

FILED
SUPREME COURT
STATE OF WASHINGTON
11/29/2018 2:20 PM
BY SUSAN L. CARLSON
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No. 96383-5

IN THE SUPREME COURT
OF THE STATE OF WASHINGTON

LOWE'S HOME CENTERS, LLC,

Petitioner,

v.

DEPARTMENT OF REVENUE, STATE OF WASHINGTON,

Respondent.

MEMORANDUM OF AMICUS CURIAE
KOHL'S DEPARTMENT STORES, INC.
IN SUPPORT OF PETITION FOR REVIEW

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I. IDENTITY AND INTEREST OF AMICUS CURIAE

Kohl's Department Stores, Inc. (Kohl's) operates retail department stores throughout the country, including nineteen in Washington State. Kohl's offers a store-branded, or private-label, credit card, which is issued by a third-party bank. Kohl's qualifies for a federal bad-debt deduction associated with losses on the credit card sales.

Respondent Department of Revenue previously audited Kohl's and disallowed the retail sales tax credit and retailing business and occupation (B&O) tax deduction that Kohl's claimed under RCW 82.08.037 and RCW 82.04.4284. The Department's determination is the subject of litigation in Thurston County Superior Court in the consolidated matter of *Macy's Northwest, Inc. and Kohl's Department Stores, Inc. v. Washington State Department of Revenue*, No. 16-2-02649-34. That matter has been stayed pending resolution of this case.

The issues raised by Kohl's in the stayed litigation are substantially similar to those now presented by Lowe's.

II. STATEMENT OF ISSUE PRESENTED FOR REVIEW

Kohl's supports the Statement of Issue as framed by Petitioner Lowe's in the Petition.

III. STATEMENT OF THE CASE

Kohl's adopts the Statement of the Case presented by Lowe's in the Petition.

IV. ARGUMENT

Petitioner Lowe's argues (Pet. 5) that the Court should accept review because the Court of Appeals' decision conflicts with *Puget Sound National Bank v. Department of Revenue*, 123 Wn.2d 284, 868 P.2d 127 (1994), *see* RAP 13.4(b)(1), and furthermore, that the Court should accept review under RAP 13.4(b)(4) because the "proper interpretation of the Bad Debt Statutes is of substantial public interest." Kohl's will supplement the "substantial public interest" point in two respects.

A. **The retailing industry has a substantial interest in the issue presented.**

Neither Petitioner nor Respondent has advised the Court of pending litigation involving Macy's Northwest, Inc. (Macy's) and Kohl's with substantially similar issues. Both Macy's and Kohl's initiated actions against the Department of Revenue in 2013 in the Washington State Board of Tax Appeals, asserting that they qualified for the sales tax credit and B&O tax deduction under RCW 82.08.037 and RCW 82.04.4284, respectively, because they were entitled to the federal bad-debt deduction under 26 U.S.C. § 166. Those cases are now consolidated before the Thurston County Superior Court and awaiting resolution of the Lowe's

matter. The issue presented in this matter relates not to a single taxpayer, but to an industry of retailers that regularly suffer bad-debt losses and seek to have the state statutes applied consistent with their language. For this reason, the Lowe's Petition involves an issue of substantial public interest that should be determined by the Court.

B. The history of RCW 82.08.037 reflects the Legislature's intent that retailers need not own the debt.

In Section VI.B of Petitioner's Argument, Lowe's explains (Pet. 17-20) that the Court of Appeals' conclusion that Lowe's must own the accounts conflicts with the law and presents an issue of substantial public interest. The statutory amendments further support Lowe's argument.

The Washington Legislature first enacted the sales tax credit in 1982. The legislation provided as follows:

A seller is entitled to a credit or refund for sales taxes previously paid [1] on debts [and 2] which are deductible as worthless for federal income tax purposes.

Laws of 1982, 1st Ex. Sess., ch. 35, § 35.

In 2003, the Legislature deleted the phrase "deductible as worthless for federal income tax purposes" and in its place inserted the phrase "bad debts under 26 U.S.C. Sec. 166" Laws of 2003, ch. 168, § 212. The amended statute provided in full:

A seller is entitled to a credit or refund for sales taxes previously paid [1] on debts [and

2] which are bad debts under 26 U.S.C. Sec.
166

Id.

Finally, the Legislature amended the statute for the last time in 2004 so that the statute now reads as follows:

A seller is entitled to a credit or refund for sales taxes previously paid on [1] bad debts, as that term is used in 26 U.S.C. Sec. 166

Laws of 2004, ch. 153, § 302.¹

There is no issue that Lowe’s was entitled to the federal bad-debt deduction under 26 U.S.C. § 166, not because it owned the underlying debt, but because it was a guarantor of the debt—the federal provisions allow either. *Lowe’s Home Ctrs., LLC v. Dep’t of Revenue*, ___ Wn. App. ___, 425 P.3d 959, 966 (2018) (“[W]hether Lowe’s qualified for a federal bad debt deduction is not at issue.”). However, whereas the state statute previously required both the payment of sales taxes “on debts” and which qualified for the federal deduction, the statute no longer requires that Lowe’s own any debt because the Legislature removed that requirement from the statute in 2004. Now, there must simply be “bad debts” as that term is interpreted under federal law. Section 166 has no requirement that

¹ In the case of the B&O tax deduction under RCW 82.04.4284, the Legislature deleted the phrase, “the amount of credit losses actually sustained by taxpayers” with “bad debts, as that term is used in 26 U.S.C. Sec. 166” See Laws of 2004, ch. 153, § 307.

Lowe's own the underlying debt. The Legislature dispensed with any prior ownership requirement in 2004. Neither the Department nor the Court of Appeals has given meaning to this statutory change.

The Court of Appeals acknowledges that “there are many forms of federal bad debt that may be claimed under 26 U.S.C. § 166, 26 C.F.R. § 1.166-1(a), (c), and 26 C.F.R. § 1.166-9(a), [but] only bad debts ‘on sales taxes previously paid’ that are ‘written off as uncollectible’ qualify for a retail sales tax refund.” *Lowe's*, 425 P.3d at 966 (citations omitted). With respect to the statutory requirement that sales taxes have been previously paid, the retailers satisfy the “directly attributable” requirement established by the Court of Appeals.

In each case, the retailer extends credit for a brief period of days until it receives payment from the bank. The retailer promptly remits sales tax to the state. The credit card holder defaults and the bank takes back, in whole or in part, the money previously forwarded to the retailer. That money taken back is directly attributable to the sales (to the sales proceeds and the retail sales tax). Kohl's agrees with the Court of Appeals, that “courts focus on the substance of a transaction,” *Lowe's*, 425 P.3d at 966, but the court in this case failed to do so. In both substance and form, Lowe's has suffered a loss of the sales proceeds and the corresponding sales tax. In substance and form, the sales tax dollars that Lowe's paid

over to the state were first recouped from the bank, but later taken back by the bank. The scenario is analogous to dishonored checks for which the Department allows the bad-debt credit and deduction. *See* Department of Revenue Industry Guide – Restaurants and Retailers of Prepared Food.² The drawee’s bank initially grants credit to the retailer’s account, but when the drawer’s bank rejects it, the drawee’s bank, through contract with the retailer, takes back the money from the retailer’s account. In substance and form, Lowe’s no longer has the money for the sales tax it paid over to the state, and as the Court previously established in *Puget Sound*, “[a]ny other rule is inequitable and entitles the State to a financial windfall. . . .” 123 Wn.2d at 290, 868 P.2d at 131.

For these reasons, Lowe’s Petition involves an issue of substantial public interest that should be resolved by this Court.

V. CONCLUSION

For the foregoing reasons, the Court should grant the Petition for Review.

² Wash. State Dep’t of Revenue, Restaurants and retailers of prepared food, Business and occupation (B&O) tax, <https://dor.wa.gov/doing-business/business-types/industry-guides/restaurants-and-retailers-prepared-food/business-and-occupation-bo-tax> (last visited Nov. 29, 2018); Wash. State Dep’t of Revenue, Restaurants and retailers of prepared food, Retail sales tax, <https://dor.wa.gov/doing-business/business-types/industry-guides/restaurants-and-retailers-prepared-food/retail-sales-tax> (last visited Nov. 29, 2018).

Respectfully submitted.

DATED: November 29, 2018.

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CERTIFICATE OF SERVICE

Today I electronically filed the foregoing document via the Washington State Appellate Courts' Secure Portal, which will automatically cause such filing to be served on counsel for all other parties in this matter via the Court's e-filing platform.

I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED: November 29, 2018, at Seattle, Washington.

s/ Betty Kawagoe

Betty Kawagoe
Legal Practice Assistant

PERKINS COIE LLP

November 29, 2018 - 2:20 PM

Transmittal Information

Filed with Court: Supreme Court
Appellate Court Case Number: 96383-5
Appellate Court Case Title: Lowe's Home Centers, LLC v. Department of Revenue, State of Washington
Superior Court Case Number: 15-2-02994-8

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