirely based upon recent controlling decisions by the Supreme Court. See decisions in Sec. III.B.

This Court should interpret “no longer subject to appeal” to apply to Judge Tabor’s Order because it was not subject to appeal at the time it was entered.<sup>25</sup> The question for this Court is whether “no longer subject to appeal” applies to a circumstance like this case. Here DOR orchestrated events (i.e., introduced legislation, delayed refunds and mis-used the appellate process). The fact that the legislature passed a law on June 13,

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<sup>25</sup> Again, the Estate adopts the arguments and evidence it made in connection with its motion to dismiss this appeal as frivolous and filed only for purposes of delay filed on May 28, 2013.

2013 does not provide a legal basis for an appeal which had no basis at the time it was filed.

**3. EHB 2075 does not require the Estate to include in the Estate the impact of a state tax election that could not be.**

Section 5 of EHB 2075 contains the new language that purports to overrule *Bracken*. This section states in Section 3:

“Notwithstanding any department rule, if a taxpayer makes an election consistent with Section 2056 of the Internal Revenue Code as permitted under this section, the taxpayer’s Washington taxable estate, and the surviving spouse’s Washington taxable estate must be adjusted as follows:

(a) for the taxpayer that made the election, any amount deducted by reason of Section 2056(B)(7) of the Internal Revenue Code is added to, and the value of property for which a Washington election under this section was made is deducted from, the Washington taxable estate.

(b) for the estate of the surviving spouse, the amount included in the Estate’s gross estate pursuant to Section 2044 (A) and (B)(1)(a) of the Internal Revenue Code is deducted from, and the value of any property for which an election under this section was previously made is added to, the Washington taxable estate.”

Only subsection (b) applies to Lillian’s Estate. The Washington State Estate and Transfer Tax Return filed by the Estate under protest (CP 28) can illustrate how subsection (b) works. Under subsection (b) the Estate would be allowed to deduct the value of Fred’s federal QTIP on

line B. 2b of the return. Under subsection (b) the Estate must then add back on line B. 2c of the return the value of any state QTIP property under RCW 83.100.047. Because Fred made no state QTIP election the value of this property must be zero. Fred could not have made this election because RCW 83.100.047 did not exist at the time of his death. Here, the Estate included the federal QTIP amount on line A (which states the total gross estate for Washington tax purposes) because the DOR mandated at that time that the federal QTIP be added to the Washington gross estate. The Estate did so under protest, and then appealed.

This illustrates best the fatal flaw in DOR's position in this appeal. That position assumes: (a) that Fred made a state QTIP election when he did not and (b) the value of the state and federal QTIPs would be equal.

These assumptions are not supportable, even under the language of EHB 2075, which clearly recognizes the difference between the two types of QTIP trusts and provides for different treatment in calculating the estate tax.

DOR recognized this distinction in its first rules adopted after the estate tax was enacted in 2005. *See*, WAC 458-57-115 (2)(d)(vi) (2007) and WAC 458-57-105 (3)(g)(vi) (2007). It then changed its position to "invent" a taxable state QTIP for a pre-2005 federal election to drag the exact value of the pre-2005 federal QTIP trust into a Washington taxable

estate. Thus, the Estate should be allowed to deduct the Federal QTIP amount and add a zero amount for the state QTIP under EHB 2075. This entitles it to the refund ordered by Judge Tabor.

**D. Application of ER 2075 Is Unconstitutional.**

Courts should decide a case on statutory grounds rather than constitutional grounds when possible. *Isla Verde International Holdings Inc. v. City of Camas*, 146 Wn.2d 740, 752, 49 P.3d 867 (2002). The Estate has presented compelling reasons in the foregoing sections to uphold the trial court's decision without having to address the abundant constitutional problems created by EHB 2075. But these also provide a basis for finding this law unconstitutional as applied in this case.<sup>26</sup> In construing the new language added by EHB 2075, the Court should presume that the legislature "intended a meaning consistent with the constitutionality of its enactment. *State ex. rel. Dawes v. Washington State Highway Commission*, 63 Wn.2d 34, 38, 385 P.2d 376(1963). Further it is well settled that "a tax statute must be construed most strongly against the taxing power and in favor of the taxpayer," *Lambtec Corp. v. Department of Revenue*, 170 Wn.2d 838, 842-43, 246 P.3d 788 (2010).

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<sup>26</sup> The challenges the Estate raise to the constitutionality of EHB 2075 are "as applied" in the context of this case. *Washington State Republican Party v. Pub. Disclosure Comm'n*, 141 Wn.2d 245,282, 4 P.3d 808 (2000).

**1. Applying EHB 2075 to the Estate violates the separation of powers.**

When establishing the balance of powers, the constitution granted to the judicial branch alone the authority to interpret the laws. *See Plaut v. Spendthrift Farm Inc.*, 514 U.S. 211, 222, 115 S.Ct. 1447 (1995). “The legislature is precluded by the constitutional doctrine of separation of powers from making *judicial* determinations.” *Washington State Farm Bureau Federation v. Gregoire*, 162 Wn.2d 284, 303-4, 174 P.3d 1142 (2007). The authority to interpret the law lies solely with the judiciary. *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 177 S 2 L.Ed. 60 1803.

Retroactive application of EHB 2075 would violate the separation of powers doctrine because it infringes, and overturns, the Washington Supreme Court’s prior judicial construction in *Bracken* of the statute that EHB 2075 amends. *State v. Maples*, 171 Wn.App. 44, 49, 286 P.3d 386 (2012). *Maples* involved the retroactive application of a law involving the sentencing authority of violent offenders, enacted by the legislature in response to a prior appellate decision. Relying on *In re Pierce Restraint of Stewart*, 115 Wn.App. 319, 331 75 P.3d 521 (2003) in *Maples* this court held that the retroactive application of the new law violated the constitutional separation of powers doctrine.

In *Maples* this Court rejected the argument that DOR makes based on *Hale v. Wellpinit School District No. 49*, 165 Wn.2d 494, 498, 198 P.3d

1021 (2009) and *Lummi Indian Nation v. State*, 170 Wn.2d 247, 241 P.3d 1220 (2010) that retroactive legislation impacting a court case is permissible.

Neither *Hale* nor *Lummi Indian Nation* presented circumstances similar to this case because they did not specifically reverse prior Supreme Court decisions nor interfere with any judicial function. This court in *Maples* noted that *Hale* did not overrule *Stewart* stating “nor could it, as *Stewart* rested on the bedrock principle that the legislature cannot contravene an existing judicial construction of a statute.” *Id.* at 50.

In *Lummi*, the court reviewed a separation of powers challenge over amendments to a statute that had some retroactive effect but were intended to operate prospectively. These amendments were refinements of, and consistent with, a prior Supreme Court case on water rights.

Lummi instructs:

“We suggested that legislative intervention to affect the rights of parties in a particular case, would overstep the legislative function. ... Retroactive legislation that interferes with vested rights established by judicial rulings, interferes with a judicial function, or results in manifest injustice or threatens the independence, integrity, or prerogatives of the judicial branch may violate separation of powers.” (citations omitted) (emphasis supplied)

*Id.* at 262.

EHB 2075 was intended to affect the rights of specific, identifiable parties to particular cases, i.e., this Estate and others similarly situated. EHB 2075 was intended to prevent these Estates from the benefit of the *Bracken* ruling and trial court orders. EHB 2075 not only interferes with a judicial function – it supplants it. EHB 2075 made the legislature the “court of last resort” and threatens the independence, integrity and prerogatives for the entire Washington judicial system by effectively negating the Supreme Court’s interpretation of the law.

Finally, as discussed throughout, EHB 2075 works a manifest injustice if it is applied retroactively, according to DOR’s views. DOR would impose the fiction that Fred’s Estate made a state QTIP election that was not possible and that this fictitious election is equal to Fred’s Federal QTIP. Then, according to DOR logic, this Federal QTIP miraculously becomes the taxable property of Lillian so that the state can tax it. All of this, of course, was made possible only by DOR’s refusal to issue a refund, while it forced legislation through.

**2. EHB 2075 violates the constitutional limit upon imposition of an excise tax.**

*Bracken* first explained the difference between a permissible excise tax, levied upon the transfer of property, and an impermissible direct tax levied upon property itself. 175 Wn.2d at 564-65. *Bracken* found for the

Washington estate tax to be a permissible excise tax there must be a transfer. It noted “the requirement for a transfer is constitutionally grounded and longstanding.” *Id.* at 564. The estate tax has long been recognized as an excise tax.” *Id.* citing *United v. Wells Fargo Bank*, 485 US 351, 355, 108 S.Ct. 1179, 99 L.Ed. 368 (1988).

To interpret the additional language as DOR argues would impose a direct tax on the value of property (Fred’s federal QTIP trust), and not upon any taxable transfer. EHB 2075 did not change bedrock trust law that “property is transferred from a trustor when a trust is created, not when an income interest in the trust expires.” *Bracken* citing *Coolidge v. Long*, 282 US 582, 605, 51 S.Ct. 306, 75 L.Ed. 962 (1931). QTIP does not pass to or from a surviving spouse. *Bracken Id.* citing *Estate of Bonner v. United States*, 84 Fed.3d 196, 198 5<sup>th</sup> Cir. (1006). Thus, “transfer,” even as modified by the new language in EHB 2075, can only mean that a transfer occurred when Fred created the trust in 1985. It was his death that shifts the economic benefit in the federal QTIP trust and not the death of Lillian, because she never owned Fred’s QTIP property.

One of the key ‘incidents’ of property ownership is the right to dispose of it according to the “will of the owner.” *Wasser and Winters Co. v. Jefferson County*, 84 Wn.2d 597, 599, 528 P.3d 471 (1974). Lillian did not possess that right – only Fred did.

Further, the rights of the remainder beneficiaries designated by Fred vested at the time that Fred's trust was created, becoming complete and indefeasible. E.g., the *Estate of Smith*, 40 Wn.App. at 797, *In re Verchot's Estate*, 4 Wn.2d 574, 582, 104 P.2d 490 (1940).

According to *In re McGrath's Estate*, 191 Wn. 496, 498 71 P.2d 395 (1937) *cert denied* 303 US 651 (1938), the state cannot impose an estate tax on property not owned by the estate (i.e. Fred's federal QTIP Trust). The Court said it is "impossible for an estate or an inheritance tax to be exacted with respect to something which the decedent did not own or have some kind of right at the time of death, for in such a case there is no transfer... ." ..."An estate tax cannot be collected with respect to property unless some right in it is transferred by the death of the decedent." *Id.* at 503.

*McGrath* dealt with a dispute as to whether certain insurance proceeds could be included in the estate of the insured at death. At issue were three insurance policies naming McGrath Candy Company as the beneficiary. Only one of the three had been taken out by McGrath who retained the right to change the beneficiary. The other two were taken out by the company, which paid all the premiums and had the sole power to designate the beneficiary. The latter two policies were not subject to the estate tax because the company was the beneficiary and had complete

control. The court said “the death of McGrath added nothing to the company’s right to the proceeds of the policies where the right was from the beginning complete and infeasible. *Id.* at 504.

The same analysis applies in this case. Lillian had no control of the disposition of Fred’s federal QTIP Trust. The fact that this trust was federally taxed at a later time due to Fred’s deferral election does not mean that this property somehow became state taxable property in Lillian’s Estate.

In sum, a “transfer,” even under its new definition, should in this case only mean the transfer that occurred when Fred created his federal QTIP Trust. No “transfer” occurred at Lillian’s death.

### **3. EHB 2075 violates the due process clause.**

Due process protects against “arbitrary and irrational legislation.” *United States v. Carlton*, 512 US 26, 30, 114 S.Ct. 2018 (1994).<sup>27</sup> Retroactive application of an amendment violates due process if it deprives a party of a vested right. *Caritas Services Inc. v. Department of Social and Health Services*, 123 Wn.2d 391, 413, 869 P.2d 28 (1994). A vested right “must be something more than a mere expectation based upon

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<sup>27</sup> The due process provisions are set forth in the U.S. Constitution Amendment XIV; Wash. Const. Article I Section 3.

an anticipated continuance of the existing law; it must have become a title, legal or equitable, to the present or future enjoyment of property, a demand, or a legal exemption from a demand by another.” *Id.* at 414.

In this case EHB 2075 violates due process because it deprives the Estate of a lawful refund under *Bracken* and the trust beneficiaries of a vested right to that refund. Fred vested in them the complete and indefeasible right to the full remainder of Fred’s QTIP Trust when that trust was created. *E.g. Estate of Smith*, 40 Wn.App. 790 797 700 P.2d 1181 (1985); *In re Verchot’s Estate*, 4 Wn.2d 574, 582 104 P.2d 490 (1940). EHB 2075 imposes separate estate taxes on the trust corpus that will deplete trust funds available to Fred’s designated beneficiaries. They and the Estate had much more than a “mere expectation” to a refund. The Supreme Court told them that the law required it, so they had a vested right.

EHB 2075 also imposes an unlawful period of retroactivity. EHB 2075 taxes an event that occurred almost thirty years before its passage when Fred’s federal QTIP trust was set up. According to DOR a trustor’s transfer of federal QTIP property at any time in the past becomes a taxable event today. This reaches back to any federal QTIP that was possible since 1981. Legislators may not reach back approximately thirty years

without violating the due process clause of the state and federal constitutions. See *McGrath*, 191 Wn.2d at 510.

“A period of retroactivity longer than the year proceeding the legislative session in which the law was enacted would raise, in my view, serious constitutional questions.” *United States v. Carlton*, 512, U.S. 26 at 38, 114 S.Ct. 2018, 129 L.Ed. 2d 22 (1994) (O’Connor, J. concurring). *Carlton* involved claims that a retroactive amendment clarifying a federal estate tax deduction for the sale of employer securities to an employee’s stock ownership plan violated due process by retroactive application. The court upheld retroactivity because a) Congress’ purpose was not illegitimate or arbitrary and b) Congress acted promptly and established only a modest period of retroactivity. *Carlton* only allows taxes to be imposed if there is a “prompt” and “modest” period of retroactivity. 512 U.S. at 32-33.

In this case, DOR would have this Court reach back 30 years to apply EHB 2075, which is considerably more than the eight-year retroactive period that DOR claims is involved.

The cases cited by DOR as to the reasonableness of the retroactive period involved considerably different facts and circumstances than those in this case and are primarily not from Washington. Our courts have held that it is “the nature of tax and the circumstances in which it is laid” that

determines the constitutional boundaries of retroactivity. *WR Grayson Co. v. Department of Revenue*, 137 Wn.2d 580, 602, 973 P.2d 1011 (1999). Washington cases have found that shorter retroactive periods fail constitutional scrutiny. See *Bates v. McCleod*, 11 Wn.2d 648, 657 120 P.2d 472 (1041) (three month retroactive tax violated due process clause); *State v. PacTel Intelco*, 9 Wn.2d 11, 17, 113 P.2d 542 (1941) (four year retroactive period was too long and any retroactive taxes only applied to “prior but recent transactions”).

In addition to the duration of the retroactive period, courts should consider the circumstances surrounding EHB 2075’s enactment. That demonstrates that the Legislature – at DOR’s prodding – enacted EHB 2075 as a convenient revenue plug. EHB 2075 was passed with the sole and specific purpose of avoiding paying lawful refunds under *Bracken* that DOR told the Legislature would be imminent.<sup>28</sup> If the approach of DOR and the Legislature in passing EHB 2075 is approved these bodies will find numerous new taxes for past events any time there is a revenue need. Why not pass a state income tax and then reach back for eight years to tax income that had never been taxed before to fill state coffers?

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<sup>28</sup> See footnote 12.

This case is no different because EHB 2075 will impose estate taxes on transfers that occurred long before a state estate tax existed. Further, EHB 2075 was passed with the specific intent of invalidating the trial court decisions for the Estate and other similarly situated. This targeting also violates constitutional due process requirements. This case is like *Tesoro Refining and Marketing Company v. Department of Revenue*, 159 Wn.App. 104, 110, 246 P.3d 211 (2010) reversed on other grounds, 173 Wn.2d 551, 559 note 3, 269 P.3d 1013 (2012). There, this Court found a retroactive effect of a B&O tax amendment violated constitutional due process requirements:

And, unlike in *Carlton*, here the legislative history of the 2009 Act shows the recent amendment was in direct response to Tesoro's refund request ... the direct references to Tesoro's lawsuit and the fact that the 2009 Act became effective the day before trial was set to begin, evidences the type of improper taxpayer targeting identified by the *Carlton* court.

512 US at 32-33, 114 S.Ct. 2018. (emphasis added)

There can be no question that EHB 2075 is a direct response to refund requests or that its emergency effective date was intended to impact refund litigation. Therefore under *Tesoro's* reasoning EHB 2075 violates due process.

In sum EHB 2075, interpreted according to DOR, deprives Lillian's Estate's vested right to receive a refund under RCW 83.100.130

and of the beneficiaries to receive the full trust remainder, as Fred intended, in violation of the Estate's due process.

**4. EHB 2075 violates the prohibition against impairment of contracts in the State and Federal Constitutions.**

EHB 2075 also violates the impairment of contracts clauses of the state and federal constitutions. Wash. Const. art. I, § 23 (no "law impairing the obligations of contracts shall ever be passed"); U.S. Const. art. I, § 1, cl. 1 ("No State shall ... pass any ... Law impairing the Obligation of Contracts."). The impairment clauses are implicated when (1) a contractual relationship exists and (2) legislation substantially impairs the contractual relationship. *Caritas*, 123 Wn.2d at 402-03.

EHB 2075 if applied, alters Fred's trust because it deprives his beneficiaries of the full value of the remainder and it imposes upon Fred an election he did not make of a fictitious state QTIP. It alters Fred's choices as reflected in the contract he made 30 years ago.

A trust is "a contract between the trustor and the trustee for the benefit of a third party". *In re Estate of Bodger*, 130 Cal.App.2d 416, 424, 279 P.2d 61 (1995). Interests in trusts have long been treated as contractual rights for impairment clause purposes. *See Coolidge v. Long*, 282 U.S. at 594-95 ("The trust deeds are contracts within the meaning of the contract clause of the Federal Constitution. They were fully executed

before the taking effect of the state law under which the excise is claimed. The commonwealth was without authority by subsequent legislation, whether enacted under the guise of its power to tax or otherwise, to alter their effect or to impair or destroy rights which had vested under them.”); *McGrath’s Estate*, 191 Wash. at 5-7-08 (quoting *Coolidge’s* analysis of impairment of trusts with approval, and concluding that taxation of indefeasible insurance policies purchased before the state death taxes applied would violate the contracts clauses of the state and federal constitution); *see also In re Estate of Bodger*, 130 Cal. App. 2d 416, 424, 279 P.2d 61 (1955).

“Alter[ing] its terms, impos[ing] new conditions, or lessen[ing] its value impairs the trust contract.” *Caritas*, 123 Wn.2d at 404 (emphasis added). *See McGrath’s Estate*, 191 Wash. at 496 (“[A]ny subsequent statute passed during the existence of the contracts providing for taxation of that right would, if enforced, impair the obligation of these contracts, for the McGrath Candy Company would then receive less than it was entitled to receive according to the terms thereof.”).

While funding for education is important, “[f]inancial necessity, though superficially compelling, has never been sufficient of itself to permit states to abrogate contracts.” *Carlstrom v. State*, 103 Wn.2d 391, 396, 694 P.2d 1 (1985). EHB 2075 would raise revenues by altering

contracts created years before any standalone tax existed in Washington and violates the state and federal impairment clauses.

**5. EHB 2075 violates equal protection.**

EHB 2075 targets a specific group of taxpayers for taxation, only pre-2005 QTIP trusts. It is intended to claim revenues from a small group of estates that they would be entitled to under *Bracken*. According to the Department, the assets of a federal QTIP trust are subject to Washington estate tax upon the death of Lillian, but the assets of other types of trusts, such as a credit shelter trust, are not—even though the terms of the two trusts may be virtually identical, their beneficiaries may be the same, and the life estate that the second spouse enjoyed in the trusts would terminate in exactly the same way: by his or her death.

There is no rational basis for exempting all trusts established before May 17, 2005, except QTIP trusts, from taxation on the death of the second spouse. No distinction can be drawn between the tax consequences to a QTIP trust and any other trust type.

The Equal Protection Clause (Const. art. I, § 12) and the Fourteenth Amendment to the United States Constitution require that “persons similarly situated with respect to the legitimate purpose of the law must receive like treatment.” *State v. Marintorres*, 93 Wn. App. 442, 450, 969 P.2d 501 (1999) (quoting *State v. Coria*, 120 Wn.2d 156, 169,

839 P.2d 890 (1992)). Economic legislation that neither sets up a suspect class nor affects a fundamental right is subject to the rational basis test. *Schuchman v. Hoehn*, 119 Wn. App. 61, 68, 79 P.3d 6 (2003). The test under rational basis “is not whether the *law* being challenged has a rational basis; it is whether there is a rational basis for the *classification* embodied by the legislative scheme.” *Marintorres*, 93 Wn. App. at 451 (citations omitted, emphasis in original). *Id* (requiring interpreter reimbursement for hearing-impaired convicts, but not non-English speaking convicts, was irrational and violated Equal Protection as applied).

To pass muster, a statutory classification must (1) apply alike to all members within the designated class, (2) be based on reasonable distinctions between those within and those outside the class, and (3) bear a rational relationship to the purpose of the legislation. Tax statutes are analyzed the same way. *See Snow’s Mobile Homes, Inc. v. Morgan*, 80 Wn.2d 283, 287, 494 P.2d 216 (1972) (distinction between similarly situated taxpayers, based only upon timing of assessment for taxation, would constitute denial of Equal Protection; “[i]t is fundamental that all persons within the same class must be treated equally”). Because EHB 2075 arbitrarily exempts other pre-2005 trusts from state taxation - but not pre-2005 QTIPS – EHB 2075 is unconstitutional.

**E. Collateral and Equitable Estoppel Requires Judgment in Favor of The Estate**

Collateral estoppel or issue preclusion prevents the Department from re-litigating *Bracken*. *Hanson v. City of Snohomish*, 121 Wn.2d 552, 561, 852 P.2d 295 (1993); *Rains v. State*, 100 Wn.2d 660, 665, 674 P.2d 165 (1983). Collateral estoppel requires that: (1) the issue decided in the prior adjudication is identical with the one presented in the second action, (2) the final adjudication ended in a final judgment on the merits, (3) the party against whom the plea is asserted was a party or was in privity with a party to the prior adjudication, and (4) the application of the doctrine does not work an injustice. *Hanson*, 121 Wn.2d 15 561. The party asserting collateral estoppel need not be a party in the earlier action. *Lucas v. Velikanje*, 2 Wn. App. 888, 894, 471 P. 2d 103 (1970). All of those factors are present here. The Stipulation in effect demonstrates the identity between this case and *Bracken*. Therefore there is no injustice in binding to DOR to follow *Bracken* in this case.

Further, because of the Stipulation DOR should be equitably estopped from not following *Bracken*. Equitable estoppel generally may apply where “the acts are within the general powers granted to [the government entity].” *Whatcom County Water Dist. No. 4 v. Century Holdings, Ltd.*, 29 Wn.App. 207, 210, 627 P.2d 1010 (1981). DOR has the general power to grant the estate tax refund unquestionably.

The doctrine of equitable estoppel is based on the idea that people should be forced to adhere to the actions or positions they take when others reasonably rely on them and when the repudiation of such actions or positions would harm the other parties. *Brevick v. City of Seattle*, 139 Wn.App. 373, 379, 160 P.3d 648 (2007). Equitable estoppel “prevents a party from making a later claim where (1) one party has made an admission, statement, or act inconsistent with the later claim; (2) another party reasonably relies on the admission, statement or act; and (3) the relying party would be injured if the first party is allowed to contradict or repudiate the admission, statement or act.” *Id.* at 378-9.

In this case, DOR should be equitably estopped because it stipulated that *Bracken* would be “dispositive” as stated in the caption of the Stipulation. The Estate reasonably relied on this and did not bring its case to final judgment. Had it done so EHB 2075 would never apply to the Estate. As a result, the DOR should be equitably estopped from enforcing the statutory amendment against litigants with whom it had stay agreements. All the elements of equitable estoppel are satisfied by the situation in which current litigants find themselves.

**F. DOR violated RAP 18.9(c) by filing a meritless, frivolous appeal solely for the purpose of delay the Estate is Entitled to Attorney's fees and costs.**

On June 25, 2013 this Court denied the Estate's Motion to Dismiss this appeal due to passage of EHB 2075. As discussed in the foregoing sections of this brief that law cannot and does not provide a legal basis for DOR's appeal. As such, the Estate respectfully requests this Court to revisit the Estate's motion to dismiss this appeal as baseless and filed solely for the purpose of delay. The Estate adopts and incorporates here in the argument and evidence submitted in support of that motion. The Estate also renews its requests for attorneys' fees based, as stated in that motion, under RAP 18.1(a) and 18.9(a). RCW 4.84.185 and RCW 34.05.598 also provides a basis for attorney's fees.

**IV. CONCLUSION**

This Court should affirm the Order Granting Summary Judgment in favor of the Estate and reject the DOR's arguments on appeal. This Court should direct the DOR to issue a refund to the Estate within two weeks.

DATED this 10<sup>th</sup> day of October, 2013.

GRAHAM & DUNN PC

By   
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Email: jendejan@grahamdunn.com  
Attorneys for Respondents

**CERTIFICATE OF SERVICE**

I declare under penalty of perjury of the laws of the State of Washington that on this day I caused to be served a true and correct copy of the **Brief of Respondents** and this Certificate of Service by the method indicated below, and addressed as follows:

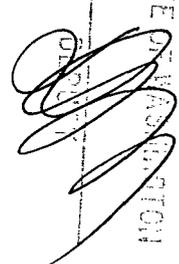
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DATED this 10<sup>th</sup> day of October, 2013, at Seattle, King County, Washington.



Donna Cauthorn

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BY 

Washington State House Floor Debate on Engrossed House Bill 2075  
2013 Special Session for June 13, 2013

[Transcribed from TVW PLAYER BEGINNING MINUTE 5:15]

Forum: Washington State House of Representatives Floor Session on Pending Legislation  
(2<sup>nd</sup> day of 2013 Second Special Session)

<u>Members Speaking</u>	<u>District</u>
Rep. Reuven Carlyle	36
Rep. Terry Nealey	16
Rep. Drew MacEwen	35
Rep. Gary Alexander	2
Rep. Maureen Walsh	16
Rep. Matt Shea	4
Rep. Jamie Pedersen	43

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House Speaker: Sixth order of business. Consent of the House, House will now consider House Bill 2075. Hearing no objection, so ordered. House Bill 2075, Clerk will read.

[. . . regarding amendments, remarks, technical amendments, reservation of comment . . . .]

Speaker: . . . Engrossed House Bill 2075 will be advanced to third reading. Hearing no objections, so ordered. Engrossed House Bill 2075 on third reading and final passage. Remarks. The gentleman from the 36<sup>th</sup> District, Representative Carlyle.

Carlyle: Thank you so much, Mr. Speaker. I rise for the third time in three legislative sessions, Mr. Speaker, to ask you once again to stand in support of the 2006 voter-supported estate tax in Washington State. It was a technical glitch of a lawsuit that had the effect of eliminating the estate tax for married couples only, not for single individuals, and I think that we can all accept that we needed to move forward with a responsible and thoughtful resolution to this particular court case. That's what this legislation accomplishes in order to invest in public education. I'm very appreciative of the hard work from the other side of the chamber to come to a resolution regarding a way to expand the eligibility for an additional deduction for family-owned small businesses. The Senate felt very strongly that that was an important part of a broader package and we were willing to engage with them in a meaningful way so long as we could do so in a way that would make it limited to truly small family-owned businesses, and we came to consensus. I would note that in accepting the Senate's suggestion that we raise the rate on the four highest rates in the estate tax in Washington State in order to make this a revenue-neutral proposal, we did feel that there was value for those small family-

owned businesses that's substantial given the fact that some businesses, warehousing or trucking or capital-intensive businesses, may not have the resources in order to pay the estate tax if that were the case. So this does help small family-owned businesses. It's responsible. It's thoughtful. We worked very hard to come to resolution and I appreciate the acknowledgment of so many members that, that this issue touches a sensitivity on some levels but there is a very real recognition that this investment in public education is essential. This is maintaining the status quo. This is in no way a tax increase in the aggregate level from the current status quo of how our estate tax has been operating for many, many years. We're merely fixing a technical lawsuit and I think we're doing it in a responsible way and, again, I appreciate the hard work of members of the Senate to try to find policy resolution on this issue. Thank you, Mr. Speaker. And I strongly ask for your support.

Speaker: Thank you. Any further remarks. Gentleman from the 16<sup>th</sup> District, Representative Nealey.

Nealey: Thank you, Mr. Speaker, and I still have some concerns about this matter. And the – I want to acknowledge that the bill has been improved. There has been a lot of work, especially in the last day or so between the Senate and the gentleman from the 36<sup>th</sup> and myself in trying to come to a better solution. It was well-stated that the changes to this bill does help small businesses even though there still some, I think, some problem with the language. We come across many small businesses that have capital, for example, buildings, assets and so forth, but not enough cash to pay the bill, to pay the tax bill, and this should help that situation out. However, Mr. Speaker, I still have very grave concerns about this bill's being retroactive. It reaches far back and affects taxes that would be owed from years ago and the problem is that those refunds are due to be paid out very soon. And according to the Supreme Court decision those are rightfully due to those estates. I think that we are bordering on the line of unconstitutionality if this bill passes. And if that were to occur and further lawsuits were to come against the Department of Revenue, i.e., the State of Washington, then we'd not only have to pay those refunds back but with interest and with attorneys' fees. It's been mentioned that these funds go into education. All of the budgets presented in this session fully fund the *McCleary* decision. We don't need this particular amount of funding to come from the *Bracken* decision to fund education, Mr. Speaker. That's a separate issue. What I'm concerned about here is the retroactivity and unconstitutionality of what we're doing today, and for that reason I would urge a no vote. Thank you.

Speaker: Thank you. Any further remarks? Representative Van De Wege.

Van De Wege: Thank you, Mr. Speaker. Please excuse Representative Farrell, Representative Hudgins, and Representative Santos.

- Speaker: Members are excused. The gentleman from the 35<sup>th</sup> District, Representative MacEwen.
- MacEwen: Thank you, Mr. Speaker. Please excuse Representatives Condotta, Crouse, Harris, Holy, Overstreet, Parker, Pike and Rodne.
- Speaker: Members are excused. The gentleman from the 2<sup>nd</sup> District, Representative Alexander.
- Alexander: Thank you, Mr. Speaker. Mr. Speaker, I share the concerns about the retroactivity probably as much as anybody about – I don't like to see decisions made retroactive that basically change the laws and the rules that are being governing our decisions. Now, Mr. Speaker, I am going to support this legislation today for one reason and one reason only. I believe we're going to have to reach some amount of give-and-take to get a budget resolved and out of this body and out of the Senate body. And I've been working with both sides and I believe that a number of the concerns of the Senate regarding this bill have been addressed in this particular striker and I think if this bill goes forward, not just the question of saving, the fact that tomorrow we pay off some paychecks – or some checks, not paychecks but checks, big checks by the way – but, more importantly, if this helps get to a resolved consensus without requiring new tax obligations on our, on our citizens that affect their daily lives then I think it's a move that out to be supported, so thank you, Mr. Speaker.
- Speaker: Thank you. Any further remarks? Lady from the 16<sup>th</sup> District, Representative Walsh.
- Walsh: Thank you, Mr. Speaker. And I certainly appreciate the sentiments from the previous speaker and have tremendous respect for him and all the work that he's done trying to get us out of here this year. But I also think there's a tremendous inherent unfairness with this bill. I just read an article about a family who had \$700,000 taken from – after their mother passed away in 2008. Now they have a son who's recently lost his wife to cancer and he's disabled and they really need the money. We did not take this money lawfully from these people. This money came because somebody boo-booed. I don't care – it was somebody's fault in government, Department of Revenue, but the reality is this money was not obtained lawfully from these families. This money – and my understanding, simplistic as it is, is that it was somewhere hovering around 160 million bucks to take care of this, to nip this in the bud, to be done with this. You know what? Maybe it's rainin'. Maybe it's a rainy day. Maybe we ought to just take 160 million dollars, pay back these families who we took this money from and be done with this. Because guess what? Constitutional issues and everything else aside, reality is this money belongs to those families because it was not lawfully taken from them in the first place. And guess what? We have seen lawsuits increased exponentially in

this place. I've been here 20 years and the amount of lawsuits against this state because of misinterpreted statutes or what have you has really grown exponentially and is *huge* right now. We need to step up, take care of this, pay back these families, and be done with this and not have this issue rear its ugly head continually as these families continue to come back and sue the state because we're going against a decision made by the Supreme Court to refund these families. That's what we should do. We should be done with this. I don't know why we're playing around and saying it's in the interests of education. We're all here for the interests of education and we're all going to do a good job to take care of education again because of a lawsuit! Why do we need to continue to step into this? We need to step away, refund these families, and be done with this for good. This is gonna keep coming back at us, folks. Let's just take care of it and call 'er good.

Speaker: Thank you. Any further remarks. Gentleman from the 4<sup>th</sup> District, Representative Shea.

Shea: Thank you, Mr. Speaker, and I also rise in opposition to the bill today for a couple reasons. Number one, this is isn't the government's money. And number two, we took an oath, Mr. Speaker, we took an oath to defend the state constitution and there's been a long-standing principle in America that we don't pass laws retroactively to hold people accountable for something they never knew they would be accountable for. And, Mr. Speaker, this is about people. If we pass this we are going to be sued as the State Washington. We are going to lose and not only are we going to have to pay back the money for all of that, we are going to have to pay attorneys' fees and we are gonna have to pay interest on that money. And you know where that money's gonna come from? It's gonna come from our children. It's gonna come from our disabled. It's gonna come from our future, Mr. Speaker. And I think that the solution to this entire dilemma is pretty simple. We should just fund education with our first dollar instead of our last dubious penny. Please vote no. Thank you.

Speaker: Thank you. Any further remarks? Gentleman from the 43<sup>rd</sup> District, Representative Pedersen.

Pedersen: Thank you, Mr. Speaker. You know, I actually agree with the gentleman from the 4<sup>th</sup> District about a number of things that he said. This is about people, this is about expectations, and this is about funding education. We're talking today about a group of roughly 70 families who met with their lawyers and made a very deliberate decision to form Qualified Taxable Investment Property Trusts so that they could delay payment of the estate taxes with the full understanding that on the death of the second spouse for federal estate tax purposes the estate tax would be payable with those trust assets. These are people who made very conscious planning decisions to defer payment of the estate tax, not to escape it entirely. Now, it's unfortunate, but not

unprecedented, that in the Legislature in developing the 2005 estate tax legislation that was ultimately approved, as my colleague from the 36<sup>th</sup> noted, by a substantial majority of the voters that there was a technical glitch. And as a result we have a system set up in which we have a profound inequity in treatment between married couples and unmarried individuals – a planning opportunity, my colleagues in estate planning would call it. That means that unless we make some change we're going to be in a situation in our state when only single people need to pay the estate tax because any married couple with the assets will be able to escape our estate tax entirely. And so this bill is about expectations and it's about, in terms of the retroactivity, weighing the expectations of those 70 families that planned to pay the estate tax later against the expectations of more than a million children whose education depends, depends on our doing a better job of funding it. I take issue with the remarks of the gentleman from the 16<sup>th</sup> District who says that we are fully funding education in this budget. We are doing nothing close to funding education amply. We need a lot more money, not just this money, to be applied to education but we'll take this as a step toward that day. On Monday morning I had the pleasure of going with my partner Eric to meet with the principal of Stevens Elementary School where our son Trig will be starting this fall. Our other three sons will be starting in two years. That system needs our help because those kids, like all of the other kids headed to school this fall, need our help. They need us to be doing more to support them. And this is an inadequate small step, but a step in the right direction, toward compliance with our constitutional obligations under the *McCleary* decision to make sure that all Washington kids have a good education. I urge your support.

Speaker: Thank you. Any further remarks? Seeing none, the question before the House is final passage of Engrossed House Bill 2075. The speaker's about to open the roll call machine. [*bell tolls*] The speaker has opened the roll call machine. Has every member voted? Does any member wish to change his or her vote? Speaker's about to lock the roll call machine. Representative Kretz, how do you vote? [*Inaudible*] Speaker has locked the roll call machine. Clerk will take the record, please.

Clerk: Mr. Speaker, there are 53 yea, 33 nay, 11 excused or not voting.

Speaker: Having received a constitutional majority, Engrossed House Bill 2075 is declared passed. [*gavel*] With the consent of the House the bill that was just immediately, that was just worked on, will be immediately transferred to the Senate. Hearing no objection, so ordered. [*gavel*] The House is now at ease subject to the call of the speaker. The House is now at ease.

**\* END of 6/13/2013 Washington State House Floor Debate on Engrossed House Bill 2075 \***

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Washington State Senate Floor Debate on Engrossed House Bill 2075  
2013 Special Session on June 13, 2013

[Transcribed from TVW PLAYER BEGINNING MINUTE 52:05]

Forum: Washington State Senate Floor Session on Pending Legislation (2<sup>nd</sup> day of 2013  
Second Special Session)

<u>Members Speaking</u>	<u>District</u>
Sen. Andy Hill	45
Sen. Mike Padden	4
Sen. James Hargrove	24
Sen. Jim Honeyford	15
Sen. Joe Fain	47
Sen. Sharon Brown	8
Sen. Sharon Nelson	34
Sen. Michael Baumgartner	6
Sen. Rodney Tom	48
Sen. John Braun	20

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Senate President: . . . and the bill be placed on final passage. Hearing no objection, so ordered. [*gave!*] Senator Hill.

Sen. Hill: Usually I work with my soccer teams. I wait when they quiet down. Mr. President, this bill clarifies some language in our Washington estate tax. It truly does close a loophole that was determined by Supreme Court order. In short order, it basically requires that marital trust property be included in the estate for the purposes of the estate tax. We also make some tweaks to the estate tax code. We provide a deduction for family-owned businesses and we adjust the – we now allow the \$2 million exemption to grow indexed at inflation on an annual basis. And it also increases the top four rates in the estate tax to make the entire change revenue-neutral. So I think what you have here is, we close a loophole, we give some needed relief to our family businesses, and in doing all of this we free up \$160 million. Now, according to my calculations we've got about \$1.9 billion of taxes coming in this year more than we did last year – I mean last biennium. When you add in our hospital safety net, our cost-shift to Medicaid expansion, and now this \$160 million, we now have roughly \$2.7 billion more than we had last biennium – 2.7 billion. And yet we have a budget that was pushed over here from the other side that could only get 700 dol- -- 700 million into basic education. And we have a Governor saying that we need to raise more taxes to get a billion into basic education. I hope that now with \$2.7 billion we can finally get a budget that both houses and the Governor can agree on that'll get us a billion dollars. Now this body has passed out two budgets that got a billion

into *McCleary*. And we have threats of shutting down the government because we need more taxes because we can't get that billion dollars. So I fully expect every dollar of this \$160 million to go to basic education, and I ask you for your vote. Thank you.

President: Senator Padden.

Sen. Padden: Tim. Evening's late but I did want to point out a few concerns I have, and certainly have tremendous respect for the gentleman from the 45<sup>th</sup> District in trying to put together a budget, certainly not an easy thing. But I have questions specifically about this. Frankly, I don't think we'll ever see this money. I think the Supreme Court will rule that this legislation, as far as the retroactivity, is unconstitutional. Certainly that was the opinion of the estate section of the Washington State Bar Association, and it wasn't just an opinion by a majority of those members, it was the unanimous opinion of each and every member of that estate tax division. I mean, the whole idea of retroactivity generally is considered unfair. And I mean I think you go back to Roman law or common law or whatever and the idea is, I mean, you ought to know what the rules are at the time that you take action, and here we're changing the rules after the fact. So certainly those estates that were involved before 2005, I just don't see the court's upholding this. I know that this new bill is an effort to have some policy changes that I support but, again, to do that they are raising the rates even more. And we have the highest estate tax rates in the country already. So I just have a lot of concerns with this. This bill did not have a hearing in the Ways and Means Committee and the last bill on this subject that had a hearing in the Ways and Means Committee didn't have enough votes to get out of the committee. So I mean, I think there's a lot of problems with this legislation and I would urge a no vote.

President: Senator Hargrove?

Sen. Hargrove: Well, thank you, Mr. President. Thank you very much. Just to make a few comments here. First of all, I'm very glad we're finally getting this particular piece done. This was \$160 million bogey that got handed to us by the court after we came here. We didn't get this news on this case until after we came to session and, if you remember, we were about 900 million in the hole on our current law budget when we came to session and then of course we knew we were going to have to make an investment in *McCleary* of, you know, whether it's a billion or a little less or a little more. Some people think more. Some people think a little less will do this year. The point is that our current law budget was upside-down by over a billion after this *McCleary* – after this estate tax decision came to us early in session. So, no matter how you look at the numbers and the math, you have to make real cuts. Things happen in our budget that are caseloads that grow, there's inflation, there's other things that are in current law that you have to make

decisions on. And we went through a long and a difficult decision-making process in our Senate budget even to end up coming up with a number of cuts that were very painful for some people that we've talked about in order to try to make these things balance. So I'm, you know – I appreciate the, the comments here. I'm very glad we're getting this particular piece done. I think it's going to be part of our go-home budget at some point in time, and I – believe me – I am very much looking forward to *going home*. Thank you very much. Encourage your support.

President: Senator Honeyford?

Sen. Honeyford: Thank you, Mr. President. A point of inquiry.

President: What is your point of inquiry?

Sen. Honeyford: Thank you, Mr. President. I notice tonight that several people have addressed the President of the Senate as President Pro Tem and I noticed that I know in the past the tradition of the Senate has been we address the President Pro Tem as President. And when we had the Vice-President Pro Tem we addressed him as President. Would you give us some direction, please?

President: Well, thank you for asking, Senator Honeyford. I believe the correct address to the presiding officer is 'Mr. President.' The President Pro Tem is elected by all the members of the Senate and, in the absence of the Lieutenant-Governor, serves in the role as President. So I believe the correct address to the presiding office is 'Mr. President.' Thank you for inquiring, Senator Honeyford. Senator Fain?

Sen. Fain: Thank you, Mr. President. I belatedly move that we suspend Rule 15 so that the chamber may be past 10:00 p.m.

[Laughter]

President: Senator Fain has moved that we suspend Rule 15 so we may belatedly be in session past 10:00 p.m. Hearing no objection [*clamor*] – so retroactively. Hearing no objection, so order. [*gavel*] Senator Brown.

Sen. Brown: Mr. President, thank you. I stand in opposition of the bill, particularly because it's retroactive and, as an attorney, I just cannot support retroactivity. The bill allows the Department of Revenue to tax a transaction with a tax that was not enacted until *thirty years* after the transfer was completed. This bill is an unconstitutional attempt to change the terms of the contract entered into prior to the enactment of Washington's estate tax and for that reason I stand in opposition of this. Thank you, Mr. President.

President: Senator Nelson?

Sen. Nelson: Thank you, Mr. President. And I stand in strong support of this legislation. The people of this state were very, very clear. They wanted an estate tax. They supported taxing the wealthiest estates for our children's education and their future. And when the Supreme Court threw a loop into the estate tax in January of this year we began our discussions and it became very clear that, if we are going to have a strong financial foundation to fund *McCleary*, we needed to take this action. We need to preserve not only the 160 million that go into refunds immediately but funding for the next biennium and the next for our kids. And ladies and gentlemen, in eight hours and fifteen minutes without this legislation we begin to refund to the wealthiest estates in Washington. We begin to mail out checks for funds that could be used for our kindergartners, for our third-graders, for everything that we believe in for our kids' futures. We need this action now. It is on the brink of being too late and in eight and a half hours, eight and a half hours, these checks go in the mail. We need this action tonight. Thank you.

President: Senator Baumgartner.

Sen. Baumgartner: Well, thank you, Mr. President. You know, I rise with some concerns and ask for a no vote. You know, I agree that the spirit of what was passed back in 2006 intended for folks to make these payments but the fact of the matter was the rule of law says that they shouldn't have. And I really think this is a trust issue with governance that if the law says that you shouldn't pay it, and you deserve to get it back, it's a fundamental trust in government to have the government reach back and take that money. You know, I think there's a lot of things going on in society right now that are eroding trust in government and I just think it's a wrong precedent for us to set here. This is a very potential slippery slope towards other times that we – you know, this is, is necessary money because we decided to greatly increase the size of government and government spending and this is a necessary accounting measure, I guess, to do that. To some extent I look at this as a short-term loan with a very high interest payment because I do expect the State is going to lose this lawsuit and these folks will get that money and will get at - be costing our future funds. But, you know, I just ask everybody to think about this basic trust in government. Does government do what it says it's going to do? And I don't think we're doing that here today. So spirit of 2006, yes. But this, this basic sense that these folks, under the rule of law, shouldn't have paid this money, and we should respect that. So I ask for a no, Mr. President.

President: Senator Tom?

Sen. Tom: Thank you, Mr. President. I would ask members to vote yes on this. I was here back when we passed this out of the Legislature. I'll be honest, I did vote no on this, and back in 2005. And the reason why I voted no is because

I don't think the estate tax is great on a state-by-state basis. I am a firm believe that an estate tax is a good tax on a national basis. I think, you know, one of the things as a country that probably we should do is have a stronger estate tax at the national and then that to fund maybe some of our higher-ed institutions, higher-ed research, and that. I don't think on an individual state basis it's a great idea. But I do think it was very clear when we passed that that the intent wasn't to have couples and singles taxed differently. I think everybody – one, that's not a logical means of having taxation policy and it surely wasn't the intent of the Legislature. So think that this is a good bill. But, more importantly, we need to make sure that if we have now \$160 million more than we did in the original Senate budget, if we were able to put a billion dollars for *McCleary* and we continue to hear off this Senate floor that education is our paramount duty and we need more money for education to make sure that our kids are prepared for a 21<sup>st</sup> Century economy, we need to make sure that this 160 goes to education, goes to *McCleary*, so that we can fund our constitutional and moral obligation. Thank you, Mr. President.

President: Senator Braun?

Sen. Braun: Thank you, Mr. President. I rise in somewhat conflicted support of this bill. You know, this bill attempts to fix the result of *Bracken* by expanding the definition of a transfer, a move that raises serious constitutional challenges under the contract clause of both the U.S. and the Washington State Constitution. It also attempts to apply a death tax enacted in 2005 to trusts created prior to 2005, again raising serious constitutional concerns. These are serious issues that deserve our careful consideration. Unfortunately, the dominant narrative has been one that pits millionaires against our children and it's created a political atmosphere that limited discussion on the issues of constitutionality. As a result, I believe we're abdicating our responsibilities to the courts. However – this is why I'm conflicted –, this has offered the opportunity to do something I believe of great benefit to our state's small family businesses that are disproportionately affected by the death tax. This bill creates a small family business deduction for our smallest employers that I believe are critical to our economic future, and our greatest risk to failure during intergenerational transfer. It does this in a revenue-neutral fashion and has high sideboards to prevent the gaming of the system. It's an important reform that was reached by finding common philosophical ground and then working in good faith to craft a compromise that met that shared vision. So, although I have great concerns about the constitutionality of this *Bracken* fix, I do trust our court system to address the issue. And I'm very proud of the good work this bill does for our smallest employers. Thank you, Mr. President.

President: The question before the Senate is final passage of Engrossed House Bill 2075. The Secretary will call the roll.

Secretary: *[calls roll]* . . . . Mr. President, 30 ayes, 19 nay.

President: Having received the constitutional majority, Engrossed House Bill 2075 is declared passed. The title of the bill will be the title of the Act.

*[gavel]*

*[procedural matters]*

**\* END of 6/13/2013 Washington State Senate Floor Debate on Engrossed House Bill 2075 \***

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## Transcription of Washington Legislative Activities re *Bracken*

**Date:** May 31, 2013

**Forum:** Senate Ways and Means Committee - Public Hearing (and Subs) on **Senate Bill 5939**

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**Chairman:** Committee will come to order. All right, let's quiet down. . . .

. . . .

*[Discussion of SB 5939 begins at RecordPlayer position 15:50:455]*

**Chairman:** . . . We now move to a public hearing on Substitute Senate Bill 5939.

**Roe:** Good morning, Senator Hill, Members of the Committee. I'm Juliana Roe, Committee Staff, and with your permission, I'll go over both 5939 and 5940, both of which are estate tax bills.

Washington created a stand-alone estate tax in 2005 that is imposed on every transfer of property located in Washington at the time of death of the owner, including real property as well as intangible assets owned by Washington residents. The Washington estate tax is based on the federal taxable estate as it existed on January 1<sup>st</sup>, 2005. Two million dollars may be deducted from the taxable estate. That's our \$2 million threshold, and there's also a farm deduction that may be taken for those who qualify. After subtracting any applicable deductions the remaining Washington taxable estate is subject to a graduated rate schedule ranging from 10 to 19%. Federal law allows certain transfers of property to marital trusts to qualify for the unlimited marital deduction, even though the surviving spouse does not have a total control of that property. This property is referred to as a Qualified Terminal Interest Property – as you all know it, as a QTIP. The QTIP is included in the federal taxable estate of the surviving spouse upon the surviving spouse's passing, and under both federal and state law, the personal representative of the first spouse to die can make the QTIP election to qualify the property for the marital deduction. Since the Washington estate tax did not take effect until May 17<sup>th</sup>, 2005, an issue arises as to whether the Washington estate tax applies to a QTIP when the first spouse passed away prior to that date, that May 17<sup>th</sup>, 2005. The State Supreme Court in *Bracken* recently held that a federal QTIP election made prior to that date is not subject to the Washington estate tax when the surviving spouse passes away after the May 17<sup>th</sup>, 2005 date. The court stated that the estate tax is triggered by the transfer of the decedent's property in QTIP so the actual transfer occurs when the first spouse passes away. They further held that because the surviving spouse is an income

submit written comments or to have further discussion about what we think is a much better bill in 5940.

And thank you. I'd be happy to answer any questions.

Shirk:

Chairman Hill, members of the Committee, I'm Drew Shirk with the Department of Revenue, here to testify in support of the portions of Senate Bill 5939 that address the clarification issue that was created by the court decision on the *Estate of Bracken* and the major impact that that decision had on the Washington estate tax and transfers.

Basically, the *Bracken* court ruled that the Washington estate tax does not apply to the surviving spouse interest in a qualified terminable interest, a QTIP. As a result of this ruling, Washington estate tax now contains an unintended consequence, where married couples, properly executing their trusts, do not owe an estate tax, where everyone else does. For the Department, that fundamental equity issue is the concern, and to restore that equity is important, that we believe is good tax policy.

The Department does not take a position as to the rates and to the thresholds, but, as those are policy decisions for you to make. But we do note that if the *Bracken* issue is not addressed, there would be a \$160 million revenue impact in the current biennium.

Based on the court's actions – recent court actions – the Department believes it is necessary to begin processing refunds beginning June 3. What's important with those refunds process is that, once we have made those, and we have cleared the estate, that you cannot recover those taxes. So the ability of the Legislature to retroactively clarify would be limited in those cases and could create more inequity.

In closing, we do support the clarification. I would note on Senate Bill 5940, the Department does not take a position on the other changes in the bill, but we do note, and we do raise concern that it does not clarify the estate tax for the future. It maintains the fundamental inequity that the *Bracken* court created in its decision, and we want to note that concern to you.

I'd be happy to answer any questions you may have.

Chairman:

Senator Conway.

Conway:

My question is really about the refunds and when they'll start. You say June 3. I've heard others question that, that you have more flexibility in terms of when you would start the refunds. What, is that a legal issue here with the Department, that they have to do this by June 3, or is this just a goal for the Department?