

NO. 50409-0-II

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

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Respondent,

v.

GAMESTOP, INC. and SOCOM, LLC,

Appellants.

GAMESTOP'S RESPONSE BRIEF

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I. INTRODUCTION

The Washington State Board of Tax Appeals (“BTA”) appropriately held that the sales tax exclusion under RCW 82.08.010(1)(a)(i) for trade-in property of a like kind applies to GameStop Inc.’s and SOCOM, LLC’s (together “GameStop”) trade-in program. The Department of Revenue (the “Department” or “DOR”) asks this Court to upend the BTA’s sensible findings and conclusions on three grounds. All three fail. *First*, The BTA demonstrated a nuanced and accurate understanding of property used for gaming when it properly found that consoles, accessories, and games all fall within the same general category of property: gaming components. *Second*, the BTA reached the right result when it concluded that a trade-in need not be contemporaneous with the acquisition of like-kind property to qualify for the exclusion. GameStop’s use of a stored-value card system to facilitate trade-ins is a reasonable consumer-friendly option that satisfies the exclusion and creates a paper trail that the Department can audit. *Third*, the BTA correctly recognized that GameStop’s program satisfies the requirement that property subject to the trade-in exclusion be “separately stated” because GameStop’s documentation isolates portions of transactions that are associated with the trade-in program.

II. ISSUES ON APPEAL

1. Did the BTA correctly treat video game components such as consoles, accessories, and games as “property of a like kind” within the meaning of RCW 82.08.010(1)(a)(i)?
2. Did the BTA correctly conclude that trade-ins need not occur contemporaneously to qualify for the trade-in exclusion under 82.08.010(1)(a)(i)?
3. Did the BTA correctly conclude that property under GameStop’s trade-in program was “separately stated” as that term is used in RCW 82.08.010(1)(a)(i)?

III. STATEMENT OF THE CASE

A. GameStop’s Trade-in Program

GameStop is a retailer of new and used video game equipment, including hardware (consoles, controllers, and other accessories), games, and other related components. Appendix A, Findings of Fact (“FOF”) 10. GameStop offers a trade-in program to consumers that allows customers to trade used gaming products for cash or in-store credit. When a consumer chooses to receive in-store credit—either as an immediate offset to another purchase or as credits loaded onto a stored-value card—GameStop treats the transaction as a trade-in subject to the Washington tax exclusion. *Id.*, FOF 11-13. These stored value cards cannot be

redeemed for cash and cannot be purchased from GameStop for cash. *Id.*, FOF 13.

Typically, customers purchase both gaming hardware and software. The purchase of a console, a controller, and a number of video games is a substantial investment. Accordingly, a cost-sensitive customer who wants to upgrade to newer hardware will likely trade in all components of his or her previous system, including the console, accessories, and games. By trading in a used Sony PlayStation 4, for example, for a \$250 credit, the customer would receive a meaningful offset against the outlay for the purchase of a new Xbox One console, controller, and game. *Id.*, FOF 19.

GameStop's trade-in program provides its customers with "a unique value proposition... generally unavailable at mass merchants, toy stores and consumer electronics retailers.' Each year, [GameStop] provides approximately \$1.2 billion in trade-in credits. The trade-in program allows GameStop to acquire an inventory of used video game products' that it can "resell to [its] more value-oriented customers.'" *Id.*, FOF 16.

B. Procedural Background

This case arises from the Department's audits of GameStop for periods January 2006 through December 2010 (for GameStop, Inc.) and January 2008 through December 2010 (for Socom, LLC). AR 244, 254.

As a result of the audits, the Department assessed a substantial sum for uncollected retail sales tax derived from the Department's position regarding the applicability of the trade-in exclusion. AR 264, 272.

The Department concluded that GameStop had improperly claimed the trade-in exclusion in three respects: (1) the trade-in of video game software on the purchase of video game hardware (consoles and accessories); (2) the trade-in of video game hardware on the purchase of video game software; and (3) the use of trade-in credits from a stored-value card. AR 246. GameStop timely petitioned the Department's Appeals Division for review. AR 260, 267. After the Appeals Division denied GameStop relief, it sought review from the BTA. AR 387.

Following a hearing under the Administrative Procedure Act, the BTA issued a final decision (AR 33, attached hereto as Appendix A) overturning the Department's audit findings. The BTA concluded that the trade-in exclusion applied to all of the disputed sales transactions and sided with GameStop on each of the three issues on appeal.

The Department filed a petition for review with the Thurston County Superior Court. CP 4. On May 18, 2017, Judge Christopher Lanese entered an order reversing the BTA. CP 38. GameStop appealed to this Court. CP 48.

IV. ARGUMENT

A. Standard of Review

The appeal of a final ruling of the BTA is governed by the Administrative Procedures Act, which places the burden on the Department to demonstrate the invalidity of the agency's action. RCW 82.03.180; RCW 34.05.570(1)(a).

The appellate court reviews the administrative agency's decision and applies the APA standards to the administrative record. *Verizon NW, Inc. v. Employment Sec. Dep't*, 164 Wn.2d 909, 915, 194 P.3d 255 (2008). The BTA's findings of fact are reviewed for "substantial evidence," which is defined as evidence of "a sufficient quantity ... to persuade a fair-minded person of the truth and correctness of the order." *Port of Seattle v. Pollution Control Hearings Bd.*, 151 Wn.2d 568, 588, 90 P.3d 659 (2004) (quoting *King Cnty. v. Cent. Puget Sound Growth Mgmt. Hearings Bd.*, 142 Wn.2d 543, 553, 14 P.3d 133 (2000) (internal quotations and citations omitted)). The reviewing court should "view the evidence and the reasonable inferences in the light most favorable to the party that prevailed" at the administrative proceeding below. *Affordable Cabs, Inc. v. Dep't of Employment Sec.*, 124 Wn. App. 361, 367, 101 P.3d 440 (2004). A court cannot substitute its judgment regarding witness

credibility or the weight given, to conflicting evidence. *Davis v. Dep't of Labor & Indus.*, 94 Wn.2d 119, 124, 615 P.2d 1279 (1980).

Conclusions of law are reviewed *de novo* with “substantial weight” given to the agency’s interpretation of statutes which it administers. *Smith v. Employment Sec. Dep't*, 155 Wn. App. 24, 32, 226 P.3d 263 (Div. 2 2010) (citing *Everett Concrete Prods., Inc., v. Dep't of Labor & Indus.*, 109 Wn.2d 819, 823, 748 P.2d 1112 (1988)).

B. The Applicable Trade-in Exclusion

Washington imposes retail sales tax on the sale of tangible personal property to consumers. The measure of tax is the “selling price,” or “sales price,” as defined in RCW 82.08.010(1)(a)(i). Originally, the value of trade-in property was included as part of the selling price paid by the buyer. *See Olympic Motors, Inc., v. McCroskey*, 15 Wn.2d 665, 671, 132 P.2d 355 (1942) (“When a seller takes used articles in trade [that] trade-in constitutes a portion of the consideration paid by the purchaser to the seller.”). In 1984 the citizens of Washington passed Initiative 464, which amended the definition of “selling price” to exclude “trade-in property of like kind.” *See* Laws of 1985, ch. 2.

The statutory definition of “sales price” now includes everything of value received in payment, “except separately stated trade-in property of like kind.” RCW 82.08.010(1)(a)(i). Under the trade-in exclusion, the

value of trade-in property is deducted from the price of the newly purchased property before assessing retail sales tax on the purchase. The statute thus imposes two requirements: Property must be of like kind and the sales documents must state the amount of the trade-in.

C. GameStop’s Trade-In Program Satisfies the Statutory Requirements.

GameStop’s trade-in program is exactly the kind of consumer-friendly service that voters would have expected to benefit from the trade-in exclusion. Yet the Department persists in trying to deprive it of that appropriate tax treatment based on a tortured reading of the statute and WAC 458-20-247 that tries to draw artificial distinctions between the different kinds of gaming components GameStop sells. Neither the statute nor the rule supports the Department’s position, which is premised on a fundamental misunderstanding of the function and use of video game components and an inapt analogy to the differences between computer software and computer hardware.

1. “Gaming Components” Is an Appropriate General Classification That Encompasses Consoles, Accessories, and Games, Which All Serve the Same Gaming Function.

To play a video game, the player must have a console and controller, as well a video game. The console and controller are hardware; the game

is software. But if you asked a person on the street to pick a category for these items, the obvious one is gaming components.

The Department attempts to avoid this obvious categorization by pointing to the requirement of WAC 458-20-247(5) that property of like kind have a similar function or use. This is the correct standard, but the Department's application in this case is at odds with the rest of the rule.

The rule provides:

The term "property of like kind" means articles of tangible personal property of the same ***generic classification***. It refers to the class and kind of property, not to its grade or quality. The term includes all property within a ***general classification rather than within a specific category in the classification***.

(emphasis added). Here the Department has ignored the obvious generic classification—gaming components—and focused on the role of each component in playing the game and whether the components are substitutes for one another. Under this line of reasoning, a knife and fork would not be property of like kind, nor would a table and chair.

The rule goes on to provide examples:

Thus, as examples, it means furniture for furniture, motor vehicles for motor vehicles, licensed recreational land vehicles for licensed recreational land vehicles, appliances for appliances, auto parts for auto parts, and audio/video equipment for

audio/video equipment. These general classifications are determined by the nature of the property and its function or use.

Thus the Department recognizes that auto parts is an appropriate general classification for a universe of different products (mufflers, carburetors, belts, et al.) that are all used together in the same kind of larger system (automobiles), and audio/visual equipment is an appropriate general classification for another such universe. So too, gaming components is an appropriate general classification for a universe of different products (consoles, accessories, games, et al.) that are all used together in the same kind of larger system (gaming). It is not necessary that one item be a substitute for another in order to be like-kind property, as the Department claims at page 21 of its brief.

The BTA recognized this when it concluded that gaming components is a proper general classification akin to “auto parts” or “audio-video equipment.” App. A, Conclusion of Law (“COL”) 12. Home audio systems generally include a number of components such as stereos, receivers, speakers, and compact disc players. While these categories of products from a *technical* standpoint serve very different functions, they are all used together as part of an audio or audio/video system. Similarly, video game components serve different technical functions—e.g., a controller is for a user to issue commands, a console is the central

processor for the game. Together, the components create a gaming system. Just as individuals will often trade in and upgrade an entire audio/video system, gamers will often trade in and upgrade their gaming system. *Id.*, FOF 6. However, unlike audio/video systems, video games are not typically compatible with other manufacturer's systems or with prior versions of a manufacturer's console, and therefore a customer who desires to upgrade their video game system must typically update both their gaming console and games *together*. The fact that there is a substantial trade-in market for these components together strongly supports the BTA's conclusion that gaming components are property of like kind.

The Department argues that "gaming components" is an inapt general category of property because GameStop once used more specific categories in a filing with the Securities and Exchange Commission. DOR Brief at 20. GameStop, as a retailer, has many occasions to describe its merchandise (e.g. AR341-42). None of these require or purport to be classifications based on function and use and are thus irrelevant.

The Department then cites a number of cases that stand for the proposition that "labels do not control when determining if a tax exemption applies." DOR Brief at 20 (collecting cases that recognize substance controls over form). But it is actually the *Department's*

position that attempts to exalt labels instead of—as the Department puts it—“the underlying nature of the property or its function or use.” *Id.* The Department argues that “[v]ideo game software performs none of the functions or uses of video game hardware, and vice-versa.” DOR Brief at 21. This position is based on a hyper-technical and ultimately improper understanding of a property’s “function or use.” The function of a gaming console is to allow users to play a game. The function of an accessory such as a controller, similarly, is to allow users to play a game. The function of a specific game on a disc or cartridge is no different: to allow users to play that game. A functional assessment of consoles, accessories, and specific games leads to exactly the conclusion the BTA reached: they are all property of a like kind that all serve a function in the gaming experience.

2. The BTA Did Not Create a New Standard for Like Kind Property.

The Department devotes a whole section of its brief, pages 22 through 25, to an argument that the BTA created a new “interdependence” standard for like kind property. A reading of the opinion shows no such standard. The BTA, in considering function and use, notes that gaming components are interdependent like the auto parts or audio/visual equipment examples used in Rule 247. App. A, COL 12-13. The BTA

also notes that the rule does not require interdependence: “The sample classifications allow the trade in of items with little similarity and no interdependence (a bookcase for a loveseat, or as the Taxpayer suggests, ‘a drug store watch for a diamond ring.’)” *Id.*, COL 13.

The BTA uses interdependence in a determinative way only in response to the Department’s argument that Rule 247 on its face precludes a finding that gaming consoles, controllers, and games are like kind property because the rule states that “computer hardware” and “computer software” are not of like kind. The BTA properly rejected this approach, which the Department argues again in its opening brief at page 18.

The BTA held that “the meaning of ‘computer hardware’ and ‘computer software’ in the Rule 247 list is controlled by the meaning of the rule’s four other paired items: ‘Under the doctrine of ‘noscitur a sociis,’ the meaning of words may be indicated or controlled by those with which they are associated.’” App. A, COL 16 (citing *Ball v. Stokely Foods*, 37 Wn.2d 79, 87-88, 221 P.2d 832 (1950); *City of Seattle v. Allison*, 148 Wn.2d 75, 81, 59 P.3d 85 (2002) (“Rules of statutory construction apply to administrative rules and regulations”). The other examples in 247(5) of property that is not of a like kind, such as “a diamond ring [and] a television set” are not interdependent items (i.e., they are not required to be used together to perform a single task). COL 14.1.

The reference to computer hardware and software similarly refers to generic hardware and software that are not interdependent.¹ That is a crucial distinction between computer hardware and software on the one hand and video game consoles and their games on the other hand.²

The Department also argues that consoles, controllers, and games are not interdependent as a factual matter because Sony components and games are not compatible with Microsoft or Nintendo components and games. This argument misapprehends the concept behind Rule 247, which is based on general classifications, not the attributes of an individual item. Under the rule, the question is whether several categories of items work together in order to obtain the desired function or use. In the audio/visual example, the receiver, CD player, and speakers are interdependent because they work together to produce music. The fact that a wireless Blue Tooth speaker may not be compatible with an older receiver does change the fact

¹ The lack of interdependence of computer hardware and software is especially apparent when considering that computers are multifunctional devices that can be used for a multitude of business or personal functions. Contrast that with video game consoles. The beauty of the gaming console is that unlike a personal computer, its core function is singular—gaming.

² The BTA also noted that, “[c]omputer hardware has become extremely varied” such that “smartphones, flat screen televisions, DVD players, digital cameras and electric automobiles” all “meet the technical definition of ‘computer hardware’ under 458-20-15501” but “would not be viewed as falling within the same general classification as a personal computer. App. A, FOF 9.

that they are like-kind items. A Ford carburetor may not be substituted for a Honda carburetor, but they are still like-kind items.

D. Trade-ins Need Not Be Contemporaneous to Reduce the Selling Price for Sales Tax Purposes

GameStop's trade-in program allows customers to (1) receive cash for their old merchandise, (2) receive an immediate credit for the old merchandise against the purchase price of new merchandise that same day, or (3) receive an immediate credit in the form of a stored value card to use against the purchase price of new merchandise at a later date.

Although RCW 82.08.010(1)(a)(i) does not require that the trade-in be contemporaneous with the new purchase, the Department continues to make a strained argument that GameStop's use of stored-value cards to facilitate non-contemporaneous trade-ins puts all of those transactions outside the scope of the trade-in exclusion. This distortion of the exclusion has no support in the language of the statute or a common sense understanding of its intended scope.

Nothing in the statute's definition of "selling price" requires that trade-ins be part of a contemporaneous, single transaction with the purchase of other items. In fact, neither the statute nor the Department's own rule states that the consideration for the "separately stated trade-in property of

like kind” be immediately applied to the purchase of like-kind property.

WAC 458-20-247(4) provides:

(4) Trade-in as consideration. Property traded in must be consideration delivered by the buyer to the seller. The sales documents must identify the tangible personal property being purchased and the trade-in property being delivered to the seller. *This does not require simultaneous transfers of the property being traded in and the property being purchased,* but it does require that the delivery of the trade-in and the purchase be components of a single transaction.

(emphasis added). GameStop’s use of stored-value cards allows merchandise to be traded in prior to the purchase of other merchandise, but the stored value is clearly “consideration” for the newly-purchased item and “consideration” is the statutory requirement. The GameStop customer could have received cash for his or her used merchandise, but chose to put it on a stored value card that is not redeemable for cash and can only be used to purchase new merchandise. Thus, GameStop “and customer agree that the agreed-upon trade-in value of the customer’s ‘gaming equipment’ will provide an offset against the customer’s purchase of ‘gaming equipment.’” App. A, COL 19.

The use of a stored value card to hold the value of the trade-in does not materially differ from the example transaction in Rule 247(4):

Sally Jones decides to upgrade from her existing motor home to a new, larger motor home. The salesperson at a local RV dealership explains that while the dealership does not currently have on hand a motor home meeting-Sally's needs, it can order one for her from the manufacturer. The salesperson also explains that if Sally trades in her motor home at the time she enters into the purchase contract, the dealership- will accept the motor home as a down payment toward the purchase of the new motor home. Sally signs the-purchase contract, the dealership orders the new motor home, and Sally delivers her motor home to the RV dealership (who accepts ownership-of the motor home). Sally's new motor home is delivered to her eight months later. Sally is entitled to the trade-in exclusion because the motor home was delivered to the RV dealership as consideration paid toward-her purchase of the new motor home.

Although the Department maintains that the non-contemporaneous nature of GameStop's stored value card transactions means the trade-in is not "consideration," the real question is whether the trade-in and subsequent purchase are part of a single transaction.³ The BTA held that they were because the clear intent of GameStop and the customer were

³ Rule 247's requirement that the trade-in be part of a "single transaction" is likely the result of the rule-writers focusing on vehicle trade-ins, which are certainly one of the most common. Because most people need a vehicle of some kind, they do not deliver their trade-ins to the dealer until they can purchase and take possession of another vehicle. That is not necessarily the case with video games or other types of trade-ins.

evidenced by the use of the stored value card, which could only be used for purchase of gaming components. App. A, COL 18-19. As the BTA correctly noted, Rule 247(4) contains four examples. In two cases, there is a single transaction even when property is not simultaneously exchanged because the parties have agreed to both the trade-in and subsequent purchase. In the other two cases, the subsequent purchase was contingent on the sale of the trade-in, thus making it a consignment, and not eligible for the trade-in exemption. The Department tries to explain away these examples at pages 30-33 of its brief, concentrating on the example in which funds from a contingent sale were placed in a trust account, but it fails to acknowledge that in this example, unlike GameStop's use of stored value cards, the taxpayer and customer have only agreed to the first step—the sale of the trade-in—and not to the subsequent purchase.

Although the BTA found there was a single transaction here, it is not necessary for this Court to do so because the single transaction requirement is not found in the statute, but instead is an extra requirement added by the Department in its rule. As the Supreme Court held in another tax case, “[t]o achieve such an interpretation, we would have to import additional language into the statute that the legislature did not use. We cannot add words or clauses to a statute when the legislature has

chosen not to include such language.” *Dot Foods, Inc. v. Department of Revenue*, 166 Wn.2d 912, 920, 215 P.3d 185 (2009).⁴

Recently the Louisiana Court of Appeals reversed Louisiana’s Revenue Department, which, like this state’s Department, had applied non-statutory timing requirements for a trade-in to GameStop:

[T]he plain language of La. R.S. 47:301(13)(a) does not restrict the timing of the trade in nor does it suggest that a trade in must occur simultaneously with the sale. Rather, La. R.S. 47:301(13)(a) merely states that the sales price is to be based on the total amount for which tangible personal property is sold, less the market value of any article traded in. Words defining a tax should not be extended beyond their clear import. *UTELCOM, Inc. v. Bridges*, 10–0654, p. 7 (La. App. 1st Cir. 9/12/11), 77 So.3d 39, 47, writ denied, 11–2632 (La.3/2/12), 83 So.3d 1046. Therefore, to the extent that a trade in occurs when GameStop accepts a customer’s merchandise and stores the predetermined market value of the item and/or items on an Edge Card, we find the subsequent application of the market value of the trade in by the customer toward the purchase of a new item of tangible personal property at GameStop comes within the statutory exclusion from sales price found in La. R.S. 47:301(13)(a).

GameStop, Inc. v. St. Mary’s Parish Sales & Use Tax Dept., 166 So. 3d 1090, 1096, rev. denied 171 So. 3d 929 (La. 2015). Accord *Department of*

⁴ Such an extra-statutory requirement is not entitled to deference. *Id.*

Revenue v. GameStop, Inc., 48 So. 3d 839 (Fla. 2010) (affirming *GameStop, Inc. v. Department of Revenue*, Florida Division of Administrative Hearings, No. 09-5759RX (May 4, 2010)). These decisions align with the BTA’s conclusion that trade-ins need not be contemporaneous.

The Department suggests that these cases are not analogous because these states do not require like-kind merchandise for the trade-in exemption, but that is not the issue in the cases. Instead the issue is the addition of a non-statutory timing requirement by the state’s revenue department to prohibit GameStop from applying the trade-in exemption in cases where a stored value card was used. This is precisely the same issue that faces us here.

Moreover, the Department has failed to identify any legitimate, principled reason for its artificially narrow reading of the statute. The requirement of simultaneity would undercut the value of trade-in programs—which encourage the reuse and recirculation of durable products, and democratize access to products through discounts for older used versions. With no discernible countervailing reason to preclude non-contemporaneous transactions, the Court should uphold the BTA’s appropriate conclusion.

E. GameStop's Trade-ins Are Separately Stated

To qualify for the sales tax exclusion, RCW 82.08.010(1)(a)(i) requires that the trade-in property be “separately stated.” This requirement ensures the clear identification of the nontaxable portion of the sales transaction and creates a paper trail for audit purposes. As the BTA noted, separate statement requirements are generally applied in the context of a “bundled” payment to allow parsing the non-taxable portion from the taxable portion. App. A, COL 7. Accordingly, it makes sense that Rule 274(4) requires “[t]he sales documents must identify the tangible personal property being purchased and the trade-in property being delivered to the seller.”

GameStop's trade-in program satisfies this requirement. The Department concedes that when a customer trades in property simultaneously with the purchase of additional property, the trade in is separately identified on GameStop's documentation. The Department does not recognize that when a customer acquires property using a stored-value card, GameStop separately documents the use and amount of trade-in credits. *Id.*, FOF 14-15. The Department does not dispute that GameStop states the amount of the trade-in and separates trade-ins from other portions of these kinds of transactions (such as use of cash to pay the difference when a stored-value credit does not contain sufficient funds for

a purchase). Instead, the Department takes issue with GameStop not naming the *specific product* traded in for a stored-value card on the same cash register receipt as the product subsequently purchased. However, each product is recorded on its own cash register receipt, and testimony at the hearing showed that an auditor could verify what was traded when stored value cards are used and connect the property involved in non-contemporaneous trade-ins. *See* VRP at 49-53.

Moreover, what the Department fails to acknowledge is that its argument boils down to a redux of its argument that the property at issue is not of a like kind. If the different gaming components at issue are all products of a like kind, then there is no need to drill down and connect the dots between specific types of video game components. The only items that GameStop accepts under its trade-in program are video game components. Old video game components will always be of like kind to new video game components.

V. CONCLUSION

For the above-stated reasons, this Court should uphold the ruling of the Board of Tax Appeals.

RESPECTFULLY SUBMITTED this 16th day of October, 2017.

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Declared under penalty of perjury under the laws of the state of
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APPENDIX A

BEFORE THE BOARD OF TAX APPEALS
STATE OF WASHINGTON

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2
3 GAMESTOP, INC., AND SOCOM, LLC,)
4 Appellants,) Docket No. 14-053
5 v.) RE: Excise Tax Appeal
6 STATE OF WASHINGTON) FINAL DECISION
7 DEPARTMENT OF REVENUE,)
8 Respondent.)

9
10 This matter came before the Board of Tax Appeals (the Board), with Marta B. Powell,
11 Chair, presiding, on December 8, 2015, for a formal hearing pursuant to the rules and procedures
12 set forth in chapter 456-09 WAC and chapter 34.05 RCW, the Administrative Procedure Act.
13 Attorney Michele Radosevich, of Davis Wright Tremaine, LLP, represented the Appellants,
14 GameStop, Inc., and Socom, LLC (collectively, the Taxpayer). Assistant Attorney General
15 Charles Zalesky represented the Respondent, State of Washington Department of Revenue (the
16 Department). Testifying on behalf of the Taxpayer were Michael L. Nichols, Senior Vice
17 President of International Finance and Treasurer of GameStop, and Randall L. McDowell,
18 District Manager for GameStop in Vancouver, Washington. Testifying on behalf of the
19 Department was Jim Nelson, a Revenue Auditor 3 with the Department. The record in this
20 matter was closed on January 4, 2016, following the parties' submission of proposed findings of
21 fact and conclusions of law, as requested by the Board under WAC 456-09-915.

22 Having heard the testimony, reviewed the evidence, and considered the arguments
23 presented on behalf of both parties, the Board now makes its decision as follows:

24 **NATURE OF THE CASE**

25 **Powell.** Washington imposes a retail sales tax on the sale of tangible personal property to
consumers. The measure of the tax is the property's "selling price," or "sales price," as defined
in RCW 82.08.010(1)(a)(i). The statutory definition of "sales price" includes everything of value
received in payment, "except separately stated trade-in property of like kind." Thus, under the

1 trade-in exclusion, the value of the purchaser's qualifying trade-in property is deducted from the
2 price of the newly purchased property prior to the calculation of retail sales tax on the purchase.

3 The Taxpayer is a retailer of video-gaming hardware (consoles, controllers, and
4 accessories), video games, and other merchandise. As part of its business practices and
5 marketing strategy, the Taxpayer purchases used video-game hardware and software from its
6 customers, either for cash or for a more generous amount of in-store credit. Customers may use
7 the trade-in credit in exchange for an immediate purchase of merchandise, or they may elect to
8 have the trade-in credit loaded onto a stored-value card for later use.

9 During the audit periods at issue in this appeal, the Taxpayer collected and remitted retail
10 sales tax on its Washington sales based on the sales price of the merchandise, less any trade-in
11 credit used by the customer to purchase the merchandise. The Department determined that,
12 under the statute and WAC 458-20-247 (Rule 247), the Taxpayer had incorrectly applied the
13 statutory trade-in exclusion and had, consequently, failed to collect and report retail sales tax on
14 the full sales price of the merchandise it sold. The Taxpayer challenges the Department's
15 determination.

16 ISSUES

17 1. Has the Taxpayer met its burden of proving that the trade-in value of its customers'
18 video-game hardware and software comes within the trade-in exclusion set forth in RCW
19 82.08.010(1)(a)(i), which excepts from the taxable "sales price" the value of "separately
20 stated trade-in property of like kind"?

21 a. Is the trade-in property "separately stated" within the meaning of the statute?

22 Brief Answer: Yes. The Taxpayer's sales receipts and transaction records
23 separately identify the nontaxable, trade-in property, as well as the purchased
24 items, with appropriate identifying information.

25 b. Are video-game hardware and software "property of like kind" within the
meaning of the statute?

Brief Answer: Yes. Gaming hardware and software are interdependent
components of a video-gaming system; often packaged together, gaming
hardware and software naturally fall within the general classification "gaming
components."

1 c. When trade-in value is loaded onto a stored-value card and applied to the later
2 purchase of like-kind property, is the transaction a “single transaction” within the
3 meaning of Rule 247(4)?

4 Brief Answer: Yes. The administrative rule’s single-transaction requirement
5 cannot be interpreted as adding a requirement not found in the statute itself. For
6 purposes of the statute and rule, a single transaction is completed when the
7 Taxpayer (1) applies trade-in credit to the customer’s immediate purchase of like-
8 kind property or (2) applies trade-in credit stored on a stored-value card to the
9 purchase of like-kind property.

10 2. If the trade-in exclusion were deemed inapplicable to the trade-in credits on a stored-
11 value card, does the customer’s use of the trade-in credits satisfy the definition of a “bona
12 fide discount” under WAC 458-20-108(7)?

13 Brief Answer: Having determined that the Taxpayer’s trade-in program for “gaming
14 components” comes within the trade-in exclusion set forth in RCW 82.08.010(1)(a)(i),
15 the Board need not consider the Taxpayer’s alternative argument under Rule 108(7).

16 FINDINGS OF FACT

17 The Taxpayer’s Identity and Retailing Business

18 1. GameStop, Inc., and Socom, LLC (referred to collectively as the Taxpayer), are
19 wholly owned affiliates of GameStop Corporation.

20 2. The Taxpayer is a retailer of video-gaming hardware (consoles, controllers, and
21 other accessories), video games, and other merchandise.

22 3. The Taxpayer operates approximately 82 retail stores in Washington.

23 4. The Taxpayer’s principal product lines include video-game hardware (such as the
24 Microsoft Xbox, Sony PlayStation, and Nintendo Wii consoles and controllers), video-game
25 software that runs on those consoles, and accessories.

5. Microsoft, Sony, and Nintendo produce their own consoles and controllers, as
well as their own video-game software. Each company’s hardware products are designed to be
used exclusively with that company’s software products. For example, Microsoft gaming
products cannot be used interchangeably with Sony gaming products, and vice versa.

6. Often, video-game software will only work on a single version of the
manufacturer’s console. When the manufacturer brings out a new version of the console, the

1 manufacturer will also bring out updated versions of its video-game software. Consequently, a
2 consumer seeking to upgrade his or her console will have to replace all of the video-game
3 software as well.

4 7. The video-game manufacturers often sell the console, controller, and one or more
5 games as a unit.

6 8. In order to play a video game, one needs both hardware and software. Video-
7 game consoles are incapable of running any of the software that runs on a PC or tablet, and a PC
8 or tablet will not accommodate video games designed for consoles.

9 9. Over the years, computer hardware has become extremely varied. Although
10 video-game consoles may meet the technical definition of “computer hardware” under WAC
11 458-20-15501, so could smartphones, flat-screen televisions, DVD players, digital cameras, and
12 electric automobiles. Such diverse products would not be viewed as falling within the same
13 general classification as a personal computer.

14 **The Taxpayer’s Trade-In Program**

15 10. The Taxpayer sells both new and used merchandise.

16 11. The Taxpayer offers its customers a trade-in program. The program enables
17 customers to trade in their used video-game products, whether hardware or software, either for
18 cash or for a more generous amount of in-store credit.

19 12. A customer who chooses to receive in-store credit is choosing to trade his or her
20 used merchandise for new or used in-store merchandise.

21 13. Trade-in credits may be used as consideration on the immediate purchase of
22 merchandise, or the credits may be loaded onto a stored-value card for the customer’s use at a
23 later date.

24 13.1. During most of the audit periods at issue in this appeal, the stored-value
25 cards were called Edge Cards, but in October 2010, Power Up Rewards Cards (PUR
Cards) replaced Edge Cards.

13.2. The PUR Cards are also used in connection with the Taxpayer’s loyalty
program, which rewards purchases, but trade-in credits are not commingled with the
points earned through purchases.

13.3. Stored-value cards cannot be redeemed for cash, nor can a customer use
cash to “purchase” a trade-in credit stored on a value card.

1 14. When a customer uses the trade-in credit on the immediate purchase of new or
2 used merchandise, the sales receipt at the time of trade-in itemizes both the property being
3 purchased and the property being traded in.¹

4 15. When the trade-in credit is loaded onto a stored-value card and used at a later
5 date, the sales invoice pertaining to the subsequent purchase of merchandise identifies the new
6 purchases and states the separate amount of trade-in credit that is being applied as an offset. The
7 Taxpayer maintains computerized business records from which the Taxpayer (or an auditor) can
8 identify each item of trade-in property that generated the credit on the stored-value card.

9 16. The Taxpayer has described its trade-in program as “a unique value proposition . .
10 . generally unavailable at mass merchants, toy stores and consumer electronics retailers.”² Each
11 year, the Taxpayer provides approximately \$1.2 billion in trade-in credits. The trade-in program
12 allows the Taxpayer to acquire “an inventory of used video game products” that it can “resell to
13 [its] more value-oriented customers.”³

14 17. The sale of used merchandise makes up approximately 25 percent of the
15 Taxpayer’s volume, but approximately 50 percent of its profit.

16 18. The Taxpayer counts some 30 million Americans as repeat customers, with one in
17 five U.S. households having at least one PUR Card member in the home.

18 19. The typical customer purchases both gaming hardware and software. The
19 purchase of a console, a controller, and a half-dozen video games is a substantial investment. A
20 customer who wants to upgrade to newer hardware will likely trade in all components of his or
21 her previous system, including the software. By trading in a used Sony PlayStation 4, for
22 example, for a \$250 credit, the customer would receive a meaningful offset against the outlay for
23 a new Xbox One System.

24 20. In sales transactions during the years at issue, the Taxpayer deducted the amount
25 of the customer’s trade-in credit from the taxable sales price of the merchandise the customer
was purchasing. The Taxpayer’s practice was the same, whether the customer was using trade-in
credits on the immediate purchase of merchandise or was applying credits previously stored on
an Edge Card or PUR Card.

¹ See Exhibits A7 through A11.

² Exhibit R17–11.

³ *Id.*

Procedural History

1 21. The audit periods at issue in this appeal are January 2006 through December 2010
2 (for GameStop, Inc.) and January 2008 through December 2010 (for Socom, LLC).

3 22. The Department's audit resulted in an assessment against the Taxpayer for
4 uncollected retail sales tax.

5 23. The Department concluded that the Taxpayer had improperly claimed the trade-in
6 exclusion in three respects: (1) the trade-in of video-game software on the purchase of gaming
7 consoles or accessories; (2) the trade-in of video-game hardware (consoles and accessories) on
8 the purchase of video-game software; and (3) the use of trade-in credits from a stored-value card.

9 24. The Taxpayer timely petitioned the Department's Appeals Division for review.

10 25. The Appeals Division denied the petition in Determination No. 13-0263 and
11 thereafter denied the Taxpayer's petition for reconsideration in Determination No. 13-0263R.⁴

12 26. The Taxpayer timely sought the Board's review.

13 Any Conclusion of Law that should be deemed a Finding of Fact is hereby adopted as
14 such.

15 From these findings, the Board comes to these

CONCLUSIONS OF LAW

16 1. Pursuant to RCW 82.03.130(1)(a), the Board has jurisdiction to hear and decide
17 this appeal.

18 2. RCW 82.08.020 imposes a retail sales tax on "each retail sale in this state," with
19 the tax measured by the "selling price" of the item sold.

20 3. Under RCW 82.08.010(1)(a)(i), the term "selling price," or "sales price," is
21 defined as "the total amount of consideration, except separately stated trade-in property of like
22 kind, . . . for which tangible personal property [and certain other goods and services] are sold,
23 leased, or rented, valued in money, whether received in money or otherwise."

24 4. The trade-in exclusion in RCW 82.08.010(1)(a)(i) is a tax exemption.⁵ Tax
25 exemptions must "be strictly construed, though fairly and in keeping with the ordinary meaning

⁴ The reconsideration petition pertained to an estoppel argument that the Taxpayers have since dropped and, therefore, is not an issue in this appeal.

⁵ *West Coast Yachts, Inc. v. Dep't of Revenue*, BTA Docket No. 97-9 (1998), at 12.

1 of the language employed.”⁶ Because “[a] tax exemption presupposes a taxable status . . . the
burden is on the taxpayer to establish eligibility for the benefit.”⁷

2 5. The Department adopted WAC 458-20-247 (Rule 247) in 1984 to implement and
3 explain the trade-in exclusion.

4 6. Rule 247(3) specifies that “[t]he buyer must deliver trade-in property to the
5 ‘seller’” and quotes the statutory definition of “seller” as “every person . . . making sales at retail
6 or retail sales to a buyer, purchaser, or consumer, whether as agent, broker, or principal.”⁸ The
7 trade-in property at issue in this appeal is property that a buyer (the Taxpayer’s customer) has
delivered to a retail seller (the Taxpayer).

8 7. The requirement in RCW 82.08.010(1)(a)(i) that the trade-in property be
9 “separately stated” ensures the clear identification of the nontaxable portion of the sales
10 transaction.⁹

11 7.1. The so-called “Separate Statement Rule” provides “that a transfer of
12 consideration for a ‘bundle’ of taxable and nontaxable goods will be treated as
13 nontaxable in part *only if the consideration for the nontaxable aspect of the transaction is*
14 *separately stated.*”¹⁰ The rule is generally applied in the context of a “bundled” payment
15 (for example, for an appliance and service agreement or for a restaurant meal and the
16 gratuity). Under the Separate Statement Rule, the nontaxable component (the service
17 agreement, the gratuity) must be “separately stated on the customer’s bill or invoice.”¹¹

18 7.2. Similarly, Rule 247(4) provides that “[t]he sales documents must identify
19 the tangible personal property being purchased and the trade-in property being delivered
20 to the seller.” Rule 247(8) explains, further, that the identification must be by “the model
21 number, serial number, year of manufacture, and other information as appropriate” and
22 “must also specify the selling price and the value of the trade-in property.”

23 ⁶ WAC 458-16-100(2)(c).

24 ⁷ *In re Sehome Park Care Center, Inc.*, 127 Wn.2d 774, 778, 903 P.2d 443 (1995). *See also* WAC 458-16-100
(2)(b).

25 ⁸ Rule 247(3)(a) (quoting RCW 82.08.010(2)(a)).

⁹ The legislation (effective July 1, 2014) related to the adoption of the streamlined sales and use tax agreement. *See*
2004 c 153 § 406; *see also* the note following RCW 82.08.0293.

¹⁰ Walter Hellerstein, *Separate Statement Rule*, STATE TAXATION ¶17.03[4] (3d ed. 2009) (emphasis added).

¹¹ *Id.* at ¶17.12 (3d ed. 2014).

1 8. In the present appeal, the trade-in property is “separately stated” within the
2 meaning of RCW 82.08.010(1)(a)(i). The Taxpayer’s sales documents separately identify the
3 consideration derived from the trade-in property.

4 9. In the present appeal, the Taxpayer satisfies the Rule 247 separate-statement
5 requirement because the “sales documents”—the Taxpayer’s sales receipts and transaction
6 records—separately identify the purchased items and the nontaxable, trade-in property with
7 appropriate identifying information.¹²

8 10. As the Board has previously summarized, “[f]or purposes of RCW 82.08.010 and
9 Rule 247, a ‘trade-in’ is property that is transferred from buyer to seller as a part of an exchange
10 of *similar* property.”¹³

11 11. Rule 247 defines “property of like kind” as “articles of tangible personal property
12 of *the same generic classification*”:

13 The term includes *all property within a general classification* rather than within a
14 specific category in the classification. Thus, as examples, it means furniture for
15 furniture, motor vehicles for motor vehicles, licensed recreational land vehicles
16 for licensed recreational land vehicles, appliances for appliances, *auto parts for*
17 *auto parts*, and *audio/video equipment for audio/video equipment*. These general
18 classifications are determined by the nature of the property and its function or
19 use.¹⁴

20 12. The gaming merchandise at issue in the present appeal—consoles, controllers,
21 video-games, and accessories—falls within the general category “gaming equipment” or
22 “gaming components.” The classification is analogous to the general classifications “auto parts”
23 and “audio/video equipment,” noted in the rule. The classification “auto parts” encompasses
24 everything related to the function of an automobile, from complex, interrelated computer systems
25 and their components to such low-tech replacement parts as wiper-blades. Similarly,
audio/visual equipment encompasses individual components, such as document cameras,
projectors, DVD players, and speakers. Like the general classifications “auto parts” and
“audio/visual equipment,” the general classification “gaming components” or “gaming
equipment” encompasses the various components of a video-game system.

13. For the type of “generic trade-in transfers” that come within the trade-in
exclusion, Rule 247(5) provides the following examples: “a sofa for a recliner chair, a pistol for

¹² See Findings of Fact (FF) Nos. 14 and 15.

¹³ *West Coast Yachts*, BTA Docket No. 97-9, at 12 (emphasis added).

¹⁴ Rule 247(5) (emphasis added).

1 a rifle, a sailboat for a motorboat, or a gold chain for a wrist watch.” Implicit in the examples are
2 the general classifications “furniture,” “firearms,” “water craft,” and “jewelry.” The general
3 classification “gaming components” is no broader than the sample classifications. The sample
4 classifications allow the trade in of items with little similarity and no interdependence (a
5 bookcase for a loveseat or, as the Taxpayer suggests, “a drugstore watch for a diamond ring”).¹⁵
6 The classification “gaming components” is a narrower, more coherent classification and, as the
7 rule elsewhere requires, is more focused on “the nature of the property and its function or use.”¹⁶

8 14. Rule 247(5) also suggests that the trade-in exclusion “does not include such things
9 as a motorcycle for a boat, a diamond ring for a television set, a battery for lumber, *computer*
10 *hardware for computer software*, or farm machinery (including tractors and self-propelled
11 combines) for a car.”

12 14.1. The meaning of “computer hardware” and “computer software” in the
13 Rule 247 list is controlled by the meaning of the rule’s four other paired items: “Under
14 the doctrine of ‘noscitur a sociis,’ the meaning of words may be indicated or controlled
15 by those with which they are associated.”¹⁷ Just as the “function or use” of the other
16 paired items precludes a classification that encompasses both items, the pairing of
17 “computer hardware” and “computer software” can refer only to computer hardware and
18 software that, in “function or use,” cannot be encompassed in a single classification. In
19 other words, the hardware and software referred to in the rule’s list can be no more
20 similar in “function or use” than, to take one of the other four examples, “a diamond ring
21 [and] a television set.”

22 14.2. Because the terms “computer hardware” and “computer software” in Rule
23 247’s list denote unrelated items of hardware and software, the terms have no bearing on
24 the computer hardware and software at issue in the present appeal. Gaming hardware
25 (consoles and controllers) and gaming software (video games) are interdependent
components of an integrated system.¹⁸ Often packaged together, gaming hardware and
software are bound together in their “function or use” and fall within the general
classification “gaming components.”

¹⁵ GameStop’s Reply Brief, p. 2.

¹⁶ Rule 247(5).

¹⁷ *Ball v. Stokely Foods*, 37 Wn.2d 79, 87-88, 221 P.2d 832 (1950). See *City of Seattle v. Allison*, 148 Wn.2d 75, 81, 59 P.3d 85 (2002) (noting that “[r]ules of statutory construction apply to administrative rules and regulations”).

¹⁸ See FF Nos. 4-8, above.

1 15. That a gaming console may perform other functions does not diminish the
interdependence between the video games and the console.¹⁹

2 16. That gaming consoles may meet the definition of “computer hardware” in WAC
3 458-20-15501 (Rule 15501) does not affect the analysis of whether gaming hardware and
4 gaming software are like-kind property for purposes of RCW 82.08.010(1)(a)(i) or Rule 247.
5 The Rule 15501 definition of computer hardware is so broad that a diverse group of products
6 could satisfy the definition without themselves comprising, in their “function or use,” a coherent
7 general classification of property.²⁰ The Rule 15501 definition of “computer hardware” is not
cited or incorporated in Rule 247.

8 17. Video-game hardware and software are “gaming components” and are “property
9 of like kind” within the meaning of RCW 82.08.010(1)(a)(i) and Rule 247.

10 18. Rule 247(4) requires that “the delivery of the trade-in and the purchase [must] be
components of a single transaction.”

11 18.1. RCW 82.08.010(1)(a)(i) does not include the phrase “single transaction.”

12 18.2. The rule’s single-transaction requirement does not restrict the trade-in
13 exclusion to the trade in of a single item for another single item. As Rule 247(2)(a)
14 explains, “if a buyer trades in two motor vehicles when purchasing one motor vehicle, the
15 buyer is entitled to a reduction in the measure of retail sales tax based on the value of
both trade-in vehicles.”

16 18.3. The rule’s single-transaction requirement does not require the
17 “simultaneous transfer of the property being traded in and the property being
18 purchased.”²¹ The purchased property may be transferred to the buyer well after the
19 buyer’s delivery of the trade-in property to the seller.

20 18.4. The rule’s single-transaction requirement is not met if the trade-in
21 transaction is contingent upon a separate transaction, such as a consignment sale. The
22 four examples provided in Rule 247(4) demonstrate this point. In examples (b) and (d),
23 the trade-in exclusion is allowable because, in each instance, the seller agrees to accept
24 the purchaser’s trade-in property as an offset against the purchase price of other property:
in example (b), Sally trades in a motor home (leaving it with the dealer) for a new motor

25 ¹⁹ See *id.* and FF No. 19, above.

²⁰ See FF No. 9.

²¹ Rule 247(4).

1 home that the dealer delivers eight months later; in example (d), John trades in a travel
2 trailer for a new one, subject to the dealer's agreement to pay certain financing costs on
3 the trade-in. On the other hand, in examples (a) and (c), the trade-in exclusion is not
4 allowable because, in each instance, the seller requires an intermediate transaction. The
5 seller declines to accept the purchaser's property as a trade-in but accepts it instead on
6 consignment. The use of the purchaser's property as a trade-in is thus contingent on the
7 seller's completion of a separate transaction with another buyer.

8 19. In the present appeal, the Taxpayer does not make its offer of trade-in value
9 contingent on an intermediate transaction (that is, on the Taxpayer's successful sale of the trade-
10 in property to another customer). The Taxpayer offers cash or trade-in value for the customer's
11 "gaming equipment." When the customer elects trade-in value, rather than cash, the Taxpayer
12 and customer agree that the customer may (1) immediately apply the trade-in value as
13 consideration for a new purchase of "gaming components" or (2) may apply the trade-in credit
14 stored on a stored-value card to the later purchase of "gaming equipment." In either case, the
15 rule's single-transaction requirement is met: the Taxpayer and customer agree that the agreed-
16 upon trade-in value of the customer's "gaming components" will provide an offset against the
17 customer's purchase of "gaming equipment."

18 20. The rule's single-transaction requirement does not explicitly or clearly impose a
19 timing requirement on the trade-in agreement between the Taxpayer and its customers. To
20 conclude otherwise would be to discern in the rule a requirement not found in the plain language
21 of the statute itself.²² RCW 82.08.010(1)(a)(i) requires that the trade-in value be "separately
22 stated" and that the trade-in property be "property of like kind." Neither the statute nor Rule 247
23 states that the consideration for the "separately stated trade-in property of like kind" be
24 immediately applied to the purchase of like-kind property.²³

25 21. Having concluded that the Taxpayer is entitled to the trade-in exclusion in RCW
82.08.010(1)(a)(i), the Board need not consider the Taxpayer's alternative argument that a
customer's trade-in credits on a stored-value card satisfy the definition of a "bona fide discount"
under Rule 108(7).

²² See *Dot Foods, Inc. v. Dep't of Revenue*, 166 Wn.2d 912, 920, 215 P.3d 185 (2009) (declining "to import additional language into the statute that the legislature did not use").

²³ See *GameStop, Inc. v. St. Mary's Parish Sales & Use Tax Dep't*, 166 So.3d 1090, 1096 (La. Ct. App. 2015) (concluding that "the plain language of [Louisiana's statutory trade-in exclusion] does not restrict the timing of the trade in nor does it suggest that a trade in must occur simultaneously with the sale").

1 Any Finding of Fact that should be deemed a Conclusion of Law is hereby adopted as
2 such.

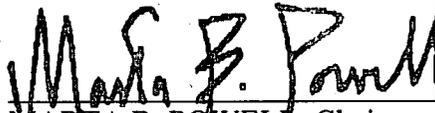
3 From these conclusions, the Board enters its

4 **DECISION**

5 Pursuant to RCW 82.03.130(1)(a) and WAC 456-09-010(1) and -920, the Board grants
6 the Taxpayer's appeal and orders the Department to amend its assessment to accord with this
7 decision.

8 DATED this 19th day of May, 2016.

9 BOARD OF TAX APPEALS

10 
MARTA B. POWELL, Chair

11 
MARK J. MAXWELL, Vice Chair

12 
CAROL A. LIEN, Member

13 **Right of Reconsideration of a Final Decision**

14 Pursuant to WAC 456-09-955, you may file a petition for reconsideration
15 of this Final Decision. You must file the petition for reconsideration with the
16 Board within 10 business days of the date of mailing of the Final Decision. The
17 petition must state the specific grounds upon which relief is requested. You must
18 also serve a copy on all other parties and their representatives of record. The
19 Board may deny the petition, modify its decision, or reopen the hearing.

20 Please be advised that a party petitioning for judicial review of a Final
21 Decision is responsible for the reasonable costs incurred by this agency in
22 preparing the necessary copies of the record for transmittal to the superior court.
23 Charges for the transcript are payable separately to the court reporter.
24
25

CERTIFICATE OF MAILING

I certify that on May 19, 2016, I personally forwarded by United States mail or e-mailed, a true and correct copy of the attached document to the following:

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