

NO. 70514-8-I

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

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

Respondent,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Appellant.

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**DEPARTMENT OF REVENUE'S SUPPLEMENTAL REPLY  
BRIEF**

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ROBERT W. FERGUSON  
Attorney General

David Hankins, WSBA No. 19194  
Senior Counsel  
Charles Zalesky, WSBA No. 37777  
Assistant Attorney General  
Revenue Division, OID No. 91027  
P.O. Box 40123  
Olympia, WA 98504-0123  
(360) 753-5528

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## I. INTRODUCTION

The Green-Eldridge estate contends that “three live issues” remain to be decided in this appeal that are not controlled by *In re Estate of Hambleton*, 181 Wn.2d 802, 335 P.3d 398 (2014). Resp. 2d Supp. Br. at 1.

The three issues identified by the Estate are:

1. Whether, under established U.S. Supreme Court precedent, it is constitutional to tax QTIP passing at the death of the second spouse.
2. Whether the Court’s holding in *Hambleton* that the 2013 Act met the due process rational basis test was wrongly decided and should be overruled.
3. Whether the Department should be prohibited from denying the Estate’s refund claim as a sanction imposed under CR 11 and RAP 18.9(a).

Of these three issues, only the third remains a “live” issue to be decided in this appeal. The Court in *Hambleton* decided the first issue identified by the Estate, holding that a “transfer” subject to the amended Washington estate tax is “broadly construed” and that “taxing QTIP assets upon the death of a surviving spouse qualifies as an excise tax” imposed on the transfer of the assets. *Hambleton*, 181 Wn.2d 832-33. The second issue (overruling *Hambleton*’s due process holding) is an issue that should be decided by the Supreme Court if it agrees to accept discretionary review of this appeal. Until then, the Court’s holding that the 2013 Act meets the due process rational basis test should be followed.

The third issue is the only issue that requires this Court's attention. The Supreme Court in *Hambleton* did not address any claim for sanctions under CR 11 or RAP 18.9(a). However, there is no merit to the Estate's "sanction" argument for the reasons explained in the Department's reply brief. *See* App. Reply at 22-24. For the reasons already briefed, this Court should reject the Estate's contention that it is entitled to an \$8,629,164 tax refund as a sanction against the Department for filing this appeal.

## II. ARGUMENT

### A. **Under *Hambleton*, It Is Constitutional To Tax QTIP Passing At The Death Of The Second Spouse.**

In *Hambleton*, one of the estates (the Macbride estate) argued that no "transfer" occurs when the second spouse dies and the QTIP passes to the remainder beneficiaries. *See* Macbride Estate's Supplemental Reply Brief (relevant excerpt attached as Exhibit B to the May 19, 2015, declaration of Rhys M. Farren). The Macbride estate argued that a "transfer" in the constitutional sense required the decedent to have the power to dispose of the property. The estate also argued that United States Supreme Court cases relied on by the Department were distinguishable and did not hold that a "shift in economic benefit" in the property at death was all that was constitutionally required for imposing an indirect estate tax on the transfer of that property. *See* Farren Decl., Ex. B., pp. 2-11.

The Supreme Court in *Hambleton* rejected the Macbride estate's constitutional arguments and agreed with the Department. *Hambleton*, 181 Wn.2d at 832. The Court explained that “[a]n estate tax is an excise tax because the tax is ‘not levied on the property of which an estate is composed. Rather it is imposed upon the shifting of economic benefits and the privilege of transmitting such benefits.’” *Id.* (quoting *West v. Oklahoma Tax Comm’n*, 334 U.S. 717, 727, 68 S. Ct. 1223, 92 L. Ed. 1676 (1948)). The Court also explained that the term “transfer” is broadly construed under relevant U.S. Supreme Court precedent, and the power to impose an estate tax on the transfer of property at death “extends to the creation, exercise, acquisition, or relinquishment of any power or legal privilege which is incident to the ownership of property.” *Id.* (quoting *Fernandez v. Wiener*, 326 U.S. 340, 352, 66 S. Ct. 178, 90 L. Ed. 116 (1945)). Applying these principles, the Court in *Hambleton* concluded that:

[T]axing QTIP assets upon the death of the surviving spouse qualifies as an excise tax. The surviving spouse had the economic benefit of using the income from QTIP assets during his or her life. And, upon the surviving spouse's death, the remainder beneficiaries of the trust gained a present interest in the assets and income. The death of the surviving spouse brought about “changes in legal relationships affecting property.” Therefore, the Estate and Transfer Tax Act is an excise tax and not subject to article VII, section 1 [of the Washington Constitution].

*Id.* at 833 (quoting *Chickering v. Comm’r of Internal Revenue*, 118 F.2d 254, 258 (1st Cir. 1941)).

The Court in *Hambleton* addressed the “transfer” issue as part of its analysis of the Macbride estate’s “uniformity” argument.<sup>1</sup> The Court applied U.S. Supreme Court cases that broadly construe “transfers” subject to estate taxation. Under this precedent, an unapportioned, indirect, excise or transfer tax may be imposed on the “shift in economic interest” in property that is brought about by the death of a person with some beneficial interest in the property. It follows that taxing QTIP passing under I.R.C. § 2044 is constitutional because the death of the surviving spouse brings about a shift in the ownership and beneficial interest in the QTIP assets.<sup>2</sup> *Hambleton* is controlling on this point. There is no “live” issue to be decided in this appeal.

In any event, if the Court is inclined to consider and decide the Estate’s claim that it is unconstitutional to tax QTIP passing at the death of the second spouse, it should reject the argument for the reasons set out in *Hambleton* and in the Department’s opening and reply briefs. *See* Br. of App. at 9-13 and 28-41 (explaining that it is constitutional to tax QTIP

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<sup>1</sup> Article VII, section 1 of the Washington Constitution provides that “[a]ll taxes shall be uniform upon the same class of property within the territorial limits of the authority levying the tax.” This uniformity requirement applies to “direct” taxes imposed on property, not indirect taxes such as the Washington estate tax. *Hambleton*, 181 Wn.2d at 832.

<sup>2</sup> A QTIP trust creates a life estate for the benefit of the surviving spouse and a future interest in the assets for the remainder beneficiaries. When the second spouse dies and his or her life estate is extinguished, the remainder beneficiaries receive a present interest in the QTIP, including the right to the income generated by the property. Consistent with the cases cited and discussed in *Hambleton*, Congress and the states are permitted to treat the shift in the economic benefit occurring at the death of the second spouse as a “transfer” subject to estate tax.

when the second spouse dies under established U.S. Supreme Court precedent); App. Reply at 5-13 (explaining that the Estate's reliance on *Coolidge v. Long*, 282 U.S. 582 (1931), is misplaced). Simply put, the shift in economic benefit of QTIP resulting from the death of the second spouse satisfies the requirement of a "transfer" in the constitutional sense. The Estate's claim to the contrary is incorrect as a matter of law.

**B. The Due Process Holding In *Hambleton* Is Binding In This Appeal.**

The Estate's argument that the *Hambleton* Court's due process holding was incorrectly decided and should be overruled is not a "live" issue in this appeal. *See* Resp. 2d Supp. Br. at 4-8. Rather, that holding "is binding on all lower courts in the state." *1000 Virginia Ltd. P'ship v. Vertecs Corp.*, 158 Wn.2d 566, 578, 146 P.3d 423 (2006). The Estate can make this argument to the Supreme Court if that Court agrees to accept discretionary review of this appeal.

**C. The Court Should Reject The Estate's Assertion That The Department Should Be Sanctioned For Filing This Appeal.**

For the reasons previously briefed, the Court should reject the Estate's argument that the Department's appeal was frivolous or that the Department should be sanctioned for providing the Legislature with time to address the fiscal and tax policy issues caused by *In re Estate of Bracken*, 175 Wn.2d 549, 574, 290 P.3d 99 (2012). *See* App. Reply at 22-

24. Taxes collected from the Washington estate tax are used to fund education. RCW 84.100.220, .230. In light of the state's paramount duty to adequately fund education, it was appropriate for the Department to give some deference to the Legislature and to permit the Legislature a reasonable opportunity to consider whether to change the Washington estate tax code to prevent QTIP from escaping tax. *Cf., McCleary v. State*, 173 Wn.2d 477, 517, 269 P.3d 227 (2012) (the Legislature has "general authority to select the means of discharging" its duty to address "the difficult policy questions inherent in forming the details of an education system"). Furthermore, the estate tax code does not establish a specific time period within which the Department must process refund claims. *See* RCW 83.100.130. Thus, the Department had the prerogative to wait for guidance from the Legislature before processing any *Bracken*-generated refund claims. *Cf., Hillis v. Dep't of Ecology*, 131 Wn.2d 373, 388 n.8, 932 P.2d 139 (1997) (when the Legislature intends for agency action to be performed in a set amount of time, it provides a time limitation in the statute).

The Department's decision to wait five months for the Legislature to take action was not illegal or unfair. Rather, it was a prudent exercise of agency discretion. Consequently, the Department should not be sanctioned, and the Estate should not be awarded a tax refund to which it is not entitled under the estate tax code as amended by the 2013 Act.

### III. RESPONSE TO ESTATE'S MOTION TO REMAND TO THE TRIAL COURT

The Court should deny the Estate's motion to remand this case to the trial court for the purpose of taking additional evidence on the merits of the case under RAP 9.11(a). *See* Resp. 2d Supp. Br. at 8-10. Remand under RAP 9.11(a) is not appropriate for at least two reasons. First, the Estate's argument that additional evidence will be helpful "to fairly resolve the Due Process issues on review" is an issue that should be addressed by the Supreme Court if it decides to accept discretionary review of this appeal. Until then, additional proof of facts is not needed to fairly resolve the merits of the single remaining "live" issue in this appeal. Consequently, the requirements under RAP 9.11(a) are not met.

Second, the proof that the Estate is seeking to obtain on remand is irrelevant to the due process issue decided in *Hambleton*. The Estate asserts in its motion that the trial court should be asked to make "an original determination . . . of the Due Process validity of the retroactive aspects of the 2013 Amendments" and to provide "an original interpretation of the estate tax statutes in light of the legislature's purpose to conform the meaning of 'transfer' to 'its broadest possible meaning consistent with established United States supreme court precedents.'" Resp. 2d Supp. Br. at 8-9. Both of these questions are questions of law that are reviewed de novo on appeal. Specifically, the constitutionality of

a statute is a question of law, *Amunrud v. Board of Appeals*, 158 Wn.2d 208, 215, 143 P.3d 571 (2006), as is the interpretation of a statute. *Dep't of Ecology v. Campbell & Gwinn, LLC*, 146 Wn.2d 1, 9, 43 P.3d 4 (2002). Remand for the purpose of allowing the trial court to decide legal issues is unnecessary, inconsistent with the purpose of RAP 9.11, and would be a waste of valuable judicial resources. The motion should be denied.

Although not part of its motion for remand, the Estate also suggests elsewhere in its supplemental brief that the Legislature should have amended the estate tax code years earlier than it did. *See* Resp. 2d Supp. Br. at 7-8. From this premise, the Estate speculates that discovery “may well show that the State Supreme Court was under-informed of the relevant facts, through no one’s fault, but to the detriment of a full Due Process analysis.” *Id.* at 8.

The Supreme Court was not under-informed. In *Hambleton*, the Court correctly recognized that the 2013 Act was a response to *Bracken* “in which we narrowly construed the term ‘transfer.’” *Hambleton*, 181 Wn.2d at 809. *Bracken* was issued in October 2012 and became final in January 2013 when the Court denied the Department’s motion for reconsideration. Prior to *Bracken*, there was no need for the Legislature to amend the estate tax code. Although there had been a few estates that had argued that QTIP was not subject to tax under the 2005 version of the

estate tax code (including the plaintiffs in the consolidated Bracken case), the Department had successfully defended each of those claims up until the date *Bracken* was decided. See, e.g., *Hambleton*, 181 Wn.2d at 816 (summary judgment awarded to the Department in the Macbride case). No court or administrative agency had ruled in favor of any estate on the tax treatment of QTIP until *Bracken*. It was the Court's narrow interpretation of the term "transfer" in *Bracken* that created the fiscal and tax policy dilemma the Legislature sought to cure.

The relevant facts pertaining to the *Bracken* decision and the Legislature's response were well-known to the Supreme Court when it decided *Hambleton*. It would serve no useful purpose to remand this case for discovery on facts and legal claims made prior to the date *Bracken* was issued. The Legislature was not attempting to fix a "drafting error" that occurred in 2005; it was attempting to fix the Supreme Court's narrow interpretation of the statute that occurred in 2012. Thus, to the extent the Estate seeks to bolster its motion for remand with the arguments contained at pages 7 and 8 of supplemental brief, the Court should deny the motion. Discovery of irrelevant facts is not a basis for remand under RAP 9.11(a).

#### **IV. CONCLUSION**

The Estate has identified one issue—its "sanction" argument—that is truly "live" and requires this Court's attention. For the reasons set out

above, the Court should decline to address the other issues identified by the Estate, and should deny the Estate's claim that the Department's appeal was frivolous and subject to sanctions under CR 11 or RAP 18.9(a).

RESPECTFULLY SUBMITTED this 17th day of June, 2015.

ROBERT W. FERGUSON  
Attorney General



DAVID M. HANKINS, WSBA No. 19194  
Senior Counsel

CHARLES ZALESKY, WSBA No. 37777  
Assistant Attorney General  
Attorneys for Appellant, OID No. 91027

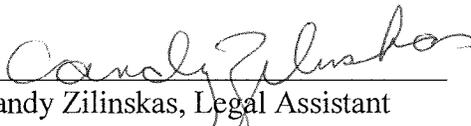
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Rhys M. Farren  
Dirk Giseburt  
Richard A. Klobucher  
Malcom Moore  
DAVIS WRIGHT TREMAINE LLP  
1201 Third Avenue, Suite 2200  
Seattle, WA 98101-3045  
[rhysfarren@dwt.com](mailto:rhysfarren@dwt.com)  
[susanbright@dwt.com](mailto:susanbright@dwt.com)

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

DATED this 17th day of June, 2015, at Tumwater, WA.

  
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Candy Zilinskas, Legal Assistant