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Washington Surtax on "Big Banks" Struck Down as Unconstitutional

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On May 8, Washington's 1.2% surtax on "specified financial institutions" (banks with at least $1 billion a year in net revenue) was struck down by a King County Superior Court judge. Judge Marshall Ferguson ruled that the tax, which is imposed on top of all other taxes, violates the Commerce Clause of the US Constitution by discriminating against out-of-state banks in both purpose and effect.

In their briefs, attorneys for the Washington Bankers Association and American Bankers Association explained that an out-of-state bank would pay a much higher tax rate (and be at a competitive disadvantage) compared to an in-state bank because its global revenue is sufficient to trigger owing the surtax. The associations presented evidence that every bank meeting the definition of "specified financial institution" was an out-of-state bank, and that no in-state bank met the definition. Further, they pointed to statements by legislators appearing to show an intent to promote "local banks" and address a national wealth disparity and regressive taxation.

The state responded that the surtax is neutral on its face, applying to all businesses with $1 billion regardless of their headquarters location, and that none of the funds were used to subsidize or reduce tax burdens on in-state banks. They also argued that the tax should be presumed constitutional and rejected the plaintiffs' standing to sue as associations. The actual effect of discrimination seemed especially persuasive to Judge Ferguson, who asked counsel for the state, "If the tax so clearly falls on non-Washington businesses, is that not a discriminatory effect?"

The state may appeal the case, Washington Bankers Association et al. v. State of Washington et al., No. 19-2-29262-8, to the Washington Supreme Court.

Practice Note: The structure of the tax struck down in this case, a surtax imposed only if the company's global income exceeds a high threshold, has been on the rise. San Francisco's gross receipts tax on businesses with over $50 million in receipts, Portland's clean energy surcharge on businesses with over $1 billion in national gross revenue, and Maryland's proposed digital advertising tax based on a sliding scale of global revenue all come to mind. This ruling may be the first sign that judges will not be afraid to subject such taxes to scrutiny under Commerce Clause analysis.

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