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Seattle Passes Municipal Income Tax; It is Almost Certainly Illegal.

Washington is one of the seven states that goes without an individual income tax, and most residents are pretty proud of that. In fact, voters in the state have voted down a constitutional amendment to allow a graduated income tax five times.

That could change though, as the Seattle City Council this week passed a local ordinance to enact an income tax on Seattle residents. The tax, which is 2.25 percent on income above $250,000 for single filers and above $500,000 for married filers, was unanimously adopted by the council on Monday.

The only problem is that the tax is almost certainly illegal under the state constitution and under state statute. As my colleagues Jared Walczak and Kari Jahnsen wrote in June, the tax would face some "serious legal hurdles":

1. ***The Constitutional Uniformity Clause.*** Article VII of the Washington constitution stipulates that all taxes must be "uniform upon the same class of property," and adopts an unusually broad definition of property that has been held to include income. The constitution also imposes a maximum combined rate of 1 percent. Seattle officials do not deny that their ordinance conflicts with current caselaw; the municipal income tax is seen as a test case to challenge the current interpretation of the uniformity clause.
2. ***A Ban on Local Net Income Taxes.*** Further compounding the city's challenges, there is a statutory prohibition against Washington localities adopting taxes on net income. The "net income" terminology was likely to exclude the local B&O gross receipts tax from the prohibition. But advocates of a Seattle municipal income tax argue that by imposing the tax on gross income rather than adjusted gross income, it cannot be said to fall on net income. This is arguably a strained interpretation of the statute. Net income is undeniably a subset of gross income, and thus subject to tax under the proposed ordinance.
3. ***Restrictions on Creating Local Taxes Not Expressly Authorized.*** The courts have held that localities must have an express grant of authority to levy a given tax, and of course, no statutes specifically authorize a local income tax. The Seattle City Council justifies the proposed income tax under statutory authority to establish licenses and permits, which may be too novel for the courts, not least because it is unclear that a right of residency could be subject to a licensing process.

For now, this tax looks to be a signaling stunt, as the Seattle Times reports that "proponents say the measure was intended to open a broader discussion about tax fairness." Councilmember Kshama Sawant even seems to recognize the unsteady legal footing of the measure, telling supporters, "If we need to pack the courts, will you be there with me?"

It of course goes without saying that purposefully enacting an illegal tax is poor policy. But as the Washington Policy Center notes, it is also likely to be an expensive exercise as the city will have to spend revenue defending the policy in court.

So, in the textbook sense, enacting an illegal tax violates the public finance principle of stability because you are creating business uncertainty about future tax burdens. But even on a more basic level, this charade invites some head-slapper questions like: if you say you need more revenue for government programs, why would you willfully set yourself up to spend revenue on a legal battle?

Tax Foundation

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