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DIVISION II, COURT OF APPEALS
OF THE STATE OF WASHINGTON

LENDINGTREE, LLC,

Plaintiff-Appellant

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Defendant-Respondent

ON APPEAL FROM THURSTON COUNTY SUPERIOR COURT
(Hon. Christine Schaller)

BRIEF OF APPELLANT

Scott M. Edwards, WSBA No. 26455
Ryan P. McBride, WSBA No. 33280
Daniel A. Kittle, WSBA No. 43340
*Attorneys for Plaintiff-Appellant
LendingTree, LLC*

LANE POWELL PC
1420 Fifth Avenue, Suite 4200
P.O. Box 91302
Seattle, WA 98111-9402
Telephone: 206.223.7000
Facsimile: 206.223.7107

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I. INTRODUCTION

This is a tax refund case focused on the proper apportionment of Appellant LendingTree, LLC's service income. LendingTree operates an online loan referral service, matching potential borrowers with interested lenders all around the country based on loan qualification criteria provided by the lenders. The lenders pay LendingTree fees for this service and, thus, the lenders—not the borrowers—are LendingTree's customers. The parties agree that proper apportionment of LendingTree's income—and the sole issue on appeal—turns on where its lender customers “received the benefit” of LendingTree's services. RCW 82.04.462(3)(b)(i).

The parties also agree that a DOR rule defines that term in this context, and dictates that LendingTree's lender customers receive the benefit of its services where the lenders' “related business activities occur.” WAC 458-20-19402(303)(c). Here, the undisputed evidence shows that LendingTree's customers conduct their lending activities at their business locations, where they receive the borrower's information from LendingTree and, in turn, process, evaluate and respond to the potential borrower's loan request. For LendingTree's out-of-state lender customers, it is also undisputed that they engage in no activity in Washington—even when their potential borrowers reside in Washington.

Flouting the plain language of its own rule, DOR ignored the undisputed location of the lenders' activities when apportioning LendingTree's income, and, instead, attributed LendingTree's income exclusively to where the potential borrowers reside. That was error. LendingTree's customers are the lenders, not the potential borrowers, and it is undisputed that the lender customers did not engage in any activities where the potential borrowers reside. The trial court's summary judgment affirming DOR's incorrect assessment must be reversed, and the case remanded for proper apportionment.

II. ASSIGNMENT OF ERROR

The trial court erred when it granted DOR's motion for summary judgment and denied LendingTree's cross-motion, thereby dismissing LendingTree's claim for a tax refund with prejudice. CP 323-24.

III. STATEMENT OF ISSUE

The proper apportionment of LendingTree's service income for purposes of B&O tax turns on where LendingTree's lender customers received the benefit of LendingTree's services. By rule, LendingTree's customers received the benefit of LendingTree's services where their "related business activities occur." The issue on appeal is whether LendingTree's lender customers receive the benefit of LendingTree's services in the state where they receive and act on LendingTree's referrals,

or in the state where potential borrowers reside (even though the lenders conduct no activities at the potential borrowers' residences).

IV. STATEMENT OF THE CASE

A. Undisputed Facts

LendingTree is in the business of matching lenders with potential borrowers through an online marketplace. CP 150 (Boardwine Decl., ¶ 3). Lenders pay LendingTree a "matching" fee when a potential borrower is directed to a lender's website or the borrower's information is forwarded to the lender. *Id.* (¶ 4). Some lenders also pay LendingTree a "closed loan" fee when the lender closes a loan stemming from a LendingTree referral. *Id.*; *see also* CP 183 (Boardwine Decl., Ex. 2, at 00078). Thus, as DOR conceded below, it is the lenders, not the potential borrowers, who are LendingTree's customers. CP 18. During the relevant period, 26 of these lender customers were located in Washington. CP 150, 156-60 (Boardwine Decl., ¶ 3 & Ex. 1).

Potential borrowers using LendingTree's website can input information about themselves, select the type of loan they seek, and request to be contacted by interested lenders. CP 151, 194-95 (Boardwine Decl., ¶ 5 & Ex. 2, at 00041-42); CP 138 (Gates Decl., ¶ 6). LendingTree compares the potential borrower's information against loan qualification criteria set by its lender customers, and then refers the potential borrower

to several lenders whose criteria match the borrower's qualifications. CP 194-95 (Boardwine Decl., Ex. 2, at 00041-42).

LendingTree makes the referral by electronically transmitting the potential borrower's information to its lender customers at a business location specified by each lender. CP 151, 195 (Boardwine Decl., ¶ 5 & Ex. 2, at 00042); CP 138 (Gates Decl., ¶ 7). The lenders receive the information at their specified business location, which can be anywhere in the country, where they process, evaluate and respond to the potential borrower's loan request. CP 151, 196 (Boardwine Decl., ¶ 6 & Ex. 2, at 00043); CP 138 (Gates Decl., ¶ 7: "That electronic information is generally received by Quicken Loans in Michigan, and Quicken Loans processes or uses that information in the course of its business activities").

B. Procedural Background

DOR audited LendingTree and assessed LendingTree additional B&O tax, penalties and interest for the period June 1, 2010 through June 30, 2014. CP 230-35. DOR determined that LendingTree's customers received the benefit of LendingTree's services "based on where the [borrower] seeking the loan is located," not where the lender is located. CP 233 (DOR 000106). Thus, for fees LendingTree earned for referring a potential borrower located in Washington to an out-of-state lender, DOR attributed the income to Washington—even though the lender customer

conducted no activity in Washington. *Id.* DOR denied LendingTree’s administrative appeal. CP 242-53.

After LendingTree paid the assessment in full, it filed this *de novo* complaint under RCW 82.32.150 and .180, seeking a tax refund in the amount of \$196,236.28. CP 1-5. LendingTree and DOR filed cross-motions for summary judgment. The trial court heard oral argument on November 16, 2018, after which it orally ruled in favor of DOR:

The service that LendingTree offers is to obtain qualification forms from consumers . . . and to have consumers seek loans from a pool of LendingTree’s clients, and this all happens where the consumer is located.

VRP at 17. The court thereafter entered a written order granting DOR’s motion for summary judgment, and denying LendingTree’s cross-motion. CP 323-24. LendingTree timely appealed. CP 325-29.¹

V. ARGUMENT

A. Standards of Review

LendingTree has the burden of showing that DOR incorrectly assessed the tax and that it is entitled to a refund. RCW 82.32.180. The

¹ LendingTree also challenged DOR’s “proportional attribution” of LendingTree’s gross income based on an improper retroactive application of the current version of RCW 82.04.462, which was not effective until June 12, 2014—a mere 19 days before the end of the audit period. Without conceding the correctness of DOR’s position on this issue, LendingTree has elected not to raise this error on appeal.

trial court upheld DOR's tax assessment on summary judgment. This Court reviews summary judgment orders *de novo*, engaging in the same inquiry as the trial court. *Irwin Naturals v. Dep't of Revenue*, 195 Wn. App. 788, 793, 382 P.3d 689 (2016). Summary judgment is proper only when there are no genuine issues of material fact and the moving party is entitled to judgment as a matter of law. *Id.*; CR 56(c).

The proper interpretation of a statute is also a question of law that this Court reviews *de novo*. *Estate of Ackerley v. Dep't of Revenue*, 187 Wn.2d 906, 909, 389 P.3d 583 (2017). The goal is to determine the legislature's intent by giving effect to the plain meaning of the statute, gleaned both from the words of that statute and those in related statutes. *Id.* at 910. "When its meaning is in doubt, a tax statute must be construed most strongly against the taxing power and in favor of the taxpayer." *Lamtec Corp. v. Dep't of Revenue*, 170 Wn.2d 838, 842-43, 246 P.3d 788 (2011) (internal quotation marks and citation omitted).

DOR's rules are not binding, but where a tax statute is subject to more than one reasonable interpretation, Washington courts may defer to DOR's interpretation. *Ass'n of Wash. Bus. v. Dep't of Revenue*, 155 Wn.2d 430, 446-47 & n.17, 120 P.3d 46 (2005). In such cases, DOR's interpretive rules are afforded "great weight" and can help "fill in the gaps where necessary." *Solvay Chem., Inc. v. Dep't of Revenue*, 4 Wn. App.2d

918, 925, 927, 424 P.3d 1238 (2018). Washington courts “apply normal rules of statutory construction” to DOR’s rules. *Id.* at 927.

B. LendingTree’s Income Must Be Apportioned Based On Where Its Customers Receive The Benefit Of LendingTree’s Services.

Washington’s B&O tax applies to gross income derived from “the act or privilege of engaging in business activities” in Washington. RCW 82.04.220(1). In computing the tax, a business engaged in service activity in more than one state is entitled to apportion its gross income so that it is only taxed on that income fairly attributed to its activities in Washington. RCW 82.04.460; *see Smith v. State*, 64 Wn.2d 323, 391 P.2d 718 (1964). To accomplish this, in 2010, the Washington legislature enacted RCW 82.04.462, which adopted a “single factor receipts” apportionment scheme for service income. *See* Laws of 2010, 1st Spec. Sess., ch. 23, § 101(2).

The statute requires the taxpayer to multiply its gross income by a fraction, the numerator of which is income attributable to Washington and the denominator of which is income earned from activities engaged “everywhere in the world.” RCW 82.04.462(2), (3)(a). To determine where income should be attributed, the statute provides that the taxpayer’s income must be attributed to the state, “[w]here the customer received the benefit of the taxpayer’s service.” RCW 82.04.462(3)(b)(i).

DOR issued WAC 458-20-19402 (Rule 19402) to give guidance on its interpretation of the statute. And, in particular, Rule 19402(303) explains how to determine where a taxpayer's customer receives the benefit of the taxpayer's service. The rule provides in relevant part:

If the taxpayer's service does not relate to real or tangible personal property, the service is provided to a customer engaged in business, and the service relates to the customer's business activity, then the benefit is received ***where the customer's related business activities occur.***

WAC 458-20-19402(303)(c) (emphasis added). The statute and rule define "customers" as the person or entity "to whom the taxpayer . . . renders services or from whom the taxpayer otherwise receives gross income of the business." RCW 82.04.462(3)(b)(viii); WAC 458-20-19402(106)(e).

There is no dispute that LendingTree's customers are the lenders that pay LendingTree the matching and closed loan fees.² CP 18. Thus, for purposes of apportioning LendingTree's income, RCW 82.04.462 and Rule 19402 dictate that the lenders received the benefit of LendingTree's services where the *lenders'* "related business activities occurred." For the reasons explained below, LendingTree's out-of-state lender customers' related business activities occurred in the states where their businesses

² In 2010 and 2011, LendingTree also earned commission revenue from real estate brokerage services and other minor, miscellaneous income during the audit period. LendingTree did not challenge DOR's sourcing of this other income, only its matching and closed loan fee income.

were located, not where potential borrowers happened to reside. The record is undisputed that LendingTree's lender customers did not engage in any activities at the potential borrowers' residences.

C. LendingTree's Customers' Related Business Activities Occur Where They Are Located And Act On LendingTree's Referrals, Not Where The Potential Borrowers Reside.

In assessing B&O tax, DOR attributed LendingTree's matching and closed loan fee income exclusively to the states where the potential borrowers resided, rather than the states where LendingTree's lender customers conducted their business activities. CP 230-35 (audit); CP 242-53 (appeal). The trial court did the same thing. VRP at 17. In so doing, both DOR and the trial court erroneously ignored the plain meaning of DOR's own interpretive rule and the undisputed facts.

RCW 82.04.462(3)(b) dictates that LendingTree's gross income must be apportioned according to "where the customer received the benefit of the taxpayer's service." DOR recognized that this term is inherently subject to more than one interpretation because the taxpayer, the taxpayer's customer, the consumer, and the taxpayer's service may all be sourced to different states. So DOR promulgated Rule 19402 to give taxpayers an "explanation and examples" to "provide the framework for determining where the benefit of a service is received." WAC 458-20-

19402(301)(a) & (303). Rule 19402 is therefore entitled to great weight and should control here. *Solvay Chem.*, 4 Wn. App.2d at 927.

The rule supplies a straightforward analysis. In cases not involving property, the benefit is received “where the *customer’s* related business activities occur.” WAC 458-20-19402(303)(c) (emphasis added). The rule focuses on the taxpayer’s customer (in this case, the lender), not the consumer (in this case, the potential borrower). Giving these terms their plain and ordinary meaning, then, one must determine *what* LendingTree’s lender customers’ “related business activities” were, and *where* those activities occurred. For LendingTree’s out-of-state lenders, the rule dictates that LendingTree’s income cannot be attributed to Washington.

First, as to the “what,” the parties agree that LendingTree’s customers were the lenders. LendingTree matched potential borrowers with the lenders based on the borrowers’ information and the lenders’ loan criteria, and then forwarded that information to appropriate lenders for evaluation, processing and use. CP 150-51 (Boardwine Decl., ¶¶ 3-6); CP 138 (Gates Decl., ¶¶ 6-7). Plainly, LendingTree’s loan matching, filtering, and referral services related to its customers’ activities in offering, considering and authorizing consumer loans. Indeed, not only is that the lenders’ *related* business activity, the record contains no evidence that LendingTree’s lender customers engaged in any *other* business activity.

Second, as to the “where,” it is undisputed that LendingTree’s customers conducted their lending activities at their specified business locations. That is where LendingTree sent and the lenders received the borrowers’ information, and where the lenders evaluated and responded to loan requests—and, when potential borrowers were qualified, where the lenders authorized the loans. CP 151 (Boardwine Decl., ¶¶ 5-6); CP 138 (Gates Decl., ¶¶ 4-7). Putting the “what” and “where” together, Rule 19402(303) dictates that when LendingTree’s lender customers specified an out-of-state business location, none of the fees they paid LendingTree can be attributed to Washington for purposes of apportionment. Conversely, all of the income LendingTree earned from its 26 lender customers located in Washington is attributable to Washington.

It was error for DOR (and the trial court) to source income to Washington in those instances where the out-of-state lender’s potential borrower resided in Washington. Under Rule 19402(303)(c), the benefit of the taxpayer’s services is received where the taxpayer’s *customer* conducts its business, not where the customer’s ultimate consumer resides or even where the taxpayer performs the service. Because it is undisputed that the lender customers conduct no activity there, the location where the lenders’ potential borrowers resided and/or accessed LendingTree’s online service

is entirely irrelevant to determining “where the [lenders] received the benefit of the [LendingTree’s] service.” RCW 82.04.462(3)(b).

Indeed, there is no evidence whatsoever that LendingTree’s out-of-state lender customers performed *any* business activities in Washington. Regardless of where a potential borrower resided, it is undisputed that the lender received the borrower’s information, evaluated it, responded to the borrower’s loan request, and acted on it *from* the lender’s out-of-state business location. Even if it is presumed that potential borrowers interacted with lenders from their residences in Washington, the activities of the borrowers are irrelevant under Rule 19402(303)(c). Again, the lenders, not the borrowers, are LendingTree’s customers—and, thus, only the activities of the lenders count for purposes of apportionment.

In sum, when LendingTree’s lender customer is located in Washington, the lender receives the benefit of LendingTree’s service in Washington. When the lender is located and conducts its activities outside Washington, the benefit of LendingTree’s service is received outside Washington. LendingTree properly reported income based on where its customers were located and therefore received the benefit of its services. DOR improperly attributed income according to the residence of the potential borrower. Since LendingTree’s customer, the lender, did not

engage in any activity at the potential borrower's residence, DOR's assessment is contrary to its own rule and the statute it implements.

VI. CONCLUSION

The trial court's judgment must be reversed, and judgment entered in favor of LendingTree with instructions to remand the case to DOR for proper attribution and apportionment of LendingTree's income based on where the business activities of LendingTree's lender customers occurred.

Respectfully submitted this 26th day of February, 2019.

LANE POWELL PC

By s/Scott M. Edwards

Scott M. Edwards, WSBA No. 26455

Ryan P. McBride, WSBA No. 33280

Daniel A. Kittle, WSBA No. 43340

Attorneys for Appellant LendingTree, LLC

1420 Fifth Ave. Ste. 4200

Seattle, WA 98111-9402

Telephone: 206-223-7000

edwardss@lanepowell.com

CERTIFICATE OF SERVICE

I hereby certify that on February 26, 2019, I caused to be served a copy of the foregoing document to be delivered in the manner indicated below to the following person at the following address:

Charles Zalesky Assistant Attorney General Attorney General's Office 7141 Cleanwater Drive SW Olympia, WA 98504-0123 ChuckZ@atg.wa.gov Jamief@atg.wa.gov REVOlyEF@atg.wa.gov	<input checked="" type="checkbox"/> by JIS/ECF <input type="checkbox"/> by Electronic Mail <input type="checkbox"/> by Facsimile <input type="checkbox"/> by U.S. First-Class Mail <input type="checkbox"/> by Hand Delivery <input type="checkbox"/> by Overnight Delivery
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DATED: February 26, 2019.

s/Lou Rosenkranz

Lou Rosenkranz, Legal Assistant
Email: rosenkranzl@lanepowell.com

LANE POWELL PC
1420 Fifth Ave., Suite 4200
P.O. Box 91302
Seattle, WA 98111-9402
Telephone: 206.223.7000
Facsimile: 206.223.7107

LANE POWELL PC

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