91072-3

NO. 71663-8-I

IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON
DIVISION I

STEVEN KLEIN, INC., d/b/a KLEIN HONDA,

Appellant,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Respondent.

PETITION FOR REVIEW BY THE SUPREME COURT

Michele Radosevich
Davis Wright Tremaine LLP
Attorneys for Klein Honda

1201 Third Avenue, Suite 2200
Seattle, WA 98101-3045
(206) 622-3150 Phone
(206) 757-7700 Fax

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Rules

I. Identity of Petitioner

Steven Klein, Inc. d/b/a Klein Honda ("Klein") asks review of a decision of Board of Tax Appeals ("BTA"), which was affirmed by the Court of Appeals.

II. Citation to the Court of Appeals Decision

Division One of the Court of Appeals filed a published 2-1 decision on November 3, 2014, in case number 71663-8-I. A copy is attached hereto as Appendix A.

III. Introduction

At issue here are amounts received by Klein from American Honda Motors Company ("Honda" or "factory") in the form of rebates on the sale of certain vehicles during specified time periods (referred to herein as "dealer cash"). No additional services were performed by Klein in exchange for dealer cash other than selling the vehicle, and the Department of Revenue ("Department") concedes that Klein properly paid the retailing B&O on this activity.

The BTA held that dealer cash was taxable because "a taxpayer can have taxable income from business activity without providing any specific services." AR 27. [1] The Court of Appeals majority agreed that dealer cash need not represent compensation for additional services to be

[1] The Administrative Record is referred to herein as "AR."

taxable, and that no business activity need be identified: "[T]he B&O tax is not a tax on only specific enumerated business activities, but rather on "the gross revenues received in the course of doing business." Slip op. at 9.

The dissent correctly takes issue with this conclusion, noting that "gross income is taxable only after identification of a business activity that is subject to taxation." Slip op. at 1 (Becker, J., dissenting in part) ("Dissent"). In this case, the dissent finds, the business activity exchanged for dealer cash is retailing, and the measure of the retailing tax does not include dealer payments.

The rationale for imposing the B&O tax on business activities, not income, goes back to two 1933 cases. In *State ex rel. Stiner v. Yelle*, 174 Wash. 402, 25 P.2d 91 (1933), the Court held that the B&O tax was constitutional because it was an excise tax imposed on the privilege of engaging in business activities, and not on the income from these activities:

> This act does not concern itself with the income that has been acquired, but only the privilege of acquiring, and that the amount of the tax is measured by the amount of the income in no way affects the purpose of the act or the principle involved.

174 Wash. at 407. On the same day that it issued its opinion in *Stiner,* the Court handed down *Culliton v. Chase*, 174 Wash. 363, 25 P.2d 81 (1933), striking down the income tax as an unconstitutional form of property tax. These two cases form the foundation for Washington's tax statutes.

The majority opinion of the Court of Appeals thus calls into question long-established statutory interpretations based on this case law, and, in fact, directly conflicts with *Stiner*. This Court should grant review based on (1) the conflict, and (2) the substantial interest the public has in clearly understanding the basis for taxation.

IV. Issues Presented for Review

Did the BTA (and the majority opinion of the Court of Appeals) err in holding that the business and occupation ("B&O") tax is a tax on income rather than on business activity?

Did the BTA (and the majority opinion of the Court of Appeals) err in finding that incentive payments from Honda to Klein were taxable even though no discrete business activity, other than retailing, was associated with such payments and even the Department admits that dealer cash is not taxable under the retail classification?

V. Statement of the Case

Klein is an automobile dealership conducting business in Washington State. VTP 31.[2] The taxpayer sells new and used vehicles, provides automobile repair services and sells automobile accessories. *Id.* Klein is a Honda franchisee. *Id.* The relationship is governed by the Sales and Service Agreement between the parties. AR 309.

Klein and other Honda dealers must purchase vehicles from Honda. AR 314. The dealers have little discretion over their inventory. As Tom Hunt, the general manager at Klein, testified, Honda sends the dealer a presumptive order. VTP 38-39. The dealer may remove vehicles from the order but it cannot add them. *Id.* The order is based on prior sales history. VTP 39. Honda then ships the ordered vehicles to the dealer, issuing an invoice to the dealer for each vehicle when it ships. VTP 41, 43. AR 765, 767, 769. The invoice states a price, and the dealer remits that amount to Honda. *Id.*, VTP 43.

The invoice also states: "Dealer's invoice may not reflect dealer's ultimate vehicle cost given any rebates, allowances, collections, discounts, holdback, incentives, etc." AR 765, 767, 769; VTP 49. These adjustments to the dealer's cost come in several forms. Dealer cash is credit from Honda to Klein that is predicated on the sale of a particular

[2] The Verbatim Transcript of Proceedings is referred to herein as "VTP."

vehicle model during a particular period of time. AR 285. Honda tracks the sale of Honda vehicles by model. On a regular basis, Honda will issue a marketing bulletin to its dealers offering credit back on the sale of certain models within a specified time frame. AR 723 et seq. At the hearing, witness Tom Hunt described the theory behind dealer cash:

> Dealer cash is a means by which American Honda kind of puts more momentum behind a particular vehicle line or model. And when I say that, I mean that what they do is they adjust the vehicle's presence in the marketplace, usually as a reaction to competitive action, which typically would be rebates, consumer rebates, and allowing the Honda dealers to remain in a competitive position on that particular model.

VTP 50. For instance, the bulletin at AR 727 shows that Honda offered the dealers $500 back for each Civic Coupe sold between June 3, 2003 and September 30, 2003. The rebate is contingent only upon selling the designated car within the designated time. AR 285, 727. Klein does not have to do any marketing or advertising or adjust the retail price. At any given time, Honda may offer dealer cash on several models. VTP 51.

Klein does not market cars differently when they carry dealer cash. As Tom Hunt testified:

> In the sales process, it comes down to ultimately being competitive in the marketplace. And that's what the dealer incentives allow the Honda dealer to do, allows Klein Honda to do. If, for example, Toyota puts a significant rebate on a Corolla, and we have a customer cross shopping with a Civic, without the dealer incentive, you can have a

> $1,000, $1,500 difference in acquisition costs. And having the dealer incentive to the Honda dealer allows us to reprice our cars so they can be competitive. So it essentially allows us to lower our price to be competitive in the market.

VTP 52.

There are minimal, if any, additional clerical tasks associated with dealer cash. Klein is already required to report ***all*** sales to Honda on a daily basis by VIN number, using Honda's proprietary network. VTP 53-54, AR 771. Honda computers recognize the specific models from the VIN numbers. On a monthly basis, Honda prepares a miscellaneous credit advice for the dealer showing the amount of dealer cash earned by VIN number. VTP 71, AR 779. The actual credit is made via the balance forward statement that summarizes every transaction between the factory and the dealer for the month, except for new car purchases. AR 772, *see also*, *e.g.*, AR 728. This statement, prepared by Honda, offsets items purchased by the dealer, like parts, against credits for warranty work, holdback, flooring, and dealer cash. AR 772. It is used by the dealer to prepare a monthly reconciliation between it and the factory.

Two other credits that lower the dealer's cost are holdbacks and flooring assistance. The so-called "holdback" refers to a credit that Honda provides for every vehicle. VTP 44. The amount of the credit is actually listed on the invoice in a somewhat obscure fashion. For instance, the

invoice at AR 769 shows a MSRP of $17,310.00 and in the same line shows the number 51930. Adding a decimal point makes this number $519.30 or exactly three percent of the MSRP. This three percent is the holdback paid by Klein, then credited back by Honda.

Similarly, Honda provides a "flooring" credit for each vehicle. It is intended to help offset the dealer's cost of financing inventory. VTP 45. Like the holdback it is paid as a credit on the monthly statement. The Department recognizes that these credits reduce the dealer's purchase price for the vehicle and does not subject them to B&O tax. *See* Auto Dealers Industry Guide, AR 172-74.

There are also payments by Honda to Klein that are taxable payments for services, such as pre-delivery inspection, warranty work, and advertising. VTP 48, 51.

VI. Argument

This Court should accept review because the published decisions of the BTA and Court of Appeals conflict with this Court's prior cases distinguishing excise taxes from income taxes and this issue is of continuing importance to Washington taxpayers. RAP 13.4(b)(1) and (4).

A. Prior Case Law Establishes That the B&O Tax Is Levied on the Privilege of Doing Business and Not on Income.

Excise taxes are imposed on the privilege of doing business:

> (T)he obligation to pay an excise is based upon the voluntary action of the person taxed in performing the act, enjoying the privilege or engaging in the occupation which is the subject of the excise, and the element of absolute and unavoidable demand, as in the case of a property tax, is lacking. * * * 1 Cooley, Taxation, s 46, at p. 132 (4th ed. 1924).

Black v. State, 67 Wn.2d 97, 99, 406 P.2d 761 (1965).

Beginning with *Stiner*, this Court has long distinguished excise taxes from income or property taxes. *See, e.g., Morrow v. Henneford*, 182 Wash. 625, 626-31, 47 P.2d 1016 (1935) (sales tax upheld as excise); *Vancouver Oil Co. v. Henneford*, 183 Wash. 317, 320-21, 49 P.2d 14 (1935) (use tax upheld as excise); *State ex rel. Hansen v. Salter*, 190 Wash. 703, 705-06, 70 P.2d 1056 (1937) (motor vehicle tax measured as percentage of vehicle's value upheld as excise); *City of Spokane v. State*, 198 Wash. 682, 89 P.2d 826 (1939); (tax on use of personal property purchased at retail upheld as excise); *Klickitat County v. Jenner*, 15 Wn.2d 373, 380, 130 P.2d 880 (1942) (sales tax on courthouse construction upheld as excise); *St. Paul & Tacoma Lumber Co. v. State*, 40 Wn.2d 347, 354, 243 P.2d 474 (1952) (use tax on timber company's use of its logs and lumber products in its own operations upheld as excise); *Mahler v. Tremper*, 40 Wn.2d 405, 243 P.2d 627 (1952) (real estate conveyance tax upheld as excise); *Black v. State*, 67 Wn.2d 97, 99-100, 406 P.2d 761 (1965) (sales tax on lease of vessel as floating hotel upheld

as excise); *P. Lorillard Co. v. City of Seattle,* 83 Wn.2d 586, 589-92, 521 P.2d 208 (1974) (city business tax on wholesalers of tobacco held an excise); *High Tide Seafoods v. State*, 106 Wn.2d 695, 699-700, 725 P.2d 411 (1986) (tax on transfer of commercial food fish held an excise), *app. dismissed*, 479 U.S. 1073, 107 S. Ct. 1265, 94 L. Ed. 2d 126 (1987); *Covell v. City of Seattle*, 127 Wn.2d 874, 889-91, 905 P.2d 324 (1995) (fee on all residential property owners for improvement of city streets held a property tax). *See Harbour Village Apartments v. City of Mukilteo*, 139 Wn.2d 604, 610, 989 P.2d 542 (1999) (Talmadge, J., dissenting) (collecting cases).

Although these cases compare excise taxes with property taxes, *Culliton* established that a tax on the receipt of income was a property tax. Some lawyers and political leaders may question whether the Court would come to the same conclusion today, but this fundamental distinction is a cornerstone of Washington's statutory tax scheme and reflects the Legislature's intent in crafting the structure and language of today's B&O tax, which dates to 1935.

B. The Court of Appeals Majority Contradicts *Stiner* and Calls the Statutory Tax Scheme Into Question.

The Court of Appeals majority flatly denies that the B&O tax is an excise tax as that term is used in Washington law, instead holding that the

tax is imposed on gross revenue. Although the majority cites *Budget Rent-A-Car v. Department of Revenue*, 81 Wn.2d 171, 173, 500 P.2d 764 (1972), for that proposition, the cited language merely stated that the B&O was a tax on gross rather than net income in response to the taxpayer's claim that it made no profit on the transaction: "Thus, taxpayer's claim, that it realized no profit in selling the cars for less than it paid for them, is without relevance for the statute imposes the tax regardless of whether the business is losing or making money on the transaction." The case said nothing about the nature of excise taxes.

The majority confuses the imposition of the B&O tax on business activities with the measure of tax. As the dissent points out: "Gross income is taxable only after identification of a business activity that is subject to taxation. The tax is then 'measured by the application of rates against the value of products, gross proceeds of sales, or gross income of the business, as the case may be.' RCW 82.04.220(1)." Dissent at 1. Instead, the majority skipped this analysis and relied instead on a very broad reading of RCW 82.04.080 dealing with the gross income of a business even though this measure of tax does not apply if the only activity is retailing.

To further confuse its holding, the majority, while stating that the B&O tax is not a tax on enumerated activities, also stated that Klein's

business activity was "accepting the offer of American Honda to apply for dealer cash, selling specific models during specific times, documenting those sales as required by the manufacturer, applying to the manufacturer for dealer cash, and accepting payment." Slip op. at 9. However, as the dissent points out, these are business activities associated with retailing, upon which Klein properly paid tax. Dissent at 4. The same exact activity cannot be taxed a second time under the "services and other" B&O category in RCW 82.04.290.

Even more importantly, "accepting payment" cannot be a business activity under the case law or statutes because it would swallow whole the distinction between income taxes and excise taxes. If dealer cash—a payment—is itself a business activity as the majority opinion assumes, then the B&O is a direct tax on gross income, in contradiction to this Court's holding in *Stiner*.

C. The Fundamental Distinction Between Excise Taxes and Income or Property Taxes Is of Continuing Importance.

Culliton and *Stiner* form the foundation of Washington's statutory tax scheme under the Revenue Act of 1935, which relies to a very great extent on excise taxes—B&O and sales tax. Because these cases state that an income tax is an unconstitutional form of property tax, they would

require a constitutional amendment in order to enact an income tax on either business or personal income.

While some dispute the necessity for a constitutional change, Klein Honda does not present the Court with a constitutional argument requiring it to decide whether an income tax requires a vote of the people. The argument in this case is based on Washington statute. However, if the Court of Appeals decision is left standing, it will call into question long-established understandings regarding the B&O tax and undermine the current statutory scheme. If the B&O tax is actually a tax on gross income rather than on business activity, can the differential rates for various types of businesses be sustained? Would the Legislature be free to convert the B&O to a net income tax rather than a gross income tax without a constitutional amendment? The Court of Appeals majority raises more questions than it answers.[3]

The constitutionality of an income tax is an issue that should await a case that squarely presents that issue. That possibility was very real as recently as 2010 when voters were asked to approve Initiative 1098, creating a state income tax by statute. If the Court of Appeals is allowed to erode the statutory scheme and legislative intent that flow from the

[3] The original issue briefed to the BTA was simply whether Klein performed any additional services to justify imposing tax on the alleged "service" activity. AR 163. Both the BTA and the Court of Appeals substantially changed the thrust of the case by holding that no services were actually necessary.

Court's 1933 rulings without addressing those cases directly, it will send conflicting signals to taxpayers, legislators, and lower courts about the validity of the current scheme.

VII. Conclusion

For the above stated reasons, this Court should accept review.

RESPECTFULLY SUBMITTED this 2nd day of December, 2014.

Davis Wright Tremaine LLP
Attorneys for Klein Honda

By _____
Michele Radosevich, WSBA #24282

CERTIFICATE OF SERVICE

I hereby certify that I caused the document to which this certificate is attached to be delivered to the following as indicated:

Heidi A. Irvin
Andrew Krawczyk
Office of the Attorney General
Revenue Division
7141 Cleanwater Lane SW
P.O. Box 40123
Olympia, WA 98504-0123
heidii@ATG.WA.GOV
AndrewK1@ATG.WA.GOV

☐ Messenger
☑ U.S. Mail, postage prepaid
☐ Federal Express
☐ Facsimile
☑ Email

Declared under penalty of perjury under the laws of the state of Washington dated at Seattle, Washington this 2nd day of December, 2014.

Elaine Huckabee

APPENDIX A

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

STEVEN KLEIN, INC., d/b/a KLEIN HONDA, Appellant, v. STATE OF WASHINGTON, DEPARTMENT OF REVENUE, Respondent.	)	No. 71663-8-I DIVISION ONE PUBLISHED OPINION FILED: November 3, 2014

APPELWICK, J. — Klein Honda is a car dealership in Washington. Dealer cash is an incentive payment that Klein Honda receives from the manufacturer for selling specified vehicle models during specified periods of time. The sole issue on appeal is whether dealer cash is subject to Washington's B&O tax. We hold that it is and affirm the decision of the Board of Tax Appeals.

FACTS

Steven Klein Inc., doing business as Klein Honda, operates an automobile dealership in Everett, Washington. Klein Honda is an independent franchisee of American Honda Motor Company Inc. Klein Honda purchases vehicles at wholesale from American Honda and sells them to customers at retail. It also sells used vehicles, provides maintenance and repair services, and sells parts and accessories.

When Klein Honda sells a new vehicle to a customer, it communicates the sale to American Honda through an electronic form. The form includes the vehicle identification number, the names of Klein Honda personnel associated with the sale, the name and address of the customer, and information about the type of financing. According to Klein Honda's general manager, "This is how American Honda knows who bought what product and also starts the warranty clock."

American Honda also makes regular payments and credits to Klein Honda, which are reflected in a monthly balance forward statement. These payments include a marketing allowance credit for Klein Honda's advertising, as well as a fuel charge credit for Klein Honda providing a full tank of gas to customers when they purchase a vehicle. They also include holdbacks, which are a percentage of the manufacturer's suggested retail price that American Honda credits Klein Honda in the month following the wholesale purchase. These payments are reflected in the vehicle invoice and are automatic: Klein Honda does not have to do anything to receive the payments other than purchase the vehicle from American Honda.

American Honda also periodically offers an incentive program called "dealer cash" to its dealers, including Klein Honda. Under the dealer cash program, American Honda offers dealers a specified amount of cash for each sale they make of a particular Honda model during a specified period of time. American Honda issues marketing bulletins to dealers to announce the dealer cash incentive programs. For example, a marketing bulletin from 2003 offered $1,000 in dealer cash for each sale of 2003 Honda Insight models from April 1, 2003 to June 2, 2003.

The marketing bulletins provide substantial detail about which vehicles and which vehicle sales qualify for the incentive payment. The bulletins also specify the records dealers must keep and actions they must take to receive the incentive payment. For instance, dealers must conduct a self-audit at the conclusion of each dealer cash program and verify by signed affidavit that all listed vehicle sales meet the eligibility requirements for the program.

The owner, Steven Klein, stressed the need for dealers to comply with each requirement set forth in the marketing bulletin in order to be eligible for dealer cash: "And basically what you want to do is you read these backwards and forwards, because this is our contract with the factory to get our money, and if we don't do everything to the letter of these bulletins they can say, we're not going to give you the dealer cash." Klein Honda's general manager also described the marketing bulletin as a "conditional offer." At times, Klein Honda made sales of specified models during specified periods, but did not meet the requirements of the marketing bulletin, and therefore did not receive dealer cash for those sales.

The dealer cash program is designed to stimulate sales of the specified models. The number of dealer cash programs that American Honda offers is not guaranteed, but rather depends on market climate. If the market becomes challenged or a competitive product is viewed as comparable, American Honda will offer more dealer cash programs to keep the product selling. American Honda compensates Klein Honda for making qualified dealer cash sales by issuing a credit to Klein Honda's monthly balance forward statement.

On October 11, 2007, the Washington State Department of Revenue (Department) Audit Division assessed Klein Honda $16,963 in business and occupation (B&O) tax for the audit period January 1, 2003 through December 31, 2006. During that time, Klein Honda received $1,037,450 in dealer cash from American Honda.

Klein Honda paid the assessment, but petitioned the Department's appeals division for a refund. Klein Honda argued that dealer cash represents a discount or reduction in its cost of purchasing the vehicles from American Honda. Thus, Klein Honda asserted, dealer cash is not income derived from business activities. The appeals division disagreed and upheld the assessment in a final determination issued on August 19, 2010. It explained that dealer cash "is a payment to the Dealer for certain action: the sale of a particular car model within a specific timeframe. This award was not part of the negotiated price; in other words, it was not contemplated at the time the Dealer purchased the vehicle from the manufacturer."

Klein Honda sought review from the Board of Tax Appeals (Board). The Board entered an initial decision affirming the Department's tax assessment. It concluded that a "taxpayer engaged in any business activity not specifically set forth in chapter 82.04 RCW shall be taxed at a rate of 1.5 percent. There is no separate B&O tax." The Board further concluded that under the statutory definition of gross income of business, a "taxpayer can have taxable income from business activity without providing any specific services." Therefore, "Klein Honda is liable under the statutes of the state to pay B&O tax on amounts received during the audit period from the manufacturer denominated as dealer cash." Klein Honda did not petition the Board for further review, and so the initial decision became final after 20 days. WAC 456-09-930.

Klein Honda then petitioned Thurston County Superior Court for review. The superior court affirmed the Board's decision on July 19, 2013. Klein Honda appealed.

DISCUSSION

The issue on appeal is whether dealer cash is subject to the B&O tax. Klein Honda characterizes the issue as "whether dealer cash is a rebate that reduces the dealer's vehicle cost, in which case it is not taxable, or whether dealer cash is a payment for service." We address this argument in two parts. First, we consider Klein Honda's argument that dealer cash is not taxable, because it is simply a payment and not a business activity or extra service apart from selling vehicles. Second, we address Klein Honda's alternative argument that dealer cash is not taxable, because it is an adjustment or bona fide discount to the wholesale purchase price of the vehicles.

I. Dealer Cash Is a Business Activity Subject to the B&O Tax

We sit in the same position as the superior court and review the record before the administrative agency, not the record before the superior court. Valley Fruit v. Dep't of Revenue, 92 Wn. App. 413, 417, 963 P.2d 886 (1998). The Administrative Procedure Act (APA), chapter 34.05 RCW, governs our review of the Board's decision. RCW 82.03.180. The appealing party bears the burden of demonstrating the invalidity of the Board's actions. Olympic Tug & Barge, Inc. v. Dep't of Revenue, 163 Wn. App. 298, 306, 259 P.3d 338 (2011), review denied, 173 Wn.2d 1021, 272 P.3d 850 (2012). A party appealing a Board order may do so on nine different grounds under RCW 34.05.570(3), including (d) erroneous interpretation or application of the law. Id.

Statutory interpretation is a question of law. Id. We review questions of law de novo, but give substantial weight to the agency's interpretation of the statutes it administers. Everett Concrete Prods., Inc. v. Dep't of Labor & Indus., 109 Wn.2d 819, 823, 748 P.2d 1112 (1988). Our primary duty in construing a statute is to ascertain and carry out the legislature's intent. Lake v. Woodcreek Homeowners Ass'n, 169 Wn.2d 516, 526, 243 P.3d 1283 (2010). In doing so, the language at issue must be evaluated in the context of the entire statute. Simpson Inv. Co. v. Dep't of Revenue, 141 Wn.2d 139, 149, 3 P.3d 741 (2000). We avoid interpretations that are strained, unlikely, or unrealistic. Id.

The B&O tax code, chapter 82.04 RCW, provides an "extremely broad and all-inclusive tax scheme" in Washington. Budget Rent-A-Car of Washington-Oregon, Inc. v. Dep't of Revenue, 81 Wn.2d 171, 175, 500 P.2d 764 (1972). It taxes "the gross revenues received in the course of doing business." Id. at 173. Taxation is the rule and exemption is the exception. TracFone Wireless, Inc. v. Dep't of Revenue, 170 Wn.2d 273, 296-97, 242 P.3d 810 (2010). "[W]here there is an exception, the intention to make one should be expressed in unambiguous terms." Id. at 297 (quoting Columbia Irrig. Dist. v. Benton County, 149 Wn. 234, 240, 270 P. 813 (1928)). Therefore, we construe ambiguous provisions strictly, though fairly, against the taxpayer. Grp. Health Coop. of Puget Sound, Inc. v. Wash. State Tax Comm'n, 72 Wn.2d 422, 429, 433 P.2d 201 (1967).

In adopting our state's B&O tax system, "'the legislature intended to impose the business and occupation tax upon virtually all business activities carried on within the state.'" Simpson, 141 Wn.2d at 149 (quoting Time Oil Co. v. State, 79 Wn.2d 143, 146,

483 P.2d 628 (1971)). This is evidenced by the "sweeping language," id., of RCW 82.04.220, which states:

> There is levied and collected from every person that has a substantial nexus with this state a tax for the act or privilege of engaging in business activities. The tax is measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be.

"Engaging in business" is broadly defined and means "commencing, conducting, or continuing in business." RCW 82.04.150. RCW 82.04.140 provides even greater breadth by defining "business" as "all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or to another person or class, directly or indirectly." See Simpson, 141 Wn.2d at 149.

The specific B&O tax rate is then "measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be." RCW 82.04.220(1). "Gross income of the business" means:

> the value proceeding or accruing by reason of the transaction of the business engaged in and includes gross proceeds of sales, compensation for the rendition of services, gains realized from trading in stocks, bonds, or other evidences of indebtedness, interest, discount, rents, royalties, fees, commissions, dividends, and other emoluments however designated, all without any deduction on account of the cost of tangible property sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses.

RCW 82.04.080(1). "Value proceeding or accruing" is defined as "the consideration, whether money, credits, rights, or other property expressed in terms of money, actually received or accrued." RCW 82.04.090.

The Department imposed the tax on dealer cash at a rate under RCW 82.04.290(2), which states, in pertinent part:

> (a) Upon every person engaging within this state in any business activity other than or in addition to an activity taxed explicitly under another section in this chapter or subsection (1) or (3) of this section; as to such persons the amount of tax on account of such activities is equal to the gross income of the business multiplied by the rate of 1.5 percent.
>
> (b) This subsection (2) includes, among others, and without limiting the scope hereof . . . , persons engaged in the business of rendering any type of service which does not constitute a "sale at retail" or a "sale at wholesale."

(Emphasis added.) Klein Honda does not claim that dealer cash is not taxable under this section because it is taxable under another section of the chapter. This case is not about an incorrect rate. Rather, Klein Honda argues that there is no business activity defined in the chapter to trigger any applicable rate. Specifically, Klein Honda asserts that some additional service—beyond the mere retail sale of vehicles—must be provided to constitute a taxable business activity.

We disagree with Klein Honda that dealer cash needs to represent compensation for an additional service to be taxable. Rather, the B&O tax applies to gross income of business. See Budget Rent-A-Car, 81 Wn.2d at 173. The definition of "gross income of the business" demonstrates that this includes many activities that are not services, such as interest, royalties, dividends, and other emoluments. Likewise, RCW 82.04.290(2) nowhere requires an additional service for the 1.5 percent tax rate to apply. Rather, receiving income from providing services is sufficient, but not necessary to trigger RCW 82.04.290(2).

The "all-encompassing" definitions quoted above "leave practically no business and commerce free of the business and occupation tax." Id. at 175; Simpson, 141 Wn.2d at 149. Indeed, "[b]roader language could hardly be devised to convey the idea implicit in the foregoing definitions that the tax applies to everything that is earned, received, paid over to[,] or acquired by the seller." Engine Rebuilders, Inc. v. State, 66 Wn.2d 147, 150, 401 P.2d 628 (1965).

Therefore, contrary to Klein Honda's argument, the B&O tax is not a tax on only specific enumerated business activities, but rather on "the gross revenues received in the course of doing business." Budget Rent-A-Car, 81 Wn.2d at 173. Dealer cash received by Klein Honda in the course of conducting its auto dealership business was connected to a business activity. The business activity was accepting the offer of American Honda to apply for dealer cash, selling specific models during specific times, documenting those sales as required by the manufacturer, applying to the manufacturer for the dealer cash, and accepting the payment. It was a discrete business activity beyond the mere retail sale of those vehicles.[1] As our Supreme Court noted in response to another ingenious argument, to hold otherwise "would import an exemption into the tax statutes where none now exists." Time Oil, 79 Wn.2d at 147. The dealer cash received in the course of that business activity is taxable under RCW 82.04.290(2).[2]

---

[1] "Sale at retail" means sale to consumers. RCW 82.04.050(1)(a). Klein Honda receives dealer cash from the manufacturer.

[2] Klein Honda relies on Peshastin Lumber & Box, Inc. v. State, 61 Wn.2d 413, 378 P.2d 420 (1963), to argue to the contrary. However, the holding of Peshastin is consistent with our conclusion. There, the taxpayer logged timber pursuant to contracts with the United States Forest Service. Id. at 414. These contracts required the taxpayer to build logging roads to remove the timber, which the Forest Service would

II. Dealer Cash Is Not a Bona Fide Discount in the Wholesale Price

Klein Honda also argues that dealer cash is an adjustment or bona fide discount to the wholesale purchase price of the vehicles and is therefore not taxable. A bona fide discount is not subject to the B&O tax under WAC 458-20-108. The rule states, in relevant part:

> (1) When a contract of sale is made subject to cancellation at the option of one of the parties or to revision in the event the goods sold are defective or if the sale is made subject to cash or trade discount, the gross proceeds actually derived from the contract and the selling price are determined by the transaction as finally completed.
>
> . . . .
>
> (5) **Discounts.** The selling price of a service or of an article of tangible personal property does not include the amount of bona fide discounts actually taken by the buyer and the amount of such discount may be deducted from gross proceeds of sales providing such amount has been included in the gross amount reported.

(Emphasis added.) The Department promulgated this rule pursuant to its rulemaking authority in RCW 82.32.300. Discount Tire Co. of Wash. v. Dep't of Revenue, 121 Wn. App. 513, 523, 85 P.3d 400 (2004).

Klein Honda's argument fails, because its wholesale purchase of vehicles from American Honda is not made "subject to" the dealer cash payment, as required by the emphasized language in WAC 458-20-108(1). Unlike holdbacks, for instance, dealer

---

thereafter maintain. Id. The cost of building the roads was included in the appraiser's estimate of the timber's market value. Id. However, the taxpayer received no payment for building the roads. Id. at 415. They were a necessary cost of doing business. Id. The court held that building roads was not a taxable activity under the B&O tax code, because "[t]here was, in short, no showing that the [taxpayer] received any remuneration, expressible in terms of money." Id. at 417. The opposite is true here: Klein Honda received remuneration—dealer cash—for complying with the terms of the dealer cash offer after selling specified vehicles during specified times.

cash payments are not automatic upon Klein Honda's vehicle purchases from American Honda. Rather, dealer cash applies to eligible vehicles already in Klein Honda's inventory and is contingent upon Klein Honda selling those vehicles during a specified time period.

Klein Honda nevertheless insists that the Department's guidance to taxpayers concerning bona fide discounts to grocers is inconsistent with this interpretation of WAC 458-20-108. The Department's Excise Tax Advisory No. 3173.2013 applies to grocery stores and distinguishes bona fide discounts as follows:

> A bona fide discount is, for example, when the distributor grants the grocer either a discount or some form of payment for doing nothing more than purchasing products from the distributor.
>
> . . . .
>
> Generally, a bona fide discount negotiated by the grocer upon purchase of the goods does nothing more than encourage the grocer to make sales they were already going to make.

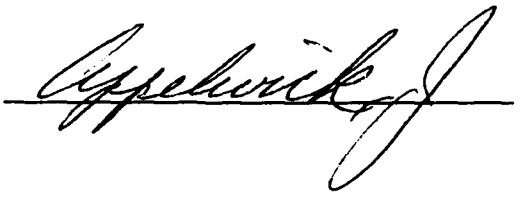
Wash. Dep't of Revenue, Excise Tax Advisory No. 3173.2013, at 1 (Jan. 7, 2013), available at http://dor.wa.gov/Docs/Rules/eta3000/3173.pdf (Distributor Discounts/ Allowances to Grocery Stores).

Dealer cash is distinguishable from the above language for two reasons. First, it is not a discount for Klein Honda purchasing vehicles from American Honda. And, second, dealer cash is not negotiated by Klein Honda upon the purchase of vehicles from American Honda. The Department's position is not inconsistent with its excise tax advisory for discounts given by distributors to grocers.[3] Therefore, we hold that dealer

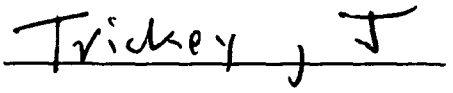
[3] Klein Honda's reliance on Discount Tire Co., is also inapposite here, because that case involved "use tax" and sales tax on returned, defective, or damaged goods.

cash is not an adjustment or bona fide discount to the wholesale price of the vehicles, because Klein Honda did not purchase the vehicles subject to the dealer cash payment.

We affirm.



WE CONCUR:



121 Wn. App. at 521-23. The court expressly stated that the B&O tax was not at issue. Id. at 521.

Klein v. Department of Revenue, No. 71663-8-I

BECKER, J. (dissenting in part) — I respectfully dissent from the majority's conclusion that the business and occupation (B&O) tax is properly imposed on dealer cash.

The business and occupation tax is levied "for the act or privilege of engaging in business activities." RCW 82.04.220(1). The Supreme Court in another context has said that "the tax is on the gross revenues received in the course of doing business." Budget Rent-A-Car of Wash.-Or. v. Dep't of Revenue, 81 Wn.2d 171, 173, 500 P.2d 764 (1972). This statement, cited by the majority to show that the business and occupation tax scheme is very broad, does not literally mean that all gross income received by a business is taxable. Gross income is taxable only after identification of a business activity that is subject to taxation. The tax is then "measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be." RCW 82.04.220(1).

The statutes identify many categories of business activity and specify the method of measurement and the rate applicable to each. For example, "Upon every person engaging within this state in the business of making sales at wholesale," the tax is imposed on the gross proceeds of sales at the rate of .484 percent. RCW 82.04.270. "Upon every person engaging within this state in the business of making sales at retail," the tax is imposed on the gross proceeds of sales at the rate of 0.471 percent. RCW 82.04.250(1). Klein Honda primarily engages in the business of making sales at retail. Klein Honda does not dispute

its obligation to pay the B&O tax of 0.471 percent on the gross proceeds of its retail sales.

The statute involved in this appeal imposes the B&O tax upon persons engaged in the business of rendering services or engaging in some "other" business activity not otherwise taxed:

> (2)(a) Upon every person engaging within this state in any business activity other than or in addition to an activity taxed explicitly under another section in this chapter or subsection (1) or (3) of this section; as to such persons the amount of tax on account of such activities is equal to the gross income of the business multiplied by the rate of 1.5 percent.
>
> (b) This subsection (2) includes, among others, and without limiting the scope hereof (whether or not title to materials used in the performance of such business passes to another by accession, confusion or other than by outright sale), persons engaged in the business of rendering any type of service which does not constitute a "sale at retail" or a "sale at wholesale." The value of advertising, demonstration, and promotional supplies and materials furnished to an agent by his or her principal or supplier to be used for informational, educational, and promotional purposes is not considered a part of the agent's remuneration or commission and is not subject to taxation under this section.

RCW 82.04.290(2).

In addition to making sales of cars at retail, Klein Honda performs pre-delivery inspections, warranty work, and advertising for American Honda Motor Company Inc. By doing so, Klein Honda engages in the business of rendering services that do not constitute a sale at retail or wholesale. Klein Honda does not dispute its obligation to pay the B&O tax of 1.5 percent on the gross income it receives for these services, as required by RCW 82.04.290(2)(b).

The Department of Revenue argues that by meeting the terms of American Honda's dealer cash marketing bulletins, Klein Honda engages in the

business of rendering a further service to American Honda that is taxable under RCW 82.04.290(2)(b). According to the Department, the service benefits American Honda "by moving vehicles out of Klein Honda's inventory and putting Klein Honda in a position to make more wholesale purchases from American Honda." Brief of Respondent at 23. The problem with this argument is that to be taxable under RCW 82.04.290(2)(b), the service rendered may not constitute a sale at retail. Moving vehicles out of inventory, whether in response to a marketing bulletin or not, is accomplished by selling cars at retail. Every sale of a vehicle that Klein Honda makes in response to a dealer cash incentive program constitutes a sale at retail and consequently is not taxable under RCW 82.04.290(2)(b).

This leaves RCW 82.04.290(2)(a) as a possible source of taxation. "Upon every person engaging within this state in any business activity other than or in addition to an activity taxed explicitly under another section in this chapter . . . the amount of tax on account of such activities is equal to the gross income of the business multiplied by the rate of 1.5 percent." The business activity of selling cars at retail is explicitly taxed under RCW 82.04.250(1). Therefore, RCW 82.04.290(2)(a) applies only if dealer cash is produced by a business activity "other than or in addition to" selling cars at retail. It is not enough to point out that dealer cash is gross income for Klein Honda. The first question is, what is the "other" business activity?

The majority identifies the "other" business activity as "accepting the offer of American Honda to apply for dealer cash, selling specific models during

specific times, documenting those sales as required by the manufacturer, applying to the manufacturer for the dealer cash, and accepting the payment. It was a discrete business activity beyond the mere retail sale of those vehicles." Majority at 9.

The majority's distinction is unsatisfactory. It confuses the *reporting* of business activity with business activity. The only business activity that Klein Honda engages in that produces dealer cash is the business activity of making sales at retail. Making a particular number of retail sales of a particular model within a specified time period is subsumed within the business of making sales at retail. I would conclude that documenting a sale in order to qualify for dealer cash is not a separately taxable "other" business activity.

Whether dealer cash represents a bona fide discount, and is thereby excludable from "gross proceeds of sales" under WAC 458-20-108(5), is irrelevant. Analyzing that issue presupposes the existence of an identifiable and taxable business activity. Klein Honda simply participated in an incentive program designed by the wholesaler to move inventory. By moving inventory, Klein Honda did not engage in a business activity other than selling cars at retail. I would hold that Klein Honda is entitled to a refund of tax paid on dealer cash.

Becker, J.