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# Proposition 40's Greatest Challenges Would Begin After Election Day

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## Executive Summary

Proposition 40, the California Billionaire Tax Act (CBTA), would impose a 5 percent one-time tax on the worldwide net worth of California residents, based on a snapshot residency date of January 1, 2026, measured by wealth as of December 31, 2026, and payable in 2027. It would be the first wealth tax ever adopted by a U.S. state. This paper examines the legal and administrative challenges raised by the tax, along with the surprising — and in some cases unintended — consequences of its provisions. The paper concludes that the measure's valuation, residency, and apportionment rules are constitutionally unsound, that its implementation timeline is unrealistic, and that the only certainty, should voters adopt the new tax, is that California will face years of costly litigation.

**Valuation.** The initiative's default formula for private business valuations systematically overstates net worth, measures ownership by voting control rather than economic interest, and fully taxes mutually exclusive conditional profit interests. Valuation by controlling interest could also extend to super-voting shares in public companies, causing founders to be taxed on an amount several times their actual ownership stake. Key valuation issues are unlikely to be resolved by the time taxpayers are required to file.

**Trusts and transfers.** Transfers made at any point in 2025 or 2026 are added back to the transferor's net worth. For 2026 contributions, the measure adds back the entire value of the trust rather than the amount contributed, applying to assets that may never have belonged to the taxpayer and have no connection to California. Sales deemed to be for less than fair market value also yield an addback of the full value of the asset in addition to proceeds received, not just the difference between sales price and fair market value. The 2025 addback reaches transactions completed well before the wealth tax initiative was public.

**Residency, retroactivity, and apportionment.** Liability attaches under the CBTA based on residency as of a single day, then taxes 100 percent of worldwide net worth a year later,

without apportionment for time spent elsewhere and without exclusion of wealth accrued post-departure. The U.S. Supreme Court has held that a wholly new tax cannot be applied retroactively on due process grounds, and the default apportionment regime implicates the Commerce Clause of the U.S. Constitution. Taxpayers may seek alternative apportionment where constitutionally required, a concession that apportionment is a constitutional necessity, but an apportionment floor then denies full apportionment in practice.

**Marriage.** The CBTA imposes mandatory aggregation of a nonresident spouse's property for tax purposes, running afoul of the Supreme Court's Commerce Clause jurisprudence. The tax also imposes a substantial marriage penalty, and its provisions regarding transfers to related parties would impose tax on assets the taxpayer no longer possesses because they were obligated or transferred in a divorce settlement.

**Out-of-state property.** The tax exempts real property owned directly, but taxes out-of-state real property held through LLCs. It also potentially double-taxes foreign assets, with no applicable credit, raising further constitutional concerns.

**Administrability.** The California Franchise Tax Board (FTB) would have only a few months between election certification and the tax filing deadline to hire and train staff, draft regulations, issue forms, and build out new administration and audit functions. Taxpayers would have limited time to value assets that have never been valued in trade, potentially before any valuation rules have been promulgated. Wealth tax regulations and guidance are exempt from the Administrative Procedure Act until after the tax is due, and penalties for a substantial divergence between a taxpayer's self-assessment and the FTB's determination, under potentially unpublished rules, are significant for taxpayers and potentially ruinous for their appraisers.

**Litigation and refunds.** Facial challenges to the constitutionality of the CBTA must be filed within 60 days and resolved on an expedited basis in a single venue, before the FTB has interpreted the statute. Some plaintiffs' claims may be dismissed as unripe in the absence of an FTB interpretation of certain contested provisions and then may be barred permanently by the time those interpretations exist. Even if the tax survives facial challenges, it is likely to face as-applied challenges from many taxpayers, which could take years to litigate. If the tax fails in whole or in part in 2028 or later, or if as-applied challenges succeed, refunds with interest would come from the General Fund, since most of the tax revenue is earmarked for health programs and would not be available for refunds.

**Existing revenue streams.** The tax imposes costs on California regardless of whether it is upheld. Billionaires who leave in anticipation of the tax, or to preserve their ability to

contest it, are unlikely to return, depriving the state of future revenue under existing taxes. The state will also have to spend years on costly litigation that it may well lose, in whole or in part. If those losses come after revenues have already been collected, the resulting refunds of money already spent — plus interest — could precipitate a budget crisis.

## Introduction

Designing an entirely new tax is inherently challenging. Setting the tax base as billionaires' often hard-to-value worldwide assets only exacerbates the difficulty. An intensive focus on anti-avoidance provisions adds even more complexity. Attempt all this with a ballot measure, where language cannot be amended once submitted for certification, and you get the California Billionaire Tax Act (CBTA).

Any attempt to levy a state-level wealth tax would raise serious constitutional questions, create substantial economic risk,[1] and add significant complexity to the tax code. But the CBTA, appearing on the November ballot as Proposition 40, is remarkable for the breadth of its legal and administrative shortcomings. The tax's nexus, apportionment, and valuation rules are all deeply flawed and constitutionally unsound. Drafting errors yield outlandish results that proponents never intended, while other provisions, possibly drafted with greater intent, extend the tax far beyond what is commonly understood. And the drafters failed to account for many scenarios, designing a tax that cannot easily survive contact with the real world.

The CBTA's drafters did, of course, anticipate that a wealth tax would draw intense legal scrutiny. They also understood that prospective taxpayers would be incentivized to leave the state or transfer their wealth to reduce or eliminate tax liability. They sought to shore up the tax base with aggressive anti-avoidance provisions and to insulate it from legal challenges wherever possible by embedding preemptive defenses in the tax's design.

But sometimes these goals are at cross purposes. Some provisions designed to lock in taxpayers enhance the tax's legal vulnerability. Other provisions contain drafting flaws and ambiguities. Many provisions yield extraordinary complexity and over-taxation. And some

[1] See, e.g., Jared Walczak, "Proposed Wealth Tax Creates Long-Term Budget Risks for California," *Orange County Register*, Jan. 14, 2026, https://www.ocregister.com/2026/01/14/proposed-wealth-tax-threatens-long-term-budget-risks-for-california/; Id., "California Can Learn From European Countries That Tried Wealth Taxes," *CalMatters*, Feb. 19, 2026, https://calmatters.org/commentary/2026/02/wealth-taxes-europe-countries-california/.

challenges of a state-level wealth tax — both legal and economic — simply cannot be overcome, no matter how creative the design.

This paper explores the CBTA's procedural shortcomings, legal vulnerabilities, administrative challenges, drafting errors and ambiguities, and overly aggressive provisions. It documents the often-surprising ways the tax would apply, should it survive legal scrutiny, along with the many reasons to believe that it would fail on constitutional grounds. California could easily drive away some of the state's wealthiest taxpayers, scare off future startup founders, and commit itself to years of costly litigation, without ever collecting a single dollar in wealth tax revenue — or, perhaps worse, collecting revenue and then being forced to refund amounts already spent.

## What the Tax Would Do

The CBTA imposes a one-time tax of 5 percent on the global net worth of billionaires deemed California residents as of January 1, 2026, based on wealth measured as of December 31, 2026. The tax falls on all assets, tangible and intangible, except real estate and some pension and retirement accounts. It contains distinct valuation methods and requirements based on asset class.

Proponents have estimated that the tax will generate about $100 billion,[2] an estimate that assumes full lock-in of all known California billionaires, while critics have estimated as little as $40 billion in wealth tax revenue and a negative net present value once forgone future tax payments from departing billionaires are taken into account.[3] California's Legislative Analyst's Office declined to refine an estimate beyond "tens of billions of dollars spread over several years."[4]

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[2] Brian D. Galle, David Gamage, Emmanuel Saez, and Darien Shanske, "Expert Report On The California 2026 Billionaire Tax: Revenue, Economic, and Constitutional Analysis," University of Missouri School of Law Legal Studies Research Paper No. 2026-01, Dec. 31, 2025, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=5996554.

[3] Joshua Rauh, Benjamin Jaros, Gregory Kearney, John Doran, and Matheus Cosso, "The Net Present Value of the Billionaire Tax Act: An Assessment of the Fiscal Effects of California's Proposed Wealth Tax," Hoover Institution Expert Report, Mar. 4, 2026 (updated Mar. 17, 2026), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=6340778. See also Jared Walczak, "Ongoing State Tax Revenue Implications of the 2026 California Billionaire Tax Act," California Tax Foundation, Apr. 23, 2026, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=6628261.

[4] California Legislative Analyst's Office, "Proposition 40: Imposes One-Time Tax on Certain Taxpayers. Initiative Constitutional Amendment and Statute," ballot measure analysis, https://lao.ca.gov/ballot/2026/prop40-110326.pdf.

The tax itself is designed as an excise tax on the "activity" of "sustaining excessive accumulations of wealth," and taxpayers subject to the tax would have the option of remitting the entire amount owed with their 2026 income tax payment or paying it in five annual installments, with a 7.5 percent annual deferral charge on the unpaid balance. Certain liquidity-constrained taxpayers would be eligible for Optional Deferral Accounts, under which the state would stake a claim to future realizations from illiquid assets.

Proponents rely on the excise tax framing to argue that the taxable activity is ongoing throughout 2026, providing an end-run to problems of retroactivity and apportionment. However, as will be discussed, not only is the characterization of dubious legal value, but it also cuts against the measure in important ways.

The tax was designed to apply to slightly more than 200 taxpayers, though migration in response to the ballot measure could significantly reduce the taxpayer count. The California Franchise Tax Board (FTB) would be charged with administering the tax, with administrative funding appropriated from the tax's own revenue. Ninety percent of net tax revenue would be deposited in a health account, and the remaining 10 percent would be earmarked for education, food assistance, and tax administration. Revenues from the measure are exempt from the state appropriations limit as well as the Proposition 98 school funding formula.[5]

Despite drafters' efforts to lock billionaires into the tax with a January 1 "snapshot" residency date, the measure's residency, valuation, and apportionment rules are all constitutionally vulnerable, giving potential taxpayers good reason to believe that later departures will reduce or eliminate their liability under the proposed wealth tax. That belief is itself consequential: so long as the tax appears vulnerable to challenges to its residency, valuation, and apportionment rules, billionaires have a strong incentive to leave to preserve their capacity to reduce or eliminate their liability through litigation, meaning that the measure inflicts harm on California's economy regardless of the outcome of that litigation.

## Business and Asset Valuation Issues

Valuing non-traded assets is a substantial undertaking, one the CBTA largely devolves to taxpayers themselves. While shares in publicly traded companies have a definite, market-derived valuation as of December 31, 2026, other assets — ranging from artwork and

[5] Legislative Analyst's Office & Department of Finance, "Fiscal Impact Estimate Report, Initiative 25-0024A1," (Dec. 11, 2025).

jewelry to privately held businesses — are more difficult to value, and in many cases have never been valued in trade.

This challenge applies to a wide range of assets, but in practice, most of the concern is concentrated in non-traded intangible assets, especially privately owned businesses. They are not only among the most difficult assets to value, but also an extremely important component of the intended tax base. And while publicly traded assets should not be hard to value, poor drafting raises the real concern that founders' special voting shares could be subject to excessive levels of taxation, with possible alternative valuation regimes lacking any clear rules or guidance.

Meanwhile, aggressive anti-avoidance rules and an apportionment floor reach assets not controlled by the taxpayer and wealth generated after departing California. The measure's drafters devised valuation rules that systematically overstate net worth, and in some instances reach assets that taxpayers do not own.

## Private Business Valuations

For privately held businesses, including startups that have not yet gone public, the CBTA requires valuation under rules that can generate overvaluations and tax multiple owners or investors on the same interests. Startups may still be pre-earning, and because these businesses are private, owners may lack liquidity, making any wealth tax — let alone one levied on an artificially high valuation — extremely onerous.

The measure establishes fair market value for non-public businesses as their Generally Accepted Accounting Principles (GAAP) book value plus 7.5 times their average annual profits over a three-year window as the default, and any alternative appraisal-driven valuation would have to demonstrate why it is superior to this default. Notably, book value already includes accumulated retained earnings; the measure adds 7.5 times current earnings on top. Many private businesses do not use GAAP accounting, though the larger problem is the reliance on book profit, an accounting concept that does not align with market pricing.

The trading price of shares in a publicly traded company reflects not just current book value, but also risks, cyclicality, regulatory exposure, capital intensity, and liquidity. None of these factors, which can reduce market value, are captured under the CBTA's valuation structure for private businesses. The CBTA also sets a book profits floor of $0, meaning that

while profits unsurprisingly increase a business's value for tax purposes, actual losses do not reduce its taxable value.[6]

The CBTA then exacerbates this overvaluation with a requirement that a business's value for tax purposes must be at least equal to the valuation reflected in any funding round or equity sale within the two years preceding the valuation date unless the taxpayer can demonstrate by clear and convincing evidence that the valuation significantly overstates the entity's value.[7] This is an unreasonable standard, not just because company valuations can change markedly in two years — many startups spike in value and then decline — but also because equity rounds often confer preferred terms on funders that are not available to all owners and are insufficiently representative to be used as a valuation floor for the entire company.

An owner or investor in a private business, moreover, may have no realistic avenue for selling stakes in the company, or may have good reason to wish to avoid such dilution of control. Realistic valuations of private businesses involve discounts for minority interests and lack of marketability (a stake in an illiquid company is not worth the same as a similar stake in a publicly traded one where ownership interests are liquid), but such valuation discounts are disallowed by the CBTA.

Similarly, if a billionaire has a profit interest in a private business, their ownership share is presumed not to be less than their maximum interest in the company's profits that they could earn subject to conditions being met, even if those conditions have not been met. This provision taxes interests the taxpayer does not actually possess. Worse, if multiple owners have mutually exclusive profit interests, it will tax all of them even though it is impossible for them to all be realized.[8]

Consider, for instance, a primary investor who receives 100 percent of profits up to a 5 percent return on investment, after which a general partner receives 100 percent of the next 5 percent return, after which they split profits by some ratio. The first investor has a maximum interest of 100 percent (at anything up to a 5 percent return), and the second investor has a maximum interest of 50 percent (at exactly a 10 percent return), meaning that the business might be taxed as if it had 150 percent ownership.[9]

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[6] California Proposition 40 (2026), § 50303(c)(3)(E).
[7] Id., § 50303(c)(10).
[8] Id., § 50303(c)(3)(D).
[9] Under another reading, it is even possible that the business could be taxed as if it had 200 percent ownership, since both investors have a stake in 100 percent of marginal returns over some window.

Alternatively, a company might have triggers for owner-operators in a pre-public company, and the CBTA would count each taxpayer's trigger as if it were the only one triggering an equity distribution, even if multiple parties achieving their goals could dilute the equity pool. Similarly, if two executives each held a profit interest that would vest only if they became CEO, each would be presumed to own the full percentage, even though at most, one of them can ever vest.

Owners of private companies, moreover, have their ownership interest determined based on their control or voting rights in the company, not their economic interests, meaning a startup owner who has brought in outside investors may be taxed on a value that is several multiples of the economic value of their stake in the company. Outside funding may confer an economic interest without matching voting interests, to maintain founders' control. In this case, the founders would be taxed as if they owned far more of the company than they do. To the extent that they are forced to sell further interests in their company to pay the wealth tax or accept a functional lien on a portion of the business under the Optional Deferral Account (ODA) payment method, discussed later, this can involve a share of their holdings far greater than the 5 percent indicated by the tax rate.

If, by way of example, a pre-IPO founder owned 20 percent of the company but maintained 50 percent control, the resulting effective tax rate on the 20 percent economic stake would be 12.5 percent, not 5 percent.[10] They could be forced to sell that much of their stake — plus enough to cover other federal and state taxes on the sale — just to pay the wealth tax, surrendering a significant amount of control in their startup before it goes public.

This requirement can also lead to taxation on total value exceeding the company's worth. If a private company's billionaire founder is taxed on voting interests, and the other investors are also California-taxable billionaires who are taxed on their economic stakes, the result is taxation of more than 100 percent of the company's value. Taxation based on voting interests could also remain an issue for founders of businesses that have gone public, as discussed in the next section.

## Special Control Shares

The CBTA establishes distinct valuation methods and requirements for different kinds of assets, distinguishing (1) publicly traded assets, (2) sole proprietorships, and (3) "all interests in any business entities, including all equity and ownership interest, all debt

[10] Mathematically: a rate of 5 percent on 50 percent control yields a tax of 2.5 percent of company value, on a 20 percent stake, equaling a 12.5 percent rate on that stake.

interests, and all other contractual or noncontractual interests" except for publicly traded assets and sole proprietorships.[11] For assets in this third category, voting and direct control rights establish a valuation floor: "For any interests that confer voting or other direct control rights, the percentage of the business entity owned by the taxpayer shall be presumed to be not less than the taxpayer's percentage of the overall voting or other direct control rights."[12]

Just like pre-IPO founders, the founders of public companies frequently hold special control ("super-voting") shares that enable them to retain control over their company disproportionate to their economic ownership stake. For instance, Larry Page and Sergey Brin own about 11.3 percent of Alphabet (Google) but control a combined 52.3 percent of voting rights, while Mark Zuckerberg owns about 13.6 percent of Meta but retains 61 percent voting control.[13] All three of these founders have taken steps that could allow them to avoid some or all wealth tax liability.

Alphabet and Meta are publicly traded companies, with known share values. But these founders' special control shares are non-tradable assets. Their additional voting interests clearly confer value, but that value cannot be realized on the market, because the shares cannot be sold without undergoing a transfer-based conversion to ordinary shares, under which they lose their special voting privileges. The special control shares are not themselves publicly listed. At issue is whether these special control shares are publicly traded assets for purposes of the CBTA.

The measure defines a publicly traded asset as "an asset that is traded on an exchange; traded on a secondary market in which sales prices for such asset are frequently updated; available on an online or electronic platform that regularly matches buyers and sellers; or any other asset that the [Franchise Tax] Board determines has a value that is readily ascertainable through similar means."[14] These shares are not traded on exchanges or on secondary markets where prices are regularly updated, nor are they available on other digital markets. Everything hinges, therefore, on whether the FTB determines that the assets have a value that is "readily ascertainable through similar means."

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[11] California Proposition 40 (2026), § 50303(c).
[12] Id., § 50303(c)(3)(C).
[13] Originally calculated in Jared Walczak, "The Proposed California Wealth Tax Is Far Higher Than 5 Percent," Tax Foundation, Jan. 14, 2026, https://taxfoundation.org/research/all/state/california-wealth-tax-billionaires-proposal/. Voting rights and ownership figures were obtained from Fintool, and market caps were obtained from Google Finance as of January 2026. Figures are approximate, based on available public information.
[14] California Proposition 40 (2026), § 50308(j).

If the FTB concludes that these shares are identical in value to ordinary shares with regular voting privileges, then such values are readily ascertainable. But if they conclude that this is not the appropriate measure of their value, then these shares could be included in the third class of business interests, and thus — regardless of what premium a valuation might ordinarily place on such shares — be valued based on the taxpayer's voting share rather than their economic share. Mark Zuckerberg could be taxed as if he owns 61 percent of Meta, even though this is about 4.5 times his actual ownership stake.

The measure's drafters have denied that this was either their intent or the consequence of their language, though in denying the effect, they have insisted that the measure "says expressly" that it "does not apply to shares in publicly traded entities," which is inaccurate; the measure says that the control-based valuation rule does not apply to publicly traded assets, not to shares in publicly traded entities. It is possible that the FTB will adopt an interpretation conflating these definitions to avoid an absurd result.[15]

Potential taxpayers will certainly hope for such an outcome, arguing that the FTB should not adopt an interpretation that leads to such an outlandish outcome, and one that the drafters have expressly disclaimed well in advance of any vote on the measure. But given the plain text of the measure and the FTB's history of aggressive interpretations of law, such administrative discretion is not a hope they may wish to bank on. It is little wonder that some of the most prominent tech founders have already left California.

Drafters also have argued that the CBTA contains a second line of defense against such an extreme valuation, noting that "[t]axpayers who believe that an appraisal best represents the value of their assets can submit an appraisal" instead of relying on the default valuation rules.[16] As discussed at greater length below, the option of challenging default rules or even pursuing litigation to yield a defensible outcome is not a legitimate justification for default rules that routinely deliver indefensible ones. And it is particularly inadequate here, as there is no accepted convention for the additional value, if any, conferred by special voting

[15] For a more comprehensive treatment of this issue, including a response to proponents' dismissal of these concerns, see Jared Walczak, "Valuation of Controlling Shares of Publicly Traded Companies Under the Proposed California Wealth Tax Remains a Key Concern," California Tax Foundation, Jan. 23, 2026, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=6122688.

[16] Brian D. Galle, et al. "Expert Report on Valuation of Controlling Shares of Publicly Traded Companies Under the California Billionaire Tax Act (CBTA)," University of Missouri School of Law Legal Studies Research Paper No. 2026-04, Jan. 15, 2026 (revised Feb. 27, 2026), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=6073728.

rights. Given the sharp penalties for submitting valuations with which the FTB substantially disagrees (discussed below), this is a highly salient concern.

Uncertainty about how this provision will apply adds one more legal conundrum. As will be discussed elsewhere, the measure contains a narrow 60-day window for challengers to file facial challenges to the validity of the statute, meaning challengers will have to litigate the measure without knowing how the FTB will interpret the provision. A challenge to valuation by controlling interest may be dismissed as premature prior to FTB regulations or guidance, and by the time rules are issued, the window is likely to have closed, potentially deeming the matter forever facially incontestable. It is, at minimum, questionable whether a ballot initiative can shut down legal challenges in such a fashion.

## Appraisals

Should the CBTA pass, both taxpayers and tax administrators will be in a race against the clock. An entirely new tax, on a hard-to-value base, would require estimated payments by April 15, 2027, a mere 163 days after Election Day and 126 days after the measure's passage would be certified. Because the tax base is valued as of December 31, valuations could not begin until January 1, giving affected taxpayers a mere 105 days to have their assets (including private businesses) valued, and to file under the new regime, or to make estimated payments — which itself requires a valuation — and then file under a six-month extension.[17]

In response to a prior California wealth tax proposal (AB 259) under which the state, rather than taxpayers, would have been responsible for appraisals, the FTB expressed concern about the availability of certified appraisers to complete the necessary valuation work for a wealth tax. The agency noted that, at the time (2023), there were fewer than 1,000 personal property appraisers focused on fine and decorative arts nationwide.[18] Appraisers qualified to handle complex valuations of business interests and other assets of billionaires are likewise in short supply.

The earlier wealth tax proposal captured many more potential taxpayers, as it was slated to begin as a billionaire tax but then expand to cover wealth above $50 million, expanding the tax base from about 200 to roughly 16,000 taxpayers. This is a very real and meaningful

[17] There are various ways, discussed previously, that taxpayers can defer part of their tax *remittance*, but filing (which requires a valuation) is required by April 15, 2027.
[18] California State Assembly, Committee on Revenue and Taxation, "AB 259 (Lee)," revised bill analysis, January 9, 2024, https://leginfo.legislature.ca.gov/faces/billAnalysisClient.xhtml?bill_id=202320240AB259, 10.

distinction. But even with a small pool of taxpayers under the current proposal — an estimated 212 as of early 2026, and potentially far fewer now, though residency would doubtless be litigated in many cases — those subject to the CBTA possess a large share of the wealth that would have been assessed under AB 259, and much of the complexity that runs with it.

California billionaires would have only a few months to value some of the country's most complicated private holdings, including pre-IPO tech startups, for tax purposes under complicated and aggressive valuation formulas, and subject to considerable uncertainty — knowing that if the FTB takes sufficient issue with their valuation, there will be substantial penalties for both the taxpayers and their appraisers. They would be competing with the FTB, meanwhile, to hire from the small pool of individuals qualified to appraise such assets, since the agency would require the capacity to make its own determinations and to challenge taxpayers' assessments.

Should the FTB disagree with a taxpayer's self-assessment, the consequences are considerable: a 20 percent penalty for understating tax liability by the greater of $1 million or 20 percent, and a 40 percent penalty for understatements of the greater of $10 million or 40 percent. A 40 percent understatement of tax liability, compared to whatever valuation the FTB settles on, is significant, but not unreasonable or indicative of bad faith given the range of valuations that could be attached to private business interests, particularly in the tech industry.[19]

Even more significantly, penalties can also attach to appraisers, at rates of 2 percent or 4 percent of the understatement of liability.[20] If an appraiser valued a private company at $4 billion and the FTB decided it was worth $5 billion, the appraiser — who is decidedly not a billionaire — would face a penalty of $1 million. If they valued it at $3 billion, their penalty would be $4 million.[21] Such penalties could be ruinous and might be difficult to insure against.

Appraisers already are employed in valuing assets for estate and gift taxes, as well as income tax deductions for non-cash charitable contributions. At the federal level, appraisers' penalties are capped at the lesser of 10 percent of the underpayment or 125

[19] California Proposition 40 (2026), § 50312.
[20] Id.
[21] Mathematically: The understatement of tax liability on a $2 billion valuation differential is $100 million at a 5 percent rate, and a 4 percent penalty on that understatement is $4 million.

percent of the fee received for the appraisal, ensuring proportionality.[22] The CBTA, by contrast, has no upper limit based on fees received.

Under *United States v. Bajakajian*, a fine is unconstitutionally excessive if it is grossly disproportionate to the gravity of the offense,[23] and the Excessive Fines Clause was incorporated against the states in *Timbs v. Indiana* in 2019.[24] Tax penalties are not automatically fines, but the courts are more likely to interpret penalties as fines, subject to the Excessive Fines Clause, when they take on the form of a monetary punishment.[25] These unusually severe penalties — which will make it even harder for taxpayers to find appraisers willing to take the job — are good candidates for such a determination, as they appear punitive rather than remedial. Excessive Fines Clause jurisprudence has been inconsistent over the years,[26] but the CBTA offers a particularly powerful fact pattern for a tax-related challenge.

## Trusts and Transfers

The measure's treatment of trusts and transfers is both a valuation issue and a taxable nexus problem. The CBTA's drafters were keenly on guard against potential avoidance activity, seeking to identify and shut down any avenue for reducing tax liability. They were less focused on exploring the consequences of these anti-avoidance rules, which are dramatically overbroad.

The measure disregards transfers that would reduce wealth tax liability, adding the transferred value back to the transferor's net worth. If billionaires transfer wealth or incur debt to their children, transfer property to a trust, or sell assets to someone at a price below fair market value, the value of these transfers (and sometimes much more) is added back to their own net worth for tax purposes. Taxpayers' motivations are irrelevant. The state does not need to show that tax avoidance was the intended purpose; it only matters that a transfer took place in 2025 or 2026. The result is taxation of wealth that may genuinely be outside their control. Grantor trusts do not involve an addback because the assets remain associated with, and are taxed against, the taxpayer regardless. Only transfers to tax-exempt (charitable) trusts avoid the addback.

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[22] 26 U.S.C. § 6695A(b). These appraisals are for federal estate and gift tax purposes, as well as income tax deductions for non-cash charitable deductions.
[23] *United States v. Bajakajian*, 524 U.S. 321 (1998).
[24] *Timbs v. Indiana*, 586 U.S. 146 (2019).
[25] *Austin v. United States*, 509 U.S. 602 (1993).
[26] See, e.g., Beth A. Colgan, "The Burdens of the Excessive Fines Clause," 63 *Wm. & Mary L. Rev.* 407 (2022).

The addback of transfers contains the CBTA's most aggressively retroactive element: it adds back 75 percent of the value of property transferred at any time in 2025, for an initiative that was initially submitted to the Attorney General on October 21, 2025, was cleared for circulation on December 26, 2025, declared eligible for the ballot on June 17, 2026, and formally qualified for the November 3 ballot on June 25, 2026, with final election result certification on December 11, 2026.[27]

While retroactive taxation is not *per se* unconstitutional and some level of retroactivity is not uncommon in tax statutes, the Supreme Court has ruled that it is unconstitutional to levy a wholly new tax retroactively, making highly dubious the addback of transfers at any point retroactive to the tax's adoption, but especially reaching all the way back to January 1, 2025, well before the tax was even proposed. The retroactivity issue will be considered at greater length in the context of the law's residency standards, but the same constitutional challenges also apply here.

The clawback of transfers made in 2026 raises a further issue. Regarding transfers made in 2025 and 2026, the measure states, "[N]et worth shall for all purposes include the value of property held by any trust (other than a grantor trust or tax-exempt trust) to which the individual transfers property in 2026, and seventy-five percent of the value of such property transferred in 2025."[28] The intention may have been to tax the full value of *transfers* made in 2026, just as the CBTA would tax 75 percent of the value of transfers made in 2025. But for 2026, the language does not mention transfers, but rather "the value of property" held by a trust to which a transfer was made in 2026 — that is, the *entire* value of the trust. If a taxpayer contributes to a trust in 2026, they are taxed on the trust's entire value (even if most of it came from other sources, or from contributions made long prior to 2025) as if it were their own wealth.[29]

While this would seem like a drafting error, it may not have been, because the same provision also accounts for proportional allocation of a trust's value if it received

[27] Suzanne Jimenez, letter to California Attorney General Rob Bonta requesting title and summary for the proposed "2026 Billionaire Tax Act," October 21, 2025; California Department of Justice, Office of the Attorney General, "Imposes One-Time Tax on Certain Individuals and Trusts: Initiative Constitutional Amendment and Statute," title and summary for Initiative 25-0024A1, December 26, 2025; California Secretary of State, "Eligible Statewide Initiative and Referendum Measures"; California Secretary of State, "California Secretary of State Shirley N. Weber, Ph.D., Certifies Measures for the November 3, 2026, General Election Ballot," June 25, 2026.
[28] California Proposition 40 (2026), § 50303(c)(6)(B).
[29] Id.

contributions from multiple billionaires. This would not be necessary if each were only taxed on their own contribution.

Why drafters would have chosen to tax billionaires on the total value of a trust that the taxpayers do not control, much of which may have been funded by others (and thus never associated with them), simply based on a contribution made at any time in 2026, is unclear, since it seems an absurd result. Whether the FTB could establish a saving interpretation to avoid this result and the legal challenges to which it gives rise is unclear, but enforcement of the provision as written yields presumptively unconstitutional results, as it can tax assets that have never had any connection to the taxpayer.

Even if the provision taxing the entirety of the trust were narrowed through administrative action or a court ruling, it still would be unconstitutionally broad. The Supreme Court has held that even the in-state residency of beneficiaries is insufficient to tax a trust's undistributed income when beneficiaries have not received distributions and cannot fully rely on receiving them.[30] Under the CBTA, California would assert the right to tax trusts even if they have no in-state beneficiaries, no in-state administration, and indeed no remaining tie to any California taxpayer, just because the trust previously received a contribution from a California taxpayer. This is unsupportable under Due Process.

The CBTA does not tax the trust itself based on the settlor's contribution but instead attributes the trust assets to the settlor's own net worth, taxing an individual on property they have irrevocably given away. The Supreme Court emphasizes a taxpayer's possession, control, and ability to access trust property, none of which apply here. The CBTA, moreover, adds back the contributions to any trust to which a billionaire has contributed at any point in 2025 or 2026, whereas due process requires that a connection exist with the object of the tax at the time that interest is taxed.

The proposed wealth tax also seeks to counteract any avoidance through sales or transfers of assets for less than fair market value after October 15, 2025, a date that precedes the initiative's submission to the Attorney General by almost a week and thus reaches conduct that occurred before the measure was public. This likewise involves taxing people on wealth they no longer possess, though it is a logical extension of disregarding transfers. If a billionaire is taxed on a transfer made to an adult child as if they still possessed that asset or share of wealth, for instance, then drafters would want to ensure that a taxpayer could not evade the constraint by transferring a valuable asset for a nominal price. As written,

[30] *Safe Deposit & Trust Co. of Baltimore v. Virginia*, 280 U.S. 83 (1929); *North Carolina Department of Revenue v. Kimberley Rice Kaestner 1992 Family Trust*, 588 U.S. 262 (2019).

however, the provision mirrors the 2026 trust addback's flaw: the amount added back to net worth is the *entire* value of the transfer, not the difference between the sales price and fair market value.[31]

Since the provision applies to any sales or transfers, regardless of relationship with the other party, this overinclusion is especially consequential. Consider, for instance, the sale of a share in a private business. It is inherently difficult to value such an asset. If the FTB decided that the sale was for an amount below fair market value, California would not only tax the seller on the amount deemed below market value (itself highly subjective), but on *the entire value* of the business share they no longer possess. If a share of a business sold for $1 billion but the FTB deemed the appropriate price to be $1.1 billion, the taxpayer would be taxed on the $1 billion they received in exchange, *plus* the $1.1 billion value the FTB attached to the transferred share. Here too, the FTB may elect not to take as aggressive a posture as is contemplated by the measure's language, but the measure as drafted creates significant risk.

## Residency, Nexus, and Apportionment Issues

The CBTA vastly overreaches, with constitutional implications, in how it defines residency for tax purposes, which individuals it claims a connection to for tax purposes, which transfers and trust contributions it declines to recognize, and in how it apportions — or rather, fails to apportion — wealth for taxpayers who can also be claimed by other states.

### Residency Determinations

Despite generally downplaying out-migration concerns, the drafters of the CBTA were sufficiently cognizant of the strong incentive a 5 percent wealth tax creates for billionaire departures to seek to circumvent them with a residency provision designed to lock billionaires into the tax base before they had the opportunity to depart. Drafters have expressed doubt about whether any prospective taxpayers could have succeeded in effecting a change in domicile under their rules even if billionaires reacted as soon as the tax measure was unveiled.[32]

The tax is imposed on billionaires who resided in California on January 1, 2026, and measured based on wealth as of December 31, 2026. California uses a facts-and-circumstances-based evaluation of where a person's "closest connections" lie, meaning

[31] California Proposition 40 (2026), § 50303(c)(11).
[32] Brian D. Galle et al., "Response to 'The Net Present Value of the Billionaire Tax Act' March 4, 2026," March 17, 2026, https://eml.berkeley.edu/~saez/responsetorauh26.pdf, 2-3.

that even a person who irrevocably departed the state in late December may not have established themselves in a new state to such a degree that their closest connections were clearly outside California as of the specific January 1 snapshot date. For individual income taxes, residency is determined based on an entire year's worth of activity, not on a single determination of domicile at one moment in time. The CBTA blends a test designed to determine residency based on location and connections over an extended period with a bright-line rule, compressing a year-long inquiry into a snapshot-date determination.

This approach might fail to capture the reality that a taxpayer departed prior to January 1. It is certainly — intentionally — indifferent to their domicile the rest of the year. Mid-year movers are fully taxed just as if they never left California, rather than having their tax liability apportioned or allocated based on time in the state. This approach gives rise to at least three significant legal challenges. First, it retroactively imposes a wholly new tax, which the Supreme Court has held to violate the Due Process Clause. Second, it defaults to taxing mid-year movers on 100 percent of their wealth, with no apportionment, which raises fair apportionment questions under the Commerce Clause. And third, in the case of those mid-year movers, it taxes wealth acquired or accrued after departing for another state, yielding unconstitutional extraterritorial taxation.

## Retroactivity

Retroactive tax changes are not particularly unusual, and they are presumptively constitutional within certain limits. The CBTA, however, crosses one of the lines that the Supreme Court has drawn, as it is not just a retroactive change to an existing tax, but the retroactive adoption of a wholly new tax. In two cases involving the adoption of the federal gift tax, *Blodgett v. Holden* (1927) and *Untermyer v. Anderson* (1928), the Supreme Court struck down the new tax's retroactive application. The Court observed that, while authority for retroactive tax changes existed, due process was denied by the retroactive application of a wholly new tax.[33]

There is no question that the wealth tax would be entirely new. Not only does Proposition 40 create a new tax, but it is an entirely new *kind* of tax. The measure itself characterizes it as an excise tax on sustaining wealth, though in its substance, it is a property tax on the global net worth of billionaire taxpayers. In either form, it has no precedent in California. Commenting on a prior wealth tax proposal, the FTB noted the novelty of the proposed tax,

[33] *Blodgett v. Holden*, 275 U.S. 142 (1927); *Untermyer v. Anderson*, 276 U.S. 440 (1928).

observing that branching into an entirely new form of taxation would require significant retooling of the agency's capabilities.[34] If ever there were a wholly new tax, this is it.

The CBTA's self-characterization as an excise tax rather than a property tax on global assets is intended to provide a defense against challenges to the measure's retroactivity. If the tax is on the "activity" of sustaining wealth, then if the wealth is sustained for any portion of the year after voter approval, the bulk of the tax is no longer retroactive — though this does nothing to address addbacks of 2025 transfers.

However, the excise tax framing is ultimately meaningless. Courts, federally and in California, hold that the character of a tax is determined by its substance, not its form or label.[35] Likewise, it is a maxim of California jurisprudence that "[t]he law respects form less than substance."[36] A tax measured by a taxpayer's net worth on a particular date, and imposed on the wealth itself without reference to any transfer or realization event, is a property tax with a base of virtually all the taxpayer's California tangible and global intangible assets.

Proponents can call the tax an excise tax if they wish: virtually anything can be labeled that way, including taxes on real estate, but relabeling a real property tax as an excise tax on the privilege of sustaining ownership in real property would not, for instance, eliminate the property tax protections of Proposition 13. Likewise, no matter what it is labeled, the proposed wealth tax does not cease to be what it is in substance.

Additionally, even if this were a tax on continuing activity, there is no reason why liability should be based on the taxpayer's residence as of a single day rather than on where the taxed activity took place. And the addback provisions for transactions completed in 2025 are completely inconsistent with the tax's characterization. The "excise tax" label does not short-circuit constitutional challenges to the tax's retroactivity.

Notably, the restriction on retroactive application of a new tax applied in *Untermyer* even when the taxpayer made gifts in anticipation of the imminent adoption of the gift tax law. The Court ruled that "[t]he taxpayer may justly demand to know when and how he becomes liable for taxes — he cannot foresee and ought not to be required to guess the outcome of pending measures."[37] Similarly, while a taxpayer is certainly aware (by now, though not by the January 1, 2025, and October 15, 2025, dates used for some retroactive provisions,

[34] California State Assembly, Committee on Revenue and Taxation, "AB 259 (Lee)."
[35] *Ingels v. Riley*, 5 Cal. 2d 154 (1936); see also *Weekes v. City of Oakland*, 21 Cal. 3d 386 (1978).
[36] Cal. Civ. Code § 3528 (2025).
[37] *Untermyer v. Anderson*.

discussed elsewhere) that a wealth tax may be approved by voters this year, she is not constitutionally required to presuppose the outcome of the ballot measure.

Proponents point to a 1994 case, *United States v. Carlton*, in which the majority expressed skepticism about the approach under which these prior cases were decided,[38] but crucially, they chose not to overturn it, distinguishing the case before them because "the amendment at issue here certainly is not properly characterized as a wholly new tax." Justice Sandra Day O'Connor, concurring that the tax changes before the Court did not constitute a new tax, wrote separately to emphasize the Court's existing jurisprudence, writing that "a wholly new tax cannot be imposed retroactively" and further citing *United States v. Hemme*, a 1986 case, which likewise affirmed the distinction.[39]

In *Carlton* and other cases, moreover, the Supreme Court emphasized that the retroactive changes were modest, which certainly cannot be said of the tax that would be created with the passage of Proposition 40. Even if members of the *Carlton* majority were not fully committed to the precedent on wholly new taxes, the CBTA's proponents would have to convince federal courts to repudiate those rulings.

The Ninth U.S. Circuit Court of Appeals has read the "wholly new tax" limitation narrowly,[40] but even a narrow reading would likely be fatal to the CBTA's retroactive residency date, and the U.S. Supreme Court may take a more expansive view. Even under a very narrow reading like the Ninth Circuit adopted in *Quarty v. United States*, which prohibited retroactivity only "when the taxpayer has no reason to suppose that any transactions of the sort will be taxed at all,"[41] the wealth tax would count, because global net worth is dissimilar to any other base currently included in the tax code.

California courts have also affirmed the "wholly new tax" distinction. *NetJets Aviation, Inc. v. Guillory* struck down the retroactive portion of a statute assessing property tax on fractionally owned aircraft since it was a wholly new tax. In a unanimous ruling, California's Fourth District Court of Appeal held that "the new tax assessment imposed by the Legislation may not constitutionally be applied retroactively," as retroactive application

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[38] The tax's proponents have also cited *Brushaber v. Union Pacific Railroad Co.* (1916) as evidence that the courts do not care about "wholly new tax" distinctions, but not only does it blur the timeline of the tax in question, it ignores the order of cases as well. A 1916 case that did not make a "wholly new tax" distinction does not control, given that two cases, decided later, expressly do so.
[39] *United States v. Carlton*, 512 U.S. 26 (1994). See also, *United States v. Hemme*, 476 U.S. 558, 568 (1986).
[40] *Quarty v. United States*, 170 F.3d 961, 967 (9th Cir. 1999); *Moore v. United States*, 36 F.4th 930 (9th Cir. 2022). The U.S. Supreme Court affirmed the *Moore* decision, but did not reach the retroactivity question because plaintiffs failed to seek review on those grounds.
[41] *Quarty v. United States*.

"violate[s] due process."[42] The extension of property tax onto fractionally owned aircraft is, of course, a much narrower and less novel change to the tax code than the creation of a wealth tax.

Despite the drafters' public dismissal of these concerns, they clearly recognized the precarity of this part of the tax structure, embedding provisions in the CBTA requesting that courts engage in juridical reformation to set later dates if the measure's stated residency and valuation dates are deemed unconstitutional. Even if California's courts agree to reform the laws to address this constitutional impediment, any revised dates that cure the legal defects would spare mid-2026 movers from some, or quite possibly all, wealth tax liability.

There is reason, moreover, to be skeptical that the courts can revise the dates, notwithstanding the measure's built-in request for judicial reformation. California courts are permitted, under their own precedent, to "reform a statute to satisfy constitutional requirements if it can conclude with confidence that (i) it is possible to reform the statute in a manner that closely effectuates policy judgments clearly articulated by the enacting body, and (ii) the enacting body would have preferred such a reformed version of the statute to invalidation of the statute."[43] But California's courts have expressed grave doubts about their ability to make subjective judgments, particularly in the realm of tax, where they have been reluctant to apply judicial reformation, declining to do so when the cure requires a policy choice.[44]

Judicial reformation is available only when there is a clear way to effectuate the policy judgment of the Legislature (or voters), and when it would not alter the effects of legislation or a ballot initiative in such a way that might have affected proponents' judgment about the measure's adoption. But there is no single, obvious replacement date or method for the constitutionally dubious residency date, and any revised date would have significant policy implications, yielding a universe of potential taxpayers markedly different from the one that voters were told to expect. The courts could well strike down the tax outright over the chosen snapshot dates, especially combined with other provisions (discussed elsewhere) potentially requiring judicial reformation, which multiply the quasi-legislative choices the courts would be obligated to weigh.

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[42] *NetJets Aviation, Inc. v. Guillory*, 207 Cal. App. 4th 26 (2012).
[43] *Kopp v. Fair Political Practices Commission*, 11 Cal. 4th 607 (1995).
[44] *Abbott Laboratories v. Franchise Tax Board*, 175 Cal. App. 4th 1346 (2009); *Ventas Finance I, LLC. v. Franchise Tax Board*, 165 Cal. App. 4th 1207 (2008); *Ceridian Corp. v. Franchise Tax Board*, 85 Cal. App. 4th 875 (2000).

## Non-Apportionment of Wealth

The CBTA attributes 100 percent of taxpayers' worldwide wealth to California, "without reduction or multiplier based on residency history."[45] The measure essentially repudiates the notion of apportionment, taxing the entirety of a billionaire's wealth as of December 31, 2026, even if they left California months prior and even if they accrued some of the wealth post-departure.

The measure's bright-line snapshot residency and valuation rules are combined with California's existing facts-and-circumstances-based residency test that examines a taxpayer's "closest connections" to decide domicile. A taxpayer could permanently leave the state in, say, December 2025, never to return, but this departure might not be immediately accepted by California as a change in domicile, since the taxpayer has — or, until recently had — a broad range of close connections to California (organizational membership, business and financial ties, voter registration, a primary doctor, school enrollment for children, a home containing their principal possessions, etc.). A snapshot judgment as of January 1 might not establish whether the taxpayer had genuinely left California, even if they truly did so.

For income tax purposes, where income is apportioned or allocated, this domiciliary determination would be based on the portion of 2026 during which the person was a resident or non-resident of California, but the wealth tax contains no such apportionment regime. A taxpayer might be determined to be a resident as of January 1 even if they were genuinely domiciled elsewhere the entirety of 2026. Furthermore, if they were a Californian as of the start of the year but left mid-year, California would tax them fully, unlike with an income tax, where liability would reflect the portion of the year spent in California.

States are constitutionally permitted to tax residents' worldwide assets and interests.[46] It may violate a sense of fairness for California to tax the total wealth of, for example, someone who generated all their wealth in New York before moving to California in late 2025, an outcome even the drafters acknowledge as a less-than-desirable outcome.[47] It is not, however, unconstitutional for the state to do this. But due process requires that there be "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax,"[48] and that connection must be in place when the

[45] California Proposition 40 (2026), § 50306(a).
[46] *Curry v. McCanless*, 307 U.S. 357 (1939).
[47] Brian D. Galle et al., "Expert Report On The California 2026 Billionaire Tax: Revenue, Economic, and Constitutional Analysis."
[48] *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 344–45 (1954).

interest is taxed.[49] Establishing domicile elsewhere severs the connection between California and the taxpayer's assets outside the state, yet the measure explicitly continues to tax them, even on post-departure accrual of wealth, with no proration for their time spent as a resident of a subsequent state.

*Complete Auto Transit, Inc. v. Brady* establishes a four-prong test for tax validity under the Commerce Clause,[50] and *Comptroller v. Wynne* makes clear that the test, originally applied to business taxes, also holds for taxes on individuals.[51] The *Complete Auto* test requires:

1. Substantial nexus: a clear, active connection between the taxpayer and the taxing state;
2. Nondiscrimination: no discriminatory treatment of non-resident taxpayers or interstate commerce compared to resident taxpayers and intrastate commerce;
3. Fair apportionment: taxation limited to the apportioned share of activity within the taxing state; and
4. Fair relationship: a fair relationship of the tax to services provided to the taxpayer by the state.[52]

All four of these prongs create issues for the wealth tax. Fair apportionment, which requires both internal and external consistency, is of particular note. Another case, *Oklahoma Tax Commission v. Jefferson Lines*, stipulates that apportionment must reasonably reflect the in-state component of an identified taxable event to pass the "external consistency" test.[53] The internal consistency test, meanwhile, requires that if every state adopted an identical tax regime, it would not result in double taxation or yield greater burdens on interstate commerce or on interstate movers than on intrastate commerce or stayers.[54]

It is hard to imagine how a default of 100 percent apportionment (really, a policy of non-apportionment) regardless of time spent in California or the share of one's wealth accrued there is consistent with the fair apportionment requirement, or how a fair relationship exists between the tax and services provided by California to the taxpayer when the tax is imposed on a period after the taxpayer's departure, and on wealth accrued after establishing domicile in another state.

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[49] *North Carolina Department of Revenue v. Kimberley Rice Kaestner 1992 Family Trust*.
[50] *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977).
[51] *Comptroller v. Wynne*, 575 U.S. 542 (2015).
[52] *Complete Auto Transit, Inc. v. Brady*.
[53] *Oklahoma Tax Commission v. Jefferson Lines, Inc.*, 514 U.S. 175 (1995).
[54] *Comptroller v. Wynne*.

The measure's characterization as an excise tax harms it here. Ultimately, the tax is not an excise tax, certainly not to the exclusion of what it truly is: a property tax on net worth that requires apportionment. But if proponents succeeded in their characterization, that would make the lack of apportionment even more incoherent. If the tax is imposed on the act of sustaining wealth throughout 2026, then assignment of all wealth to California based on a January 1 snapshot date makes no sense if the wealth was sustained in another state thereafter. The drafters seem to want Proposition 40 to be an excise tax on a continuing activity where they think it might help quell retroactivity concerns, but also need it to be a status-based levy that ignores continuing activity for apportionment purposes.

The CBTA permits taxpayers to pursue a lesser apportionment percentage on a case-by-case basis. This, however, is an inadequate response to a constitutional defect for at least two reasons. First, it abdicates the state's responsibility to apportion the tax constitutionally, instead requiring taxpayers to rebut the state's presumption under a "clear and convincing evidence" standard. Second, the measure sets an apportionment floor of 25 percent unless courts determine, in litigation, that a lower percentage is "required to avoid grossly disproportionate taxation" that plainly violates the Constitution.[55] Consequently, California seeks at least 25 percent apportionment even in situations where the facts argue for a lower share, which is in tension with the courts' concerns about cumulative tax burdens on interstate commerce.[56]

The CBTA allows credits for taxes paid to other states to address a hypothetical issue where another state adopted a similar wealth tax, and both states taxed the same wealth.[57] These credits, however, are based on the number of days in the year that the taxpayer was a resident of another state, which is inconsistent with the measure's snapshot or status-based taxation. The credits are apportioned against an unapportioned tax. That the measure's relief mechanism is built on the premise denied by the apportionment rule is telling. It suggests that drafters implicitly understood that a tax on wealth accumulated over time must be apportioned over time, yet the measure denies taxpayers such apportionment. The credits also do nothing to avoid California taxation of post-departure wealth in states without their own wealth tax.

Both the alternative apportionment regime and the day-denominated credits implicitly concede that apportionment is necessary, yet neither satisfies the requirements of

[55] California Proposition 40 (2026), § 50306(b).
[56] Walter Hellerstein, "Commerce Clause Restraints on State Taxation: Purposeful Economic Protectionism and Beyond," 85 *Mich. L. Rev.* 758 (1987).
[57] California Proposition 40 (2026), § 50307(a).

apportionment. Alternative apportionment, in particular, involves conceding that apportionment is constitutionally required, then setting a floor that has no relationship to any measure of in-state time or activity, while shifting the burden to the taxpayer to overcome it by clear and convincing evidence.

If California can assert the right to tax a former resident's assets post-departure — including newly acquired assets — then the taxpayer's new domiciliary state's claim on those same assets, under a hypothetical scenario where they both imposed identical wealth taxes, yields dual taxation of the same assets that a day-denominated credit system cannot fully cure, violating internal consistency. Importantly, the tax fails regardless of whether any other states currently have such overlapping laws.[58]

The CBTA contains a payment mechanism for liquidity-constrained taxpayers, called Optional Deferral Accounts (ODA), under which the state asserts a claim against the taxpayer's illiquid assets, including their share of ownership in any private businesses, and taxes them whenever value is realized, withdrawn, or transferred. If the taxpayer's private business appreciates in value over the years, all while the taxpayer is a resident of another state, California would continue taxing that clearly post-departure growth, which is inconsistent with both the fair apportionment (under both internal and external consistency) and fair relationship requirements.

Whether substantial nexus exists in such cases is doubtful as well. States sometimes recognize a limited doctrine of "trailing nexus" in business taxation, which permits a state, for a time, to continue to tax a business that no longer has nexus to the state, on taxable activity undertaken in the state while they still had nexus. But this is not relevant here, since the tax extends to activity and wealth accumulation that is entirely post-departure. The amount collected is not just a deferral of tax liability and is not based on a fixed valuation date. Liability increases with out-of-state post-departure increases in the value of the assets.

Nor is it sufficient to argue that the so-called Optional Deferral Accounts are, as the name implies, "optional," as if they are simply a voluntary payment plan. For the owner of a private business, particularly if their controlling interests exceed their economic interests, there may be no realistic way to liquidate the assets necessary to pay the tax upfront. The state cannot impose a tax "so arbitrary as to constrain to the conclusion that it was not the

[58] Michael S. Knoll and Ruth Mason, "The Economic Foundation of the Dormant Commerce Clause," 103 *Va. L. Rev.* 309 (2017).

exertion of taxation, but a confiscation of property,"[59] and if ODAs are the mechanism by which that is avoided, the state cannot rely on the notion that they are merely a taxpayer's payment option of choice as a cure to defects in nexus.

Notably, a taxpayer is expressly eligible for an ODA only if disposing of all their liquid assets is insufficient to meet their wealth tax obligations. In the original paper designing "unliquidated tax reserve accounts" (ULTRA), the progenitor of ODAs, the accounts were anticipated as optional alternatives to accepting the state's assessments of hard-to-value assets, not as the only way that an illiquid taxpayer could meet their obligations. The concept's creators, who are also the CBTA's drafters, emphasized that their ULTRAs were consensual agreements, which was important since, "because of possible federal constitutional limitations, California might face difficulties collecting the deferred tax liabilities. This could potentially create problematic, perverse incentives for taxpayers to move out of state to escape the wealth tax."[60]

The ULTRAs were designed to give California a "contractual claim that California's tax authorities could enforce even if the taxpayer might subsequently leave the state."[61] By contrast, the ODA regime is deficient in consent and contractual form, leaving it vulnerable to the very challenges the drafters previously acknowledged.

## Marriage and Family

The wealth tax's drafters saw families as a potential threat to the wealth tax base. A nonresident spouse might dilute the household's net worth, and if assets held in trust for children or grandchildren were out of reach, revenues would likewise fall short of expectations.

Lacking better data, all estimates of potential wealth tax revenue have begun with Forbes data, which tends to aggregate households. The net worth listed for a particular billionaire can sometimes encompass multiple households, some of which may be located outside California.[62] Even before any tax avoidance activity, wealth is already distributed in ways that erode the notional tax base. Proposition 40's drafters made a concerted effort to

[59] *Brushaber v. Union Pacific Railroad Co.*, 240 U.S. 1, 24–25 (1916).
[60] Brian D. Galle, David Gamage, and Darien Shanske, "Solving the Valuation Challenge: The ULTRA Method for Taxing Extreme Wealth," 72 *Duke L.J.* 1257 (2023), at 1315.
[61] Id., 1316.
[62] Aggregation varies. For instance, the Forbes California list includes multiple Pritzkers, each of whom have identifiably separate net worths, though even within these, each listed taxpayer's wealth may also encompass wealth already transferred to their children or other related persons.

recombine that wealth. The aggressiveness of these provisions yields overreach, leading to absurd and sometimes unconstitutional results.

Some of these issues have already been addressed in the discussion of trusts and transfers, which give rise to clear nexus challenges. The measure's treatment of spouses is similarly fraught.

The CBTA applies to the net worth of the taxpayer and their spouse, even if the spouse's assets are not marital property and even if that spouse is not a California resident and thus themselves out of reach of the wealth tax. Furthermore, even when both spouses are California residents, marriage can yield tax liability that would not exist in its absence, since the tax is levied on household net worth above $1 billion. A couple with a combined net worth above $1 billion is subject to the tax, but two unmarried individuals, each with valuations just below the $1 billion threshold, would avoid taxation.

Divorce also yields complications. The CBTA adds back debts to related persons incurred at any time, and defines related persons as "any person that is related to the taxpayer … as of January 1, 2026."[63] Any indebtedness incurred due to a division of assets could see the transferred assets added back to the taxpayer's net worth for tax purposes, as if the debt did not exist, and any actual transfers in 2025 or 2026 could likewise be taxed as if the assets still belonged to the taxpayer. As with other instances in which the CBTA would tax assets the taxpayer does not own, the due process implications are clear.

California is a community property state, and states are permitted to tax a spouse's community interest in property. However, the CBTA goes further with mandatory aggregation of a nonresident spouse's separate, out-of-state wealth. This conflicts with *Hoeper v. Tax Commission*, a case in which the U.S. Supreme Court invalidated a Wisconsin law that reached a non-resident spouse's separate income. There, the Court ruled that "any attempt by a state to measure the tax on one person's property or income by reference to the property or income of another is contrary to due process."[64] If one spouse has no legal interest in the out-of-state property of the other, over which California does not otherwise have nexus, California cannot legally measure the tax based on that property.[65]

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[63] California Proposition 40 (2026), § 50308(k).
[64] *Hoeper v. Tax Commission of Wisconsin*, 284 U.S. 206 (1931).
[65] In some cases where spouses have invoked *Hoeper*, courts have found that taxpayers actually had a legal interest in the other spouse's property, or the taxing state had nexus over it separately. Aggregation's constitutionality depends on the specifics of each case. The CBTA, however, with its universal rule of mandatory aggregation, provides no protection for truly separate property.

Attribution of a non-resident spouse's wealth to California also fails the internal consistency test. If two states had identical wealth taxes, both taxing "the taxpayer and their spouse worldwide … wherever such spouse is resident,"[66] then both states would tax the entirety of the couple's assets. Credits for taxes paid to other states provide no relief, since the overlapping taxation would involve two taxpayers. This is a facial defect.

Spouses in separate states could also exacerbate the problems with the CBTA's trust provisions, discussed previously. If spouses with separate legal domiciles jointly funded a trust, and each of their states imposed a wealth tax, then both states would tax the trust in full.[67] The trust apportionment provision would fail, since even if the trust were apportioned between them, both states would capture the other spouse's share through aggregation.

## Out-of-State Property

States are prohibited from taxing real or tangible personal property permanently located outside their borders.[68] The CBTA partially addresses this with exclusions for personal property kept outside California for at least 270 days in 2026, and by excluding out-of-state real property if held directly or through a revocable trust. However, the real property exclusion does not extend to real property held through a business entity, which is taxed as an interest in that entity. Properties are often owned through limited liability companies (LLCs), and California would tax billionaires' out-of-state real estate if held by an LLC, while excluding it if owned in their own name.

The distinction is hard to justify, though proponents will argue that it is constitutionally admissible because the tax is on the membership interest in the LLC, not on the land itself. That may be the case — but it is still a design choice with scant justification. If two states adopted similar wealth and property tax regimes, then property held in LLCs in one state by owners in the other would always be taxed twice, under one state's wealth tax and the other state's property tax.

The CBTA is a tax not just on nationwide but on worldwide net worth, which means it also taxes foreign assets and interests in foreign entities. Taxes on foreign commerce face requirements going beyond those articulated in *Complete Auto*, including the requirement that the tax not create an enhanced risk of multiple international taxation.[69]

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[66] California Proposition 40 (2026), §§ 50308(f), 50301(a).
[67] Id., §§ 50301(a), 50303(c)(6), 50308(b).
[68] *Curry v. McCanless*; *Union Refrigerator Transit Co. v. Kentucky*, 199 U.S. 194 (1905); *Frick v. Pennsylvania*, 268 U.S. 473 (1925).
[69] *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979).

While wealth taxes are extremely rare across the world, they do exist in several countries. Additionally, countries have other taxes that apply to foreign assets taxed by the CBTA. The CBTA's credits are not relevant here, at least as designed, as they are based on the number of days a taxpayer resides in the other taxing jurisdiction. A California billionaire who never takes up residence abroad, therefore, receives no credit. Under the stricter test for international commerce, the resulting double international taxation raises serious constitutional questions.

The measure allows credits for taxes paid elsewhere "to the extent required by the United States Constitution,"[70] a savings clause designed to address any unconstitutional outcomes, but this clause supplies no rule for how to deal with an issue likely to arise routinely, as billionaires are particularly likely to have foreign assets or interests in foreign businesses or other entities. It also requires appeals or litigation initiated by the taxpayer to avoid an unconstitutional tax.

Additionally, the CBTA's tax base fails to exclude U.S. Treasury bills, notes, and bonds from its base, even though federal law prohibits state taxes from falling on these federal obligations.[71] This omission is unlikely to be fatal to the CBTA as a whole: either the FTB would implement an exclusion or the courts would order them to do so. It does, however, suggest a likely avoidance channel for liquid assets of affected billionaires, who could not, under federal law, be subject to wealth tax on any assets they convert into Treasury investments by the CBTA's December 31 valuation date.

## Administrability

If approved by the voters in November, time would be at a premium. The FTB would be tasked with standing up a new tax with astonishing speed. Courts would have to hear complex legal challenges, and weigh reformation, severing provisions, or striking the measure down in its entirety to the extent that the courts identify constitutional defects. And, as previously considered, taxpayers would have to comply with an unprecedented tax with very little time, with an April 15, 2027, obligation even though they presently lack any FTB-promulgated rules, guidance, or even tax forms.

The FTB's ability to implement the tax responsibly on the timeline established by the measure is in serious doubt. The FTB was designed to administer income and franchise taxes. While it has significant in-house expertise, no state revenue agency has ever

[70] California Proposition 40 (2026), § 50307(b).
[71] 31 U.S.C. § 3124(a).

implemented a wealth tax, and Proposition 40 gives the agency practically no time to build out the necessary capacity.

In response to the 2023 wealth tax proposal, the FTB noted that it would require "significant lead time" to implement the tax, which might "require the equivalent of a new division within the Department to receive and process Wealth Tax returns, payments, and related business and trust information returns and to verify compliance,"[72] as a wealth tax represents "an entirely new tax model" and the FTB currently lacks "staff sufficiently sized or knowledgeable in the value of asset group categories [...]."[73] The agency noted that "[a]ll aspects of implementation; administration including systems changes, collection, taxpayer education; the hiring and training of new staff; and the procurement of outside experts or counsel could not begin until after the enactment of this bill along with the voter approval," just as the FTB could not begin implementation of the CBTA until after voter approval of Proposition 40.[74]

For the prior tax, the FTB suggested "adding language that would provide at least approximately three to four years from the ... voter approval date to the [wealth tax] operative date."[75] Here, the tax's effect is immediate — retroactive, in fact — and filing (or securing a six-month extension) and payment is due mere months after voter approval. While this year's proposal involves far fewer potential taxpayers, that narrower scope does nothing to change the complexity of building out the technical and technological capability to administer a wealth tax.

The prior proposal appropriated a minimum of $300 million the first year, and $100 million in all subsequent years, to administer the wealth tax.[76] The FTB considered the ongoing support inadequate, suggesting $200 million to 300 million per year at a minimum, with startup costs in excess of this amount.[77] The wealth tax that voters will decide in November contains no appropriation for tax administration, instead funding it from the tax's own revenue and with a $50 million loan against that future revenue.

California's Legislative Analyst's Office (LAO) believes that the CBTA can be administered for substantially less than the FTB estimated for the broader wealth tax, suggesting costs of

[72] California State Assembly, Committee on Revenue and Taxation, "AB 259 (Lee)," 11.
[73] California Franchise Tax Board, "Bill Analysis: AB 259 — Wealth Tax Act," January 19, 2023, 15, https://www.ftb.ca.gov/tax-pros/law/legislation/2023-2024/AB259-011923.pdf.
[74] California State Assembly, Committee on Revenue and Taxation, "AB 259 (Lee)," 11.
[75] Id.
[76] A.B. 259, 2023–2024 Reg. Sess. § 4 (Cal. 2023).
[77] California Franchise Tax Board, "Bill Analysis: AB 259 — Wealth Tax Act," 19.

tens of millions of dollars annually. The LAO estimate may be too optimistic, but it embeds a real and important change: whereas prior proposals assigned appraisal responsibility to the state, the new tax shifts that initial responsibility to taxpayers. This reduces the state's direct costs of valuation at the expense of taxpayers themselves, though to the extent that the FTB challenges taxpayers' appraisals, it is critically important that the agency has sufficiently sophisticated in-house assessment expertise to do so. The LAO has estimated what the state is likely to spend, which is different from what the state would need to spend to administer such a novel tax adequately.

It is problem enough that the FTB would have only a few months to stand up a tax that it previously estimated would take several years to implement. But the compressed timing adds one more problem: most of the revenues to build the collections regime arrive only after collections begin, with the FTB granted only a $50 million start-up loan to build out these systems, which may or may not be sufficient.[78] Any separate funding for administration would have to run through the Budget Change Proposal cycle, which would come far too late. The FTB would need to hire and train new staff, build out new technological capacity, determine how to implement an entirely new tax, create an appeals function, and undertake the necessary rulemaking to allow it to operate, all before it has much of the new funding designed to facilitate this work.

Rulemaking, in particular, does not operate at that pace — or at least, it should not. Rulemaking for market-based sourcing under the corporate income tax took more than a decade, even though in that case, the state could draw upon the experience and regulations of dozens of other states. The CBTA will require complex valuation regulations, appraisal standards, forms, and dispute procedures in place before returns can be filed, and arguably before valuations are even undertaken.

To expedite this process, the CBTA takes shortcuts, exempting all FTB regulations, standards, procedures, notices, guidelines, and guidance on the wealth tax from Administrative Procedure Act (APA) requirements until January 1, 2028, which is, of course, after the tax is imposed.[79] The measure relies on rushed non-APA guidance, strips away notice-and-comment safeguards, and forces the FTB to patch together what it can — for an extraordinarily complex new tax — extremely quickly.

The notional window for taxpayers to have their assets valued begins January 1, but no FTB valuation rules will exist by then. Taxpayers and appraisers, who can face stiff penalties for

[78] California Proposition 40 (2026), § 16355(e).
[79] Id., § 50309(b)(2).

understatement of tax, will have their valuations scrutinized under rules the FTB will issue without notice, comment, or public participation, and without any review by the Office of Administrative Law — and quite possibly not even publicly promulgated by the time taxpayers are forced to submit their valuations. An absence of formal rules will show up in taxpayers' as-applied challenges, and the FTB may be particularly hard-pressed to defend its valuations and the rules they are based on when those rules were adopted outside the APA process and lack an ordinary rulemaking record.

The FTB must, moreover, build out permanent tax capability for what has been designed as a one-time tax. They would need to establish what is practically a new division, and to go on a significant hiring spree for roles that would, in many cases, only last a few years. Setting aside litigation, which could postpone the tax's implementation or, through as-applied challenges, generate lengthy delays before taxpayers remit any payments, a significant portion of the work is frontloaded, even as some functions would have to remain in place for decades, handling deferred obligations for illiquid taxpayers.

The FTB would be tasked with hiring and training a specialized valuation and audit workforce, much of which would not be needed after the first tax season, while a smaller contingent would continue working for decades on a tax that (if not later made permanent, notwithstanding the insistence that this is a one-time levy) was imposed for just one year.

## Remedies and Refunds

The CBTA's many defects exceed the plausible limits of judicial reformation. To save the tax, courts could be required to revise the residency and valuation dates, adjust the apportionment rules for part-year taxpayers, modify or eliminate spousal aggregation, curtail the provisions on trusts and transfers, and eliminate liability on foreign assets or federal obligations, among other changes.

Drafters embedded a specific request for any reformation necessary to save the tax, directing courts to "preserve the imposition of the tax authorized, including by reforming dates or periods specified, using the most limited adjustment possible to cure any constitutional or other legal defect."[80] But just because drafters invited reformation where legally necessary to save the tax does not mean that courts are always empowered to do so.

[80] Id., § 50311(b).

In addition to reformation of the measure's language, courts have a more traditional remedy available: striking provisions that offend the Constitution without striking the measure in its entirety. The CBTA contains a severability clause, urging courts to sever provisions as necessary rather than invalidating the entire statute over a legal defect, in addition to the request that courts make modifications where necessary.

Some provisions are more amenable to judicial reformation than others, but few, if any, are straightforward. If, for instance, the courts were confident that the inclusion of the entirety of a trust in a taxpayer's net worth based on a transfer to that trust was a mere drafting error, and concluded that this provision was radically inconsistent with multiple prongs of the *Complete Auto* test, they might simply revise the measure to stipulate that only the portion contributed in 2026 was subject to tax. (Even this, of course, invites serious constitutional scrutiny.) But the measure's related provision about allocating the trust's assets among contributing taxpayers casts serious doubt on the notion that this was an accidental provision rather than an aggressive but intentional overreach. Courts would have a much harder time second-guessing the drafters' decisions rather than simply striking down the CBTA in its entirety.

Other provisions are even more difficult to sever, or to reform without engaging in a legislative function that the courts rightly reject. When several possible cures are available, asking courts to choose among them exceeds the judicial function and implicates the separation of powers. The drafters cannot expand the court's jurisdiction through the plea for judicial reformation.

Under California court rulings, reformation is possible only where a court can be confident that the enacting body — here, the voters — would have preferred a reformed statute to invalidation.[81] The lock-in effect, based on a January 1 residency date, features prominently in the measure's design and in how it has been sold to voters, and a later date would yield a materially different tax than the one presented to voters.

Under a validation action in the measure, the courts are obliged to determine the CBTA's facial validity on an expedited schedule in early 2027, and the measure purports to make the tax facially incontestable thereafter.[82] Facial challenges must be filed within 60 days of the measure's approval, and anything not facially challenged within that time is deemed facially valid and legally incontestable thereafter. The Sacramento County Superior Court is directed to hear the matter, with a final decision no later than April 1, 2027, and with any

[81] *Kopp v. Fair Political Practices Commission*.
[82] California Proposition 40 (2026), § 50314.

decision on appeal to the California Supreme Court entered by November 1, 2027. This is an extremely compressed schedule to deal with a raft of complex constitutional challenges.

The timeline also means that challengers must file their constitutional litigation before the FTB has issued any rules interpreting it. Several important implications of the tax are disputed, with differing interpretations of provisions regarding the valuation and inclusion of property. Some constitutional objections only arise under certain interpretations, but the interpretation taken by the FTB will be unknowable when challengers are required to file their case and may still be unknown as litigation unfolds.

Some claims may not yet be justiciable during the window for filing a claim. A facial challenge to control-share valuation might be ruled unripe before the FTB issues an interpretation of the provision, and that dismissal could create a permanent bar to litigating the issue should the FTB later promulgate rules adopting an aggressive interpretation. If the measure's language functionally prevents key constitutional questions from being litigated, due process is denied.

The 60-day facial validation window cannot, of course, prevent as-applied challenges. Even if the measure survives broad constitutional challenges, individual taxpayers could challenge the validity of the tax's imposition on them. But it does force the central questions to be identified and litigated quickly, absent vital knowledge of how the tax's provisions will be interpreted and applied.

Under the federal Tax Injunction Act, moreover, federal courts are prohibited from enjoining state tax collections when state tax law affords a plain, speedy, and efficient remedy. Taxpayers raising federal constitutional objections to the CBTA must originate them in California courts, and the only federal venue for review is on petition of certiorari to the U.S. Supreme Court.[83]

This means that, so long as the Tax Injunction Act applies, plaintiffs could never seek federal review of any constitutional defect not raised and resolved within the window afforded by the measure, potentially even if they were prevented from doing so because raising a particular claim would have been premature during the 60-day window for filing facial claims. It is possible, of course, federal courts might be called upon to consider whether the CBTA's allowable remedies are truly plain, speedy, and efficient if they curtail due process.

[83] 28 U.S.C. § 1341; *California v. Grace Brethren Church*, 457 U.S. 393 (1982).

While expedited review has precedent, forcing a binding decision on all facial constitutional challenges for such a fraught statute is a dramatic overreach. The CBTA yields an entirely new tax with no precedent in the United States, imposes a 60-day cutoff for filing any facial challenges, forces the litigation into a single venue, holds the courts to an extremely abbreviated schedule for considering complex constitutional questions, and declares the tax's essential validity incontestable thereafter. These provisions themselves could well become the subject of future litigation.

### Existing Revenue Streams

Should the tax be invalidated, in whole or in part, after significant revenues have been collected, this could create a meaningful budget hole. When tax payments are required before challenges can take their course, a taxpayer victory requires refunds with interest.[84] If the tax were invalidated under the expedited schedule, revenues would still be available for refunds, less the amount spent on tax administration and litigation. But if the tax failed in whole or in part in 2028 or later, or if as-applied challenges from specific taxpayers generated substantial refunds, revenues appropriated under the CBTA would no longer be available to the state, which would be forced to process refunds from the General Fund. In a scenario where substantial revenues were collected and directed to health programs, refund obligations could precipitate a state budget crisis.

## Conclusion

The CBTA piles complexity upon complexity. The potential to tax company founders based on their controlling interests rather than their economic stakes, the inclusion of the full value of any trust to which a taxpayer contributes, the lack of apportionment, the taxation of post-departure wealth, the retroactive imposition of a wholly new tax, the near-impossibility of properly administering or complying with this tax by the deadline: all of these issues add up to a legal and administrative crisis should the measure pass in November.

If the CBTA is adopted, it could easily fail on facial challenges. Even if it survives, it might do so under modifications that lose most of the intended tax base. As-applied challenges to liability for individual taxpayers would follow. California could be tied up in litigation for years, attempting to build out a costly new tax administration regime while fighting an expensive legal battle the state could easily lose. And to the extent that revenues have

[84] *McKesson Corp. v. Division of Alcoholic Beverages & Tobacco*, 496 U.S. 18 (1990); *Reich v. Collins*, 513 U.S. 106 (1994).

already been collected, refunds (with interest) would be required, draining the General Fund. The billionaires who have already left by that time, meanwhile, are unlikely to return.

Under Proposition 40, California's lawyers will do well. It may not be possible to say the same about the rest of California.

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