No. 98470-1

COURT OF APPEALS, DIVISION I
FOR THE STATE OF WASHINGTON
No. 78946-5-I

IN THE SUPREME COURT OF THE STATE OF WASHINGTON

CITY OF SEATTLE, a municipal corporation,

Petitioner,

v.

KMS FINANCIAL SERVICES, INC., a Washington corporation,

Respondent.

PETITION FOR REVIEW

PETER S. HOLMES
Seattle City Attorney
JENNIFER GILMAN, WSBA #21234
SEATTLE CITY ATTORNEY'S OFFICE
701 Fifth Avenue, Suite 2050
Seattle, WA 98104
(206) 615-0047

MATTHEW J. SEGAL, WSBA #29797
SARAH S. WASHBURN, WSBA #44418
PACIFICA LAW GROUP LLP
1191 Second Avenue, Suite 2000
Seattle, WA 98101-3404
(206) 245-1700

Attorneys for Respondent City of Seattle

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I. INTRODUCTION AND IDENTITY OF PETITIONER

The Court of Appeals erroneously declared that Petitioner the City of Seattle's (the "City's) Business and Occupation ("B&O") tax is unconstitutional "as applied" to Respondent KMS Financial Services, Inc. ("KMS"), a securities broker dealer, and in doing so also substantially undermined a compulsory and widely-used statewide taxing methodology. In reaching its conclusion, the Court of Appeals failed properly to apply the test for apportionment under the federal Commerce Clause, or the separate state law test governing intrastate activity. By holding that the City could not exclude independent contractors from a portion of its apportionment formula, the Court of Appeals also created significant confusion as to how, or if, cities may constitutionally apply the state enabling legislation and their corresponding model ordinances. Review is warranted in this case on three alternative grounds—it presents significant constitutional questions, it involves an issue of substantial public importance, and it conflicts with this Court's authority. The City respectfully requests that this Court grant review, reverse the Court of Appeals, and reinstate the trial court's decision finding no constitutional violation.

II. COURT OF APPEALS DECISION

The City seeks review of a published opinion (the "Decision") of Division I of the Court of Appeals, filed February 24, 2020. The Court of Appeals denied the City's motion for reconsideration on April 21, 2020.[1]

III. ISSUES TO BE REVIEWED

A. Did the Court of Appeals err in declaring the City's B&O tax unfairly apportioned and therefore unconstitutional?

B. Did the Court of Appeals err in granting KMS the tax advantage of treating independent contractors as employees?

C. Did the Court of Appeals err in applying an alternative method of apportionment after the fact, even though KMS did not timely petition for alternative apportionment?

IV. STATEMENT OF THE CASE

A. KMS Uses Independent Contractors to Conduct Its Service Business.

KMS is a Washington corporation with its headquarters in Seattle. It is engaged in the securities, insurance, and investment advisory business as a broker-dealer under the Securities and Exchange Act of 1934. CP 9-10. During the time period relevant to this case, KMS employed approximately 50 workers at its Seattle home office. In addition to those

[1] Copies of the Decision and order on reconsideration are attached as Appendices A and B, respectively.

Seattle employees, KMS relies on approximately 350 "registered representatives" to sell stocks and other financial products inside and outside the City. CP 9-10. KMS pays registered representatives commissions from 50% to 95% of gross sales, based upon calendar year earnings. CP 11, 29-30. The Seattle staff supports the registered representatives' sales activities, processes clients' payments for stocks and other financial instruments, and generates trade reports. CP 11-12.

It is undisputed that KMS' registered representatives are independent contractors. CP 10-11, 26. The record does not reflect how many of KMS' registered representatives work inside versus outside the City, nor does the record allow a determination of how many registered representatives work inside versus outside of Washington State.

B. State Law Requires the City to Consider Employee, But Not Independent Contractor, Compensation in Apportioning Income for B&O Tax Purposes.

The City of Seattle imposes a B&O tax on all persons engaging in business activity within city limits. Seattle Municipal Code ("SMC") 5.45.050. The tax is calculated "by application of rates against gross proceeds of sale, gross income of business, or value of products," and the tax rate varies depending upon the type business activity. SMC 5.45.050(A)-(F). The tax is applied to gross receipts, without any deductions for expenses or costs of doing business. SMC 5.30.035(D)-

(E). "Engaging in business" includes "commencing, conducting, or continuing in" business activity in the City. SMC 5.30.030(B).

When a service business like KMS claims to earn income both inside and outside the City, the portion of that business's income attributable to Seattle must be determined. The Model B&O Tax Ordinance ("Model Ordinance"), codified in chapter 35.102 RCW, dictates the method of apportionment the City must use.[2] Since January 1, 2008, the Model Ordinance has required cities that levy the B&O tax to apportion income, so as to address the issue of multiple taxation. RCW 35.102.130(3)[3] establishes a mandatory two-factor apportionment formula that all cities in Washington must use to calculate the portion of a company's gross income attributable to its activities inside city limits. This formula requires the taxpayer to calculate a "service income" factor and "payroll" factor. *Id.*[4]

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[2] All cities with a B&O tax were required to adopt the Model Ordinance no later than December 31, 2004. The Model Ordinance mandated certain definitions, penalty and interest provisions, and payment periods. *See* RCW 35.102.040.

[3] This statute was amended effective January 1, 2020. *See* Laws of 2019, ch. 101. All citations herein are to the prior version effective until January 1, 2020, as that version was in effect when the events relevant to this dispute took place.

[4] Each of these factors is expressed as a fraction: for payroll, total compensation paid to employees in a city is the numerator and total compensation paid to employees everywhere in the country is the denominator; likewise, service income in a city is the numerator and service income everywhere is the denominator for the income factor. Those two resulting fractions or percentages (payroll and service income) are then added together, divided by two, and multiplied by the company's taxable income. The result is the income on which a company must pay B&O tax in a particular city. CP 12-14; RCW 35.102.130; SMC 5.45.081; *see also* Appendix C for a visual representation of the apportionment formula.

The dispute in this case is solely about KMS's payroll factor. The Model Ordinance provides as to that factor:

> (a) The payroll factor is a fraction, the numerator of which is the total amount paid in the city during the tax period by the taxpayer for compensation and the denominator of which is the total compensation paid everywhere during the tax period. Compensation is paid in the city if:
> (i) The individual is primarily assigned within the city;
> (ii) The individual is not primarily assigned to any place of business for the tax period and the employee performs fifty percent or more of his or her service for the tax period in the city; or
> (iii) The individual is not primarily assigned to any place of business for the tax period, the individual does not perform fifty percent or more of his or her service in any city, and the employee resides in the city.

RCW 35.102.130(3)(a). For purposes of this factor, "compensation" is defined as "wages, salaries, commissions, and any other form of remuneration paid to individuals for personal services that are or would be included in the individual's gross income under the federal internal revenue code." RCW 35.102.130(4)(b). "Individual" is defined as "any individual who, under the usual common law rules applicable in determining the employer-employee relationship, **has the status of an employee of that taxpayer**." RCW 35.102.130(4)(c) (emphasis added).

Effective January 1, 2008, the City adopted by ordinance the two-factor test set forth in the Model Ordinance, including the payroll factor and relevant definitions quoted above. SMC 5.45.081(F), (H). Since that

time, pursuant to the Model Ordinance, the City has consistently interpreted "compensation" for purposes of the payroll factor to include only compensation paid by a taxpayer to its **employees**. The City excludes from the payroll factor commissions paid to **independent contractors**.

C. The City Discovers KMS Miscalculated Its Payroll Factor.

Without informing the City, KMS took the opposite approach. During the January 2012 through March 2016 audit period, KMS erroneously included its independent contractors' commissions in its payroll factor, such that the resulting payroll factor was a much smaller number than it would be if independent contractors were excluded. As a result, KMS underpaid B&O tax during the audit period by $460,972. CP 14.[5] The City audited KMS in 2016 and discovered KMS' incorrect payroll factor calculation. The City issued an assessment to recover the underpaid amount as well as interest and penalties. CP 13-14, 34.

KMS paid the assessment and then filed a complaint for refund in King County Superior Court, claiming the City improperly excluded independent contractor compensation from the payroll factor calculation. CP 1-3. Both parties moved for summary judgment on that single issue. CP 43-65. After briefing and oral argument, the trial court ruled in favor of the City. CP 116-17.

[5] KMS also underpaid its taxes from 2008 through 2011, but the City is not attempting to recover those taxes due to "lookback" limitations in the SMC. *See* SMC 5.55.095.

D. The Court of Appeals Rules the City's B&O Tax Unconstitutional as Applied to KMS.

The Court of Appeals reversed. *City of Seattle v. KMS Fin. Servs., Inc.*, 12 Wn. App. 2d 491, 459 P.3d 359 (2020) ("*KMS* II"). Despite stating the general rule that courts give considerable deference to the construction of a challenged ordinance by the officials charged with its enforcement, *see id*. at 501, the Court of Appeals summarily rejected the City's consistently-applied interpretation of the Model Ordinance and its own code adopting the same. In doing so, the court relied heavily on its prior decision in *KMS Fin. Servs., Inc. v. City of Seattle*, 135 Wn. App. 489, 146 P.3d 1195 (2006) (*KMS* I). That case, which pre-dated the two-factor apportionment test at issue here, addressed whether the City could attribute all of KMS' income to Seattle simply because its home office was located there. In *KMS* I, the court concluded that federal and state law prohibited such attribution and held that the City must fairly apportion KMS' gross receipts based on where the income-generating activity occurred. 135 Wn. App. at 509, 512.

In the present matter, the Court of Appeals acknowledged the law on apportionment had changed, but invalidated the new formula. Apparently relying on the Commerce Clause of the United States Constitution—which applies to attempts to tax income generated out of

state[6]—the court ruled the B&O tax "unconstitutional as applied because it was not fairly apportioned." *KMS* II, 12 Wn. App. 2d at 504; *see also id*. at 494, 502 (discussing Commerce Clause's fair apportionment requirement). Ignoring the Model Ordinance's definition of "individual," the court rejected the City's claim that compensation paid to KMS' independent contractors must be excluded from the payroll factor and held that whether a taxpayer does business through independent contractors or employees is constitutionally insignificant. *Id*. at 505. The court focused on the income-generating function of KMS' independent contractors:

> In essence, the City attributes most of KMS's income to the work of approximately 50 employees based in the city when it is undisputed that the bulk of KMS's income comes from the work of the 300-plus registered representatives based outside the city.
>
> Because the City failed to consider where and how KMS generated its income, the tax is not externally consistent as applied to KMS. Therefore, the B&O tax is not fairly apportioned to KMS. Because the tax is not fairly apportioned, it is unconstitutional as applied to KMS.

Id. at 506.

But the court did not stop there. In the name of "constitutional avoidance," it retroactively applied a statutory option KMS never timely

[6] The exact basis of the court's holding is not entirely clear, but its use of the term "fairly apportioned" apparently refers to the federal Commerce Clause standard. The court also cited Washington law's "similar limitation" on the City's power to tax income generated outside of Seattle but within the State of Washington, *see id*. at 494-95, 503, but it did not evaluate the City's B&O tax under Washington's test.

invoked. The court granted KMS alternative apportionment of its income under RCW 35.102.130(3)(c), which provides that if the two-factor formula does not "fairly represent the extent of the taxpayer's business activity in the city or cities in which the taxpayer does business, **the taxpayer may petition for** or the tax administrators may jointly require" an alternative apportionment method. (Emphasis added); *see also KMS II*, 12 Wn. App. 2d at 506-07. Despite the fact that KMS did not petition for alternative allocation prior to the City's audit, the court ruled the City should have *sua sponte* employed a different method. *Id*. at 507. The court then concluded that the City "could logically consider [KMS'] registered representatives to be employees for an alternative apportionment calculation of the B&O tax." *Id*. at 509.

V. ARGUMENT

The City seeks review of the Decision for three alternative reasons. First, under RAP 13.4(b)(3), this case involves a significant question of law under the Constitution of the United States. The Court of Appeals incorrectly held the City's apportionment method unconstitutional, seemingly under the Commerce Clause of the United States Constitution. Second, under RAP 13.4(b)(4), this case involves issues of substantial public interest that this Court should determine. The Decision introduces substantial confusion for every city charging B&O tax in Washington

State regarding application of the apportionment methodology required under the Model Ordinance. It also undermines voluntary compliance by authorizing taxpayers to request alternative apportionment after an audit reveals improper reporting. Third, under RAP 13.4(b)(1), the Decision conflicts with this Court's authority, most prominently *Dravo Corp. v. City of Tacoma*, 80 Wn.2d 590, 496 P.2d 504 (1972).

A. This Case Involves a Significant Question of Law Under the United States Constitution.

An ordinance is presumed constitutional, and the challenger bears the burden to prove it is unconstitutional "beyond a reasonable doubt." *City of Seattle v. Huff*, 111 Wn.2d 923, 928, 767 P.2d 572 (1989). Further, under the SMC, "the City's assessment is prima facie correct." *Wedbush Sec., Inc. v. City of Seattle*, 189 Wn. App. 360, 363, 358 P.3d 422 (2015).

"A B&O tax is assessed for the privilege of conducting business in the taxing jurisdiction." *Id*. The Court of Appeals held the City's B&O tax "unconstitutional as applied because it was not fairly apportioned," apparently invoking the Commerce Clause. *KMS* II, 12 Wn. App. 2d at 504.[7] The Commerce Clause requires that a state tax imposed on activity in interstate commerce be (1) "applied to an activity with a substantial

[7] The Commerce Clause of the United States Constitution provides that "Congress shall have the power . . . [t]o regulate commerce with foreign nations, and among the several states, and with the Indian tribes[.]" U.S. Const. art. I, § 8, cl. 3.

nexus with the taxing State," (2) "fairly apportioned," (3) nondiscriminatory with respect to interstate commerce, and (4) "fairly related to the services provided by the State." *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274, 279, 97 S. Ct. 1076, 51 L. Ed. 2d 326 (1977).

The Decision appears to focus solely on the second prong of the *Complete Auto* test—the requirement that a tax be "fairly apportioned" under the Commerce Clause. "A tax is fairly apportioned if it is internally and externally consistent." *Goldberg v. Sweet*, 488 U.S. 252, 261, 109 S. Ct. 582, 102 L. Ed. 2d 607 (1989), *abrogated on other grounds*, *Comptroller of Treasury of Md. v. Wynne*, 575 U.S. 542, 135 S. Ct. 1787, 191 L. Ed. 2d 813 (2015). Here, KMS has not argued internal consistency is at issue, and the Court of Appeals accordingly limited its analysis to external consistency. *See KMS* II, 12 Wn. App. 2d at 506. External consistency requires that "the factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated." *Container Corp. of Am. v. Cal. Franchise Tax Bd.*, 463 U.S. 159, 169, 103 S. Ct. 2933, 77 L. Ed. 2d 545 (1983).

External consistency looks to the economic justification for the claim upon the value taxed, to discover whether a tax reaches beyond that portion of value that is fairly attributable to economic activity within its jurisdiction. *Gen. Motors Corp. v. City of Seattle*, 107 Wn. App. 42, 58, 25

P.3d 1022 (2001) (quoting *Okla. Tax Comm'n v. Jefferson Lines*, 514 U.S. 175, 185, 115 S. Ct. 1331, 131 L. Ed. 2d 261 (1995)). The external consistency test focuses on the "real possibility of multiple taxation," *Gen. Motors Corp.*, 107 Wn. App. at 61, but KMS neither alleged nor proved it is subject to multiple taxation. Still, the Court of Appeals held the City's B&O tax is "not externally consistent as applied to KMS" and "not fairly apportioned to KMS." *KMS* II, 12 Wn. App. 2d at 506.

The Decision cited *KMS* I for the conclusion that the City "failed to consider where and how KMS generated its income" for purposes of external consistency. *Id.* But the law and the City's apportionment methodology has changed significantly since *KMS* I, and the Court of Appeals' reliance on its earlier decision to invalidate the City's apportionment was constitutionally erroneous and warrants review. In *KMS* I, the Court of Appeals held that the City's imposition of a B&O tax on KMS's entire gross income—without apportioning it in any way—exceeded constitutional limitations. 135 Wn. App. at 505-09. Under the tax code in effect at the time of *KMS* I, the City assessed B&O tax on all commissions generated by registered representatives. *Id.* at 505-06. But the Model Ordinance's two-factor apportionment method has superseded that code. *See Wedbush*, 189 Wn. App. at 364 ("On January 1, 2008, RCW 35.102.130 established new allocations and apportionment requirements for cities with a gross receipt

business tax."). Under the applicable formula, the **income factor** looks at both income earned inside the City and income earned elsewhere. RCW 35.102.130(3)(b)(i-iii). Here, where income is earned outside Seattle, the City's formula—per state law—accounts for that. The rationale the Court of Appeals used in *KMS* I no longer applies.

The Decision improperly conflates the current apportionment formula's payroll and income factors to reach the conclusion that the City unconstitutionally apportioned KMS' income. The **payroll factor** in the City's apportionment formula looks only at the total compensation paid in the city and the total compensation paid everywhere. It is a good indicator of where states incur costs related to the protections, benefits, and services provided to taxpayers and their employees. Maureen Pechacek & Karen Nakamura, *The Payroll Factor: Whose Factor Is It Anyway?*, SYMPOSIUM EDITION, STATE AND LOCAL TAX LAWYER 155 (2009). KMS chooses for business reasons to treat its registered representatives as independent contractors rather than employees, thereby saving the employer's share of Medicare and Social Security, unemployment taxes, and worker's compensation, as well as the costs of licensing, office space, equipment, and benefits for employees. CP 26. It stipulated for purposes of this case that the registered representatives are independent contractors. CP 11. The registered representatives are in business for themselves, and their

commissions are properly excluded from payroll.

As noted above, however, the **income factor** takes into account income earned in the City and income earned everywhere. RCW 35.102.130(3)(b). Unlike in *KMS* I, the apportionment in this case fully reflects, **in the income factor**, where KMS earned its income. The City does not source to Seattle any of the income earned from KMS' independent contractors unless, as required under the formula, the contractor's customer location is in the City. As a result, the numerator of the income factor (income in Seattle) is small (11.17% - 15.29% over four years) and the denominator (income everywhere) is large. CP 32.[8]

It is "not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing the business." *Complete Auto*, 430 U.S. at 279 (internal quotation omitted). The income factor reflects the economic reality of where revenue is generated, whereas the payroll factor reflects the economic reality of where expenses are incurred to generate the income. The Court of Appeals nevertheless incorrectly applied the requirements of the income factor to the payroll factor. The payroll factor's exclusion of independent contractors is simply not at issue in determining external consistency.

[8] KMS has not argued the income factor was wrongly calculated.

Further muddying the waters, the Court of Appeals cited *Scripto, Inc. v. Carson*, 362 U.S. 207, 80 S. Ct. 619, 4 L. Ed. 2d 660 (1960) for the proposition that there is no "constitutional significance" to the distinction between employees and independent contractors. *KMS* II, 12 Wn. App. 2d at 505 (quoting *Scripto* at 211-12). But *Scripto* addressed whether a business had a sufficient connection ("nexus") with the taxing state, holding that a business can create nexus with multiple jurisdictions by using independent contractors around the country. 362 U.S. at 210-12. As noted above, the sole issue in this case is "fair apportionment" under *Complete Auto*'s Commerce Clause test. The "nexus" prong is not at issue. *Scripto* does not hold that independent contractor status has no relevance to the payroll component of fair apportionment.[9]

Finally, although the Court of Appeals appears to have decided this case based on the federal Commerce Clause, it also cited Washington's "similar limitation" on taxing authority. *See KMS* II, 12 Wn. App. 2d at 494-95, 503. But these tests are not identical. The Commerce Clause test

[9] Thus, in *Pandora Indus., Inc. v. State Dep't of Revenue Admin.*, 118 N.H. 891, 395 A.2d 1241 (1978), the New Hampshire Supreme Court held that a multi-state business organization with its principal place of business in New Hampshire could not include commissions paid by it to "independent nonemployee salesmen" in calculating its payroll factor. In holding the commissions paid to independent contractors had no bearing on the amount of activity engaged in by the taxpayer within New Hampshire, and should not be included in the payroll factor, the court reasoned: "[S]ervices performed by independent contractors are their own activities and not those of their supplier." *Id*. at 895; *see also Appeal of Lipps, Inc*., 87-SBE-017 (Cal. St. Bd. Of Equal., March 3, 1987) (holding only amounts paid directly to "employees" are included in the payroll factor; payments made to an independent contractor are excluded).

(*Complete Auto*) applies only where a state or local jurisdiction is taxing out-of-state activity. *See Ford Motor Co. v. City of Seattle*, 160 Wn.2d 32, 49, 156 P.3d 185 (2007) ("The fair apportionment prong ensures that each State taxes only its fair share of an **interstate transaction**." (emphasis added)). By contrast, the state test applies where local jurisdictions attempt to tax activity occurring outside their borders but within the state. *See KMS* I, 135 Wn. App. at 510-12. The Court of Appeals did not distinguish between the two tests, nor did it (or the record) distinguish between KMS' in-state versus out-of-state activities. The Court of Appeals' application of the Commerce Clause was, therefore, both incorrect and overbroad. Review is warranted under RAP 13.4(b)(3).

B. This Case Presents Issues of Substantial Public Interest.

Review should also be granted because the Decision raises issues of substantial public interest that this Court should determine. RAP 13.4(b)(4). Although the Court of Appeals claimed to hold Seattle's ordinance unconstitutional "as applied," in reality the Decision calls into question the application of ordinances across the State as well as the enabling statute behind them. Moreover, in retroactively applying as a remedy an alternative apportionment provision that KMS invoked only after the City's audit, the Decision encourages other taxpayers across

Washington to similarly calculate their payroll factors incorrectly, and then only if the taxing jurisdiction notices, seek a retroactive adjustment.

As to the first point, Seattle is required by statute to use a two-factor apportionment formula, which specifically includes in payroll only "compensation" paid to **employees**—not independent contractors. *See* RCW 35.102.130(3)(a), (4); SMC 5.45.081(F)(1), (H). These same obligations apply to every other jurisdiction that imposes such a tax. According to the Association of Washington Cities ("AWC"), 47 municipalities in the State of Washington impose a B&O tax. Forty-three of those cities, including Seattle, tax the gross receipts of service businesses. *See* Appendix D. As required under RCW 35.102.130, each such city uses the same two-factor apportionment method as Seattle.[10]

The Decision calls into doubt the constitutional application of the payroll factor. The Decision would require all taxing jurisdictions to conduct a nuanced legal and factual analysis of whether each taxpayer uses employees or independent contractors, even when the taxpayer does not seek alternative apportionment and admits it uses independent contractors. Even if a taxing jurisdiction agrees with the taxpayer as to that classification, and even absent an alternative apportionment petition, each

[10] *See, e.g.*, Bellevue Municipal Code 4.09.077(F)-(G); Bellingham Municipal Code 6.04.77(F)-(G); Everett Municipal Code 3.24.077(F)-(G); Kent Municipal Code 3.28.077(F)-(G); Longview Municipal Code 5.05.103(6)-(7); Olympia Municipal Code 5.04.105a(F); Tacoma Municipal Code 6A.30.077(F)-(G).

city would seemingly be required to investigate the taxpayer's status in each individual case.

In a similar vein, the Decision encourages manipulation of the voluntary compliance system by permitting a taxpayer to disclaim the manner in which it designates its own personnel and retroactively reapportion under a different formula, even if it did not request that remedy at the outset. The Court of Appeals ruled that KMS should receive alternative apportionment of its income under RCW 35.102.130(3)(c), which provides that if the two-factor formula does not "fairly represent" the extent of the taxpayer's business activity in the city, the taxpayer may "petition for" an alternative apportionment method. (Emphasis added); *see also KMS II*, 12 Wn. App. 2d at 506-07; SMC 5.45.081(F)(3).[11]

Although the Model Ordinance began requiring service businesses like KMS to use the two-factor formula in 2008, KMS has never applied this methodology correctly, nor did it timely "petition" for an alternative formula as required under the above provision.[12] For the entirety of the

[11] The Court of Appeals did not discuss or apply "constitutional" alternative apportionment, which applies when a taxpayer demonstrates "by clear and cogent evidence that the income attributed to the State is in fact out of all appropriate proportion to the business transacted . . . in that State or has led to a grossly distorted result." *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 274, 98 S. Ct. 2340, 57 L. Ed. 2d 197 (1978) (internal quotations and citations omitted).

[12] KMS implied at oral argument that it had so petitioned, but this is not true. *See* Division I Court of Appeals, Oral Argument Recording (9/27/2019) at 5:45 et seq., *available at* https://www.courts.wa.gov/content/OralArgAudio/a01/20190927/3.%20KMS%20Financi

audit period and preceding it, KMS included independent contractors' commissions in its payroll factor. CP 9-14. Only after the City discovered this fact did KMS request alternative apportionment. CP 35-42.

Under the Decision, a taxpayer may thus report its payroll factor incorrectly for years and then, once caught, avoid the consequences of its improper reporting by petitioning for alternative apportionment after the fact. That cannot be what the Legislature intended. If the voluntary compliance system is to function effectively, a taxpayer's desire for alternative apportionment must be brought to the attention of the taxing jurisdiction before an unfavorable audit and assessment.

For both of these reasons, the Decision raises an issue of substantial public interest to local governments and taxpayers statewide.

C. The Decision Conflicts with Supreme Court Authority.

Finally, this Court should grant review based on a conflict with its precedent. RAP 13.4(b)(1). As noted above, the Court of Appeals appears to have held the City's B&O tax ordinance unconstitutional as applied under the Commerce Clause. In doing so, however, it failed to distinguish between activity by KMS outside the State of Washington, and within the State. Yet, this Court held in *Dravo Corp.* that the Commerce Clause does not apply to intrastate activity. 80 Wn.2d at 601; *see also Ford Motor Co.*,

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al%20Services%20Inc.%20v.%20City%20of%20Seattle%20%20%20789465.mp3. Nothing in the record shows any such petition was made.

160 Wn.2d at 49. With respect to intrastate activity, this Court has applied a separate test based on the due process clause: whether there is "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." *Dravo Corp.*, 80 Wn.2d at 598-99 (internal quotations and citations omitted). And while the Court in *Dravo Corp.* did not rule on the issue of apportionment, it confirmed that under state law, "the burden would be on the taxpayer to establish the [alleged] multiple tax burden." *Id.* at 603. Here, the Court of Appeals acknowledged a separate test governed under state law. 12 Wn. App. 2d at 494-95, 503. But it never applied the intrastate test this Court articulated, nor did KMS present evidence of alleged double taxation as required. For these reasons, the Decision conflicts with *Dravo Corp.*, further warranting review.

VI. CONCLUSION

The City respectfully requests that the Court grant review of the Decision pursuant to RAP 13.4(b)(1), (3), and (4).

RESPECTFULLY SUBMITTED this 19th day of June, 2020.

PETER S. HOLMES
SEATTLE CITY ATTORNEY

By /s/ Jennifer Gilman
Jennifer Gilman, WSBA #21234

PACIFICA LAW GROUP LLP

By /s/ Matthew J. Segal
Matthew J. Segal, WSBA #29797
Sarah S. Washburn, WSBA #44418

Attorneys for Respondent City of Seattle

APPENDIX A

FILED
2/24/2020
Court of Appeals
Division I
State of Washington

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

CITY OF SEATTLE a municipal corporation, Respondent, v. KMS FINANCIAL SERVICES, INC., a Washington corporation, Appellant.	No. 78946-5-I DIVISION ONE PUBLISHED OPINION FILED: February 24, 2020

MANN, A.C.J. — This is a taxation case. The sole issue is whether the city of Seattle (City) used an unlawful method to calculate business and occupation (B&O) taxes owed by KMS Financial Services, Inc., between January 2012 and March 2016 (the audit period).

The Commerce Clause of the United States Constitution requires state and local taxes be "fairly apportioned" so that the tax is imposed only on the portion of income reasonably attributed to the taxpayer's instate activities. Washington law imposes a similar limitation on local government taxes. To comply with these requirements, the City's B&O tax utilizes a two-factor apportionment method to calculate taxable revenue for service related businesses. One of those factors, the "payroll factor," compares the

amount of compensation the taxpayer pays in Seattle to the compensation it pays outside the City. As a result, the more a taxpayer pays for work performed outside the City, the less its income is apportioned to the City—which means a lower B&O tax.

KMS is headquartered in Seattle, but generates most of its income through the sale of securities by registered representatives located outside the City. In calculating the payroll factor for its B&O tax, KMS included the compensation paid to its registered representatives. During an audit, Seattle determined that KMS's registered representatives were not "employees" and therefore did not consider their income in determining the payroll factor. The result roughly tripled KMS's B&O tax liability.

KMS sought review in the King County Superior Court. After cross-motions for summary judgment, the superior court granted the City's motion and dismissed KMS's challenge. We agree with KMS that the City's B&O tax, as applied to KMS, is not fairly apportioned and is unconstitutional. In order to avoid unconstitutionality, the City should have instead treated KMS's registered representatives as employees which would have resulted in a valid, fairly apportioned tax. We vacate the trial court's order and remand for the trial court to grant KMS's motion for summary judgment.

I.

A. KMS and Registered Representatives

The parties stipulated to the undisputed, material facts.[1] KMS is a Washington corporation, headquartered in Seattle. KMS engages in the securities, insurance, and investment advisory business. KMS is a broker-dealer under the Securities Exchange Act of 1934 (1934 Act), and is registered with the Securities & Exchange Commission

[1] See also KMS Financial Services, Inc. v. City of Seattle, 135 Wn. App. 489, 493-95, 146 P.3d 1195 (2006) (explaining further KMS's use of registered representatives).

(SEC), the Financial Industry Regulatory Authority (FINRA) and the state securities regulators of all 50 states.

Under federal securities laws, a broker-dealers acts primarily through "registered representatives." Registered representatives are individuals, often referred to as stockbrokers or account executives, who provide a variety of investment related services. Under the 1934 Act, all individuals in the business of assisting others with securities trades are required to be registered representatives of a registered broker-dealer. KMS does not, except through its registered representatives, generate investment advice, make securities recommendations, or solicit the sale of securities or other financial products.

As a broker-dealer, KMS must supervise its registered representatives, oversee their licensing status, and require them to comply with industry rules and standards of conduct and procedures set out in its policy manual.

For federal income tax purposes, broker-dealers typically structure their operation so that the registered representatives are either deemed employees (Form W-2), or independent contractors (Form 1099). A broker-dealer's control and supervisory obligations under the 1934 Act and by FINRA with respect to the broker-dealer's registered representatives are identical regardless of whether the registered representatives are deemed independent contractors or employees for federal income tax purposes.

The National Association of Securities Dealers (NASD) Notice 86-65 provides that:

> Irrespective of an individual's location or compensation arrangements, all associated persons are considered to be employees of the firm with which

> they are registered for purposes of compliance with NASD rules governing the conduct of registered persons and the supervisory responsibilities of the member. The fact that an associated person conducts business at a separate location or is compensated as an independent contractor does not alter the obligations of the individual and the firm to comply fully with all applicable regulatory requirements. [2]

A SEC letter dated June 18, 1982, addresses the status of registered representatives as employees of their associated broker-dealer. The letter addressed whether independent contractors are subject to the 1934 Act. "The critical question is whether a so-called independent contractor's activities are subject to control by a broker-dealer within the scope of Section 3(a)(B) of the Act." The letter explains that an independent contractor can be subject to the control of an employer under agency law. "It has been a long-standing policy of the Commission that independent contractors whose selling activities were controlled by their broker-dealer employers could be characterized as employees for the purposes of the Act."

KMS's revenue, through the sale of securities, is generated by approximately 350 registered representatives operating throughout the United States. By contract, KMS classifies its registered representatives as independent contractors. During the relevant period, KMS employed approximately 50 W-2 employees, most of whom worked in its Seattle headquarters. The registered representatives cultivate customers, process the opening of client accounts, provide investment advice, make securities recommendations, enter orders, and receive checks. The KMS W-2 employees handle administrative functions. KMS's W-2 employees do not provide or generate investment advice, make securities recommendations, or solicit the sale of securities and other financial products.

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[2] NASD was the predecessor to FINRA. Notice 86-65 continues to be in full force and effect.

A typical sale of securities involves: the client tells the registered representative to purchase or sell a security; the registered representative enters the client's order with KMS's primary clearing firm, Pershing LLC (Pershing); Pershing executes the trade and records it in the client's account; the client writes a check to KMS or to Pershing to pay for the transaction; the registered representative forwards the check to KMS, and a trade report is generated in KMS's office; after settlement of the trade (usually within three days), KMS receives a commission from Pershing and then pays the registered representative a commission based on its contract with the registered representative; KMS pays the registered representative between 85 and 90 percent of the commission from Pershing, depending on its contract with the registered representative who generated the order.

During the audit period, KMS paid its W-2 employees between approximately $2.6 million and $4 million annually, almost all of which (approximately 95 percent) went to Seattle-based employees. For that same period, KMS paid its registered representatives between approximately $70 million and $79 million, the vast majority of (around 85%) which went to representatives working outside of Seattle.

B. Seattle's B&O Tax

Seattle imposes a B&O tax on all persons engaging in business activity within the City. Seattle imposes B&O tax on KMS's "gross profits" under the "service and other" activity classification rate. SMC 5.45.050(F); see KMS Financial Services, Inc. v. City of Seattle (KMS I), 135 Wn. App. 489, 496, 146 P.3d 1195 (2006). When a business earns income both inside and outside of Seattle, the portion of that business's income attributable to Seattle must be determined. Beginning in 2008, all Washington cities

with a gross receipts B&O tax were required to apportion service business income using a two-factor apportionment formula that averages a service income factor and a payroll factor. Seattle adopted the two-factor apportionment in SMC 5.48.081(F). The service income factor and payroll factors are reflected as a fraction. The fractions are added together and then divided by two. The resulting number is then multiplied by the taxpayer's total taxable income, without regard to its source, to derive the amount of income that can be allocated to the taxpayer's Seattle activities. SMC 5.48.081.

The parties do not dispute the method KMS used to calculate its service factor. The only dispute is the calculation of the payroll factor. Under the Seattle Municipal Code, the payroll factor is described as:

> 1. The payroll factor is a fraction, the numerator of which is the total amount paid for compensation in the city during the tax period by the taxpayer and the denominator of which is the total compensation paid everywhere during the tax period. Compensation is paid in the city if:
>
> a. The individual or employee is primarily assigned within the city;
>
> b. The individual is not primarily assigned to any place of business for the tax period and the employee performs fifty percent (50%) or more of his or her service for the tax period in the city; or
>
> c. The individual is not primarily assigned to any place of business for the tax period, the individual does not perform fifty percent (50%) or more of his or her service in any city, and the employee resides in the city.

SMC 5.45.081(F)(1).

C. 2016 Audit

During the January 2012 through March 2016 audit period, KMS included the compensation it paid to its registered representatives when calculating the payroll factor. Because most of the compensation paid by KMS is in the form of commissions paid to its registered representatives, and most of the registered representatives work

outside the City, the payroll factor calculated by KMS was between 14% and 20%. After averaging this payroll factor with the undisputed service income factor, KMA calculated, reported, and paid $187,998.34 in Seattle B&O tax during the audit period.

During the audit, the City took the position that compensation paid to registered representatives should be excluded from both the numerator and denominator in calculating the payroll factor. According to the City, compensation paid to KMS's registered representatives should have been excluded because they were not "employees." Because nearly all of KMS's W-2 employees work in Seattle, exclusion of the commissions paid to the registered representatives increased the payroll factor by almost 100%. By excluding compensation paid to the registered representatives, the average of KMS's service income and payroll factors roughly tripled, thereby tripling the amount of tax calculated due.

As a result of the audit, the City assessed KMS with additional $460,972 of B&O tax, $20,501.78 of interest, and $23,048.64 in penalties, for a total of $504,532.22.

KMS timely paid the additional assessment and then filed a complaint for a refund of taxes paid in the King County Superior Court. Both parties moved for summary judgment. KMS argued that all registered representatives of broker-dealer are deemed to be employees for securities law purposes because of the broker-dealer's control and supervisory obligations. The City argued that the registered representative are independent contractors, not employees, and therefore are not supposed to be counted in the payroll factor.

The superior court granted the City's motion for summary judgment and denied KMS's motion for summary judgment. KMS appeals.

II.

Because this case was resolved below on cross-motions for summary judgment, our review is de novo. Cmty. Telecable of Seattle, Inc. v. City of Seattle, Dep't of Executive Admin, 164 Wn.2d 35, 41, 186 P.3d 1032 (2008). "Likewise, the proper construction of a city taxation ordinance is a legal question that is reviewed de novo on appeal, but the 'burden is on the taxpayer to prove that a tax paid by him or her is incorrect.'" Avanade, Inc. v. City of Seattle, 151 Wn. App. 290, 297, 211 P.3d 476 (2009) (quoting Ford Motor Co. v. City of Seattle, Exec. Servs. Dep't, 160 Wn.2d 32, 41, 156 P.3d 185 (2007)). The reviewing court "gives considerable deference to the construction of" the challenged ordinance "by those officials charged with its enforcement." Ford Motor Co., 160 Wn.2d at 42 (citing Gen. Motors Corp. v. City of Seattle, 107 Wn. App. 42, 57, 25 P.3d 1022 (2001)).

A.

As we explained in KMS I: "Federal and state constitutional law limit a jurisdiction's power to tax activities occurring outside its boundaries. Because KMS's registered representatives operated in Seattle, in other Washington state locations, and in locations outside Washington state, the City's tax must meet both state and federal constitutional requirements." KMS I, 135 Wn. App. at 503.

"The federal constitution's commerce clause—preserving to Congress the authority to regulate interstate commerce—may, by negative implication, render a local tax regulation unconstitutional if the regulation has the effect of burdening interstate commerce with the risk of multiple taxation." Avanade, 151 Wn. App. at 301. To determine whether a tax violates the commerce clause, the United States Supreme

Court has set out a four-factor test. "First, the tax must apply to an activity with 'substantial nexus' to the taxing state. Second, it must be 'fairly apportioned.' Third, it must not discriminate against interstate commerce. And fourth, it must be fairly related to services or benefits provided by the state." KMS I, 135 Wn. App. at 504 (citing Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 97 S. Ct. 1076, 51 L. Ed. 2d 326 (1977)).

The second factor, fair apportionment, is at issue here. "A gross receipts tax is 'simply a variety of tax on income, which [is] required to be apportioned to reflect the location of the various interstate activities by which it was earned.'" KMS I, 135 Wn. App. at 504 (quoting Ok. Tax Comm'n v. Jefferson Lines, Inc., 514 U.S. 175, 190, 115 S. Ct. 1331, 131 L. Ed. 2d 261 (1995). As we explained in KMS I:

> The Constitution does not require a single apportionment formula. Rather, "a tax is fairly apportioned [if] it is internally and externally consistent." Goldberg, 488 U.S. at 261. Internal consistency requires a tax to be "structured so that if every State were to impose an identical tax, no multiple taxation would result." Goldberg, 488 U.S. at 261. "The external consistency test asks whether the State has taxed only that portion of the revenues from the interstate activity which reasonably reflects the in-state component of the activity being taxed."

KMS I, 135 Wn. App. at 504 (quoting Goldberg v. Sweet, 488 U.S. 252, 261-62, 109 S. Ct. 582, 102 L. Ed. 2d 607 (1989)). The tax must actually reflect a reasonable sense of how income is generated. KMS I, 135 Wn. App. at 505.

In KMS I, we reviewed a similar effort by the City to impose a B&O tax on KMS. At that point in time, KMS had approximately 300 registered representatives working in approximately 210 business locations in nine western states, including Washington. KMS I, 135 Wn. App. at 494. During the period January 1999 through March 2003, the City assessed the B&O tax on all commissions received in the KMS Seattle office, no

matter where the registered representative who generated the commission was based. The City maintained that because the Seattle office was KMS's sole office, KMS was not entitled to apportionment under the City's tax code. KMS I, 135 Wn. App. at 494.

We held that "attributing the entire proceeds of KMS's registered representatives to KMS's Seattle office because that is KMS's sole office violates the external consistency requirement of federal commerce clause jurisprudence." KMS I, 135 Wn. App. at 509. Adopting the rationale of a Pennsylvania court, we reasoned that this was so because taxing the entire gross proceeds of an out-of-city transaction, based solely on the fact that the transaction occurred in a state in which the taxpayer did not have an office, resulted in a tax that "was 'out of all appropriate proportion to' and had no 'rational relationship' with" the taxpayer's business activities within Seattle. KMS I, 135 Wn. App. at 506-08 (quoting Northwood Constr. Co. v. Twp. of Upper Moreland, 579 Pa. 463, 486, 856 A.2d 789 (2004)).

Similar to federal law, Washington imposes a three-part test on a city's power to tax: (1) the relevant taxable event must be identified; (2) the taxable event must occur within the municipality's territorial limits; and (3) there must be a minimum connection between the municipality and the transaction it seeks to tax. KMS I, 135 Wn. App. at 510 (citing Dravo Corp. v. City of Tacoma, 80 Wn.2d 590, 594-95, 496 P.2d 504 (1972)).

With respect to the application of state law to the City's imposition of its B&O tax on KMS based solely on its office being in Seattle, in KMS I, we concluded:

> that the City cannot tax income generated by securities transactions within Washington state but outside Seattle city limits when the incident of taxation is the privilege of doing business in the City. Whether or not KMS maintains an "office" as defined by the City's tax ordinance is not a

> determining factor in the state law test of the limits of a municipality's taxing power. The City must fairly apportion KMS's gross receipts based on where the income-generating activity occurred. The assessment did not fairly apportion KMS's gross receipts.

KMS I, 135 Wn. App. at 512.

B.

KMS first argues that the City's B&O tax is unconstitutional as applied because it was not fairly apportioned. This is so, KMS contends, because the City ignored that most of KMS's taxable income is generated by registered representatives that work out of the city and state. We agree.

An "as applied" constitutional challenge to statute is "characterized by a party's allegation that application of the statute in the specific context of the party's actions or intended actions is unconstitutional." City of Redmond v. Moore, 151 Wn.2d 664, 668-69, 91 P.3d 875 (2004). This does not totally invalidate that statute, only its future application in a similar context. Id.

A tax assessed on gross income, such as the City's B&O tax, must be fairly apportioned to reflect "the location of the various interstate activities by which it was earned." KMS I, 135 Wn. App. at 504. In order to insure compliance with this mandate, in 2008 (after KMS I), the legislature enacted RCW 35.102.130, requiring all Washington cities with a B&O tax to use a two-factor apportionment formula based on service income and payroll. Wedbush Sec., Inc. v. City of Seattle, 189 Wn. App. 360, 364, 358 P.3d 422 (2015). The City incorporated the requirements of RCW 35.102.130 in SMC 5.45.081. Wedbush, 189 Wn. App. at 364, n.3. Under RCW 35.102.130(3)(a) and SMC 5.45.081(F)(1), the payroll factor takes into account the location of the of the employees and individuals that generate the income.

The City's payroll factor does this by comparing the compensation paid to individuals and employees "in the city" to compensation paid to individuals "paid everywhere." SMC 5.45.081(F)(1). Compensation is defined to include "commissions . . . paid to individuals for personal services that are or would be included in the individual's gross income under the federal Internal Revenue Code." SMC 5.45.081(G)(2). In reporting its B&O tax liability, KMS included the commissions paid to its registered representatives in the payroll factor because most of KMS's taxable income was generated through the sale of securities and services by the registered representatives.[3]

The City's argument that compensation paid to KMS's registered representatives must be excluded from the payroll factor because they are classified as independent contractors instead of employees necessarily fails. Whether a taxpayer does business through independent contractors or employees is "without constitutional significance." Scripto Inc. v Carson, 362 U.S. 207, 211-12, 80 S. Ct. 619, 4 L. Ed. 2d 660 (1960). Moreover, the point of fair apportionment is to ensure that a city only taxes income attributable and proportional to a taxpayer's income-generating activity in the city. KMS I, 135 Wn. App. at 506-09, 512; Avanade, 151 Wn. App. at 304. It does not matter whether income is generated by independent contractors or employees working outside the city. Either way, they are not working in the city; the city has no claim to a "fair share" of the income they generate.

[3] It is undisputed that KMS's registered representatives must report commissions as gross income in their individual federal tax returns. See Watson v. Commissioner, T.C. Memo. 2007-146 (U.S. Tax Ct. 2007), aff'd, 277 Fed. App'x 450 (5th Cir. 2008).

While the law has changed, the City's argument here suffers the same defect it did in KMS I. The City again ignores where KMS's registered agents work and generate income in calculating the payroll factor. In calculating the payroll factor Seattle allocates more than 95% of KMS's compensation to the city because this is where KMS's W-2 employees work. In essence, the City attributes most of KMS's income to the work of approximately 50 employees based in the city when it is undisputed that the bulk of KMS's income comes from the work of the 300-plus registered representatives based outside the city.

Because the City failed to consider where and how KMS generated its income, the tax is not externally consistent as applied to KMS. Therefore, the B&O tax is not fairly apportioned to KMS. Because the tax is not fairly apportioned, it is unconstitutional as applied to KMS.

C.

As a matter of constitutional avoidance, if a statute is susceptible to more than one interpretation, courts should construe it "to avoid constitutional doubt." Utter v. Bldg. Indus. Ass'n of Wash., 182 Wn.2d 398, 434-35, 341 P.3d 953 (2015). KMS argues that the Seattle Municipal Code provides a safety net: that if the allocation and apportionment provisions of the B&O tax do not fairly represent the extent of the taxpayer's business activity, the City may employ another method to allocate the taxpayer's income and thereby avoid a constitutional violation. We agree.

In RCW 35.102.130, the Legislature specifically provided at catchall to the apportionment formula. When Seattle adopted the RCW in SMC 5.45.08, it also adopted this relevant portion:

> If the allocation and apportionment provisions of this subsection do not fairly represent the extent of the taxpayer's business activity in the city or cities in which the taxpayer does business, the taxpayer may petition for or the tax administrators may jointly require, in respect to all or any part of the taxpayer's business activity, that one of the following methods be used jointly by the cities to allocate or apportion gross income, if reasonable:
>
> (i) Separate accounting;
> (ii) The use of a single factor;
> (iii) The inclusion of one or more additional factors that will fairly represent the taxpayer's business activity in the city; or
> (iv) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

RCW 35.102.130(3)(c); SMC 5.45.081(F)(3).

Here, when KMS challenged the City's tax apportionment, KMS argued that "Seattle's B&O tax can be fairly apportioned by including compensation paid to KMS's registered representatives in calculating the compensation factor of Seattle's apportionment formula, as KMS did when preparing and filing its Seattle taxes."[4]

KMS has provided for an additional method by which the City could have apportioned the tax so that the tax would fairly represent KMS's activity in the city. As discussed above, the City's application was not fairly apportioned to KMS and did not fairly represent how KMS conducts its business in Seattle. The catchall created by the Legislature gives the City authority to use a different method to apportion the tax without adhering to the two-factor formula in a way that is fair. Because the Legislature provided a catchall in the RCW, the City should have employed a different method to reach a fairly apportioned tax.

[4] The City does not claim that KMS did not challenge the apportionment and provide an additional method of calculating the B&O tax.

D.

KMS argues that a plain language reading of SMC allows for the City to consider the registered representatives as employees for an alternative apportionment calculation. We agree.

The relevant definition of the code are:

> 3. "Individual" means any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee of that taxpayer.

SMC 5.45.081(G).

The common law "right to control" test for determining whether a worker is an employee or an independent contractor is derived from the common law of torts. Anfinson v. FedEx Ground Package Sys., Inc., 159 Wn. App. 35, 53, 244 P.3d 32, 41 (2010), aff'd, 174 Wn.2d 851, 281 P.3d 289 (2012). The right to control another's conduct is often the most decisive factor in determining if an agency relationship exists. Massey v. Tube Art Display, Inc., 15 Wn. App. 782, 787, 551 P.2d 1387 (1976). For tort purposes, the principle does not need to show complete control, rather, substantial evidence of control is sufficient. Massey, 15 Wn. App. at 787.[5]

Here, it is undisputed that both the SEC and FINRA consider a broker-dealer's registered representatives to be its employees because they are, by law, subject to the broker-dealer's control—even if they are classified as independent contractors.

Additionally, KMS's registered representatives fall within the definition of individual under SMC 5.45.081(G). An individual is considered an employee under the

[5] The City cites to Seattle Rule 5-039, which distinguishes employees from persons engaging in business. The rule provides a list of factors to determine if a person is an employee. The rule also states that "while no one factor definitely determines employee status, the most important consideration is the employers right to control the employee."

common law rules if the employer exercises control over the individual. Under federal law, "as a broker-dealer, KMS must supervise its registered representatives, oversee their licensing status, and require them to comply with industry rules and standards of conduct and procedures set out in its policy manual." Therefore, the City could logically consider the registered representatives to be employees for an alternative apportionment calculation of the B&O tax.

We conclude that the City's interpretation of its payroll factor as applied to KMS fails to fairly apportion the City's B&O tax and is unconstitutional as applied to KMS. The constitutional defect can be avoided, however, by applying the interpretation offered by KMS and including its registered representatives in the payroll factor for calculating its B&O obligation.

We vacate the order granting summary judgment to the City and remand with instruction for the trial court to grant KMS's motion for summary judgment.

Mann, ACJ

WE CONCUR:

Leach, J.

Dwyer, J.

APPENDIX B

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

CITY OF SEATTLE a municipal corporation, Respondent, v. KMS FINANCIAL SERVICES, INC., a Washington corporation, Appellant.	No. 78946-5-I DIVISION ONE ORDER DENYING MOTION FOR RECONSIDERATION

Respondent City of Seattle filed a motion to reconsider the court's opinion filed on February 24, 2020. Appellant KMS Financial Services, Inc. filed a response. The panel has determined that the motion should be denied.

Therefore, it is

ORDERED that the motion for reconsideration is denied.

FOR THE COURT:

Mann, C.J.

APPENDIX C

Apportionment Formula – RCW 35.102.130

Income Factor		Payroll Factor		
Service Income in Seattle / Total Service Income Everywhere	+	Compensation* Paid in Seattle / Total Compensation Paid Everywhere ÷ 2	=	Apportionment Factor

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Apportionment Factor	x	Total Apportionable Income (Total service receipts – deductibles)	=	Total Taxable Service Income
Total Taxable Service Income	x	Service Tax Rate (0.415%)	=	B & O Tax Payable to Seattle

***Paid to *employees* – not independent contractors**

APPENDIX D

Local business & occupation (B&O) tax rates^

Effective January 1, 2020

City	Phone #	Manufacturing rate	Retail rate	Services rate	Wholesale rate	Threshold	
						Quarterly	Annual
Aberdeen	(360) 533-4100	0.002	0.003 e	0.00370 e	0.003 e	$5,000	$20,000
Algona	(253) 833-2897	0.00045	0.00045	0.00045	0.00045	$10,000	$40,000
Bainbridge Island	(206) 780-8668	0.001	0.001	0.001	0.001		$150,000
Bellevue	(425) 452-6851	0.001496	0.001496	0.001496	0.001496		$170,000
Bellingham	(360) 778-8010	0.0017	0.0017	0.0044 e	0.0017	$5,000	$20,000
Blaine	(360) 332-8311	0.002			0.002		$250,000
Bremerton	(360) 473-5311	0.0016	0.00125	0.002	0.0016		$220,000
Burien	(206) 241-4647	0.001	0.001	0.001	0.001		$200,000
Cosmopolis	(360) 532-9230	0.002	0.002	0.002	0.002	$5,000	$20,000
Darrington	(360) 436-1131	0.00075	0.00075	0.00075	0.00075		$20,000
Des Moines	(206) 878-4595	0.002	0.002	0.002	0.002		$50,000
DuPont	(253) 964-8121	0.001	0.001	0.001	0.001	$5,000	$20,000
Everett***	(425) 257-8610	0.001	0.001	0.001	0.001	$5,000	$20,000
Everson	(360) 966-3411	0.002			0.002		$1,000,000
Granite Falls**	(360) 691-6441					$5,000	$20,000
Hoquiam	(360) 532-5700	0.002	0.002	0.002	0.002	$5,000	$20,000
Ilwaco	(360) 642-3145	0.002	0.002	0.002	0.002		$20,000
Issaquah	(425) 837-3054	0.0012	0.0012	0.0015	0.0012	$25,000	$100,000
Kelso	(360) 423-0900	0.001	0.001	0.002	0.001		$20,000
Kenmore	(425) 398-8900	0.002 *				$5,000	
Kent	(253) 856-6266	0.00046	0.00046	0.00152	0.002	$62,500	$250,000
Lacey	(360) 491-3214		0.001	0.002		$5,000	$20,000
Lake Forest Park	(206) 368-5440	0.002	0.002	0.002	0.002	$5,000	
Long Beach	(360) 642-4421	0.002	0.002	0.002	0.002	$5,000	
Longview	(360) 442-5040	0.001	0.001	0.002	0.001		$20,000
Lyman	(360) 826-3033	0.002	0.002	0.002	0.002	$5,000	$20,000
Mercer Island	(206) 275-7783	0.001	0.001	0.001	0.001		$150,000
North Bend	(425) 888-1211	0.002	0.002	0.002	0.002	$5,000	
Ocean Shores	(360) 289-2488	0.002	0.002	0.002	0.002	$5,000	$20,000
Olympia	(360) 753-8327	0.001	0.001	0.002	0.001	$5,000	$20,000
Pacific	(253) 929-1100	0.002	0.002	0.002	0.002	$5,000	$20,000
Port Townsend	(360) 385-2700	0.002	0.002	0.002	0.002	$0	$100,000
Rainier	(360) 446-2265	0.002	0.002	0.002	0.002	$5,000	
Raymond	(360) 942-3451	0.002	0.002	0.002	0.002	$5,000	$20,000
Renton	(425) 430-6400	0.00085	0.00050	0.00085	0.00085		$500,000
Roy	(253) 843-1113	0.001	0.002	0.002	0.001	$5,000	$20,000
Ruston	(253) 759-3544	0.00110	0.00153	0.00200	0.00102	$5,000	$20,000
Seattle	(206) 684-8484	0.00222 v	0.00222 v	0.00427 v	0.00222 v		$100,000
Shelton	(360) 426-4491	0.001	0.001	0.001	0.001	$5,000	$20,000
Shoreline	(206) 801-2324	0.001	0.001	0.002	0.001	$125,000	$500,000
Snoqualmie	(425) 888-1555	0.0015	0.0015	0.0015	0.0015	$5,000	
South Bend	(360) 875-5571	0.001	0.002	0.002	0.002	$5,000	
Tacoma	(253) 591-5252	0.00110	0.00153	0.00400 e	0.00102		$250,000
Tenino	(360) 264-2368	0.002	0.002	0.002	0.002	$5,000	$20,000
Tumwater	(360) 754-5855	0.001	0.001	0.002	0.001	$5,000	$20,000
Westport	(360) 268-0131	0.0025 e	0.005 e	0.005 e	0.0025 e	$5,000	
Yelm	(360) 458-3244	0.001	0.002	0.002	0.001	$5,000	

(v) = voter approved increase above statutory limit

(e) = rate higher than statutory limit because rate was effective prior to January 1, 1982 (i.e., grandfathered).

*Kenmore's B&O tax applies to heavy manufacturing only.

**Granite Falls repealed its B&O tax for all businesses other than extracting.

***For manufacturing gross reciepts over $8 billion, the B&O rate drops to 0.00025.

NOTE: Tax rates may apply to businesses categories other than those above. Thresholds are subject to change. Exemptions, deductions, or other exceptions may apply in certain circumstances. Contact the city finance department for more information.

^ Tax rates are provided for cities with general local B&O taxes as of the date listed. If a city is not listed, they have not reported to AWC that they have a local B&O tax. Contact the city directly for specific information or other business licenses or taxes that may apply.

PACIFICA LAW GROUP

June 19, 2020 - 4:02 PM

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Appellate Court Case Title:	KMS Financial Services, Inc., Appellant v. City of Seattle, Respondent

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