

# Wash. Capital Gains Tax Foes Pivot To Voters To Kill The Tax

By Maria Koklanaris

Law360 (March 22, 2024, 6:55 PM EDT) -- Opponents of the capital gains tax in Washington state, having been frustrated in attempts to quash the tax in the courts, have now moved to trying to do so at the ballot box, hoping that voters, not the courts, will have the last word on the tax.



A ballot initiative that would repeal Washington state's controversial tax on capital gains has garnered more than 400,000 certified signatures, sending the fate of the tax to the November ballot. (AP Photo/Elaine Thompson)

Few issues in Washington have been as hard fought over in the last five years as the capital gains tax **enacted in 2021** and fully implemented in 2023. The 7% tax on capital gains exceeding \$250,000 has been the subject of years of litigation over whether it is legal, and even whether it should be characterized as an income tax or an excise tax.

Proponents of the tax were hoping the issue would be settled once the U.S. Supreme Court **declined in January** to review a state Supreme Court decision declaring the tax valid. But Initiative 2109 to repeal the tax **has garnered** more than 400,000 certified signatures, sending the fate of the tax to the November ballot, and setting up yet another contentious campaign.

Proponents of the tax will be fighting to save what they consider a vital source of revenue that funds education and child care. The tax brought in nearly \$900 million in its first year according to the state Department of Revenue, a figure that exceeded expectations. Proponents will ensure that voters

understand the stakes, said Melinda Young-Flynn of the left-leaning Washington State Budget and Policy Center.

"Initiative 2109 is a cynical attempt by some ultra-wealthy people and special interests to undo this policy so that rich people can keep hoarding their wealth," Young-Flynn told Law360. "It slashes almost \$900 million per year in funding for early learning, child care and schools in Washington while making our tax code more inequitable."

Meanwhile, Invest in Washington Now, a group largely funded by unions including the Washington Education Association, is gearing up for a Tuesday meeting where it will work on its efforts to defeat Initiative 2109.

"We're not backing down," the group's executive director, Treasure Mackley, said. "We know that Washington needs the capital gains tax, and we know that Washingtonians support the capital gains tax."

But tax opponents such as state Rep. James Walsh, R-Aberdeen, who sponsored Initiative 2109, and Rep. Chris Corry, R-Yakima, say the state has plenty of money and can afford to fund education without the capital gains tax.

"I-2109 won't 'steal' anything from [Washington] public schools. Zero. Nada," Walsh told Law360 on Friday. "The state's operating budget is in surplus. That surplus, plus a few smart priority decisions, can 'buy' I-2109's reform without touching K-12 school funding. At all."

In a statement, Corry contended that the tax has "already led companies and individuals to leave Washington," citing as an example Amazon founder Jeff Bezos, who has announced plans to relocate to Florida.

"Unfortunately, initiative opponents are resorting to scare tactics, claiming that a vote to repeal the capital gains tax is a vote to roll back critical investments in our schools," Corry said. "But that is simply not true."

Walsh, Corry and other Republicans backed four other tax initiatives in the current legislative session. Two others, I-2117, which would repeal the state's cap-and-trade program, and I-2124, which would allow employees to opt out of the state's long-term care insurance program and payroll tax, are on the November ballot with Initiative 2109. But it may be I-2111, which the Washington Legislature approved overwhelmingly in early March and thus becomes law without a vote of the electorate, that may have the most influence on what happens with the capital gains tax, close observers told Law360.

Washington has never had a personal income tax, and I-2111 is another big step toward ensuring that it never will. The initiative passed the House 76-21 and the Senate 38-11 and does not need the approval of Democratic Gov. Jay Inslee. I-2111 "prohibits the state, counties, cities, and other local jurisdictions from imposing or collecting income taxes, defined as having the same meaning as 'gross income' in the Internal Revenue Code," according to language from the initiative.

Tax opponents, mainly Republicans in the majority-Democratic Legislature, hailed the passage of I-2111, while Democrats, saying the state wasn't planning to create a personal income tax, mostly shrugged. But for opponents of the capital gains tax repeal initiative, getting the income tax referendum approved by the Legislature, and thus off the ballot, may have helped their cause, observers said.

"If that is a standalone issue on the ballot, it is more palatable to voters to vote against that initiative," said Michelle DeLappe, tax partner at Fox Rothschild LLP. "They can say, 'well, that's a narrow tax, that's just affecting rich people.'"

However, DeLappe said, if the income tax ban were alongside the capital gains tax repeal, voters — who are strongly against a personal income tax in the state — might be inclined to view the two as a package.

"Then I think the voters' antipathy toward having a general income tax in this state would possibly bleed over into capital gains because they would look at 'oh, yeah, capital gains — that is a type of income,'" DeLappe said. "To everyone except for certain judges and legislators."

DeLappe referred to the position of tax proponents that the capital gains tax is not an income tax but an excise tax. The Washington Supreme Court majority adopted that position and the U.S. Supreme Court declined to review it.

Jason Mercier, vice president and research director at the libertarian-leaning Mountain States Policy Center, said there is a certain irony in that. With the passage of I-2111, there shouldn't be a need for I-2109, Mercier said. He said he doubts that would happen anywhere else, because all other states with capital gains tax, as well as the federal government, consider them taxes on income.

In other places, an income tax ban would foreclose the ability to tax capital gains, Mercier said. But in Washington, the capital gains tax is not considered a tax on income but on the transaction that is made. The income tax ban does not affect it, and so there is a separate initiative just to repeal the capital gains tax, he said.

"The problem is, because of that Supreme Court ruling, Washington isn't like anywhere else in the world," Mercier said.

--Editing by Tim Ruel and Roy LeBlanc.

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