

# Capital gains tax is legal in Washington, Supreme Court rules

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The Temple of Justice, where the state Supreme Court is housed, in Olympia. (By Albert James / The Spokesman-Review) [Buy this photo](#)

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OLYMPIA — Washington's new capital gains tax is legal.

The state Supreme Court issued a ruling Friday reversing [a Douglas County Superior Court](#) decision last year that struck down the tax because the judge characterized it as an income tax, not an excise tax as argued by the state.

In a 7-2 decision in the case Chris Quinn v. State of Washington, the Supreme Court determined the tax is a valid excise tax under Washington law.

The Legislature in 2021 passed a 7% tax on the sale of stocks, bonds, businesses and other investments, if profits exceed \$250,000 annually. Exceptions include the sale of real estate, livestock and family-owned businesses.

Many thought of the capital gains case as another opportunity for the state Supreme Court to rule on the constitutionality of an income tax in Washington, which has been struck down many times before. Because the court found the tax is a valid excise tax, however, it did not revisit old rulings regarding the constitutionality of income taxes.

Supporters say the tax is a step toward ensuring lower-income taxpayers pay a smaller share of their income on taxes than high-earners. Opponents of the tax say it is an income tax, which is unconstitutional in Washington.

In a decision written by Justice Debra Stephens, the court found the tax is consistent with precedent that recognizes excise taxes as those levied on actions associated with property ownership, such as selling or exchanging, rather than taxes levied on the property itself.

“The capital gains tax is appropriately characterized as an excise because it is levied on the sale or exchange of capital assets, not on capital assets or gains themselves,” Stephens wrote in her brief.

The 14th Amendment of the state’s constitution says all taxes in the state must be “uniform upon the same class of property.” Property is defined as “everything, whether tangible or intangible, subject to ownership.”

The Supreme Court has shot down other attempts from the Legislature and voters to pass taxes on earnings. In the 1933, the state Supreme Court struck down a voter-approved graduated income tax because it considered income to be property, which needed to be taxed uniformly.

In this case, the court found the new capital gains tax is not considered a property tax, and therefore is not subject to the uniformity requirements as used in previous cases.

“This court’s decisions from that era still shape Washington tax law today,” Stephens wrote in her brief, adding the capital gains tax must be understood in the context of Washington’s tax history.

In the decision, Stephens cites historic cases, like the 1933 case, as leading to Washington being the most regressive tax code in the nation, where low learners pay a higher share of their income as compared to high earners.

Attorneys for the state [argued in a hearing in January](#) that the capital gains tax does not apply simply by owning capital assets. Instead, it is applied once they are sold. It only applies to the amount of gain from the sale, not the value of the asset itself.

Thus, the state said, it is an excise tax, which are levied on specific goods, such as cigarettes, alcoholic beverages or gasoline.

“A person can own limitless stocks or bonds, can own them for years. They can increase dramatically in value,” attorney for the state Noah Purcell said in the oral arguments. “The person owes no tax that whole time. It is only when they sell the assets that they owe that tax.”

The court agreed with this analysis. Stephens wrote in her decision that no one owes the tax merely by owning the asset. Instead, they only owe it when the asset is sold or exchanged.

“One can own capital assets without ever owing the tax,” Stephens wrote.

Attorneys for the opponents of the tax, on the other hand, said a property tax is one that falls upon the owner simply because they own the property, and an excise tax is imposed on a voluntary act of the taxpayer. The capital gains tax does not apply to every sale or transfer of capital assets, and an individual doesn’t need to voluntarily act to be subject to it, according to the opponents.

Former Republican Attorney General Rob McKenna said during oral arguments that every other state treats a capital gains tax as an income tax, not an excise tax.

“There is nothing new under the sun when it comes to this issue,” McKenna said in January. “Trying to call an income tax an excise ... has been tried several times in this state by the state Legislature, and it’s been struck down every time.”

Stephens wrote in the ruling that other taxes that have been tried in court have applied to the taxpayer’s net income and weren’t reliant on any specific activity, such as selling or exchanging them.

“Here, the capital gains tax does not capture net income sources but instead narrowly applies to capital transactions resulting in realized gains,” Stephens wrote.

The new tax, which the state will begin collecting next month, would affect fewer than 1 in every 1,000 residents, but it is estimated to bring in about \$500 million to be spent on child care and early learning.

State lawmakers are currently in the process of writing their budgets for the next two years. The Senate Democrat proposal, released Thursday, assumed the capital gains tax is constitutional.

Senate Ways and Means Committee Chair Sen. Christine Rolfes, D-Bainbridge Island, said in a statement Friday that the court’s decision provided certainty to budget writers.

“We are eager to expand support for working families, and today’s ruling locks in dedicated funding to increase access to affordable early learning and childcare,” she said.

Top Republican on the Senate Ways and Means Committee Lynda Wilson, R-Vancouver, said in a statement Friday that the taxpayers should be “on their guard” because Democrats may try to make this tax apply to more people over time.

“That is not what our state needs, especially with an economic downturn on the horizon,” Wilson said. “There’s too much government greed already.”

House Democrats will release their budget proposal on Monday.

Two justices, Sheryl Gordon McCloud and Charles Johnson, dissented. In a dissenting opinion, Gordon McCloud wrote that capital gains are considered income, and in Washington, income is considered property.

“A Washington ‘capital gains tax’ is therefore a property tax,” she wrote.

The tax is measured by the amount of income gained by a transaction, Gordon McCloud wrote, and therefore, it is an income tax.

Further, she said that it is not up to the court to determine how to make Washington’s tax structure less regressive. It is up to the Legislature or the people through a constitutional amendment.

“The duty of the judiciary when faced with a direct conflict between a statute and the constitution is to uphold the constitution,” Gordon McCloud wrote.

Opponents of the tax say this decision could lend itself to other income taxes in Washington.

Jason Mercier, of the conservative Washington Policy Center, called the ruling “unreal.” Mercier said in a statement Washington’s capital gains tax is the “first standalone excise tax on capital gains income on the planet” as every other tax jurisdiction considers capital gains taxes income taxes.

“With this ruling, the rules surrounding income taxes in Washington are now unclear,” Mercier said. “What will be the next type of income tax to be redefined by lawmakers? It is up to the voters now to respond.”

Supporters of the tax said the court’s decision was a win for children, as most of the revenue from the tax will go toward education, child care and early learning.

Attorney General Bob Ferguson said in a tweet that the decision is an important win for education in Washington that protects significant funding for child care and early education.

“We have a long way to go, but when we insist that everyone – including the wealthiest Washingtonians – pay what they truly owe in taxes – we begin to undo decades of

racism and disinvestment that hurts families, communities, and small businesses,” said Treasure Mackley, executive director of invest in WA Now, a progressive group that signed on in support of the capital gains tax.

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