

# Appendix B: Income Tax Constitutional Issues

## History of Court Decisions

In 1933, the Washington State Supreme Court overturned a graduated state income tax that had been proposed by initiative and approved by more than 70 percent of the voters. *Culliton v. Chase*, 174 Wash. 363, 289 P.2d 81 (1933). Many people assume that *Culliton* is still good law and that Washington courts would reach a similar decision today. If that is true, a constitutional amendment would be necessary before the state could impose any income tax other than a flat tax on gross income at a rate no more than 1 percent. However, there is ample reason to believe that a modern income tax, established by the Legislature or by the voters, would now be upheld. The basic reason is that *Culliton* was based on an earlier Washington case which the State Supreme Court clearly misread. More importantly, the earlier case was based on a line of United States Supreme Court cases that have subsequently been reversed. Our Court would likely take a “clean slate” approach to the income tax today.

*Culliton* relied on *Aberdeen Savings & Loan Assoc. v. Chase*, 157 Wash. 351, 289 P. 536, *reh'g den.* 157 Wash. 391, 290 P. 697 (1930). The lead opinion in *Culliton* stated that *Aberdeen* had held that income is property, that a tax on income must therefore be uniform, and that a nonuniform income tax violated Washington’s Constitution. As it happens, *Aberdeen* did not decide that income was a form of property, at least not under the Washington Constitution. In *Aberdeen*, the plaintiffs challenged a tax on savings and loan associations that was higher than taxes on banks organized as corporations. The primary thrust of the savings and loans’ challenge was that under a United States Supreme Court ruling, *Quaker City Cab Co. v. Pennsylvania*, 277 U.S. 389 (1928), the differential tax treatment of corporate and non-corporate businesses violated the U.S. Constitution’s Equal Protection Clause. The plaintiffs also argued that *MacAllen Co. v. Massachusetts*, 279 U.S. 620 (1929), prohibited state taxation of federal bond interest. *Aberdeen* never discussed the issue of whether an income tax was equivalent to a property tax. In fact, the majority opinion in that case assumed that the proposed levy was an excise tax on the privilege of financial institutions to engage in business. Because the Attorney General and a 1930 Advisory Tax Commission were concerned that *Aberdeen* might be misunderstood as disapproving an income tax, they expressly asked the Court to clarify whether a determination that income was or was not property was necessary for a resolution in that case. While denying reconsideration in *Aberdeen* and a companion case, the Court said that its opinions “were rendered with a view to determining the questions present by the cases at bar, and those questions only.” 157 Wash. at 392. The Court also stated that its decisions were based on United States Supreme Court precedents relating to the Equal Protection Clause. *Id.* Both in the main *Aberdeen* opinion and in the opinion denying the petitions for rehearing, the

Court took pains to emphasize that it was issuing limited rulings based on the U.S. Constitution and was not ruling on the character of the corporate tax under Washington's Constitution.

In decisions rejecting later income tax proposals, the Court repeated the mistaken view that it had treated income as property in *Aberdeen*, readopted that approach in *Culliton*, and therefore regarded the matter as settled. (See, e.g., *Jensen v. Henneford*, 185 Wash. 209, 53 P.2d 607 (1936); *Power Inc. v. Huntley*, 39 Wn.2d 191, 235 P.2d 173 (1951)). But in fact the matter had not been settled in *Aberdeen*, and the United States Supreme Court decisions relied upon in *Aberdeen* have all been reversed. Today there are only two states (Pennsylvania and Washington) whose courts have not reversed earlier decisions treating income as property. In all other states where this issue has been considered, the income tax is treated as a form of excise tax or in a category of its own. Accordingly, there is a reasonable likelihood that if the Washington State Legislature or voters enacted an income tax today, Washington's courts would approach the issue with a fresh view and might very well decide the matter in a manner consistent with the dominant view in other states with similar constitutional provisions.

*(This discussion has been prepared by Committee member Hugh Spitzer, based on his article, A Washington State Income Tax—Again? 16 U. Puget Sound L. Rev. 515 (1993).)*