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THE CONSTITUTIONAL ASPECTS OF WASHINGTON'S FISCAL CRISIS

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I

The State of Washington today is critically hampered in the financing of its government at all levels by a fiscal straitjacket that has been materializing over a period of nearly thirty years. Legal and financial expedients of the last decade signify its increasing pressure. Government so confined obviously cannot respond to basic social and economic changes, and many such changes are observed in Washington. Dramatic increases in population, the trend toward increased industrialization, growing urbanization throughout the state, the development in the Puget Sound area of one of the nation's major urban complexes with accompanying expansion of the role of governmental services in the life of the regional culture, all cumulate and interact.[1] Meanwhile, the state's legal and administrative mechanisms for drawing upon economic capacity no longer suffice to underwrite needed governmental services. The aim of this paper is to sketch the

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[1] These trends and their proportions are familiar. It is worth noting, however, that the State of Washington grew 37% in population during the decade 1940-1950. Since 1950 the growth rate has slowed substantially. But the impact upon governmental services of the growth that was concentrated in that decade is significant. Population density (1950) was estimated at more than twice that of other Pacific Northwest states. In that same year, Washington's percentage of urban population was at the national average. Notable also was the 1950 census disclosure that 54% of the population of the state had been born in some other state or in a foreign country, more than twice the national average. These data are cited in PACIFIC NORTHWEST ASSEMBLY, THE STATES IN THE PACIFIC NORTHWEST 7 (1957). A working paper submitted to the Washington State Tax Advisory Council by James K. Hall, Professor of Economics, University of Washington, cites these growth rates, 1930-1957: Aggregate personal income 417%; per capita personal income 203%; tax revenues 1034%.

scope and nature of the current problem, to explore the legal rigidities that dominate it, and to suggest the apparent steps prerequisite to realistic, durable and workable solutions.[2]

There are many indications of the dimensions of the problem. The general fund of the state treasury, the fund used to finance the major proportion of general services rendered by the state government, is seriously overdrawn. Careful analysis of its apparent condition, and a projection to the end of the current biennium, show the probability of an accumulated overdraft of between 80 and 100 million dollars.[3] The likelihood is that this overdraft can be financed for the immediate future, as it has been in the recent past, by interfund loans and advances from other funds and accounts in the treasury.[4] But this practice cannot continue indefinitely. Unless corrective action is taken, the condition of the fund will grow progressively worse and more difficult to correct. The point is that the state has not in recent years, is not now, and cannot in the foreseeable future, support expenditure commitments from the authorized revenues of the fund. Past efforts to avoid inevitable charges by postponement have made showings of improvement, but such showings were temporary.[5] There is no avoiding responses to the social and economic forces that control the scope and volume of public services. Needs postponed, whether

[2] At the writing of these comments, the Washington State Tax Advisory Council, established by the Legislature (Wash. Laws 1957 c. 291; RCW 43.38) is engaged in a comprehensive review of the problems of financing state and local government in Washington. Much of the material used here was prepared for the use of the Council and is contained in various working papers which will be cited. These were made available to the authors and were used through the courtesy of the Council.

[3] The general fund consists of a general, or generally available account, and more than thirty special, or dedicated, accounts. However, the balances of the fund as a whole are available for authorized expenditures from the fund. The special accounts were added to the fund in 1955 and 1957. RCW 43.79. The current overdraft is in the general account; balances in the special accounts are sufficient to show a cash balance for the fund as a whole without, however, taking contingent liabilities into consideration. The estimate of overdraft at the end of the biennium is for the general account.

[4] WASHINGTON STATE TREASURER, MONTHLY REPORT 142-43 (June, 1958), reports, as of the close of business June 30, 1958, a consolidated gross cash balance of $102.4 million, of which $82.7 million is held in current investments. This balance, of course, does not take into account items in transit. Interfund loans and advances are authorized by RCW 43.84.100.

[5] For example, the overdraft at the end of the 1949-1951 biennium of $44.1 million was reduced slightly to $43.6 million by the end of the 1951-1953 biennium. During the next period, 1953-55, the "deficit" increased to $58.1 million and then declined at the end of the 1955-1957 biennium to $29.3 million. General fund appropriations for the 1957-1959 period exceed originally estimated revenues by some $33 million. Because of general economic conditions, it is improbable that the original revenue estimate will be realized. A "loss" of $20 million is a reasonable estimate. Meanwhile expenditure requirements respond to population, price levels and economic conditions. "Recession" conditions, for example, could easily produce an appropriation deficiency of $20 million in public assistance.

for more adequate services or for the capital plant to house them, simply accumulate to become all the more urgent and perplexing. Inattention or wishful thinking will not turn back the clock to a more comfortable, less puzzling set of issues. Nor will these problems solve themselves. The central issues must be faced.[6]

Local government problems are counterparts to the state's, and in a genuine sense they are state problems as well. The cities report current deficiencies, after pushing legally available revenue sources to the practical limit, of a conservative twenty-five million dollars a year exclusive of capital outlay. High crime rates reflect serious undermanning of police protection. Underwriters' surveys in a number of communities have resulted in higher fire insurance rates due to the need for improved fire protection.

The counties of the state report need for an over-all increase of five per cent in their general revenue. This does not include the increase in statutory compensation of elective county officials that will occur in 1959 and is estimated to produce, over-all, an additional million dollars in annual expenditures. Nor does it consider the operating deficits that have accumulated in twelve counties.[7] The problems of the school districts can also be regarded as state government concerns. For all practical purposes, the state revenue system underwrites whatever costs the school districts are unable to meet, when the items involved are regarded as justified educational costs.[8]

Precise financial statistics of revenue, expenditure and debt for the state and its subdivisions as a whole are hard to come by. Those available provide, at best, no more than a shaky basis for interpretations and evaluations. The reasons for this obscurity are far too numerous and too complex to explain in detail here. The fact remains that literally no one is now in a position to know definitely the present financial condition of the state's governments, or to determine the total amount expended for public services from taxes, special revenues, service charges, local fund income and a variety of other sources. However, there is no conclusive evidence that the people of the state of Washington, as compared with other states with similar personal income and public service levels, are making disproportionate

[6] This is discussed in SUBCOMMITTEE ON LOCAL GOVERNMENT FINANCE, WASH. STATE TAX ADVISORY COUNCIL REPORT TO THE TAX ADVISORY COUNCIL, 8-12 (May, 1958); *Id.* Appendix II, items 5, 6.

[7] *Id.* at 13-18; *Id.* Appendix III, items 2, 4.

[8] This is done by legislative appropriation for the support of common schools. Funds are distributed under a complex formula. RCW 28.41.

payments toward the support of state and local government.[9] On the other hand, it can be said with all emphasis that the legal framework within which the governmental fiscal system must operate makes a flexible and realistic financing of government next to impossible.

The difficulties and awkwardness of the present system will intensify in the years ahead. The need for greater flexibility is underlined by a ten-year projection, indicating that the need for services, assuming the present quality level, will probably grow at two and a half times the rate of growth of the yield of the present revenue system.[10] The basis for this estimate was the state's general fund and related operations, particularly those involved in the financing of the common schools. The reasons for the ten-year trend are found in the more rapid growth of the school age and over-65 age groups in the population than of the income-producing age groups. The growth of the yield of the present revenue system will fall far behind the increase in service requirements. The estimated result, assuming no change in the revenue system, and no change in the scope and quality of services rendered, would be a general fund overdraft for the 1967-1969 biennium of some 300 million dollars. This does not include any accumulations of overdrafts for previous fiscal periods.[11] Projections of this sort are always open to debate because, if they are to be made at all, they involve some choice of population and income assumptions and one or another method of estimating.[12] However, it does seem

[9] The following are taken from a working memorandum, Comparative Statistics on Tax Collections of State and Local Governments, prepared by Professor Hall for the Tax Advisory Council. They are for 1953, the last year for which state and local government data are available. State and local tax collections as a percentage of personal income received in the state were estimated at 7.9%, as compared with a 48-state average of 7.4%. Other states were California 8.2%, Oregon 8.2%, Idaho 9.2%, Minnesota 9.1%, Iowa 9.4%, and Wisconsin 8.7%. Washington was twenty-sixth or about the median in the ranking of all the states.

[10] This projection was prepared for the Tax Advisory Council by Philip Cartwright, Associate Professor of Economics, University of Washington, and was summarized by him at a panel discussion at the Institute of Government, University of Washington, July 7, 1958.

[11] In this projection, estimates were made for the biennium 1967-1969 only. On this basis a difference of $325 million appeared between estimated revenue yields and estimated appropriation requirements. Under the same assumptions, intervening bienniums would also show overdrafts of increasing proportions, which could not be liquidated within the present revenue of the general fund. These overdrafts would accumulate to some amount, for those purposes not estimated, which would be outstanding at the beginning of the 1967-1969 biennium. The $325 million estimated for that biennium therefore would be added to the total already accumulated.

[12] Significant assumptions were: *Population,* no net in-migration; *industrial employment,* no industrial growth in the next decade comparable to that of the aircraft industry in the last decade; no *major depression; services and service cost,* a fairly constant level of service quality, rendered to more people (particularly in the school-age and over-65 age groups) at higher costs reflecting a general increase in the costs of personal services and construction throughout the economy.

beyond question that state and local government, over the next decade, will be drawing a larger proportion of individual income. Only the size of this larger proportion is a matter for speculation.

The general fund projection, of course, does not take several other areas of governmental activity into account. There is the matter of highways, for example. No ten-year estimate of requirements is at hand. Nevertheless, all indications are that highway revenues will have to be increased in rate to support not only the back-log of needed construction, but to keep pace with future increases in traffic density. As for local government needs, they can be expected to grow at least at a rate approximating that projected for the state general fund. Increasing density of population in the urban and growing "exurban" areas will mean more service requirements and higher service costs. Some of this increase can be handled on a non-tax, or service charge, basis. But the cost will be there nonetheless.[13]

Altogether, the probability is strong that, of the estimated income received by individuals in the state, the eight to eight-and-one-half per cent now paid in state and local taxes could increase over the next decade to twelve per cent. This statement needs a number of qualifications because it assumes a given rate of increase in service costs against a much lower rate of increase in personal income in the state. Nevertheless, it poses an urgent question: In view of the probability that a larger proportion of income received by individuals will be applied to the support of state and local services over the next decade, what changes in the legal framework for state and local government are needed to permit sound and workable readjustments?

In passing, it should be noted that this prospect is not unique to the state of Washington. It is nation-wide.[14] Since World War II state and local expenditures have risen at a much higher rate than those of the federal government. So also has bonded debt. The Tax Foundation's projections for the nation as a whole are quite consistent with those

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[13] Cities in Washington make wide use of the fee for service for the support of such services as water, sewer, garbage, and refuse disposal and the like. See RCW 35.21.130-.150 (garbage collection and disposal); RCW 35.67.190 (sewers). Closely related, of course, is the special assessment method for financing capital improvements frequently employed through the local improvement districts. RCW 35.43.040.

[14] TAX FOUNDATION, INC., PROJECT NOTE No. 43; THE FINANCIAL CHALLENGE TO THE STATES 10 (March 1958). Heller, *Financing State-Local Government in an Age of Expansion*, State Government, June, 1957, p. 140. Professor Heller cites the following indices of growth for state-local changes and for federal changes: *State-Local* (1946-1956), revenues 250, expenditures 324, gross debt 306; *Federal* (1947-1957), cash receipts 188, cash expenditures 212, gross debt 105. *Id.* at 141.

for Washington. Other estimates support the anticipated trend.[15] The Tax Foundation reports many states engaged in analyses of their revenue systems.[16] Washington's problem with respect to basic social and economic trends is only a part of a nation-wide concern. In the legal and fiscal aspects of the problem, however, Washington stands apart.

The rather different situation in Washington has a background. Prior to 1930, the state was a property tax state. Governmental services were for the most part underwritten by levies upon property.[17] The adoption of the "forty-mill" limitation policy, first by initiative and later by a constitutional amendment, forced a shift to other sources of revenue.[18] The state became in effect an excise tax state, relying more heavily upon this form of taxation than any other. For all practical purposes, the property tax has been abandoned as a source of state government support.[19] At the same time, the levying capacity of local government upon property was frozen by levy limitations. But the assessment level, while constitutionally defined as fifty per cent of actual value, was left open to erratic and so far uncontrollable

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[15] TAX FOUNDATION, *op. cit. supra* note 14, at 31. A ten-year projection in 1955 by the Tax Foundation anticipated a possible 1965 level of state-local expenditures about two thirds over the 1953 level. However, in the three years 1953-1956, the expenditures level rose by almost half of the projected increase to 1965. Heller, *op. cit. supra* note 14, at 141, remarks that it would seem reasonable to expect a state-local total of expenditures for all states of at least 60 billion dollars by 1965. While this would be a 100% increase over 1953, it would be only a 50% increase over 1956. This rate may prove an underestimate, since the increase 1946-1956 was more than 200 per cent. It may be estimated that, nationwide, this trend would leave a gap of from $9 to $10 billion to be filled in 1965. If this gap were to grow at an even rate, this would mean a $1 billion increase in taxes a year over the period 1956-1965.

[16] TAX FOUNDATION *op. cit. supra* note 14 *at* 20. Thirty-one studies were authorized in 1955 alone in twenty-seven states. From January, 1954, to December, 1956, reports were issued by fifty state tax study groups. Thirteen additional ones were issued in 1957.

[17] John F. Sly, Professor of Politics, Princeton University, cites the trend in his *Property Taxes in the State of Washington,* WASH. STATE RESEARCH COUNCIL POCKET REPORT SERIES 15 (1958). The property tax as a percentage of all state and local taxes in Washington was: 1931, 80%; 1936, 46%; 1941, 32%; 1955, 28%.

[18] The limitation was Initiative 64 adopted in 1932. Re-enactments occurred in successive bienniums until the adoption of amendment 17 to the constitution in 1944. See note 179 infra.

[19] U.S. BUREAU OF THE CENSUS, DEPT. OF COMMERCE, COMPENDIUM OF STATE GOVERNMENT FINANCES IN 1957, 52 (1958), table 38, "Per capita amounts of selected financial items, by states; 1957" lists the following per capita collections of general sales or gross receipts taxes by states: Washington, $74 per capita the highest state against a forty-eight-state average of $20.27; next in order, West Virginia, $68.44; California, $44.79; New Mexico, $43.44; and Michigan, $43.38. The two-mill levy now used for state purposes was until recently a county levy allocated to general public assistance purpose. Both the support of recipients and the two-mill levy were transferred to the state. This move increased the yield of the tax and simplified financing by making proceeds available throughout the state rather than in the county of collection only. RCW 74.04.150-.151.

variations.[20] As a result, the locally administered services that could not be supported from the available property tax levies had to be maintained from service charges or from locally imposed excise taxes. The latter, of course, were limited in application and rate, both by practical considerations and by the use of excises on the part of the state.[21] Basic services increasingly become a state responsibility. In time, all public assistance was assumed by the state government as a directly administered and financed state service. Roads and highways became a charge against special highway revenues; the local road system became, for the most part, a secondary state highway system, and while county administered, was largely supported by distributions of state-collected taxes. Public education was progressively recognized as primarily a responsibility of the state. Public education costs that could not be met from the limited school district levies became a charge upon the state treasury. The result is that the state of Washington, in 1953, showed state taxes as 69 per cent of the total of state and local taxes in the state, as compared with a national average of 50.5 per cent. The Washington proportion appears to be the highest of any of the higher income states.[22]

It was noted earlier that the state is attempting to operate within an extraordinarily rigid legal and fiscal framework. The framework itself is familiar; its principal dimensions apply to any governmental jurisdiction. At the outset, of course, there is the allocation of service responsibilities between the state and its political subdivisions. The assumed objective is to lodge in local government the responsibility for those activities that are governed primarily by local needs, that require local policy control, that fall within local administrative capacity, and that can be supported by local fiscal capacity. State services are regarded as reflecting the other side of the coin. They are governed primarily by state-wide needs, they require uniform state-wide policy control, they necessitate administrative methods

[20] For discussions of efforts to control the local assessment level, *infra* at 269-274. For the results of a state-wide survey of variations, SUBCOMMITTEE ON REVENUE AND TAXATION, WASH. STATE LEGISLATIVE COUNCIL, 1953-1955 BIENNIUM, A STUDY OF REAL PROPERTY ASSESSMENTS IN THE STATE OF WASHINGTON (1954).

[21] A catalogue of potential revenue sources for local government with an identification of those legally pre-empted by the state and those pre-empted for all practical purposes by rate levels is contained in SUBCOMMITTEE ON LOCAL GOVERNMENT FINANCE, *op cit. supra* note 6, Appendix I, item 5.

[22] Statistics for the United States and for the Pacific Northwest states are in PACIFIC NORTHWEST ASSEMBLY, *op. cit. supra* note 1, at 9, table 6. Data for 1953 showed the percentage distribution of revenue collection for Washington as state, 68.7% and local 31.3%. The percentages after distribution to the level administering services were state, 40% and local, 60%.

beyond the scope of the local units, and they require a broad base of fiscal support. An intermediate variety of services consists of such activities as the mandatory support of essentially state services by the counties, and the local administration, with partial state financing, of some services that are mixed state and local.[23] Generally, each service level needs to have the considerations mentioned above substantially in balance, and it needs the types of institutions and operating mechanisms that can administer its service responsibilities effectively.

Next, each service level needs the administrative and managerial means to assure well-coordinated, productive service operations. This involves capacity to plan, budget, and coordinate and control related governmental operations so that operating effectiveness can be realized. The capacity depends upon a form of organization that makes management possible; the avoidance of essentially independent, self-sufficient activities within the structure becomes highly important. Also important is the legal authority to employ such appropriate managerial methods as budgeting, accounting, operating controls and the like. Related to this is the capacity to develop a competent staff of administrators and employees to perform operating activities.

A third category of considerations is in the area of fiscal methods. Governmental jurisdictions, if they are to operate effectively, need to be able to use their fiscal resources as a whole in a flexible, well-planned way. The practice of breaking up total fiscal capacity into a variety of dedicated or earmarked sources of revenue, each assigned to some favored service, results in inbalance and inflexibility. Some services are well-supported; they may have more income than they need. Others are "poor relations"; whatever the need, the income is always short. These relationships are frozen into the treasury structure by the pattern of revenue dedications. No room is left for managerial flexibility. Another restrictive arrangement seen in Washington is that of conducting operations on a special or "local" fund basis in a way that does not involve appropriations, general operating coordination nor even the processing of transactions through the treasury.[24] Such practices inevitably stunt the develop-

[23] Familiar examples of essentially state services administered at the county level are elections, certain public record functions such as land records, and courts of record. Mixed services include the common schools and local highways.

[24] Most of these seem to have at least general statutory authorization. The largest of them use the funds of the State Liquor Commission, RCW 43.66.060-.070, and those connected with the administration of unemployment compensation by the Department of Employment Security, RCW 50.16. For another type of activity, see the State Apple Advertising Commission, RCW 15.24.

ment of the quality of public management that present day government requires.

Fourth, and most frequently considered, is the matter of the revenue system, the scheme by which the cost of governmental operations is charged back to the income-producing capacity of the state. What is important here is that legislative bodies at each level have the breadth of judgment, the policy-making capacity, to distribute governmental costs over the available tax base in the manner that public attitudes regard as most equitable and most conducive to economic well-being. The point is put in these terms because, whatever the several groups in the society regard as desirable or undesirable about a tax structure, their varying attitudes and values will, in the long run, come to some equilibrium, an acceptable working formula which reflects a balance among competing pressures. The important consideration is that this competition of alternatives be permitted to work in a flexible way, and that choices be broad enough that the working formula can embrace as large a variety of balancing factors as may be necessary to reach negotiated agreement. The democratic process should be permitted to function.

Attention now turns to the question of the constitutional and related legal limitations, if any, that make intelligent adjustments to changing conditions difficult. What is emphasized here is the availability of the legal capacity to exercise choice—to respond to changing conditions intelligently. No emphasis will be put upon policies, either those now pursued or those that in the future might be deemed desirable.

With respect to the allocation of service responsibilities, the state seems to be relatively free from serious difficulties. To be sure, the constitution appears to contemplate that the state shall not assess taxes for local purposes, and that it shall not support purely local services.[25] But no real difficulty need arise over these provisions so long as revenue-raising capacities are broad enough in local government to cover the administrative responsibilities assigned by the legislature. Provisions of this sort rarely cause rigidity in themselves. They can cause difficulty when other provisions, usually relating to taxation, channel unusual pressure in their direction.[26]

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[25] WASH. CONST., art. XI, § 12. See the discussion *infra* at 262-269.

[26] States that have resorted to rigid limitations upon the yield of the local property tax have encountered constitutional difficulties in the replacement of the revenue loss for the support of purely local services. When locally available revenues are sharply reduced, some services, such as roads and public welfare, can be moved to the state

The constitution does place limitations upon capacity to revise the organization of local government.[27] The alteration of county boundaries raises special questions.[28] The need for such alteration has not arisen in sharp and acute form, but it may well do so. In time, urban areas will spill across county lines, leaving the need for a consolidated form of city government in an area located in at least two counties. The time is approaching when the organization of county government will need reconstruction. In Washington, as elsewhere in the nation, the function of the county seems to be changing from the exercise of delegated state functions over an essentially rural area, to the assumption of local service responsibilities, possibly in a proprietary capacity, on behalf of urban clusters of population that are either too small to operate efficiently as cities or which do not require the full range of municipal activities.[29] The reconstruction of the county seems to be the indicated solution for the present profusion, and confusion, of overlapping special and "junior" taxing districts in many parts of the state. State constitutional provisions, therefore, should be revised to clear the way for such a development. Even more serious are the constitutional prescriptions regarding the organization of state government which impose insuperable burdens upon state management. These will be commented upon below.

Under contemporary conditions state and local government is big business. Its operations are large, complex and often technical enough to discourage the interest of all but the most persistent. The comfortable assumption seems to be that somehow the requirements

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level. Others can be regarded as delegated state services, or mixed state-local services such as schools and can be substantially supported by state grants. However, purely local services, for example the types that are rendered in incorporated areas only, are more difficult to justify as state responsibilities. When state-imposed taxes are used for their support, taxpayers who have no access to the benefits are required to share in financial support. On occasion, the argument has been pressed in state legislatures that state-wide taxation to support services rendered only in incorporated areas are not taxes for a public purpose so far as taxpayers in unincorporated areas are concerned.

[27] WASH. CONST. art. XI, § 5, specifies county officials who shall be popularly elected. Amendment 21 authorizing county home rule charters provides that the charter shall not affect the election of prosecuting attorneys, the county superintendent of schools and judicial officers.

[28] WASH. CONST. art. II, § 28, prohibits the enactment of any special law changing county lines. Article XI, § 3, provides for the creation of new counties and probably for the alteration of county lines, under provisions of general law. The only statutory provision relating to a change in county lines, RCW 36.08 (originally enacted in 1891), is limited in application to the transfer of territory where a city's harbor lies in two counties. The definition of applicability is so specific with respect to territorial characteristics as to make this provision for all practical purposes a special, rather than a general law.

[29] California and Utah have enacted interesting county service areas laws. WEST'S ANN. CAL. CODES 25210.1-.90; Utah Sess. Laws 1957 c. 28, at 62.

that are readily accepted for the administration of other large-scale organizations do not apply to the state. There seems to be little public concern over the fact that the state of Washington cannot be managed.[30] The reasons for this situation are many; some derive from the constitution. These deserve identification and explanation. Basic to all other considerations is the fact that Washington is a "long ballot" state. The executive branch, unlike that of the national government, consists of a variety of separately-elected state officers.[31] Among them the governor has only such stature as he can win for himself. He is not the head of the executive branch.[32] Often state officials are not candidates of the same political party. The beginning of this difficulty is in the constitutional provision that establishes these multiple offices. An administrative reorganization that placed responsibilities where functionally they belong would assign several of the officers to subordinate positions within larger operating agencies.[33] In other instances elective officials direct operating programs that should be integrated with the rest of the state government.[34] These elective

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[30] See the discussion in SUBCOMMITTEE ON LOCAL GOVERNMENT FINANCE, *op. cit. supra* note 6, at 22 ff. and Appendix I.

[31] WASH. CONST. art. III, § 1. The legislature is authorized to abolish the offices of lieutenant-governor, auditor and commissioner of public lands (§ 25). The office of insurance commissioner is statutory (RCW 43.13).

[32] WASH. CONST. art. III, § 2, provides that the supreme executive power of the state is vested in the governor. Section 5 provides that the governor may require information in writing from the offices of the state on matters relating to their duties and shall see that the laws are faithfully executed. But these provisions have little practical meaning. The governor cannot discipline an elective state officer. His power of removal does not extend beyond officers appointed by him and not subject to impeachment. RCW 43.06.070. In the administration of the budget, appropriations made to elective state officers are not subject to executive expenditure control, RCW 43.87.010. The assumption is that these officers are directly responsible to the people, not to the governor.

[33] Under contemporary conditions, the treasury operation is regarded as a subsidiary and essentially ministerial aspect of fiscal management. This larger concern is, in turn, only one side of the total management of state government, which needs to be integrated into the governor's authority and responsibility for the administrative operations of the state. The popular election of the treasurer is now an administrative anachronism. The office of secretary of state is almost wholly ministerial. In the state government the directors of the "code" departments exercise much more important policy responsibility. See the comment by Professor Paul Beckett of Washington State College in PACIFIC NORTHWEST ASSEMBLY, *op. cit. supra* note 1, at 29; COUNCIL OF STATE GOVERNMENTS, REORGANIZING STATE GOVERNMENT, 107 ff. (1950).

[34] The two programs that most clearly need operating coordination with the rest of the state government and which are headed by elected officials are natural resources and insurance regulation. In both instances, however, the elective offices could be abolished by the legislature. Note 31 *supra*. Because of the growing importance of public education as a state-directed, if not wholly state-administered, program and because of the proportion of the total state budget it represents, there are impressive reasons for drawing this function into a much closer administrative relationship with the executive branch. In any case, the elective superintendent of public instruction is regarded as obsolete. See for example STRAYER, PUBLIC EDUCATION IN WASHINGTON 1 (1946).

officials are regarded, and they regard themselves, as directly responsible to the electorate of the state. Appropriations made to their agencies are immune from general administrative control. No one is in a position to supervise their actions, to coordinate their operations, or to assure that sound administrative practices are followed. Where they are members of ex-officio bodies, some of which exercise important responsibilities, there is no administrative accountability for their action, and no way of enforcing it.[36] Here is a point of constitutional obsolescence.

With respect to appropriations, article 8, section 4, of the state constitution has an effect that probably was never contemplated. It provides that no monies shall be paid from the treasury or any of its funds except in accordance with an appropriation which shall specify the sum and the object. Payments shall be made from appropriations within one month following the end of the next ensuing fiscal biennium. This provision has had two consequences that seriously impair the executive's capacity to manage the state's affairs. First, its rigidity makes the use of revolving and special income funds extremely difficult. Thus the practice has developed of holding these funds outside the treasury, immune both from the state's accounting system and from executive supervision of their use. Nor are the funds subject to appropriation or any regular legislative review. Estimated transactions of these "local" funds for the current biennium exceed 500 million dollars. There is no central record of their working balances.[37] Another consequence of this provision is the

[36] A partial list of agencies composed in whole or in part of elective officials acting *ex officio* includes the State Canvassing Board, RCW 29.62.100; State Employees Retirement Board, RCW 41.40.030; State Finance Committee, RCW 43.33.010; Voting Machine Committee, RCW 43.35.010; State Capitol Committee, RCW 43.34.010; Toll Bridge Authority, RCW 47.56.020; Board of Natural Resources, RCW 43.30.40; and Law Library Committee, RCW 43.36.010.

[37] There is no statutory requirement that the status and transactions of these funds be reported either to the auditor or the director of the budget. The estimate referred to was developed by the office of the budget and was made available to the revenue administration subcommittee of the Tax Advisory Council. These cases indicate some of the differences that can occur in the treatment of various funds. In Washington Toll Bridge Authority v. Yelle, 195 Wash. 636, 82 P.2d 120 (1938), it was held that the legislature had directed that the funds available for the building of the Narrows Bridge, consisting of the proceeds of the sale of revenue bonds, a federal grant and a Pierce County contribution, were to be held by the treasurer as "not a state fund" and consequently could be disbursed to pay proper charges without a specific appropriation. However, it would seem that these monies were at least funds under treasury management within the meaning of art. VIII, § 4. In its decision the court appears to have made a distinction (646-49) between non-tax receipts, which need not be paid into the treasury, and "taxes," which art. VII, § 6, requires shall be paid into the treasury. However in Ajax v. Gregory, 177 Wash. 465, 32 P.2d 560 (1934), the court had previously held that license fees collected in connection with the control of alcoholic beverages were not taxes levied and collected for state purposes and might be paid into a

convention that the legislature is precluded from authorizing the governor to transfer sums among appropriation items to obtain maximum effectiveness in the use of funds.[38] As a result, interrelated appropriations may prove to be too low in some instances and too high in others. The governor cannot be authorized to equalize them in the light of operating experience. When the next legislature meets, the short appropriations require special deficiency supplementation. To avoid such developments, the legislature is inclined to set some appropriations at levels that should avoid all difficulties, and to employ contingent item appropriations for use if need be.[39] The result is to increase the total of appropriations to a fictitious level. The entire practice is an expedient to avoid the assumed effect of article 8, section 4.

On balance, then, there is little scope for executive management in

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revolving fund, relying upon State v. Sheppard 79 Wash. 328, 140 Pac. 332 (1914). Subsequently in 1941 in Ernst v. Hingeley, 11 Wn.2d 171, 118 P.2d 795 it was held that art. VII, § 6, refers to property taxes and consequently the fact that unemployment compensation payroll collections are not paid into the treasury does not preclude the assumption that they are taxes. Up to this point there was some basis for assuming that a dedicated revenue might be technically outside of the treasury although in the hands of the treasurer as custodian. However, the position of two of the members of the court in Clark v. Seiber, 48 Wn.2d 783, 296 P.2d 680 (1956), should be noted in this connection. They were of the opinion that art. VII, § 6, would require that the proceeds of a property tax levied upon state-equalized assessments for common school support should be paid into the state treasury.

Two other cases suggest that the intent of the legislature rather than the nature of the funds controls the application of article VIII, sec. 4. In Mason-Walsh-Atkinson-Kier Co. v. Department of Labor and Industries, 5 Wn.2d 508, 105 P.2d 832 (1940), the court considered whether a refund of industrial accident contributions, claimed to have been improperly assessed, could be refunded without a legislative appropriation. It was held that since the legislature had provided that accident fund receipts be paid into the treasury, and since appropriations from the fund failed to specify the payment of refunds, a disbursement could not be made. On the other hand, in State Employees Retirement Bd. v. Yelle, 31 Wn.2d 87, 195 P.2d 646, *modified on rehearing*, 201 P.2d 172 (1948), the question was whether refunds of contributions to employees leaving the state service could be made without a specific appropriation. In this instance the legislature had directed that such refunds be paid from a specific fund. It was held that, although the treasurer was the custodian of the fund, he acted as a member of the retirement board and not in his constitutional capacity. The proceeds of the system were not state funds but the property of members of the retirement system. Hence, by legislative direction they may be disbursed for authorized purposes without a specific appropriation.

These complexities argue convincingly for the amendment of art. VII, § 6, and art. VIII, § 4, to permit publicly held and administered accumulations of monies to be handled on a consistent and orderly basis.

[38] It does not appear that any case has been decided by the state courts upon this point. However, in the preparation of the state budget, and in making appropriations, the convention referred to is accepted as required by art. VIII, § 4.

[39] A good example is the use of the contingent receipts fund, RCW 43.79.250, as a treasury receptacle for the receipt of unanticipated federal aid and for the allocation of such receipts for the purposes for which granted. The amount is not high enough to cover all possibilities. Also, it should be noted that a major purpose of the governor's contingent fund is to surmount the difficulties caused by an inability to transfer among appropriations.

the state because of the meaning attributed to the status of the independently elected officials, the constitutional provision relating to appropriation, and other influences and conventions. With respect to the general fund, this point is worth remembering. Constitutional exemptions and a variety of statutory exclusions, some legally necessary for educational, trust and public assistance grant purposes, place an estimated 535 million dollars of the 690 million dollars of appropriations made from the general fund outside the governor's control.[40] Practical considerations, such as the unavoidable necessity of feeding and housing patients in state institutions, reduce the governor's actual control to less than 100 million dollars, or less than 15 per cent, of the amount appropriated.

In the area of fiscal methods, the state has developed the engaging theory that monies received and administered under the state law fall into three different categories. "State" or fully public funds are those wholly subject to the requirements of article 8, section 4. Presumably all revenues generally available for legislative appropriations are paid into the treasury and can be expended only in accordance with an appropriation that meets all constitutional requirements.[41] Then there is a category of "quasi-public" funds such as the income from enterprise activities, the liquor control and toll bridge systems for example, and the collections of the payroll tax for unemployment compensation. These funds are not subject to appropriation.[42] Finally, there seem to be "non-public" funds accruing where the function of the state, or one of its agencies, is that of trustee or agent. Examples are the trust and endowment for such purposes as employees' retirement. These may or may not be administered by the treasurer as custodian, but not in his official capacity as treasurer.[43] The proceeds and transactions are reported as part of treasury operations, but it appears that payments may be authorized by the legislature without resorting to the biennial appropriation method.[44] Some funds in the

[40] The total of 535 million dollars includes transfers to the current school fund (231 million), appropriations for higher education (71.3 million), public school bond redemption (5 million), teachers retirement and pension reserve (20.2 million), elective officials, legislative, and judiciary (7 million). The remainder, a little over 200 million dollars, is the estimated amount of public assistance grants which are substantially controlled by the statutory formula, RCW 74.08.040.

[41] This seems to follow from WASH. CONST. art. VII, § 4. To hold receipts outside the treasury, some specific legislative action, usually a dedication, would be necessary. Once in the treasury, the rigid appropriation requirement applies.

[42] Liquor control, RCW 43.66.060-.070; toll bridges, RCW 47.56.150-.160; unemployment compensation, RCW 50.16.

[43] State Employees Retirement Bd. v. Yelle, 31 Wn.2d 87, 195 P.2d 646, *modified on rehearing*, 201 P.2d 172 (1948).

[44] In this connection see the monthly treasurer's reports, "Statement of Fund Re-

"non-public" category, however, are really operating funds collected, held and expended without recourse to the treasury or to legislative appropriation.[45] These three classifications fail to capture a number of intermediate situations. Probably no classification could. In fact, no one is entirely certain how much money is collected, held and disbursed in one or another official capacity, under the authority of state law.[46]

The dedicating or earmarking of monies deserves a word of comment. Two types of revenue sources are constitutionally dedicated. These are for schools and highways.[47] However, statutory dedications are commonplace. There are at least 160 of these, exclusive of "local" funds held outside the treasury.[48] The purposes of dedication include the support of specific operations, insurance payments, retirement payments, debt service, revolving funds and special transactions accounts.[49] The net effect is the distribution of the monies of the state into so many mutually exclusive pockets that the total condition of the state is obscure. For example, as has been noted, the general account of the general fund is in an overdraft condition amounting, as of the end of the first year of the current biennium, to 37.6 million dollars, which could reach between 80 and 100 million dollars by the end of the current biennium.[50] Meanwhile, special and temporary

ceipts, Disbursements and Transfers for the Month of . . ." In this statement, under the category of Benefit and Retirement Funds both the Accident Fund and the Employees Retirement Fund are listed. See Note 37 *supra*.

[45] Interesting examples are the fifteen certification, inspection or license funds administered through the Department of Agriculture. There are at least seven additional commissions in the general field of agriculture administering their own funds outside of the treasury and without appropriation.

[46] No more than an estimate is possible. The best guess of the total of all state government transactions during the current biennium, including transfers among funds, is 2.3 billion dollars. A net figure would be about 2 billion. Rounded items are general fund and special accounts, 830 million; special funds (at least 130), 964 million; and "local" funds held outside the treasury 508 million.

[47] For schools, the permanent school fund, WASH. CONST. art IX, § 3; for highways, amendment 18.

[48] The revenue administration subcommittee of the Tax Advisory Council noted 131 earmarked revenue funds and 33 special accounts within the general fund. See its *Report* p. 8.

[49] As examples of types; specific operation, the motor vehicle fund (highways); insurance payments, the accident fund (workmen's compensation); retirement payments, state employment retirement fund; debt service, war veterans compensation (bonuses); revolving, public service revolving; special transactions, suspense fund.

[50] This estimate is derived as follows: Assuming that revenue receipts will fall no more than 20 million dollars below original estimates, and that unobligated balances and appropriation deficiencies will balance out, the overdraft would then be about 82 million. The overdraft at the beginning of the biennium, 29 million; excess of appropriations over estimated revenues, 33 million; revenue shrinkage below estimates 20 million. However, should appropriation deficiencies substantially exceed unobligated balances, as now seems likely because of increased costs in public assistance due to unemployment, and should revenue losses exceed 20 million, which is also entirely possible, the overdraft would be increased.

balances in the special accounts of the general fund, which are dedicated, are sufficient to give the general fund as a whole a cash balance of 25.7 million dollars.[51] Remaining funds in the treasury have a working margin of 102.4 million dollars, of which 82.7 million dollars is held in current short-term investments.[52] Thus a so-called "deficit" in the general account of the general fund is not a cash deficit at all in terms of the general condition of the treasury. If the assets of funds held outside the treasury were considered, another picture would emerge. Its proportions must be left to speculation.

Although the state as a whole is solvent, it should not be assumed that no fiscal problems exist. The point of the matter is that one compartment of the treasury receives the pressure of the increasing costs of general services. That is the general account of the general fund. The revenues attributable to this account are not adequate to support the expenditure commitments against it. For the present, the overdraft can be carried by interest-bearing interfund loans and advances within the treasury.[53] This practice cannot be continued indefinitely; neither is it necessary or desirable to liquidate all of the overdraft. An overdraft of some thirty million dollars would appear to be manageable.[54]

On balance, the conclusion is inescapable that the fiscal system of the state needs revising so that all monies collected, administered and expended under the authority of law can be processed through the treasury, so that the fiscal resources of the state as a whole can be utilized in a sound and flexible way, and so that the fiscal condition of the state, inevitably complex, can nevertheless be reduced to a more

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[51] The 1955 legislature abolished ten special funds in the treasury and paid their balances into the general fund. Also it converted twenty-seven separate treasury funds and two local funds into special accounts within the general fund. This was done by the amendment of RCW 43.79. While these special accounts maintain their separate identity in the records of the budget office and the auditor, and their use is restricted to "ear-marked" purposes, their balances are merged with the general account of the general fund in the treasurer's records. Consequently the treasurer's general fund balance can include credits that are only temporary. For example, the present general fund balance on the treasurer's records is made possible by the deposit in the fund of the proceeds of bond sales for construction purposes which proceeds are not wholly obligated. This provides currently some 53 million dollars, of which about 30 million will probably not be expended during the current biennium. All amounts, and those in the text, are derived from the general fund report issued by the director of the budget, as of June 30, 1958.

[52] See the monthly report of the treasurer, June, 1958, *Statement of Fund Receipts, Disbursements and Transfers for the Month of June, 1958,* p. 142.

[53] Authorized by RCW 43.84.100.

[54] The 30 million dollars is an estimate based upon the apparent requirements of the treasury for working cash. If all of the overdraft were to be liquidated over a single biennium the result would be to increase the treasury cash balances available for short-term investment.

understandable statement. This will necessitate the amendment of article 8, section 4 as amended by amendment 11.[55]

There remains the fourth dimension of the context in which state and local government functions. This is taxation. Over the years of its statehood, Washington has accumulated an impressive tangle of constitutional provisions and of judicial decisions applying them. So complex, and so forbidding, is this area of the law that a much more intensive exploration becomes essential. To this attention is now turned.

II

The power of taxation is universally recognized as one of the most important attributes of a sovereign state. Without this power, the state cannot exist. Notwithstanding virtually universal recognition of this proposition, the taxing power of a state is substantially restricted. The first of the operative limitations upon legislative selection of the objects of taxation are economic and social factors, together with their concomitant political pressures. The second of the restrictions, or limitations, are those which are imposed by the constitutions and judicial interpretations of constitutional provisions.

Under the form of government which exists in the United States, the constitutional limitations upon the taxing power of a state, and of its legislature, are also dual. The first are those which inhere in the federal system of government. These are the limitations and restrictions which are found in, or implied from, the Constitution of the United States. The second type of limiting provisions are those in the constitution of the state.

Federal Constitution

The provisions of the Federal Constitution which significantly affect the taxing power of the states are not numerous, but these provisions play an important part in the shaping of state tax policies. Notwithstanding their importance, only a few general comments will be made with respect to the federal constitutional provisions in this review of the constitutional restrictions upon the taxing power in the state of Washington.

The due process, equal protection, and privileges and immunities clauses of the fourteenth amendment of the United States Constitu-

[55] This exploration omits the problems of bonded debt. These are so involved that separate treatment is essential.

tion[56] have been construed to apply to all types of state-levied taxes. Although provisions of similar import are included in the state constitution,[57] the opinions of the United States Supreme Court and other federal courts interpreting the provisions of the Federal Constituition, rather than those of the state courts, are controlling,[58] and the federal court, rather than the state court, has final say with respect to compliance or non-compliance by a state taxing act with the requirements of the Federal Constitution.[59] The cases which must be considered are legion in number. And because of the variety of tax types and variations, ranging from minor to major, in the provisions of the tax laws considered in different cases, the decisions are difficult to classify and frequently difficult, if not impossible, to reconcile.[60]

Due process of law. The requirement of due process of law has both substantive and procedural aspects in its application to state taxing laws. In its substantive aspect it guards against extraterritorial application of taxes levied either by the state or by its municipal subdivisions. Due process problems arise under state laws imposing taxes on property, tangible[61] or intangible,[62] on transfers at death,[63] on net income,[64] and on the sale or use of tangible personal property.[65]

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[56] U.S. CONST. amend. XIV, § 2.

[57] WASH. CONST. art. I, § 3 (due process). WASH. CONST. art I, § 12 (special privileges and immunities); the Washington court has stated that this section is comparable in meaning to the equal protection and privileges and immunities clauses of U.S. CONST. amend. XIV, § 2. Texas Co. v. Cohn, 8 Wn.2d 360, 112 P.2d 522 (1941); State v. Vance, 29 Wash. 435, 70 Pac. 34 (1902).

[58] See cases cited note 57, *supra.*

[59] U.S. CONST., art. VI, cl. 2.

[60] For a collection of cases and other materials relating to the problem, see 1 FREUND, SUTHERLAND, HOWE, BROWN, CONSTITUTIONAL LAW CASES AND OTHER PROBLEMS 488-665 (1954).

[61] Recent cases involving state taxation of the operating properties of interstate air carriers are illustrative: Northwest Airlines, Inc., v. Minnesota, 322 U.S. 950 (1944); Braniff Airways v. Nebraska Bd., 347 U.S. 590 (1954).

[62] Wheeling Steel Corp. v. Fox, 298 U.S. 193 (1936), is a leading case on the "commercial domicile" aspect, which is only one of many aspects with respect to intangibles.

[63] Among many cases involving such taxes are Frick v. Pennsylvania, 268 U.S. 473 (1925) (tangible personalty) and Curry v. McCanless, 307 U.S. 357 (1939) (intangibles).

[64] For example, New York *ex rel.* Cohn v. Graves, 300 U.S. 308 (1937) (resident's income from land outside the taxing state) and Shaffer v. Carter, 252 U.S. 37 (1920) (non-resident's income from property and business within the taxing state).

[65] Miller Bros. Co. v. Maryland, 347 U.S. 340 (1954) and General Trading Co. v. State Tax Comm'n, 322 U.S. 335 (1944) involve the extent of the state's power to require an out-of-state vendor to collect use tax when selling goods to residents of the taxing state. The opposing results in the cited cases illustrate the difficulties encountered by the states under this constitutional requirement in establishing effective collection procedures. On the aspect of territorial application of such taxes, see Graubard, *Special Problems in the Levy of Municipal Excise Taxes,* 8 LAW AND CONTEMP. PROB.

Judicial attitudes with respect to the extent of the restrictions imposed have also varied. Such changes have been most pronounced in the area of taxation of intangible personal property. For a period of ten years the view prevailed that taxation of intangibles by more than one state violated due process.[66] "The Court acted as arbiter of the competing claims of the states by fixing a single and exclusive *locus* for the taxation of each type of intangible—whether the state of the creditor, the debtor, incorporation, or commercial domicile."[67] The majority of the Court now seems to have returned to the view that the due process clause prohibits extraterritorial application of a state's taxing laws but does not prohibit taxation of intangibles by more than one state. Professor Hellerstein's comment regarding the present status is most enlightening:

> It is interesting to note the similarity of the conception of extraterritoriality as the basis for invalidating taxes under the Due Process Clause and the requirement of apportionment as the prerequisite of validation of certain taxes under the Commerce Clause. Both simmer down to essentially the same result, namely, that a state can tax only what it "justly attributable" to it. Under both clauses, the judgments of what is "justly attributable" to a state is made by the Court.[68]

The due process requirement unquestionably poses many and difficult problems for the state in framing tax laws of every kind. The procedural aspects of due process can be met with careful planning and drafting, but from the substantive aspect the problems are more intricate. Although the restrictions are not as stringent under the present approach of the Supreme Court as they were in earlier years, the restrictions confronting the states under this constitutional requirement are substantial. It seems, moreover, that the obstacles encountered in connection with taxes on property and taxes on net income are, at the present time, less formidable than those arising in connection with taxes on gross income and taxes on the sale, or the use, of property.

Equal protection. The requirement of equal protection of the laws[69]

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613 (1941) and Brown, *Some Legal Aspects of State Sales and Use Taxes,* 18 IND. L. J. 77 (1943).

[66] See HARDING, DOUBLE TAXATION OF PROPERTY AND INCOME (1933).

[67] HELLERSTEIN, STATE AND LOCAL TAXATION CASES AND MATERIALS 486 (1952).

[68] *Ibid.*

[69] U.S. CONST. amend. XIV, § 2. The Washington court holds that WASH. CONST. art I, § 12, imposes a similar requirement, although § 12 is phrased in terms of a prohibition of special privileges and immunities, Texas Co. v. Cohn, 8 Wn.2d 360, 112 P.2d 522 (1941).

also applies to all types of state and local taxes.[70] The equal protection clause imposes a general requirement of reasonableness in the classification of the persons and property to which a tax is applicable. It forbids selection of the tax subject on an arbitrary basis and bars the drawing of lines between taxability and nontaxability without reason to justify the difference in tax treatment. The legislature, however, has a broad discretion under this provision. The following statement of the United States Supreme Court is indicative of that Court's interpretation of the constitutional language and its method of applying it to state tax statutes:

> The States, in the exercise of their taxing power, as with respect to the exertion of other powers, are subject to the requirements of the due process and the equal protection clauses of the Fourteenth Amendment, but that Amendment imposes no iron rule of equality, prohibiting the flexibility and variety that are appropriate to schemes of taxation. The State may tax real and personal property in a different manner. It may grant exemptions. The State is not limited to ad valorem taxation. It may impose different specific taxes upon different trades and professions and may vary the rates of excise upon various products. In levying such taxes, the State is not required to resort to close distinctions or to maintain a precise, scientific uniformity with reference to composition, use, or value. To hold otherwise would be to subject the essential taxing power of the State to an intolerable supervision, hostile to the basic principles of our government and wholly beyond the protection which the general clause of the Fourteenth Amendment was intended to assure.[71]

The approach of the Washington court is the same with respect to taxes governed by this constitutional provision.[72] The fact that the equal protection clause and its state counterpart allow this latitude to the legislature in the selection and classification of tax subjects is a most significant one in this state. In the case of all state-levied taxes, other than taxes on "property" within the meaning of article 1, section 1, of the state constitution,[73] the boundaries of the state legislature's power of classification are determined under the equal protection clause, rather than under the much more highly restrictive "uniformity"

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[70] The requirement in WASH. CONST. art. VII, § 9, that local "taxes shall be uniform in respect to persons and property within the jursidiction of the body levying the same" is similar in effect. Tekoa v. Reilly, 47 Wash. 202, 91 Pac. 769 (1907).

[71] Ohio Oil Co. v. Conway, 281 U.S. 146, 159 (1930).

[72] Among other cases, see State *ex rel.* Stiner v. Yelle, 174 Wash. 402, 25 P.2d 91 (1933) (state-levied excise tax); Tekoa v. Reilly, 47 Wash. 202, 91 Pac. 769 (1907) (city-levied poll tax).

[73] WASH. CONST. amend. 14 (1930).

requirement of the above article 1, section 1. Numerous cases, hereafter discussed, illustrate the enormous differences which flow from this constitutional distinction.

Not all state taxes are upheld by the courts when challenged under the equal protection clause,[74] but the requirement of equal protection, unlike other constitutional provisions here discussed, does not substantially deprive a state of the flexibility which it needs to formulate a fair and adequate tax structure.[75]

Commerce clause. "The Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."[76] The restrictions upon state taxing power of this, the commerce clause, are the most far-reaching of any of the federal constitutional provisions. As a clearly recognized principle of constitutional law, the doctrine that the interstate commerce clause imposes restrictions upon the states in the exercise of their taxing power, even though Congress has not seen fit to legislate on the matter, goes back to 1872.[77] Since action by Congress defining the limits of state power has not been regarded as necessary,[78] the standards by which the validity of a state tax is determined are wholly of judicial origin and development. The nature of the test which the Court applies in deciding whether a state tax is valid or invalid under this clause has been, and still is, vague and uncertain.

From 1872 until 1938, the Court reiterated in case after case a meaningless verbal formula that a state tax which imposes a burden on interstate commerce is void, but that a tax is valid if the burden on such commerce is indirect. Professor Hartman's comment on this verbal formula, in his excellent treatise, is both enlightening and apt:

> The view that interstate commerce is immune from taxation, with its concomitant expressions of 'direct' and 'indirect' effects and burdens, for many years remained the alleged test by which the Court struck down a wide variety of state taxes. This conceptual and un-

[74] Examples, at the state level, are Aberdeen Sav. & Loan Ass'n v. Chase, 157 Wash. 351, 289 Pac. 536, 290 Pac. 697 (1930) (a case, it appears, of misplaced reliance upon Quaker City Cab Co. v. Pennsylvania, 277 U.S. 389 (1928); State v. Inland Empire Refineries, 3 Wn.2d 651, 101 P.2d 975 (1940); but see Texas Co. v. Cohn, 8 Wn.2d 360, 112 P.2d 522 (1941).

[75] For an excellent discussion of the equal protection requirement see Sholley, *Equal Protection in Tax Legislation*, 24 VA. L. REV. 229, 338 (1938), 5 SELECTED ESSAYS ON CONSTITUTIONAL LAW 39 (1938).

[76] U.S. CONST. art. I, § 8, cl. 3.

[77] Case of State Freight Tax, 82 U.S. (15 Wall.) 232 (1872). Adoption of this view was undoubtedly forecast in earlier decisions.

[78] For a discussion of the conflicting views and theories see HARTMAN, STATE TAXATION OF INTERSTATE COMMERCE 5-13, 25-27 (1953).

> realistic mode of judicial thought gave very little consideration to the practical question of economic burden of the tax. What condemned the tax was not any actual or probable hampering effect of the exaction on the commerce; the vice of an invalid tax was simply the "direct" bearing of the tax on interstate commerce and that alone. That brand of doctrinal declaration, of course, assumed a trustworthiness in the test which did not exist. It gave very little help to the legislator, the lower courts or the taxpaying business man in predicting whether a particular tax would be valid. The alleged test simply implied the impotence of state power; it described a result reached, not the reasons for that result. The Court was more concerned with captions than with consequences.[79]

Under the leadership of Justice Stone, a more realistic approach was taken for a period of about eight years:[80]

> In 1938, he [Justice Stone] began to lay the foundation for an approach to the question of the validity of state taxes which would give more consideration to the possible economic effect of the particular tax on interstate commerce and less consideration to the formal aspects of the tax. Explicit, too, in his approach is the essential fairness that interstate commerce bear its fair share of the cost of local governments whose protection it received. . . .
>
> Regardless of the approach, Justice Stone greatly expanded the power of States to tax. Never before had such integral parts of an interstate transaction been considered as taxable. He made "taxable events" blossom where they never had budded before. He made interstate commerce "pay its way."[81]

In 1946, however, the approach espoused by Justice Stone "was fairly well shunted aside . . . in *Freeman v. Hewitt,* which marked a recrudescence of what was tantamount to the old, imprecise and unreliable 'direct-indirect' burdens test for determining the constitutionality of a state tax."[82]

Under the decisions of the Court, the interstate commerce clause is held to impose restrictions, varying in nature and extent, upon all types of state-levied taxes, including property taxes on articles transported in interstate commerce and on the vehicles or instrumentalities employed in such transportation,[83] privilege taxes,[84] taxes for the use of

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[79] *Id.* at 31.

[80] The beginning of the period is marked by Justice Stone's opinion in Western Live Stock v. Bureau of Revenue, 303 U.S. 250 (1938). Its end is marked by Justice Frankfurter's opinion for the majority in Freeman v. Hewitt, 329 U.S. 249 (1946).

[81] HARTMAN, *op. cit. supra* note 78, at 33-34, 40.

[82] *Id.* at 41.

public facilities, [85] use and sales taxes, [86] gross receipts taxes,[87] and capital stock franchise taxes.[88]

Although the impact of the commerce clause is significant in connection with all of these taxes, the restrictive effects are greatest in connection with sales taxes and taxes measured by gross income. In this state, which relies so heavily upon sales and gross income taxes, the impact of the constitutional provision is, consequently, enormous. The retail sales tax cannot be applied to many sales made by distributors doing busines in this state.[89] Gross income or gross proceeds of sales derived from activities performed within the state, or partly within and partly outside the state, are in most instances completely immunized from a state-levied business and occupation tax.[90] These effects are in marked contrast to the lighter impact of the interstate commerce clause upon state net income taxes. Although a state tax measured by net income cannot be imposed upon one whose sole activities in the state are interstate in character,[91] a state tax on net income of a person or corporation doing both intrastate and interstate business can be levied with respect to receipts from the interstate, as well as the intrastate, activities.[92] Receipts, substantial in amount, which are excluded from the tax base when the state imposes its tax upon gross income may, thus, enter into the tax base when the state imposes its tax upon net income.

STATE CONSTITUTION

In addition to the general requirements of due process and equal protection previously discussed, the constitution of the State of Washington also contains a number of provisions which relate specifically to

[83] *Id.* at 73, c. IV. Professor Hartman's treatise is a study of the impact of the interstate commerce clause on state taxing power. It is comprehensive, thorough, and informative. The treatise is recommended as the best guide to the problems of state taxation under this constitutional provision.

[84] *Id.* at 96, c. V.

[85] *Id.* at 122, c. VI.

[86] *Id.* at 131, c. VII.

[87] *Id.* at 180, c. VIII.

[88] *Id.* at 215, c. IX.

[89] See Tax Commission of the State of Washington, Excise Tax Division, Rules Relating to the Revenue Act of the State of Washington 118, Rule 193 (1956).

[90] Cases holding the Washington act invalid as to particular types of business activities are Fisher's Blend Station v. State Tax Comm'n, 297 U.S.650 (1936) (radio broadcasting); Puget Sound Stevedoring Co. v. State Tax Comm'n, 302 U.S. 90 (1937) (stevedoring services); Gwin, White & Prince, Inc. v. Henneford, 305 U.S. 434 (1939) (fruit brokers); Columbia Steel Co. v. State, 30 Wn.2d 658, 192 P.2d 976 (1948) (wholesale distributor selling articles produced outside the state).

[91] Spector Motor Serv., Inc., v. O'Connor, 340 U.S. 602 (1951).

[92] Memphis Natural Gas Co. v. Beeler, 315 U.S. 649 (1942). See HARTMAN, STATE TAXATION OF INTERSTATE COMMERCE 63 (1953).

taxation. The seventh article of the constitution is devoted wholly to the subject, and it is the most far-reaching in effect of all the specific tax provisions.[93]

Article seven, section one: taxes on property. Amendment fourteen, adopted 1930, consolidated into a single section a revision of constitutional provisions which were originally set forth in the first four sections of the article. The first sentence, which prohibits suspension or surrender of the power of taxation, applies to all taxes. The second clause of the second sentence, which sets forth a public purpose requirement, has also been construed to apply to "all taxes."[94] The first clause of the second sentence, as well as the following five sentences of the section, have been held applicable to property taxes only.[95]

The first clause of the second sentence reads as follows: "All taxes shall be uniform upon the same class of property within the territorial limits of the authority levying the tax . . ." This permits classification[96] of property for tax purposes but requires uniformity within each class.[97] The power to classify property is, however, limited by the fourth sentence: "All real estate shall constitute one class: *Provided*, That the legislature may tax mines and mineral resources and lands devoted to reforestation by either a yield tax or ad valorem tax at such rate as it may fix, or by both." The legislature, consequently, may tax real estate differently than personal property, but all real estate except mines, mineral resources, and lands devoted to reforestation, must be taxed alike. Personal property, however, may be divided into different classes if the legislature so desires, and each class of personal property taxed in a different manner or at a different rate.[98] The court has stated that the legislature has a very wide discretion in classifying personal property for tax purposes, that the question of what property consti-

[93] WASH. CONST. art. VII has been amended four times since the constitution was adopted in 1889. Only one other article of the constitution has been more frequently amended—article II, relating to the legislative department. The score favors article II only because an amendment relating to taxes on motor vehicles was inserted as a new section in that article rather than in article VII, where it might well have been placed.

[94] State *ex rel.* Collier v. Yelle, 9 Wn.2d 317, 115 P.2d 373 (1941).

[95] Among numerous cases so holding are State *ex rel.* Stiner v. Yelle, 174 Wash. 402, 25 P.2d 91 (1933); Vancouver Oil Co. v. Henneford, 183 Wash. 317, 49 P.2d 14 (1935); and Gruen v. State Tax Comm'n, 35 Wn.2d 1, 211, P.2d 651 (1949).

[96] Prior to amend. 14 (1930), WASH. CONST. art. VII, § 2 (1889), required that taxes on property be both uniform and equal. The latter requirement—that taxes be "equal"—barred all classification. Amendment 14 eliminated this "equality" requirement to permit classification.

[97] State *ex rel.* Mason County Logging Co. v. Wiley, 177 Wash. 65, 31 P.2d 539 (1934).

[98] All personal property within each class must be taxed uniformly. State *ex rel.* Mason County Logging Co. v. Wiley, 177 Wash. 65, 31 P.2d 539 (1934).

tutes a class is one primarily for the legislature, and that the courts cannot interfere with the legislative determination unless the classification is clearly arbitrary and without any reasonable basis.[99] The apparent freedom of legislative choice is, however, limited by the mandatory exemptions stated in the sixth sentence of this section: "Property of the United States and of the state, counties, school districts and other municipal corporations, and credits secured by property actually taxed in this state, not exceeding in value the value of such property, shall be exempt from taxation."

Passing without comment, at this point, the clause exempting property of the United States, the state, and its subdivisions, the clause exempting "credits" is a highly significant limitation upon the general power to classify personal property for tax purposes. The constitutional language has never been construed by the court,[100] and its meaning is far from clear. It exempts only those credits which are "secured by property actually taxed in this state." What are credits so "secured"? A note secured by a mortgage on land in this state is obviously exempt if the land is assessed and the tax levied thereon is paid. But is the note constitutionally exempt if there is a default in payment of the tax levied on the land? Is a vendor's right to receive payments under an executory, forfeitable contract for the sale of land, upon which real property tax is levied and paid, a credit so secured? Such *payments* are not "secured" by the taxed land. The vendor may repossess the land upon a default in payment; but the right to receive payments is, thereby, obliterated—not secured. Does this constitute a credit which is "secured" in the constitutional sense? What if the subject matter of the conditional sale contract is an automobile, which is subject to an annual excise in lieu of personal property tax? Or a refrigerator purchased by a homeowner for use in his own home, which is specifically exempted by statute from personal property tax?[101] Is the right of the seller of the automobile or the refrigerator to receive the balance of the sale price a "credit" which is constitutionally exempt? Is a share of corporate stock in a Washington corporation,

[99] Bates v. McLeod, 11 Wn.2d 648, 120 P.2d 472 (1941); Libby, McNeill & Libby v. Ivarson, 19 Wn.2d 723, 144 P.2d 258 (1943).

[100] In 1931 (the legislative session immediately following adoption of this constitutional provision), the legislature exempted all credits from the property tax. Wash. Laws 1931, c. 96, § 1. This exemption has not been altered or repealed. See RCW 84.36.070. The constitutional validity of this exemption was sustained in State ex rel. Atwood v. Wooster, 163 Wash. 659, 2 P.2d 653 (1931).

[101] RCW 82.44.020; 82.44.130 (motor vehicle excise tax, in lieu of personal property tax thereon); RCW 84.36.110 (1) (exemption of household furnishings of homeowner).

all of the assets of which consist of taxable real estate in Washington, a credit "secured" in the constitutional sense? A shareholder is not a creditor. Is his ownership interest "secured" in the constitutional sense? If it is, then what is the extent of the constitutional exemption in the more true to life situation in which the corporation's assets consist of some taxed real estate, some taxable tangible personal property, some specifically exempted cash, some bank deposits, some school district bonds, and, possibly, a block of General Motors or United States Steel shares? And then there is the case of the state resident, an individual, who owns ten shares of the common stock of a foreign corporation which has a branch office and warehouse in this state. What part of the value of the ten shares is constitutionally exempt from personal property tax under the "credits" clause and its qualifying modifier "not exceeding in value the value of such property"?

Meditation upon these relatively simple factual patterns leads inevitably to the conclusion that the complexities of interpretation and the practical difficulties of administration under this constitutional language are insurmountable as applied to any credits which have even a remote relationship to real or tangible personal property which is subject to taxation in this state. Conceding that the constitutional language permits (1) taxation of the full value of credits representative of interests in, or "secured" by property, or rights enforceable against persons wholly outside this state, (2) taxation of the full value of credits representative of rights solely against persons or in or "secured" by untaxed property within the state, and (3) taxation of some portion of the value of various other credits, the legislature is confronted with another constitutional hurdle. While framing a tax on credits which meets the requirements of the Washington constitutional provision, it must also comply with the requirements of the privileges and immunities clause and of the equal protection clause of the Federal Constitution.[102] This tangle of federal and state constitutional problems, coupled with the administrative complexities, including the burdens of special accounting records to supply the data required for prorating of value, which would be imposed on the taxpayer, means that for all practical purposes the Washington constitutional provision forbids the imposition of a property tax upon all forms of intangible personal property.

The fifth, sixth, and seventh sentences of amendment fourteen relate

[102] U.S. CONST. amend. XIV.

to exemption of property from taxation. The fifth sentence states: "Such property as the legislature may by general laws provide shall be exempt from taxation." This general statement of legislative discretion respecting exemptions is qualified by the sixth sentence,[103] providing constitutional exemption of the property of the United States, the state, counties, school districts, and other municipal corporations,[104] as well as certain credits. The general statement of this sentence would, furthermore, appear to be limited by the requirement of the preceding sentence that all real estate, except mineral and reforestation land, constitutes one class of property. The court, however, has construed the words "such property" in the general exemption power provision to embrace real property as well as personal property, notwithstanding the clear statement in the preceding sentence that all real estate constitutes one class.[105] This shows vividly how the strait-jacket has been bound around the state legislature. With two exceptions of very limited applicability, the legislature is forbidden to classify real estate for the purpose of raising revenue for governmental operations. But the legislature is given complete freedom to classify real estate for the purpose exempting property from taxation.

With respect to personal property, the power of the legislature to exempt classes of such property is unlimited, except for the limitation in the final sentence of the section,[106] which, seemingly imposes a ceiling of three hundred dollars upon the amount of the exemption which the legislature may grant with respect to the personal property of the head of a family. In practice this limitation seems to have been disregarded without challenge.[107]

[103] For text see page 249, *supra.*

[104] The constitutional provision is self-executing and grants mandatory exemption of both the land and personal property of the specified governmental units. Puget Sound Power & Light Co. v. Cowlitz County, 38 Wn.2d 907, 234 P.2d 506 (1951).

[105] State *ex rel.* Atwood v. Wooster, 163 Wash. 659, 2 P.2d 653 (1931); Kennewick Irrigation Dist. v. Benton County, 179 Wash. 1, 35 P.2d 1109 (1934).

[106] "The legislature shall have power, by appropriate legislation, to exempt personal property to the amount of three hundred ($300.00) dollars for each head of a family liable to assessment and taxation under the provisions of the laws of this state of which the individual is the actual and bona fide owner." This language was added to the original § 2 of art. VII by amend. 3, adopted 1900. Under the uniformity *and equality* requirement of § 2 at that time, this provision was essential to permit such exemption of personal property. It does not appear to be necessary when the sole requirement is "uniformity" and the legislature has the power to exempt personal property by general law, as the previous sentence states. The same language was, however, carried over into § 2 as revised. Its sole effect in this context appears to be to impose a limitation upon the legislature with respect to the dollar value of this type of personal property which it may exempt.

[107] RCW 84.36.110 (1) exempts *all* household goods and furnishings actually used by a *homeowner* in his residence and *all* personal effects of any person. There is no limitation as to the value of the property exempted under this subsection. RCW

With the two exceptions previously mentioned, amendment fourteen is applicable to property taxes only. The third sentence of the section contains the following definition: "The word 'property' as used herein shall mean and include everything, whether tangible or intangible, subject to ownership." The language leaves no doubt that the intent is to give to the word its broadest denotation, and the court has consistently so construed it.[108] On the basis of this constitutional definition of the word "property," the court has also consistently held that a net income tax—whether levied on net income as such,[109] upon individuals for the "privilege of receiving income,"[110] or upon corporations as an excise for the privilege of exercising the corporate franchise[111]—is a tax on property within the meaning of this constitutional provision. Being a tax on "property" within the meaning of this section of the constitution, the tax is subject to the uniformity and restricted classification requirements of this provision. Whether denominated as "upon" net income or as an excise measured by net income, the tax as applied to rental from land is treated as a tax upon real estate, a treatment which creates a prohibited classification in distinguishing between income-producing and non-income-producing real estate.[112] Also, graduation of the rates of tax and the granting of exemptions of different amounts dependent upon marital status have been held violative of amendment fourteen uniformity, because "all net income constitutes a single class of property."[113] Why this is so, the court has never attempted to explain. The reason for this lack of explanation seems apparent. The wording of the amendment does not support it,[114] and the decisions of other courts, federal and state, uphold such legislative

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84.36.110 (2) provides a further exemption of personal property of the *head of a family*, not exempted under subsection (1). The exemption under subsection (2) is limited to $300 of actual value. The constitutional validity of the dual exemptions granted by this section has not been raised in the state supreme court.

[108] See, e.g., American Smelting & Refining Co. v. Whatcom County, 13 Wn.2d 295, 124 P.2d 963 (1942).

[109] Culliton v. Chase, 174 Wash. 363, 25 P.2d 81 (1933).

[110] Jensen v. Henneford, 185 Wash. 209, 53 P.2d 607 (1936).

[111] Power, Inc., v. Huntley, 39 Wn.2d 191, 235 P.2d 173 (1951).

[112] Jensen v. Henneford, 185 Wash. 209, 222, 53 P.2d 607, 612 (1936).

[113] *Id.* at 220 and 222, 53 P.2d at 611 and 612.

[114] As pointed out above, art. VII, § 1 (amend. 14), permits classification of personal property. After eliminating income from real estate (see note 112, *supra*), the net income which remains must be, under the court's theory, personal property. The court's statement that "'net income,'... under the fourteenth amendment, constitutes one class of property" has no support whatever in the language of that amendment. On the contrary, the well-known canon of interpretation, *expressio unius, exclusio alterius*, requires the construction that no property other than real estate (expressly stated to constitute one class) does constitute one class within the meaning of the consitutional language.

classification of net income under constitutional provisions requiring uniformity.[115]

On the other hand, the court has just as consistently held that taxes upon business activities,[116] upon retail sales,[117] and upon the use of articles of tangible personal property [118] are excise taxes and not taxes on "property" in the constitutional sense. Since they are not property taxes, the uniformity and restricted classification requirements of the fourteenth amendment are inapplicable. Each of these taxes was, then, upheld as an appropriate legislative selection of the objects of taxation under the less restrictive provisions of article 1, sections 3 and 12, of the state constitution and the equal protection clause of the Federal Constitution. This result was reached even though the tax base in some instances includes gross income attributable to the use of real estate[119] and even though the tax rates vary as between gross income, or gross proceeds of sales, derived from different sources,[120] and even though some types of gross income, or gross proceeds of sales, are entirely excluded from the tax base.[121] This, the court has consistently said, is, however, all right, because these are not taxes on "property" in the constitutional sense but are excises. If the tax

[115] When a net income tax is treated as a tax on property, the precise character of the constitutional requirement is most important in determining whether graduation of rates and other forms of classification of net income are permissible. If the constitution requires both uniformity *and equality*, classification, and graduation of rates, is barred. But if the constitution requires uniformity only, classification and graduation of rates should be permissible. The Washington court, possibly along with one or two others, has failed to recognize this most important distinction. For discussion of various aspects of constitutionality of state net income taxes, see Brown, *The Nature of the Income Tax*, 17 MINN. L. REV. 127 (1933); Harsch, *State Income Taxation as Affected by Property Tax Limitations*, 6 WASH. L. REV. 97 (1931); Comment, *Constitutionality of State Income Taxes*, 8 WASH. L. REV. 81 (1933); Recent Case, 11 WASH. L. REV. 172 (1936).

[116] State *ex rel.* Stiner v. Yelle, 174 Wash. 402, 25 P.2d 91 (1933).

[117] Morrow v. Henneford, 182 Wash. 625, 47 P.2d 1016 (1935) (general retail sales tax); Gruen v. State Tax Comm'n, 35 Wn.2d 1, 211 P.2d 651 (1949) (selective retail sales tax—cigarettes).

[118] Vancouver Oil Co. v. Henneford, 183 Wash. 317, 49 P.2d 14 (1935) (general tax on use of tangible personalty purchased at retail).

[119] Under the business and occupation tax income from the rental of real estate is specifically exempted from tax, as are gross proceeds from farming operations. In numerous instances, however, the use of land is an important factor in the production of the gross income upon which the tax is levied. An example is the charges for hotel and motel accommodations and for space in a trailer court, which enter into the base for both the business-occupation tax and the retail sales tax.

[120] For example, under the business-occupation tax the rates of tax on wholesale sales differed from the rate on sales at retail. Laws 1933, c. 191, § 2 (2) (c) and (d). The rate applicable to gross income from service businesses differs from the rate applicable to retail and wholesale sales. A different rate is applicable to wholesale grain dealers than is applicable to other wholesale dealers. RCW 82.04.250; 82.04.260; 82.04.270; 82.04.290.

[121] Examples under the business-occupation tax are gross income from rental of real estate and gross income from farming operations, *inter alia*. RCW 82.04.390; 82.04.330.

is in fact an excise—and how the legislature labels it is of no consequence in determining this "fact"[122]—the legislature's power to select the subject and to classify is limited only by the requirement that there be some reasonable basis to support the legislative determination.[123] The court cannot interfere with that determination except for arbitrary action, abuse, or constructive fraud appearing on the face of the act or from facts of which the court may take judicial knowledge.[124]

In light of these judicial pronouncements, what is it, then, that determines whether a tax is a tax on "property," which, if a tax other than the traditional ad valorem property tax, would for all practical purposes be doomed to invalidity under the "uniformity" requirement of the fourteenth amendment, or an excise, with respect to which the legislative power of selection of object and choice of rate is limited only by the test of reasonableness? No one has ever questioned the proposition that the traditional ad valorem tax on real and personal property, levied annually at rates determined by appropriate authorities of the state and its various taxing districts, is a tax on "property" within the meaning of the constitutional provision. The question is: What other taxes constitute taxes on "property" in the constitutional sense?

The fact that liability for the tax depends upon performance of an act or a continuing series of acts by the taxpayer is a significant factor,[125] but it is not the controlling factor. This is demonstrated by the decisions holding invalid a tax upon the act or privilege of receiving income—specifically denominated by the legislature an excise rather than a tax on property[126]—or upon the privilege of exercising the corporate franchise.[127] Although a property value base is an almost universal feature of property taxes as they are known to the citizen unitiated in constitutional lore, the fact that the tax base is the value of property, real or personal, does not mean that the tax is a tax on "property" in the constitutional sense. The inheritance tax, with three different classes and differing schedules of graduated rates applicable to each class, is an excise, not a property tax.[128] An annual

[122] Jensen v. Henneford, 185 Wash. 209, 217, 53 P.2d 607, 610 (1936).
[123] Gruen v. State Tax Comm'n, 35 Wn. 2d 1, 211 P.2d 651 (1949).
[124] State *ex rel.* Stiner v. Yelle, 174 Wash. 402, 25 P.2d 91 (1933).
[125] State *ex rel.* Stiner v. Yelle, 174 Wash. 402, 25 P.2d 91 (1933); Supply Laundry Co. v. Jenner, 178 Wash. 72, 34 P.2d 363 (1934); Vancouver Oil Co. v. Henneford, 183 Wash. 317, 49 P.2d 14 (1935); State *ex rel.* Hansen v. Salter, 190 Wash. 703, 70 P.2d 1056 (1937).
[126] Jensen v. Henneford, 185 Wash. 209, 53 P.2d 607 (1936).
[127] Power, Inc., v. Huntley, 39 Wn.2d 191, 235 P.2d 173 (1951).
[128] State v. Clark, 30 Wash. 439, 445, 71 Pac. 20, 22 (1902).

tax on motor vehicles, levied at a fixed percentage of the fair market value of each vehicle, is an excise tax, not a property tax.[129] A tax on producers or manufacturers of tangible personal property, at a specified percentage of the value of the property produced or manufactured, is an excise, not a property tax.[130]

Whether the tax has but a single impact upon a particular taxpayer with respect to a particular subject matter[131] or is a periodically recurring levy[132] also lacks significance in determining whether the tax is an excise or a tax on "property" in the constitutional sense.

Except for one, all other distinguishing features seem equally unfruitful. The one distinguishing feature is that of the measure of tax. If net income is utilized to determine the amount of tax liability, it is a tax on "property" in the constitutional sense. If the gross product, the gross selling price, the gross purchase price, or even the fair market value of an article[133] is utilized to determine the amount of tax liability, it is an excise, not a "property" tax in the constitutional sense. When the amount of tax is determined by reference to "net income," it is a property tax. But when the amount of the tax is determined by reference to the gross income or the gross amount or value, unreduced by costs or expenditures, the tax is not on "property" in the constitutional sense. The incongruity of the situation is apparent when the decisions are laid alongside the constitutional definition that property "shall mean and include everything, tangible or intangible, subject to ownership." The money or other property (tangible) which comes into the taxpayer's physical possession or the legally enforceable right (intangible) which comes into the taxpayer's legal possession is *not* something subject to ownership. But that which remains after reducing the gross amount received or receivable by deductions for cost (whether actually paid or legally incurred without payment) and depreciation (for which no actual outlay is currently required) and policy-determined amounts, such as the deduction for personal

[129] State *ex rel.* Hansen v. Salter, 190 Wash. 703, 70 P.2d 1056 (1937).

[130] State *ex rel.* Stiner v. Yelle, 174 Wash. 402, 25 P.2d 91 (1933).

[131] This is generally true in the case of the retail sales tax, a selective sales tax such as a tax on gasoline or on cigarettes, a tax on the use of fuel oil or of articles of tangible personal property purchased at retail. It is also true in the case of the inheritance tax and the gift tax. All of these are "excise," rather than property, taxes.

[132] This is clearly the situation in the case of the motor vehicle excise, as well as in the case of a multitude of "license" taxes, such vehicle operator's license, fishing licenses, etc. None of these are property taxes. But it is also applicable in the case of the ad valorem tax on real and personal property, which is a "property" tax in the constitutional sense.

[133] The traditional ad valorem property tax is, of course, an exception to this.

exemptions (for which the actual outlay may greatly exceed the amount deductible)—this fictitious residue, the end product of a series of arithmetic steps which the statute itself prescribes—*is* property in the constitutional sense.

Article Seven, section two: forty-mill limitation. A new section two was added to article seven of the state constitution by amendment seventeen, approved in 1944. Its major feature is stated in the first sentence, as follows: "(T)he aggregate of all tax levies upon real and personal property by the state and all taxing districts now existing or hereafter created; shall not in any year exceed forty mills on the dollar of assessed valuation . . . ." This constitutional restriction upon legislative power in the area of public finance has an interesting and informative history. Beginning in 1932, similar, but more detailed, forty-mill property tax levy limitation acts were proposed by initiative and approved by the voters at each successive biennial general election.[134] As an act approved by the electors could not, at that time, be amended or repealed by the legislature for a period of two years after it adoption,[135] the legislature was, thus, effectively barred throughout this period from authorizing any property tax levy in excess of either the aggregate or the specific rate limitations contained in the initiative measure then in effect. Nor could the legislature authorize approval by the voters of a tax levy in excess of these limitations other than in the manner, and subject to the detailed restrictions, set forth in such initiative measure. Repeated submission of a new, although sometimes unchanged in wording, rate limitation initiative measure at the general election preceding each biennial legislative session was, obviously and openly, designed to bar the legislature from increasing, or authorizing local authorities to increase, the property tax levies for either state or local purposes, regardless of what the costs of governmental operations might be. But the legislature alone was left with the responsibility of formulating and implementing a taxing program adequate to finance the costs of state and local government, whatever they might be. Prior to enactment of the first forty-mill measure, the aggregate property tax levies had been substantially in excess of the stated maximum levies in virtually every taxing district of the state. The original forty-mill limitation measure had the effect, consequently,

[134] Wash. Laws 1933, c. 4 (Init. No. 64); Wash. Laws 1935, c. 2 (Init. No. 94); Wash. Laws 1937, c. 1 (Init. No. 114); Wash. Laws 1939, c. 2 (Init. No. 129); Wash. Laws 1941, c. 176 (referendum).

[135] WASH. CONST. art. II, § 1 (c), adopted in amend. 7, approved 1912.

of reducing the rate of levy in virtually every taxing district to levels conforming with both the aggregate and the specific rate limitations stated in the measure. Flexibility in property tax levy rates was a thing of the past in virtually every taxing district. Due to the enforced reduction in the pre-forty-mill limitation levy rates, revenue to cover the deficit in existing government costs, as well as revenue to meet the increasing costs of state and local government, had to be obtained by levying taxes other than taxes on property, or by adopting more effective listing and assessment procedures, which would increase the base to which the fixed-millage-rate property tax levies could be applied.

Tiring of their self-imposed and expensive biennial task of submitting and propagandizing rate limitation initiatives, the sponsors of these restrictive measures prevailed upon the legislature, at its 1943 session, to submit a constitutional amendment embodying the forty-mill rate limitation principle. It proposed an aggregate levy limitation of forty mills for the state and all taxing districts, but eliminated the specific maximum millages, applicable to the state, counties, cities and school districts, which had been included in the earlier initiative measures. The legislature, thus, could determine the maximum rate of levy applicable to the state and to the local taxing districts, subject to the restriction that the aggregate levies of all should not exceed forty mills. This, the seventeenth amendment, was approved by the voters at the general election in October, 1944.

Coupled with the forty-mill levy limitation is the further requirement that the "assessed valuation shall be fifty per centum of the true and fair value of such property in money." This means that the *effective* rate limitation prescribed by the constitutional provision is twenty mills on the *actual value* of property in the state, not the apparent forty mills. Whatever the constitution may prescribe with respect to the ratio of assessed valuation to true value, the critical factor is the actual ratio of assessed valuation to the fair value of the property taxed. Studies have repeatedly shown that in actual practice the assessed valuations extended on the property tax rolls are in the vast majority of cases far below the constitutional ratio of fifty per cent of true and fair value of the property in money.[136] Constitutional blocks to improvement in assessment procedures, designed to correct this situation, are hereafter discussed.

[136] SUBCOMMITTEE ON REVENUE AND TAXATION, LEGISLATIVE COUNCIL, REPORT ON A STUDY OF REAL PROPERTY ASSESSMENTS IN THE STATE OF WASHINGTON (1954).

The term "taxing district" is defined to exclude port districts and public utility districts, but to include all other subdivisions, municipalities, districts, and agencies having the power to levy ad valorem taxes on property.[137] The policy of excluding port districts and public utility districts from the aggregate levy limitation was carried over from the earlier initiative measures. The reasons underlying these exclusions are obscure. If based upon the theory that the activities of such districts are proprietary, rather than governmental, in character, it is to be noted that cities and other taxing districts, subject to the aggregate rate limitations, carry on activities of a proprietary nature. It appears, however, that the maximum levy rates for port and public utility districts are frozen at the maximum rates authorized by law at the time of the adoption of the seventeenth amedment.[138]

The final sentence of the amendment, about four hundred words or three paragraphs in length, sets up detailed specifications concerning levies in excess of the prescribed rate limitation. Any levy in excess of the limitation is prohibited unless the requirements of either (a), (b) or (c) are met. Clause (a) permits an additional levy for one year if the specific additional levy is approved by sixty per cent of the electors voting on the proposition and if the number voting on it is not less than forty per cent of the number of votes cast in the taxing district at the last preceding general election. Such a proposition cannot be submitted to a vote more than twice in one year. Clause (b) permits additional levies for a period of years to pay the principal and interest on general obligation bonds, the issuance of which is authorized by the voters. Such bonds may issued "solely for capital purposes, other than replacement of equipment." The same sixty per cent majority of not less than forty per cent of the number who voted at the last preceding general election is required under (b) as is required under (a); and there is the same restriction against submission of a proposition more than twice in any period of twelve months. The maximum indebtedness provisions, which generally limit indebtedness to five per cent of the assessed valuation of property in the district, are also applicable.[139] Bond issues "to refund any obligation bonds . . . issued for

[137] "The term 'taxing district' for the purposes of this section shall mean any political subdivision, municipal corporation, district, or other governmental agency authorized by law to levy or have levied for it, ad valorem taxes on property, other than a port or public utility district." Amend. 17, second sentence.

[138] *"Provided, however,* That nothing herein shall prevent levies at the rates now provided by law by or for any port or public utility district." Amend. 17, first sentence.

[139] And Provided further, That the provisions of this section shall also be subject to the limitations contained in Article VIII, Section 6, of this Constitution."

capital purposes only" are specifically excepted from the requirements of the section. Clause (c) authorizes a levy in excess of forty mills "for the purpose of paying the principal or interest on general obligation bonds outstanding on December 6, 1934; or for the purpose of preventing the impairment of the obligation of a contract when ordered so to do by a court of last resort."

The constitutional property tax levy limitation thus limits not only legislative discretion with respect to the proportion of the total tax burden which may be imposed upon property, but also substantially restricts the voters in any taxing district from voluntarily imposing additional taxes on the property in the district for either its current operating expenses or for capital improvements.

Article Seven, section three: federal agencies and instrumentalities: Another new section was added to article VII by amendment nineteen, approved November, 1946.[140] It authorizes taxation of the United States and its agencies and instrumentalities and taxation of their property to the extent such taxation is permitted under the laws of the United States. It also specifically abrogates any other provisions of the state constitution purporting to exempt the federal government, its agencies, or their property.[141]

The background of this constitutional provision is found in the doctrine of intergovernmental immunities, which the Supreme Court of the United States held to be implicit in the federal form of government established by the United States Constitution. Beginning with *McCulloch v. Maryland*,[142] the federal Court has held that no state may utilize its taxing power in a manner which will interfere with or hamper the operations of the federal government or its agencies or instrumentalities. This implied constitutional restriction is applicable not only to state and local taxes on the property but also to all other types

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[140] The text of the amendment, which is designated as section 3 of this article, is as follows: "The United States and its agencies and instrumentalities, and their property, may be taxed under any of the tax laws of this state, whenever and in such manner as such taxation may be authorized or permitted under the laws of the United States, notwithstanding anything to the contrary in the Constitution of this State."

[141] In Boeing Aircraft Co. v. R. F. C., 25 Wn.2d 652, 171 P.2d 838 (1946), decided three months before amend. 19 was approved, the state court unanimously held that a legislative act requiring taxation of federal property to the extent authorized by Congress was effective, notwithstanding the constitutional provision exempting such property. Amend. 19 thus operated to clear up the constitutional language, even though the court had reached the desired conclusion without benefit of a constitutional amendment.

[142] 17 U.S. (4 Wheat.) 415 (1819).

or forms of state taxes.[143] Congress, however, may waive the immunity which the Constitution affords, and in the Buck Act,[144] as well as other acts,[145] Congress authorized the states to impose state taxes of specified types to designated federal agencies or instrumentalities.

The constitution of this state, however, then contained several provisions which could have been construed to bar the state from taking full advantage of the federal waivers of tax immunity.[146] The mandatory exemption provision of article VII, section 1 (amendment fourteen), specifically applied to property of the United States. This had been construed, both judicially[147] and administratively, to exempt the property of the agencies and instrumentalities of the United States. Under article twenty-five of the state constitution, the state, at the time of admission to the Union, granted to the federal Congress exclusive legislative power with respect to lands held or reserved by the United States for military and other designated purposes. This prohibited application of all state tax laws to property situated in, or to transactions occurring on, the land so held, even though the owners of the property or the parties to the taxable transactions were private citizens.[148] Furthermore, article twenty-six of the state constitution is a compact with the United States, under the terms of which the state ceded jurisdiction, including its taxing power, with respect to lands owned by any Indian or Indian tribe.[149] Section 3 of article VII, added by the nineteenth amendment, removes these limiting provisions of the state constitution which might bar the legislature from taking full advantage of Congress's waiver of federal immunities from state taxation. This, however, is far from a complete solution of the problems which confront the states under the federal immunity doctrine. Congress has not waived the constitutional immunity in all instances. The immunity

[143] See Powell, *The Waning of Intergovernmental Tax Immunities,* 58 HARV. L. REV. 633 (1945); Powell, *The Remnant of Intergovernmental Tax Immunities,* 58 HARV. L. REV. 757 (1945).

[144] 4 U.S.C. §§ 105-110 (Supp. 1952).

[145] An example is 12 U.S.C. § 548, which permits taxation of real, but not personal, property of national banks (which are federal instrumentalities) and taxation of net income, but not gross income, of such banks, in accord with detailed conditions set forth in the statute.

[146] But see comment on Boeing Aircraft Co. v. R.F.C., note 141, *supra.*

[147] See, e.g., King County v. United States Shipping Bd. Emergency Fleet Corp., 282 Fed. 950 (9th Cir. 1922).

[148] See Rupp, *Jurisdiction Over Lands Owned by the United States Within the State of Washington* (1939) 14 WASH. L. REV. 1, esp. 17.

[149] The compact expressly permits taxation of lands owned by an Indian who has severed his tribal relations. The article has been construed to permit state taxation of non-Indians doing business within the limits of an Indian reservation. Neah Bay Fish Co. v. Krummel, 3 Wn.2d 570, 101 P.2d 600 (1940).

doctrine may have application to any type of tax which a state may impose. Some recent judicial interpretations and the specific congressional waivers have opened the way to broader application of state tax laws than was formerly permissible. But the judicially evolved doctrine of federal immunity still has vitality in a variety of situations.[150] The doctrine may have greater impact in one state than in another because of the nature of the taxing structure. The existing tax structure in Washington places it in the position of being more restricted by the doctrine than are some other states. A state tax on the net income of individuals and corporations is applicable to income received as compensation for services to the United States or any of its agencies, as well as to net income from the performance of contracts with the United States and any of its agencies.[151] In the case of state taxes on sales or taxes measured by gross income, however, the federal immunity doctrine presents greater hazards. Although a state tax on the gross income of a federal contractor,[152] or upon sales to a federal contractor,[153] as well as a use tax on a federal contractor,[154] are generally not barred by the federal immunity doctrine, such taxes cannot be applied to the federal government itself, nor without congressional consent to federal agencies or instrumentalities, nor in some instances to persons performing contracts for the federal government or one of its agencies.[155] Here the type of tax and its legal incidence may be the critical factor in determining whether the state can or cannot impose a tax on transactions involved in, or proceeds derived from, a federal contract. The state which imposes a net income tax almost invariably enjoys a preferred position in situations of this kind.

An interesting problem under the final clause of amendment nineteen ("notwithstanding anything to the contrary in the Constitution of this state") is whether it overrides the state court's construction that a tax on net income is a property tax within the meaning of article VII, section 1, so that the state may now take advantage of the federal

[150] The articles by Professor Reed Powell, cited note 143 *supra,* show the status of the doctrine in the mid-forties. There have been numerous developments since these articles were published.

[151] Graves v. New York *ex rel.* O'Keefe, 306 U.S. 466 (1939). Atkinson v. State Tax Comm'n., 303 U.S. 20 (1938). See also 120 A.L.R. 1466 (1939).

[152] For example, in James v. Dravo Contracting Co., 302 U.S. 134 (1937) and Silas Mason Co. v. Tax Comm'n., 302 U.S. 186 (1937).

[153] Alabama v. King & Boozer, 314 U.S. 599 (1941), among others.

[154] Curry v. United States, 314 U.S. 14 (1941).

[155] Carson v. Roane-Anderson Co., 342 U.S. 232 (1952). This is an excellent illustration of the niceties upon which liability or non-liability for a state tax of this type may depend.

statute[156] authorizing a state tax on, or measured by, the net income of national banking associations. An earlier legislative attempt[157] to levy a tax which would meet the requirements of this federal statute was held invalid in the first of the long line of decisions which have scuttled taxes on, or measured by, net income in this state.[158] If the court would construe the language of the final clause of amendment nineteen to override the uniformity requirement of amendment fourteen, and if the court, under the equal protection clause, would uphold the classification of the financial institutions which Congress has declared to be in the same class as national banking institutions, this state could, without constitutional amendment, avail itself of this long-forbidden source of revenue which many other states are utilizing.

Other sections of article seven. Sections 5, 6, 7, and 8 of article VII do not appear to impose any substantial restrictions upon legislative formulation of state tax policies. Although three of these sections pose interesting questions in connection with state fiscal policies and procedures, discussion of them is here omitted.

Article seven, section nine and article twelve, section eleven: taxes for local purposes. The taxing power of the subdivisions of state government—counties, cities, towns, school districts, and other subdivisions existing under legislative authorization—is the subject matter of two sections of the state constitution. The first of these is article VII, section 9:

> For all corporate purposes, all municipal corporations may be vested with authority to assess and collect taxes and such taxes shall be uniform in respect to persons and property within the jurisdiction of the body levying the same.[159]

The other is article XI, section 12:

> The legislature shall have no power to impose taxes upon counties, cities, towns or other municipal corporations, or upon the inhabitants or property thereof, for county, city, town, or other municipal purposes, but may, by general laws, vest in the corporate authorities thereof, the power to assess and collect taxes for such purposes.

[156] REV. STAT. § 5219 (1875), as amended, 12 U.S.C. § 548 (1952).

[157] Wash. Laws 1929, c. 151.

[158] Aberdeen Sav. & Loan Ass'n. v. Chase, 157 Wash. 351, 289 Pac. 536, 290 Pac. 697 (1930); Burr, Conrad & Broom, Inc. v. Chase, 157 Wash. 393, 289 Pac. 551 (1930). The most recent attempt was, similarly, futile; Wash. Laws 1951 Ex. Sess., c. 10, 7(b), held invalid, for various reasons, in Power, Inc. v. Huntley, 39 Wn.2d 191, 235 P.2d 173 (1951).

[159] The second sentence only of this section is quoted in the text. The first sentence relates to local improvements and assessments or special taxes to defray the cost thereof.

These sections, which are complementary, embody two distinct precepts. One is definitive of the taxing power which may be enjoyed by local subdivisions of government; the other is a restriction upon the power of the state legislature.

Both sections indicate that counties, cities, and other subdivisions of the state, however designated, have no inherent power of taxation. These sections, however, make it clear that the legislature may grant the taxing power to such subdivisions of the state, subject to stated restrictions.[160] The restrictions applicable to a legislative grant of taxing power to a subdivision are dual in character. Under section twelve, the taxing power may be granted to counties, cities, towns, or other municipal corporations for county, city, town, or other municipal purposes. In section nine, the same restriction is phrased in the term "for all corporate purposes."[161] The other requirement, stated in section nine only, is that all taxes assessed and collected pursuant to such delegated authority "shall be uniform in respect to persons and property within the jurisdiction of the body levying the same." This constitutional requirement is implicit in every legislative delegation of taxing power to municipalities or other subdivisions of the state and applies, as well, to the provisions of the legislative act under which the power is granted.[162] The court has had few occasions to discuss the meaning of "uniformity" under this constitutional provision. It obviously requires geographic uniformity.[163] This means that a tax which a county is authorized to levy must apply alike to all persons or property within the geographic limits of the county, and a city tax must apply alike to all within the geographic limits of the city.

From the aspect of classification of the subjects of local taxation, the effect of the uniformity requirement of section nine is not the same in the case of local taxes on property as in the case of local taxes other than property taxes. As applied to property taxes which local subdivi-

[160] State v. Ide, 35 Wash. 576, 77 Pac. 961 (1904); Great Northern Ry. v. Glover, 194 Wash. 146, 77 P.2d 598 (1938); Great Northern Ry. v. Stevens County, 108 Wash. 238, 183 Pac. 65 (1919); State *ex rel.* School Dist. v. Clark County, 177 Wash. 314, 31 P.2d 897 (1934); Pacific First Federal Sav. & Loan Ass'n. v. Pierce County, 27 Wn.2d 347, 178 P.2d 351 (1947).

[161] State *ex rel.* Latimer v. Henry, 28 Wash. 38, 68 Pac. 368 (1902) (county); Denman v. Tacoma, 170 Wash. 406, 16 P.2d 596 (1932) (city); Weyerhaeuser Timber Co. v. Roessler, 2 Wn.2d 304, 97 P.2d 1070 (1940) (county).

[162] State v. Ide, 35 Wash. 576, 77 Pac. 961 (1904).

[163] Compare U.S. CONST. art. I, § 8, cl. 1: "The Congress shall have power to lay and collect taxes, duties, imposts and excises . . . ; but all duties, imposts and excises shall be uniform throughout the United States." The similarity between the latter provision and the language of § 9 is marked. The federal courts have consistently held that geographic uniformity is required under this constitutional language.

sions are empowered to levy, the "uniformity" required is that stated in section 1, article VII, because this section obviously applies to all taxes on property, whether levied by the state for state purposes or by a county, city, school district, or other subdivision for local purposes. This is taken for granted without discussion in all the cases interpreting the uniformity requirement of section one. But as to taxes on persons,[164] which are also within the contemplation of section nine, uniformity permits any reasonable classification of the subjects of taxation. It should mean the same as, and no more than, equal protection of the laws. One case so holds.[165]

Under these constitutional provisions, the legislature, in addition to withholding the power to levy and collect any particular type of tax for local purposes, may attach conditions and restrictions with respect to the taxing authority granted.[166] The extent of the taxing power to be enjoyed by municipalities and other subdivisions of the state is, consequently, entirely at the discretion of the legislature. It may grant, or it may withhold. It is clear, moreover, that this legislative discretion extends to taxes upon persons as well as to taxes upon property.[167]

The second aspect of these provisions[168] is a restriction on the taxing power of the legislature. The legislature is forbidden "to impose taxes . . . upon counties, cities, towns or other municipal corporations, or upon the inhabitants or property thereof . . . for county, city, town, or other municipal purposes." There are three requirements for application of the provision: (1) imposition of a tax, (2) application to a protected entity, and (3) imposition for a local purpose.

The *entities protected* are of three types. First are the counties, cities, towns, and other municipal corporations as such. Second are the inhabitants of counties and of the several types of municipal corporations. The residents of a local subdivision, as well as the governmental unit itself, are, thus, in the protected class. The third object in the protected class is "the property thereof." Without discussion, this

[164] This is the wording of § 9. It undoubtedly connotes all species of taxes other than taxes on property within the meaning of § 1.

[165] Tekoa v. Reilly, 47 Wash. 202, 91 Pac. 769 (1907).

[166] Great Northern Ry. v. Stevens County, 108 Wash. 238, 183 Pac. 65 (1919); State *ex rel.* King County v. State Tax Comm'n., 174 Wash. 668, 26 P.2d 80 (1933); State *ex rel.* School Dist. v. Clark County, 177 Wash. 314, 31 P.2d 897 (1934).

[167] This is implicit in the clause requiring uniformity "in respect to persons and property." For examples of taxes on persons, see State v. Ide, 35 Wash. 576, 77 Pac. 961 (1904) and Tekoa v. Reilly, 47 Wash. 202, 91 Pac. 769 (1907). The legislative practice has been to grant power to cities, in particular, to levy license taxes and certain excise taxes. This practice has not been challenged.

[168] In WASH. CONST. art. XI, § 12.

has been construed to mean the property of inhabitants,[169] although this is grammatically a questionable construction of the statutory language.[170]

The second requirement for application of the constitutional proscription is that the tax be for a *county, city, town or other municipal purpose.* If a tax imposed by the state legislature is solely for a state purpose, rather than for a local purpose, the constitutional prohibition does not apply.[171] But whether the purpose which the tax serves is solely a state purpose, solely a local purpose, or a purpose of both the state and the local subdivision is not always readily apparent.[172] If the purpose served is a combined one, having both local and state aspects, does the constitutional provision apply? Legislative acts relating to taxes for the support of the common schools have brought this question squarely before the court. *Newman v. Schlarb*[173] involved a state statute which required each county to apply a specified amount out of the county-levied property tax to the support of the common schools in the county. In a departmental decision, the court unanimously held that the tax was for a state purpose with local benefits to the county, not "upon the county for county purposes," and thus not in conflict with article XI, section 12.[174] Thus, where the tax serves a clear and

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[169] This is implicit in all cases involving property taxes. State *ex rel.* State Tax Comm'n. v Redd, 166 Wash. 132, 6 P.2d 619 (1932), State *ex rel.* Tacoma School Dist. v. Kelly, 176 Wash. 689, 30 P.2d 638 (1934) and Clark v. Seiber, 48 Wn.2d 783, 296 P.2d 680 (1956), among others, are illustrative.

[170] The question is whether the word "thereof" following the word "property" relates back to the primary subject, "counties, cities," etc., or relates back to the word "inhabitants." The word "thereof" must modify the word "inhabitants" in order to make it meaningful; in so doing, it *necessarily* relates back to the antecedent "counties, cities," etc. As a modifier of the word "property," it should have the same meaning. Grammatically, therefore, the word "property" in § 12 refers to the property of counties, cities, towns, or other municipal corporations and not to the property of inhabitants of counties, cities, towns, or other municipal corporations. Under this grammatical construction, however, § 12 would duplicate the constitutional exemption of "the property of counties, school districts and other municipal corporations" in art. VII, § 1. The court, had it considered the problem, could readily have reached the conclusion that, although the draftsmen of the constitution were inept in the art of English composition, the intent to denote the property of inhabitants, rather than the property of counties, cities, etc. only, is sufficiently indicated to warrant disregard of the normal rules of construction.

[171] Nipges v. Thornton, 119 Wash. 464, 206 Pac. 17 (1922). This proposition is either implicitly or expressly recognized in all of the cases here mentioned.

[172] As the counties, cities, districts, and other subdivisions are but parts of the state, created to perform some of the sovereign functions of the state, it may be said that everything done locally serves both a local and a state purpose.

[173] 184 Wash. 147, 50 P.2d 36 (1935).

[174] WASH. CONST. art. IX, §§ 1 and 2, which make education a "paramount duty of the state" and require the legislature to provide a uniform system of public schools throughout the state, were relied upon to establish the state purpose of the tax involved in the statute.

substantial state purpose, the local purpose requirement of section twelve is not met even though there are, at the same time, local benefits. But in the more recent case of *Clark v. Seiber*,[175] three judges, after pointing out that operation of the common schools is not solely a state purpose, but in part a local purpose, concluded that the Ryder Act[176] was invalid under section twelve. These judges thus took the position that, if the purpose served is a combination state and local purpose, the constitutional requirement of local purpose is thereby met. They also apparently believed that when there is a combination purpose it will be regarded as a local purpose unless the legislature, in some unexplained manner, demonstrates the proportion of the whole which is "state purpose." The other six judges, however, did not agree with this, but adhered to the reasoning of the court in *Newman v. Schlarb*.[177] When a combination state and local purpose is served, as in the case of operation of the common schools, the majority of the members of the court will, apparently, sustain the legislative act as one having a state purpose. But what standard the court will use in determining, under this section, the "purpose" of other and differing acts, the opinions rendered up to this time do not reveal.

The existence of both a state and a local purpose also appears to be the basis upon which the court, in *State ex rel. Board of Commissioners v. Clausen*,[178] sustained an act[179] which *required* Pierce County, alone, to levy a tax on property in that county for the purpose of financing the purchase of land in that county, which land was to be deeded to the United States for a military training camp and supply station. In a rambling opinion, which cites and quotes from a number of cases in other states without noting whether the constitutions of the other states contained a provision similar to article XI, section 12, and cites and quotes from earlier Washington cases without distinguishing between mandatory and permissive acts or acts involving taxes and assessments for local improvements, the court sustained the act. After stating that acquisition and transfer of land to the federal government for military

[175] 48 Wn.2d 783, 296 P.2d 680 (1956).

[176] Wash. Laws 1955, c. 253. This act required that the assessed valuation of property as equalized by the state board of equalization, rather than the assessed valuations determined by the county assessor and equalized by the county board of equalization, be used as the base for the levy of taxes on property for school district purposes.

[177] The Ryder Act was held invalid, however, by a vote of 5 to 4. Two of the judges concurred with the three judges referred to in the text, but based their decision wholly on conflict with another section of the state constitution. Four judges voted to uphold the act, and expressly relied upon he reasoning in Newman v. Schlarb.

[178] 95 Wash. 214, 163 Pac. 744 (1917).

[179] Wash. Laws 1917, c. 3.

purposes is a proper exercise of the sovereign power of the state, the court came to the highly questionable conclusion that a single county, as an agency of the state, can be required to perform this function and be *required* to levy taxes on property within that county *only* for the purpose of financing the project. It is submitted that, if this tax is for a county purpose, the holding flagrantly disregards the obvious intent and purpose of article XI, section 12. It is a tax levied by the state legislature on property of inhabitants of the county for a purely local purpose, which meets all three of the requirements for application of the section. On the other hand, if solely a state purpose is involved, its cost should be borne by the entire state, not by a single county. Although not violative of article XI, section 12, a tax on the property in one county only for a state purpose should have been regarded as violative of the uniformity requirement of article VII,[180] because, as a tax for state purposes, it is not imposed alike on all property in the state and thus lacks geographic uniformity. The court, however, was equally cavalier in its treatment of this constitutional objection to the act.

Nipges v. Thornton[181] is another case which involves the "purpose" requirement of the section.[182] The statute in question levied a poll tax. It was applicable throughout the state. The duty of collecting the tax and remitting eighty per cent of the proceeds to the state treasurer was placed upon a designated county officer. The statute further provided that twenty per cent of the amount collected was to be retained and put into the county expense fund. The court held that this was a tax for state, not county, purposes as to the twenty per cent retained, as well as to the eighty per cent remitted to the state. Although there was nothing in the opinion to indicate how closely the retained percentage correspond with the actual costs of collection incurred by the county, the court held that the retained portion of the collections was not a tax imposed by the state for county purposes but was a reasonable method of reimbursing the county for acting as collector of state taxes.

From the cases reviewed, it is apparent that the court has been strongly inclined to find a state purpose, rather than a local purpose, in the acts which have been presented for its consideration. The inter-

[180] At the time of this decision the general uniformity provision with respect to property taxes was in WASH. CONST. art. VII, § 2 (1889).

[181] 119 Wash. 464, 206 Pac. 17 (1922).

[182] In this case the other two requirements for application of the section were clearly present. It was a tax and it was imposed by the state legislature. Being applicable throughout the state it was upon the inhabitants of the counties.

twining character of both the activities and the fiscal problems of the state and its subdivisions would seem fully to justify this approach.

As previously stated, the three requirements for application of section twelve are that the legislative act (1) impose a tax (2) for a local purpose (3) upon a protected entity. The requirement here first stated, *imposition of a tax,* is the last of the three to be considered.

Whether the legislative act involves a tax or some other type of burden is the first problem under this requirement. An ad valorem property tax is such a tax, but a special assessment, or a special tax, for benefits accruing from a public improvement, the amount of which burden is determined by the benefits conferred and not by the value of the property, is not a tax within the meaning of this section.[183] A poll tax is a tax within the meaning of this section,[184] and, although the court has not had occasion to consider the question, it seems apparent that this is also true with respect to all types of taxes which are commonly designated as excise or privilege taxes. A statute which requires a county or city to incur expense, which may have the practical effect of increasing taxes in the local subdivision, does not constitute the imposition of a tax within the meaning of the section if the statute does not legally require taxes.[185]

The second aspect of this requirement is whether the state legislature has *imposed* a tax. Here, the issue is whether the legislature has merely authorized the appropriate authorities of the local subdivision to determine whether a tax shall be levied and collected or whether the legislature itself has made that determination without opportunity on the part of the local authorities to exercise discretion as to whether the tax shall be imposed in the particular municipality or other subdivision. This section is frequently referred to as a "home rule" provision, because its apparent purpose is to permit the legislature to authorize, but to bar the legislature from requiring, the levy and collection of any particular tax by any local governmental unit.

The distinguishing characteristic of "discretion" or the lack of it on the part of local authorities is well illustrated in three cases involving local improvement guaranty funds prescribed by the legislature.

[183] Bilger v. State, 63 Wash. 457, 116 Pac. 19 (1911); State *ex rel.* Conner v. Superior Court, 81 Wash. 480, 143 Pac. 112 (1914).

[184] Nipges v. Thornton, 119 Wash. 464, 206 Pac. 17 (1922).

[185] Hindman v. Boyd, 42 Wash. 17, 84 Pac. 609 (1906) (election expense); State *ex rel.* Clausen v. Burr, 65 Wash. 524, 118 Pac. 639 (1911) (act requiring local subdivisions to maintain a uniform system of accounts); State v. Pierce County, 132 Wash. 155, 231 Pac. 801 (1925) (act requiring county to pay to the state the cost of maintaining, in a state institution, certain patients committed from the county).

In *Hallahan v. Port Angeles*[186] a statute required cities to establish a fund to guarantee payment of local improvement bonds and interest and required annual tax levies for the guaranty fund. This was held valid under section twelve as applied to a local improvement authorized subsequent to the time the statute was enacted, because the tax required for the guaranty fund is not *imposed* by the legislature but is merely a condition attached to the power granted to the city. The tax is, thus, imposed by the local authority, not by the legislature. The local authorities could either authorize the local improvement with the attendant necessity of making the required tax levy for the guaranty fund, or they could refuse to make the improvement, thus avoiding the levy of the tax. In other words, a requirement that a tax be levied for a local purpose may be attached as a condition to an action which the city is authorized, but not required, to take. If the city authorities decide to take the action, the attendant tax levy is not *imposed* by the legislature within the meaning of this section. By taking the permitted action, the city, not the legislature, *imposes* the tax. This clearly illustrates that the legislature has great latitude with respect to the conditions which it may attach to the powers it grants to the subdivisions of the state.

On the other hand, statutes which require tax levies to finance a guaranty fund to protect the holders of bonds authorized and issued *prior* to the enactment of the state guaranty fund act constitute legislative *imposition* of a tax within the meaning of this section. The tax levies so required were directed by the legislature without opportunity for the local authorities to determine whether or not the tax burden should be locally imposed.[187]

Legislative enactments relating to assessment procedures and determination of the base upon which property taxes are levied by the counties, cities, and other municipal corporations (particularly school districts) have been a major source of litigation under this section. There is no doubt that the taxes involved in the several statutes meet two of the requirements for application of section twelve. Except in *Clark v. Seiber,*[188] the property taxes involved were for strictly local purposes. As each statute related to taxes on the property, real or personal, of inhabitants of counties, cities, school districts, or other

[186] 161 Wash. 353, 297 Pac. 149 (1931).
[187] Longview Co. v. Lynn, 6 Wn.2d 507, 108 P.2d 365 (1940); State *ex rel.* Wash. Mut. Sav. Bank v. Bellingham, 8 Wn.2d 233, 111 P.2d 781 (1941).
[188] 48 Wn.2d 783, 296 P.2d 680 (1956).

municipal corporations, the taxes to which these statutes related were upon objects within the protection of the constitutional provision. The problem in each case was whether the particular statutory provisions constituted legislative *imposition of a tax.* Involving ad valorem property taxes in each instance, each statute concerned what is admittedly a "tax" within the meaning of this clause. The sole question for consideration by the court in each case[189] was thus whether, under the act in question, a tax was *imposed* by the legislature. In some, but not all, of the cases, the court held that statutory provisions which related solely to matters concerning the tax base; that is, the assessed valuation of property, constituted an unconstitutional *imposition* of tax by the legislature. In each instance, the challenged act had nothing whatever to do with the levy of the tax. Whether or not a tax was to be levied or imposed upon the tax base as determined and the rate at which it was to be levied was solely within the control of the local authorities, subject of course, to the rate limitations established either by initiative measure or the constitutional provision previously mentioned.

The leading case is *State ex rel. State Tax Commission v. Redd.*[190] It involved an act which authorized the state tax commission, upon receipt of a protest and after a hearing thereon, to relist and revalue property in a county and required that the tax levies, for county and other local purposes and at millage rates determined solely by the appropriate county authorities, be applied to the assessed valuations as revised by the tax commission pursuant to the provisions of the act. The challenged act, thus, related solely to the tax base and in no way related to or infringed upon the power of the local authorities to determine whether a tax was to be *imposed* or the rate at which it was to be imposed. The court held that this act was violative of article XI, section 12, stating: "If the local authorities only, as we hold, have the power to list and value property within the county for local taxation purposes, no other authorities can legally relist and revalue that property for local taxation purposes."[191] The process by which the court reached the conclusion that only the local authorities have power to list and value property within the county for local tax purposes is

[189] Clark v. Seiber, 48 Wn.2d 783, 296 P.2d 680 (1956) is an exception. As previously pointed out this case also involved the aspect of state or local purpose.

[190] 166 Wash. 132, 6 P.2d 619 (1932). The opinion in this case contains a number of statements relating to constitutional requirements for which there is no apparent foundation in that document.

[191] *Id.* at 147, 6 P.2d at 625.

far from clear. The conclusion appears to be based more upon consideration of statutory provisions, other than those in the act in question, relating to property taxation than it does upon the wording of the constitutional provision. The statutory provisions for state assessment of the operating properties of railroads in more than one county were approved on the basis that they promoted the uniform application of the tax laws.[192] The fact that the legislature, in the act considered in the *Redd* case, as well as in the act directing assessment of inter-county operating properties of utilities, was seeking to attain the uniformity and equality of property taxes demanded by the constitution[193] received no consideration by the court. Neither did the court satisfactorily explain why assessment of inter-county utility properties was any less an *imposition* of taxes by the legislature within the meaning of article XI, section 12, than was the relisting and revaluation of property in the county. Since both were done for the purpose of providing the base for the county levy, it is difficult to discern the difference.

The court has upheld a statute which (1) authorizes the state board of equalization to value the operating properties of public service companies situated in more than one county of the state and (2) requires the counties to utilize the assessed valuations determined by the state board as the base upon which the local subdivisions are authorized to levy property tax. To require the county to utilize the state board's valuation of the operating property of a utility which is wholly within one county would, however, violate this constitutional provision, constituting an invalid "imposition" of a tax.[194] The court has also held that a statute abolishing the office of township assessor and the town board of review and vesting the power to make assessments and to review them in the county assessor and county board of equalization is not a violation of this section.[195]

In another case the court held that the directors of a school district cannot, on their own volition, utilize as the base for the school district levy, the valuation of property in the district as equalized by the state board of equalization for state tax purposes. The school district was

[192] *Id.* at 154, 6 P.2d at 627.
[193] WASH. CONST. art. VII, § 2 (1889).
[194] Northwestern Improvement Co. v. Henneford, 184 Wash. 502, 51 P.2d 1083 (1935). See also State *ex rel.* Yakima Amusement Co. v. Yakima County, 192 Wash. 179, 73 P.2d 759 (1937) (original assessment by state tax commission of property wholly within a county prohibited by the section).
[195] Opportunity Township v. Kingsland, 194 Wash. 229, 77 P.2d 793 (1938).

thus required to use the valuations as determined by the county assessor.[196] In reaching this conclusion, the court relied upon article XI, section 12, stating:

> It seems clear to us that to permit the appellant to make its levy on the basis of the valuation fixed by the state board of equalization would, in effect, amount to an imposition of taxes by the legislature "upon counties, cities, towns or other municipal corporations" for local purposes.[197]

It may be amusing to speculate why the legislature would, "in effect" or otherwise, impose a tax for local purposes if the school directors were permitted voluntarily to select one, rather than the other, of two assessed valuations, each fixed pursuant to statute by an officer or agency of a governmental unit separate and distinct from the school district. The court did not offer any explanation. Twenty-two years later, after extensive study by the Legislative Council of the tax imbroglio affecting all levels of government in the state and with a much more widespread understanding of the interrelation of state and local fiscal problems, the legislature tried again. This time, however, the statute *required* school districts to utilize valuations determined by the state board of equalization as the base to which the levy, at the rate determined by the directors of the district, was to be applied. This time only three members of the court believed that article XI, section 12, was violated by the legislative mandate that the state board's equalized valuations be used as the base for school district levies. The other six judges apparently all believed (four joined in a dissenting opinion expressly so stating) that this section was not violated, even though use of the state board's valuations was mandatory. The act, however, was held invalid because two of the latter six judges held it conflicted with another provision of the state constitution.[198]

It is difficult to understand why legislative selection of the agency to perform the purely administrative function of assessment, that is, of determining the factual issue of valuation of property, constitutes "imposition" of a tax by the legislature in some instances[199] but not in

[196] State *ex rel.* Tacoma School Dist. v. Kelly, 176 Wash. 689, 30 P.2d 638 (1934).

[197] *Id.* at 692, 30 P.2d at 639.

[198] Clark v. Seiber, 48 Wn.2d 783, 296 P.2d 680 (1956). The two judges who voted to invalidate the act under another section did not join in the opinion of the three who voted invalidity under art. XI, § 12.

[199] State *ex rel.* State Tax Comm'n. v. Redd, 166 Wash. 132, 6P.2d 619 (1932) (revision by state tax commission of valuations determined by the county assessor); State *ex rel.* Tacoma School Dist. v. Kelly, 176 Wash. 689, 30 P.2d 638 (1934) (optional utilization by school directors of valuations determined by state board of equalization in preference to valuations determined by county assessor); Northwestern Improve-

others.[200] Why does administrative determination of a fact constitute a prohibited legislative *imposition* of tax in one case and not in another? The cases fail to reveal any rational basis for the differing results. Certainly the differences are not required by the constitutional language.

It is also difficult to understand why the legislature has the power to attach conditions to the grant of power in some instances—even to the extent of imposing a condition that a tax must be levied, as in *Hallahan v. Port Angeles*,[201] as an incident to the exercise of a power granted to a local subdivision—but, in some but not all instances, is constitutionally barred from designating the agency to perform an administrative function which is merely preliminary to the legislative function of levying the tax. The constitutional language does not state that the distinct functions of assessment and levy are inseparable. The language is permissive. The legislature may grant the power to assess, and it may grant the power to collect. In fact, the word "levy" does not appear in the constitutional provision. A statute transferring the administrative function of assessment of all property from the county assessors to the state tax commission and requiring the counties and other municipal subdivisions to utilize the assessed values determined by the state agency should no more be in conflict with the language of article XI, section 12, than was the statute in *Opportunity Township v. Kingsland*,[202] which transferred the assessment function from the township assessor to the county assessor without disturbing the existing delegation of the levy power to the township authorities.

The constitution does not prohibit separation of the two distinct functions of assessment and of power to levy taxes. This has been expressly recognized in the case of township property and in the case of inter-county operating properties of utilities. Legislative designation

ment Co. v. Henneford, 184 Wash. 502, 51 P.2d 1083 (1935) (utilization of valuations of public utility properties by state tax commission, when the properties are situated in one county, but not when operating properties are in two or more counties); State *ex rel.* Yakima Amusement Co. v. Yakima County, 192 Wash. 179, 73 P.2d 759 (1937) (utilization of valuations determined by the state tax commission in preference to valuations determined by the county assessor).

[200] Northwestern Improvement Co. v. Henneford, 184 Wash. 502, 51 P.2d 1083 (1935) (valuations of public utility operating properties situated in two or more counties of the state); Opportunity Township v. Kingsland, 194 Wash. 229, 77 P.2d 793 (1938) (valuation of properties in a township by the county assessor, in preference to valuations by township assessor); State *ex rel.* King County v. State Tax Comm'n., 174 Wash. 668, 26 P.2d 80 (1933) (valuations determined by the state tax commission, in preference to valuations fixed by county board of equalization, under statute authorizing appeals from the county board to the state commission).

[201] 161 Wash. 353, 297 Pac. 149 (1931).

[202] 194 Wash. 229, 77 P.2d 793 (1938).

of a county officer, the county assessor, as the appropriate agency to determine the assessed valuation of property for the purposes of city school districts[203] and various other taxing districts has been consistently accepted. Selection of the officer or agency to perform the administrative function of assessment must be a matter for determination by the legislature in all, not just in some, situations, because the constitution itself draws no such lines of demarcation. It is submitted that a judicial construction of the constitutional language which imposes restrictions, not expressly and clearly stated in the constitution, upon the legislature's power to determine policies in this area constitutes an encroachment upon the powers of the legislature, contrary to the doctrine of separation of powers, which is the foundation of our form of constitutional government.

Article two, section forty: dedication of taxes to highway purposes. Another type of constitutional restriction on legislative discretion with respect to state fiscal policy is found in amendment eighteen.[204] The first sentence of this provision reads as follows:

> All fees collected by the State of Washington as license fees for motor vehicles and all excise taxes collected by the State of Washington on the sale, distribution or use of motor vehicle fuel and all other state revenue intended to be used for highway purposes, shall be paid into the state treasury and placed in a special fund to be used exclusively for highway purposes.

The second sentence contains a detailed specification of items to be included under the term "highway purposes" and concludes with a proviso which reads as follows:

> *Provided,* That this section shall not be construed to include revenue from general or special taxes or excises not levied primarily for highway purposes, or apply to vehicle operator's license fees or any excise tax imposed on motor vehicles or the use thereof in lieu of property tax thereon, or fees for certificates of ownership of motor vehicles.

While the legislature still has the right to determine whether motor vehicle license fees or excise taxes on the sale, distribution, or use of motor vehicle fuel shall be levied by the state and still has discretion with respect to the amount of such fees and excise taxes to be collected,

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[203] Express approval is implicit in Newman v. Schlarb, 184 Wash. 147, 50 P.2d 36 (1935), and State *ex rel.* Tacoma School Dist. v. Kelly, 176 Wash. 689, 30 P.2d 638 (1934).

[204] This amendment, approved in 1944, adds to art. II of the state constitution a new section, numbered 40.

this constitutional provision makes it mandatory that the entire amount of these fees and excise taxes be devoted exclusively to highway purposes. No part of such fees or excise taxes collected by the state can be utilized to defray other costs of government. Thus, although those who purchase at retail or use articles of tangible personal property other than motor vehicle fuel make a contribution to the general costs of state government at the time of making such purchase or use, the entire tax contributions of purchasers and users of motor vehicle fuel are constitutionally dedicated to one special purpose. Equal contribution to the general costs of state government by reason of such purchase or use is constitutionally forbidden. Conceding that motor vehicle license fees and taxes on motor vehicle fuel are not only an effective but a most appropriate method of obtaining funds to cover the cost of building and maintaining highways and that these taxes most fairly distribute such costs among those who derive special benefits from the use of the highways, the policy of dedication of *all* revenue from these sources may very well be open to question in a state which relies so extensively on sales and use taxes for the support of state government in general. The majority of the voters, however, accepted this policy.

What constitutes "other state revenue intended to be used for highway purposes" within the meaning of the first sentence and "revenue from general or special taxes or excises not levied primarily for highway purposes" within the meaning of the first clause of the proviso may be productive of future controversy. Does legislative intent control? In the absence of an express legislative statement that the proceeds of a particular tax are for highway purposes, is the constitutional provision applicable? Or must the legislature negative such intent? And, if it does state a negative intent, will the court review that statement and make its own independent determination? When is a tax "primarily" levied for highway purposes? These, and other unanswered questions, must receive legislative consideration in formulating a tax program for the state.

Another problem is whether this constitutional dedication, particularly with respect to taxes on the sale or use of motor vehicle fuel, is applicable only to such taxes levied by the state, as opposed to the counties, cities, or other sudivisions of the state. As the constitutional provision contains the modifying words "collected by the State of Washington," it appears that the only tax proceeds subject to the

constitutional dedication are those levied by the state itself. The legislature, consequently, may authorize the counties, cities, school districts, or other subdivisions to levy taxes on the sale or use of motor vehicle fuel for local purposes, freed from dedication to highway purposes, unless, of course, the words "State of Washington" are interpreted to have the most unusual, and unlikely, connotation of including the local subdivisions as well as the state itself.

III

The preceding sections of this paper have explored a number of inter-related problems confronting the legislature and the people of the state in planning for state and local government over the next decade. The probabilities of significant changes have been noted, particularly those that will substantially increase the proportion of personal income required for the support of the state and local government. The proportions of these future needs add unavoidable urgency. Difficult and perplexing issues of public policy must be resolved, and resolved in the proximate future, to avoid a compounding of problems that would make sound solutions all the more elusive. Taken together, the forces at work shape issues in three major areas. *First,* in designing the ways by which the economic capacities of the state can most equitably be reached for the support of state and local government, what scope of action is available ot the legislature? *Second,* in strengthening the effectiveness of public services, to assure fair value in services for fiscal support exacted, can the legislature take the steps that are indicated? *Third,* in bringing present day methods to bear upon the utilization of fiscal resources, can the legislature act with reasonable flexibility? The present situation with respect to each of these areas will now be summarized.

CONSTITUTIONAL LIMITATIONS ON TAXATION

Taxes on property. In the case of taxes on property, the constitutional restrictions which confront the legislature are many and varied in character. Some relate to the tax levy, some to assessment procedures.

The maximum property tax levy for state and local purposes specified under amendment seventeen of the constitution is fixed and, in so far as the legislature is concerned, practically inflexible. The legislature may determine the maximum rate of levy by the state and by each of the several types of local subdivisions except port and power dis-

tricts. The aggregate of the several levies by the state, the county, the city, the school district, and the other taxing districts, however, cannot exceed the constitutional forty mills on a theoretical assessed valuation of fifty per cent of true and fair value in money. By vote of the people in any taxing district, additional levies may be made. The constitutional requirements, however, are stringent. For current operations, such additional levies can be for one year only. Bonded indebtedness for capital improvements only can be authorized by vote of the people with attendant additional tax levies over a period of years to pay the principal and the interest on such indebtedness. In both instances, however, the additional levy must be approved by sixty per cent of those voting on the proposition, and at least forty (in some districts, by statute, fifty) per cent of those who voted in the taxing district at the last general election must cast votes on the proposition. This means that, by merely staying away from the polling booth, an elector in effect casts a negative vote on the proposition.

With respect to assessment, amendment seventeen stipulates that all property subject to taxation shall be assessed at fifty per cent of its true and fair value in money. A number of studies of assessed valuations as determined by county assessors and equalized by county boards of equalization have shown, beyond all doubt, that the constitutional level of fifty per cent of true value is, on the average, never attained. These studies show that the actual ratio of assessed value to sales price of single properties varies from an approximate maximum of ten times the sale price to an approximate minimum of three-tenths of one per cent of such sale price. They also show that the average ratios of assessed valuations to sale in the several counties vary from a low of 13.3 per cent to a high of 38.5 per cent. With these deficiencies in the existing procedures of assessment well known, the so-called "home rule" provision of the state constitution has been construed by the court to frustrate every effort by the legislature to establish effective procedures to attain what the constitution demands; namely, uniform taxation of all property in the state at the constitutionally prescribed percentage of its true and fair value in money. The frustration of these legislative efforts has been justified, apparently, on the theory that the level of assessed valuation of property for local tax purposes is purely a matter of local concern. This disregards two most important facts of which the legislature, but apparently not the court, is cognizant. The first is that uniformity of taxation, demanded by the constitution,

as between different classes of property does not exist, either within the boundaries of each separate county or as between the several counties. The second is that varying ratios of assessment in the several counties produce lack of uniformity of taxation throughout the state. This is true because, with constitutionally prescribed millage limitations and below-constitutionally prescribed property valuations combining to produce in the several local subdivisions less than enough to pay for the services demanded by the electors, the state has been forced to assume more and more of the costs of functions formerly financed by local property tax levies. The over-all consequence is a premium upon disregard of the constitutionally prescribed assessment ratio, because the counties assessing at the lowest ratios thereby succeed in shifting the greatest portion of the cost of their own local government to taxpayers in other parts of the state.

No one questions the proposition that property owners must bear a fair share of the cost of government. Neither is it seriously questioned that the property tax is a suitable instrument—probably the most suitable—for financing the cost of government in the local subdivisions. But it is also beyond question that the Washington legislature is impaled on the horns of a constitutional dilemma. Between the constitutionally fixed maximum levy and the judicially construed lack of legislative power to establish effective assessment procedures, the hands of the legislature are effectively tied. The solutions appear to lie in these alternatives. The first is either upward revision or complete elimination of the constitutional levy limitation. The second alternative is double-pronged. One approach would be to amend the "home rule" provision of the constitution to clearly permit effective legislative determination of assessment procedures for all purposes. The other is for the court to take a more realistic approach, reappraise its holdings, and retreat from the construction which has operated to defeat legislative efforts to attain uniformity in the actual application of the property tax throughout the state. Under either of these, the legislature must have complete power to fix the policies and the procedures through which it seeks to attain, in actual operation, uniformity to the full extent possible under modern procedures of tax administration—not just theoretical uniformity or a level of uniformity which meets the minimum legal standards thereof.

Intangibles. Taxation of intangibles as property on an ad valorem basis is frequently suggested, either as a supplement to the property

tax on real estate and tangible personal property or as an alternative to a tax on income from such intangibles. There is no doubt that intangible personal property represents a very substantial portion of the total wealth of individuals and, to a lesser extent, of corporations in this state. Intangible personal property includes bank deposits, corporate stocks, bonds, notes, other evidences of indebtedness, beneficial interests under trusts, and various other types of rights or claims. The taxation of this type of wealth under the ad valorem property tax is, in this state, subject to some specific constitutional restrictions. The taxation of some, but not all, such property is constitutionally barred. The difficulties of determining the types of credits which are constitutionally exempt and separating them from those which may constitutionally be taxed, present formidable, if not insurmountable, difficulties from the legislative standpoint, as well as from the standpoint of tax administration. These difficulties appear to be so great that, in this state, taxation of all credits appears to be, for all practical purposes, forbidden. This being the constitutional and administrative situation, it seems unnecessary to consider here the serious questions of administrative feasibility of such a tax when it is constitutionally permissible to tax credits of every kind.

Income taxes. A tax on the income of individuals and corporations can take any one of several forms. The most common form of personal income tax is the tax on net income of individuals, with graduated rates and exemptions varying in amount upon the basis of the marital status and number of dependents. By classifying such a tax as a tax on property within the meaning of the state constitution, article seven, the supreme court of this state has effectively and consistently blocked a personal net income tax with graduated rates and varying personal exemptions. Although the holding is unique in this country, a corporate franchise tax measured by net income, without graduation in rates and without exemptions, is also invalid when no state tax is levied on the net income of individuals and partnerships. Notwithstanding almost universal recognition of the essential fairness of the graduated personal net income tax, as opposed to consumption taxes and taxes measured by gross income, and wide-spread acceptance of net income as the most appropriate measure of a corporate franchise tax, taxation of the net income of either individuals or corporations in the manner such income is taxed by approximately two-thirds of the states is prohibited. Amendment of the state constitution expressly to

authorize taxation of the net income of individuals and corporations is without doubt the only means of making it possible for the legislature or the people effectively to impose such a tax.

Without such amendment, legislative effort to construct an effective tax on net income conforming with existing constitutional restrictions seems futile. When a tax on, or measured by, net income is treated as a tax on property, as it has been by the Washington court, it is subject not only to the uniformity and limited classification requirements of article VII, section 1 (amendment fourteen) but also to the forty-mill limitation of section 2 (amendment seventeen). How the forty-mill limitation would operate on a net income tax is not altogether clear. If the taxable net income, as computed, is treated as the property taxed, the forty-mill limitation would appear to impose a maximum rate of two per cent of such computed taxable net income. A further question would be whether the state could impose the tax at a flat rate of not to exceed two per cent or whether the computed taxable net income would have to be extended on the property tax assessment rolls and be subject to the levies for the state, the county, the city, the school district, and so forth, the same as real and tangible personal property. It would appear that, being personal property, net income could, under section one, be put into a class separate and distinct from other personal property and be taxed only by the state if the legislature so desired. This being permissible, under amendment seventeen the state could levy, for state purposes, the maximum permissible rate if all local subdivisions were barred from applying their property tax levies to this class of property.

However, it is possible the court might say that the tax imposed is, in effect, a tax on the property from which the taxable net income is derived, rather than a tax on the computed net income itself as property. The court has taken a similar position in the case of net income from real estate, saying that a net income tax on rent from real estate is a tax on the real estate from which the rent is derived. So treated, the maximum amount of tax permissible would have to be computed on the basis of the assessed valuation of the property from which the net income was derived, rather than by applying the rate limitation to the net income itself. As a very high percentage of personal property from which income is derived—all credits, for example—are not assessed for property tax purposes, such a construction would inject so many complexities that a property tax on net income would be infeasible from

an administrative standpoint, if not constitutionally barred because of unpredictable variations in its impact. Just how this theory would operate in the case of income derived from personal services is conjectural to the nth degree. In fact, this aspect shows how impractical and unrealistic, from the standpoint of effective fiscal planning, are the basic premises which cause this type of futile theorizing to be necessary.

Summarizing, it would seem that, without a constitutional amendment specifically authorizing a tax on net income, the legislature may possibly, but far from surely, have the power to levy a tax on net income from personal services and personal property, tangible and intangible, but excluding income from real estate. There could be no variation in the deduction for personal exemption. The tax must be levied at a flat rate. The amount of the tax could not exceed two per cent of the computed taxable net income if the court construed the tax as one on the net income itself. If the court construed the tax as one on the property from which the net income is derived, a tax on net income, even so restricted, would be either impractical because of administrative complexities or constitutionally barred because of its haphazard impact—or both.

Another form of income tax is one which utilizes gross income, rather than net income, as the measure of the tax. In sustaining the state business and occupation tax upon persons, firms and corporations engaging in business activities, the court approved a tax measured by gross income. It would seem that a tax on resident individuals and corporations doing business in the state measured by gross income from all sources, including salaries, wages, dividends, interest, and rent as well as business income, should be similarly sustained as an excise tax, rather than a tax on property in the constitutional sense. If the tax base includes gross income from sources other than business activities, however, there may be some doubt. Some statements by the court in a case involving a city-levied tax may indicate a lack of legislative power to treat the receipt of salary or other compensation for services rendered as a proper subject of excise taxation.

The federal commerce clause restrictions make a tax measured by gross income much less desirable than a tax measured by net income because of the greater restrictions and limitations applicable to the former. The experience of Indiana with its gross income tax well-illustrates this. Furthermore, widespread dissatisfaction exists in this state with respect to the business and occupation tax because of the

unfairness of the gross income measure. Thus, even though an all-inclusive tax measured by gross income might be upheld constitutionally, it is clear that a proposal to levy such a tax would meet great opposition from the business community, representatives of which are urging change in or elimination of the present tax measured by gross income.

Still another form of tax which is sometimes regarded as a tax on income is the tax on consumers. A tax on retail sales or a tax on the use of articles purchased at retail is such a tax. Although a form of income tax, such taxes are actually taxes on expenditures, or outgo, rather than on income; unspent income is accordingly excluded from the tax base, but consumption expenditures out of capital are included in it. Thus, only if the taxpayer spends all of his income, and no more than his income, for taxed articles, is this truly an income tax. This type of tax has met the test of validity under the state constitution and is in existence in this state. Broadening of the definition of the transactions to which the retail sales tax and the use tax apply is one alternative open to the legislature. Another alternative is to increase the rate applicable to the present base of these taxes. In either case, the legislature is confronted with no obstacle under the state constitution.

Business taxes. State-levied taxes on persons and other entities engaging in business activities are permissible and have been sustained under the various constitutional provisions, federal and state. The general business and occupation tax, in effect in this state since 1933, is a prime example, but only one of many examples, of a tax of this kind. Although some persons and firms doing business in the state are either partially or wholly exempt from such taxes because of conflict with the requirements of the commerce clause or the doctrine of intergovernmental immunities, such taxes encounter no substantial obstacles under the provisions of the state constitution, because they are excise taxes and not taxes on property. The legislature has broad power in its choice of the business activities to be taxed and exempted. There must be a reasonable basis for the legislative classification, but the legislative determination is most infrequently upset. The legislature may vary the rates and tax different classes at different rates. If it desires, the legislature may impose more than one tax upon persons engaging in a particular type of business. With one exception, the legislature has freedom in the choice of the tax base and may, as it has

in the past, prescribe different tax bases for different classes of taxpayers.

Other than the requirement of reasonableness of classification, the only substantial restriction under the state constitution appears to be that net income cannot be utilized as the base for determining the amount of tax payable. Whether even this restriction exists is open to doubt. Although the court has consistently disapproved taxes on, or measured by, net income heretofore enacted by either the electors or the legislature, none of the earlier acts using net income as the tax base has been framed to apply only to persons, firms, and corporations engaging in business activities in the state. The court has said that such a tax, when measured by gross values, gross proceeds of sales, or gross income, is an excise tax and not a tax on property in the constitutional sense. If only the tax base of the business and occupation tax were changed so that the amount of the tax payable were determined by reference to net income rather than gross income or other gross measure, the court might conclude that the tax is still an excise and not a property tax. Otherwise, it would be forced to say that the utilization of net income as the tax measure, and that alone, makes a tax a property tax. After saying that a tax on business activities measured by gross—the entire take—is an excise, to say that the same tax is a property tax if measured by net income would, to say the least, seem totally to disregard both the economic and practical realities. The court, however, could simply rely on its statements in *Power, Inc. v. Huntley* to classify the tax so measured as a property tax.

There is no certainty that a tax on the business activities of all individuals and other legal entities measured by net income would have the judicial sanction which is required for such an act to be operative. Utilization of net income, rather than gross income, as the tax measure provides a method of meeting the objections to the gross income measure which have been so frequently voiced on behalf of businesses operating on a low profit margin. Utilization of net income, rather than gross income, as the tax measure would also broaden the tax base by avoiding those requirements of the federal commerce clause and the governmental immunities doctrine which are more drastic with respect to state taxes measured by gross income than with respect to such taxes measured by net income.

Other excise taxes. Taxes on the performance of a variety of acts, other than engaging in business, are likewise excise taxes, rather than

property taxes, in the constitutional sense. The power of the legislature to select the activity to be taxed and to prescribe the amount of tax payable is the same as it is in the case of excise taxes on business activities. The legislature has a very broad discretion, and its policy determinations are most infrequently upset by the courts. Illustrative of taxes in this category are the retail sales tax, the general use tax, the tax on use of motor vehicles, the tax on sale, use or distribution of motor vehicle fuel, and the tax on sale of cigarettes. Also included are transfer taxes, such as the inheritance tax, the gift tax, and the tax on conveyance of real estate. The federal commerce and due process clauses operate to free some transactions from state taxes of this type, as does the governmental immunities doctrine. In addition to reducing the state tax base, these provisions create competitive inequalities between, and hardships on, distributors of taxed commodities and services. They also produce difficulties in effective administration of some of these taxes. But, from the standpoint of the state constitution, the legislature may select virtually any activity or transaction as the object of a state tax. If there is a reasonable basis for the legislative selection, the tax base, with one exception, is solely for legislative determination. The rate of the tax is, likewise, solely a matter of legislative policy. The exception mentioned above is that the state court has always held invalid any tax of this type which employed net income as the tax base. But, aside from this judicially evolved restriction, the legislature is not hampered by any substantial state constitutional restrictions upon its choice of the object, the base, or the rate of such taxes. The economic and social factors, including the weighing of the tax burden imposed by this state, in comparison with that of states which are competitive with Washington, are the most significant elements with which the legislature must deal in this area.

Poll tax. Although the capitation tax, often called a poll tax or head tax, is generally in very low repute in this country, it should be noted that there is no constitutional barrier to such a tax by the state. Such a tax, in operation for only a short period of time, has been upheld as an excise tax and not a property tax in the constitutional sense.

The legislature, consequently, has the same breadth of discretion to classify the persons subject to the tax and to determine the rate, or rates, of tax upon different classes, if any, as it has in the case of business and other excise taxes.

Municipal taxes. The power of the various subdivisions of the state to levy taxes for local purposes depends upon express legislative grant of authority to tax. The legislature may grant the taxing power, or it may withhold it. It may grant the taxing power subject to conditions which it prescribes. It may grant the power to levy a tax to one or more, but not all, types of municipal subdivisions. With respect to taxes on property, the constitutional restrictions, as well as the judicial interpretations of the constitutional provisions, are appendant to the grant of power to levy such taxes. Whenever the legislature grants to the local subdivisions the power to levy taxes, that power is subject to the constitutional requirement that the taxes so levied shall be uniform with respect to the person or property in the jurisdiction which levies the tax. This requires geographic uniformity, but allows a wide latitude with respect to selection of the object, the tax base, and the tax rate. Presumably this discretion is as broad, and subject to the same limiting factors, as is the power of the legislature to levy the same tax for state purposes. The extent to which the legislature grants the taxing power for local purposes to the local subdivisions is, consequently, dependent far more upon consideration of a wide variety of non-legal factors than it is upon existing constitutional restrictions upon legislative power.

Constitutional Limitations on Fiscal Organization

First, what is the scope within which action is constitutionally possible for strengthening the effectiveness of governmental services? This question can be considered by examining three major areas: the allocation of services among jurisdictional levels, the organizational patterns used for administration, and the possibilities for employing reliable managerial methods.

In allocating services, the important consideration is to obtain balance among the need for service, the capacity to determine policy, the capacity to administer, and the availability of fiscal support. Under present circumstances in the state of Washington, the allocation is likely to be primarily influenced by the availability of financial support. Whatever the other criteria, services tend to settle within legal reach of means for supporting them. Other and equally important elements are not marked by the same degree of constitutional rigidity. Hence they are treated as less significant, a tendency that contributes to another set of maladjustments. Amendment seventeen, in particular, introduces constitutional inflexibility that skews the application of all

criteria for the distribution of service responsibilities among service levels.

It would seem that article VII and article XI, section 12, contemplate that state services shall be supported by state-imposed revenues, and local services by locally-imposed revenues. This theory would be reasonably workable with some accommodation for the intermediate situations of mixed state-local services, and it would not be inconsistent with criteria of sound administration, if the authority of local jurisdictions to provide local support could be geared to the realities of the present day scope of local services. But this cannot be done. The fiscal capacity of the local level is harnessed to the operation of the "forty-mill limit" and the practical possibilities for sharing excises with the state and for imposing local service charges. The portion of the local service load that cannot be financed in this fashion inevitably falls back upon the state revenue system, where it competes for support with services that are inherently state-wide in nature. As a result, Washington raises approximately seventy per cent of the total of all of its state and local taxes at the state level; after redistribution through grants and sharings, the proportion remaining for the support of state services is only forty per cent. To put the point the other way around, local units raise thirty per cent of the total taxes but utilize sixty per cent for the support of the services they administer. The broader criteria of policy responsibility and administrative capacity have given way. Property tax limitation seriously impairs the legislature's capacity to allocate service responsibilities in ways that make for effective and responsible government. Also involved, of course, are other constitutional provisions, particularly article VII, section 6, and article XI, section 12, but these would seem to be minor difficulties were it not for the effect of amendment seventeen.

With respect to organization, the controlling consideration is the capacity of the legislature to establish forms of structure that will reinforce, rather than defeat, the development of operating cohesion and the use of well-understood methods for effective management. There is much about the present constitutional structure that entrenches and legitimatizes ineffectiveness. It is self-evident that until the "long ballot" of the state government is substantially shortened, the governor as the operating executive of state administration will be unable to develop operating unity and coordination. This means a comprehensive change of article three. Specifications are not neces-

sary here; the objectives are clear-cut. In county government another set of needs has emerged. The role of county government is changing. In many parts of the state it has changed. The traditional administrative role of the county is outgrown. The time is approaching when boundaries will need readjustment to fit new patterns of local service areas. The area with which county government deals in much of the state is no longer essentially rural, with families meeting the predominant share of their service needs through a self-sufficient farm establishment. Rural population is clustering in rural neighborhoods, clusters that are too small for full incorporation but still need one or another degree of essentially urban services. Some service needs, indeed, such as fire protection, fan out over large areas containing a variety of small neighborhoods. From this condition has sprung the present tangle of special and junior taxing districts, the inconvenient step-children of the tax limitation system. It seems essential that a redesigned form of county government be equipped to provide competently administered services of assured quality and effectiveness, probably on a contractual basis, to the residents of these exurban neighborhoods. The home rule provisions of amendment twenty-one are not enough. Article eleven needs a comprehensive revision.

Second, is the matter of the sound and effective utilization of the fiscal resources of the state. The state government today is an operation with net transactions of over a billion dollars a year. Only about a third of this total is reflected in what is generally regarded as the state budget. A full quarter is not even included in the central financial records of the state government or brought under regular legislative and executive scrutiny. A troublesome state "deficit" appears in a general account, disappears in a general fund, and is absorbed without a trace in the over-all condition of the treasury. This is scarcely a context within which administrative management can be expected to function, or responsibility for the affairs of the state be enforced. From the constitutional standpoint, the difficutly is rooted in the interpretation of article VIII, section 4, and to a lesser extent in article VII, section 6. In view of the judicial decisions construing these provisions, particularly the former, it is difficult to identify, short of constitutional revision, any sound course of action toward a modern and thoroughly efficient system of fiscal administration.

This survey has aimed at identifying and evaluating the constitutional boundaries within which the state of Washington must approach

its fiscal problems, present and future. The conclusion is inescapable that the state and its communities are gravely constricted by a constitutional framework designed for a wholly different set of needs and circumstances. The future calls for new and vital approaches. Imagination, resourcefulness and innovation, now denied to the legislature, must be exercised in the years ahead. Difficult as present circumstances are, it must be remembered that they do not reflect a static condition. The state is in midstream of long-range development, moving, it appears, at an accelerating pace. To live in this future with statesmanship and civic wisdom, the state needs a fresh beginning in its basic law.