Judge John Ruhl
December 6, 2017

IN THE SUPERIOR COURT OF THE STATE OF WASHINGTON
IN AND FOR THE COUNTY OF KING

S. MICHAEL KUNATH, Plaintiff, v. CITY OF SEATTLE, Defendant.	NO. 17-2-18848-4 SEA PLAINTIFF MIKE KUNATH'S MOTION FOR CR 11 SANCTIONS

I. INTRODUCTION

Plaintiff Mike Kunath brings this motion only after careful consideration. We live in a time when too many parties seek sanctions as a matter of habit and with little consideration to the reasons why sanctions are allowed in the first place. Parties must be free to make creative and novel arguments without fear that any deviation from established law will be penalized. At the same time, sanctions exist for a reason, and that reason is to prevent the assertion of truly baseless arguments.

Kunath also acknowledges that seeking CR 11 sanctions against a city is unusual. Under the facts of this case, however, the frivolous conduct is properly attributed to the City as an entity. The Ordinance was passed unanimously by the City Council, and two different mayors (Ed Murray and Tim Burgess) have elected to pursue the City's arguments in court. Jenny Durkan will take the position of Mayor before this motion is decided, and the approach that the new administration will take is not yet known. Pursuant to Article V, Section 7 of the Seattle City Charter, it will be Mayor Durkan's decision whether to continue the City's arguments on appeal, and the Court may well consider the City's decision in exercising its discretion on this motion. If the City formally accepts the Court's decision, an argument could be made that sanctions against the City would serve little purpose.

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The Economic Opportunity Institute steadfastly maintained throughout this action that the title of a bill includes the heading added by the Code Reviser after the bill has been enacted and after the legislative session has ended. The argument is contrary not only to Supreme Court precedent, but also to the purpose of those rules in the first place. The rule governs the legislative process, which has ended long before the heading is added. EOI knowingly made a false argument throughout this litigation, and it refused all opportunities to correct its course. EOI's conduct in this action is precisely the kind of thing that sanctions are intended to deter.

The City of Seattle likewise asserted a frivolous argument that the term "net income" does not include the income reported on Line 22 of IRS For 1040. As the Court said, Line 22 reports "net income" under and definition of the term, and the City's arguments to the contrary made no sense. Order at 19. By arguing that the Court should "do justice" instead of following the law, the City asked the Court to disregard the law. Dkt. 67 at 23.

The Court should send a signal that even the noblest of causes cannot justify frivolous arguments in litigation. The Court should declare EOI's arguments and the City's "net income" arguments frivolous and award appropriate terms.

II. RELIEF REQUESTED

Plaintiff requests that the Court enter a declaratory judgment that the Ordinance is invalid as a matter of law.

III. STATEMENT OF FACTS

The relevant facts are intertwined with the legal issues and discussed together below in the interests of efficiency.

III. STATEMENT OF ISSUES

Should the Court grant sanctions for frivolous litigation?

IV. EVIDENCE RELIED UPON

1. Files and records herein.

V. AUTHORITY

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Motions for sanctions are addressed to the trial court's discretion subject to a number of requirements. *Ames v. Pierce County*, 194 Wn.App. 93, 120, 374 P.3d 228, (2016).

> CR 11 requires attorneys to make certain guarantees when they sign pleadings, motions, briefs, and legal memoranda. *Biggs v. Vail*, 124 Wn.2d 193, 196, 876 P.2d 448 (1994). Specifically, an attorney's signature is his or her certification that the pleading, brief, or motion is " (1) ... well grounded in fact; [and] (2) ... warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law or the establishment of new law." CR 11(a). The rule is not meant to be a " fee shifting mechanism" or to " chill an attorney's enthusiasm or creativity in pursuing factual or legal theories," but to curb abuses of the judicial system and to deter baseless filings. *Biggs*, 124 Wn.2d at 197; *Bryant v. Joseph Tree, Inc.*, 119 Wn.2d 210, 219, 829 P.2d 1099 (1992).

Id. A trial court may not impose CR 11 sanctions unless it determines both that a filing is baseless, meaning (1) the claim was without a factual or legal basis and (2) the attorney who signed the filing failed to perform a reasonable investigation into the claim's factual and legal basis.

A. <u>The City of Seattle</u>.

The history of the Ordinance dates back to 2013, when a Millionaire's Tax became an issue in the City Council race. Newcomer Kshama Sawant proposed an income tax on people who earn more than $1 million per year, and incumbent Richard Conlin said that he agreed a progressive income tax would be welcome, "but we have no authority to do that and I see no sign that the legislature would ever give us the authority to do something like that." Exhibit A. Sawant disagreed, claiming that "the millionaire tax can be passed by the City Council as an excise tax. She also said the Economic Opportunity Institute has already created a sample ordinance as a basis for the proposed tax on people who make more than a million dollars a year." *Id.*

After Sawant was elected, the City Council began investigating the tax in earnest, but questions about its legality remained. In 2014, the Council passed a "Statement of Legislative Intent" that "requests the Law Department research the legal possibilities that exist to impose an excise tax on annual individual or household earnings in excess of $1,000,000." Exhibit B. The Report was due on April 1, 2015. *Id.*

The report was provided in April 9, 2015, but the City has refused to produce it in response to public records requests. Exhibit C. Although the contents of the opinion are unknown, efforts to enact an income tax ceased after it was issued.

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In 2017, the City Council again turned its attention the issue of an income tax, and on May 1, 2017, it adopted Resolution 31747 "expressing the City of Seattle's intent to adopt a progressive income tax targeting high-income households." Exhibit D. There is no evidence that the City Council sought another legal opinion on the validity of the proposed ordinance from the City attorney. Instead, the Council apparently relied on a March 31 2017 opinion letter from Smith and Lowney, PLLC to the Economic Opportunity Institute. Exhibit E.

Although one might expect a city to seek such an opinion from a neutral source, Smith and Lowney describes itself on its website as "committed to the public interest. whether confronting polluters, exposing corporate misconduct, or supporting community activists." Exhibit F. Claire Tonry of Smith and Lowney was one of two co-counsel for EOI leaders in 2016 litigation over a proposed income tax in Olympia. Dkt. 33 at ¶ 3. According to Tonry, "That litigation involved many of the same issues presented in the instant cases, including the constitutionality of and statutory authority for a city tax on income, as well as the constitutionality of RCW 36.65.030." *Id.* EOI and its counsel have been advocating for income taxes for a long time; they are dubious sources for an objective opinion.

When Kunath filed this action, the City took the unusual step of hiring outside counsel, Pacifica Law Group LLP. Exhibit G. As a result, City Attorney Peter Holmes did not sign the City's Motion for Summary Judgment or its Reply. Dkt. 47D at 24-25, 67 at 40. Whether the City retained outside counsel because Holmes was unable to give a CR 11 certification to its motion is unknown. The City could easily answer that question by providing the memorandum to the Court for *in camera* review.

Pacifica Law Group made different arguments than those in the Smith and Lowney memorandum, primarily arguing that the Ordinance does not tax net income. Although Pacifica Law Group itself said that net income means "the balance of gross income remaining after deducting related costs and expenses [usually] for a given period and losses allocable to the period," it nonetheless asserted that net business and other non-wage income reported on Line 22 of Form 1040 were not net income. Dkt. 47D at 6 (quoting Webster's Third New Int'l Dict. 1520 (1993)). In its ruling, this Court said that

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"Regardless of which of these definitions one uses, the conclusion is the same: the City's income tax is a tax on net income." Order at 19.

1. Definition of "Net Income."

The City has never denied that an ordinance that conflicts with RCW 36.65.030 is void. To escape the statute, it settled on the argument that "Total Income" in Line 22 of Form 1040 is not net income. The City therefore claimed that it enacted a tax on "Total Income" not on "net income."

The City therefore needed to construct an argument that the "Total Income" set forth in Line22 of Form 1040 was not "net income." Doing so proved impossible. The City offered two definitions and cited the *Audit & Adjustment* case, and the other parties added definitions from many sources (Dkt. 47D at 6), but as the Court said in its Order: "Regardless of which of these definitions one uses, the conclusion is the same: the City's income tax is a tax on net income." Order at 19.

Although its argument had no inkling of merit, the City kept repeating it over and over again as if saying it often enough would make it true. Basing a claim on a demonstrably false statement is frivolous. The Court should find the City's arguments regarding the "net tax" issue and award Kunath his attorney fees incurred in responding to it.

2. Excise Tax.

The City's argument that the tax was an excise tax appears to have been formed after this lawsuit was filed because the Ordinance was not written like an excise tax. An excise tax is a tax on a "on a taxpayer for voluntarily exercising a certain right or privilege. *Tesoro Refining and Marketing Co. v. State Dept. of Revenue,* 135 Wn.App. 411, 418, 144 P.3d 368 (2006). Income or other property interests can be used as the base or measure of the tax, but the tax itself is imposed on the right or privilege. *Watson v. City of Seattle,* 189 Wn.2d 149, 170, 401 P.3d 1 (2017).

Here, the Ordinance itself is entitled an income tax, and nothing in the Ordinance refers to an right or privilege. Moreover, the Supreme Court has already ruled that the privilege of being paid for working cannot be the subject of an excise tax in *Cary v. City of Bellingham*, 41 Wn.2d 468, 250 P.2d 114 (1952). Again, the Court's order makes it clear that this argument never had any merit at all.

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3. Other Considerations.

As stated above, whether the change in mayoral administrations makes a difference is a matter for this Court's discretion. Imposing CR 11 sanctions against city is an unusual act and should be reserved for unusual circumstances. By the same token, if the City responds by continuing to make the same false claim, that should be considered as well.

B. Economic Opportunity Institute.

This action was filed on July 14, 2017, and EOI filed its Motion to Intervene on September 6, 2017. Dkt. 31. In paragraph 38 of its Intervention Complaint, EOI alleges that "The Senate Bill embodying Chapter 36.65 RCW, Substitute Senate Bill No. 4313, is entitled 'City-County Municipal Corporations -- Clarification - An Act Relating to local government; and adding a new chapter to Title 36 RCW.'" On page 4 of its summary judgment motion, EOI asserted that "The first iteration of the bill was Senate Bill 4313, entitled 'Authorizing the formation of combined city and county municipal corporations under Art. XI, section 16 of the Constitution.'" Dkt. 47A. On page 5, it asserted that "Substitute Senate Bill 4313 ('SSB 4313') was entitled 'CITY-COUNTY MUNICIPAL CORPORATIONS ---- CLARIFICATION AN ACT Relating to local government; and adding a new chapter to Title 36 RCW.'" *Id.* On page 9, EOI claims that the title "limits the bill to clarification concerning city-counties, signaling that it will not create new substantive law." *Id.* And again on page 12, EOI says that "the title 'CITY-COUNTY MUNICIPAL CORPORATIONS – CLARIFICATION AN ACT Relating to local government; and adding a new chapter to Title 36 RCW' explicitly mentions city-counties, but fails to mention stand-alone cities and counties." *Id.*

In his response, Kunath pointed out in excruciating detail than none of this was true. Dkt. 58. He provided copies of the bills with their actual titles, explained the process and authorities behind the Session Laws. It is the same as SSB 4313: "An Act relating to local government." *Id.* The information provided by Kunath was factual and indisputable.

Even after all of this was neatly laid out by Kunath, EOI continued to make the same false statements in its Reply. It called Kunath's argument "simplistic" and repeated its assertion that "he is simply incorrect that the Court must disregard the first half of Substitute Senate Bill 4313's title, which

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reads "CITY-COUNTY MUNICIPAL CORPORATIONS ---- CLARIFICATION." Reply at 5. It asserted that "courts regularly look to the full title of the relevant session law to assess compliance with Article II, section 19 of the Constitution," but two of the three cases it cited did just the opposite. *Id.*

At oral argument, EOI stayed the course, continuing to argue that the "full" title of SSB 3413 included "CITY-COUNTY MUNICIPAL CORPORATIONS ---- CLARIFICATION." It continued to make that argument because its entire case would fail without it. In other words, EOI built its entire case on the false argument about the title of SSB 4313 even after it knew that it was wrong. That kind of conduct is the very definition of frivolous litigation.

C. The Court Should Impose Sanctions.

This truly is one of those rare cases where sanctions are warranted and may actually serve their intended deterrent purpose. With respect to the City, this motion is limited to the net income and excise tax arguments because the Court never reached the constitutional questions. For EOI, this motion addresses its entire case because all of its arguments relied on the false title of SSB 4313.

The Court should find that those arguments were frivolous and asserted without any justification. It should send the message that now matter how noble a cause may be, the law still requires good faith arguments.

VI. PROPOSED ORDER

A proposed order is submitted herewith.

Dated this 28th day of November, 2017.

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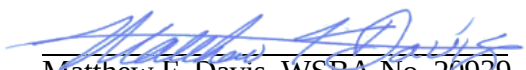

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