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**SUPREME COURT OF THE STATE OF WASHINGTON**

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HOMESTREET, INC., HOMESTREET CAPITAL CORPORATION, and  
HOMESTREET BANK,

Petitioners,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Respondent.

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**SUPPLEMENTAL BRIEF OF RESPONDENT DEPARTMENT OF  
REVENUE**

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**ORIGINAL**

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## I. INTRODUCTION

HomeStreet, Inc., HomeStreet Capital Corporation, and HomeStreet Bank (“the servicers”) originate mortgage loans but then sell them to third parties and, by contract, retain a right to service the loans in exchange for fees. The owners of the loans receive interest; the servicers do not. The income the servicers receive is compensation for providing loan administration services to the owners of mortgage loans.

In this action, the servicers seek a refund of the business and occupation (B&O) taxes they paid for the servicing fee income they received during the month of January 2003, claiming this non-interest income was deductible under RCW 82.04.4292. This statute allows a deduction from gross income for “amounts derived from interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties.” Unable to prove that they owned the loans and therefore earned interest from the loans, the servicers argue that the statute should extend to the amounts they received as servicing fees, describing those fees as “amounts derived from interest received on investments or loans.”

The servicers’ reading of “derived from” should be rejected. The phrase “amounts derived from interest” in the statute is not susceptible to the single reading the servicers advance; the words can be equally

understood as the amounts paid as interest to a lender. Indeed, reading the words in a wooden, literal manner as the servicers do would suggest that the interest income itself is not deductible because it is not “derived from” interest; it *is* interest. As shown below, when the statutory language is examined in the context of related statutes and in light of its history, the only sound conclusion is that the deduction does not extend to the servicers’ non-interest income. The judgment of the Court of Appeals should be affirmed.

## II. ARGUMENT

### A. **The Servicers’ “Plain Meaning” Arguments Ignore Sound Principles of Statutory Construction and Would Defeat Rather Than Carry Out the Intent of the Legislature**

Unable to prove that the servicing fees they received were actually interest, the servicers’ principal argument seems to be that their servicing fees qualify for the deduction in RCW 82.04.4292 under the “plain language of the statute” regardless of whether their “receipts were ‘interest.’” See Br. of Appellants at 13-14, 17; Appellants’ Reply Br. at 2-6; Pet. for Review at 1, 7-11, 13-15. The servicers’ “plain meaning” arguments are unsound.

The basic goal of all statutory construction is “to carry out the intent of the Legislature.”<sup>1</sup> In ascertaining legislative intent, a court “must look at the whole statute, rather than the single phrase at issue.”<sup>2</sup> The “plain meaning” of a statute can only be determined after examining “all that the Legislature has said in the statute and related statutes which disclose legislative intent about the provision in question.”<sup>3</sup>

As explained in more detail below, this deduction was enacted in 1970 as an amendment to former RCW 82.04.430. The deduction was recodified in 1980 in its present form as RCW 82.04.4292.

**1. The measure of the B&O tax defined in RCW 82.04.080 suggests that the phrase “amounts derived from interest” in RCW 82.04.4292 means only interest income.**

RCW 82.04.4292 provides that “amounts derived from interest received on investments or loans primarily secured by first mortgages” may be “deducted from the measure of tax” by taxpayers engaged in financial businesses. Consequently, to understand the Legislature’s intent in enacting this deduction, it is necessary to read this section in context with the rest of chapter 82.04 RCW. Financial businesses are taxed under RCW 82.04.290(2), which provides that “the amount of tax” is equal to

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<sup>1</sup> *Perry v. Island Sav. & Loan Ass’n*, 101 Wn.2d 795, 806, 684 P.2d 1281 (1984).

<sup>2</sup> *In re Sehome Park Care Ctr.*, 127 Wn.2d 774, 778, 903 P.2d 443 (1995).

<sup>3</sup> *Dep’t of Ecology v. Campbell & Gwinn, LLC*, 146 Wn.2d 1, 11-12, 43 P.3d 4 (2002).

the “gross income of the business” multiplied by the rate of 1.5%. Thus, the “measure of tax” referred to in RCW 82.04.4292 is the “gross income of the business,” which is defined in an all-inclusive manner as

the value proceeding or accruing by reason of the transaction of the business engaged in and includes gross proceeds of sales, *compensation for the rendition of services*, gains realized from trading in stocks, bonds, or other evidences of indebtedness, *interest*, discount, rents, royalties, *fees*, commissions, dividends, and other emoluments however designated[.]

RCW 82.04.080 (italics added).<sup>4</sup>

In *Clifford v. State*, 78 Wn.2d 4, 5-7, 469 P.2d 549 (1970), this Court construed RCW 82.04.390, a similarly-phrased B&O statute exempting “gross proceeds derived from the sale of real estate.” The taxpayers in *Clifford* received interest income under installment contracts for the sale of real estate as part of their gross income from subdividing and selling real estate. They argued that this statutory phrase meant not only the selling price of the real estate, but also the interest from the installment contracts. This Court rejected their argument, holding that the phrase applied only to the selling price. This Court reasoned that its interpretation of RCW 82.04.390 was in harmony with RCW 82.04.080. This Court reasoned it was evident that the Legislature in enacting chapter 82.04 RCW “did not regard interest as part of the selling price, since it

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<sup>4</sup> “Value proceeding or accruing” is defined in RCW 82.04.090 as “the consideration, whether money, credits, rights, or other property expressed in terms of money, actually received or accrued.”

listed these two items separately” as component parts of the “gross income of the business.” 78 Wn.2d at 6.

A similar analysis is appropriate here. When the Legislature enacted the first mortgage interest deduction statute in 1970, financial businesses in Washington and other states had been receiving fees for servicing mortgages for Fannie Mae, insurance companies, and other secondary market investors for several decades.<sup>5</sup> Since the Legislature recognized in RCW 82.04.080 that compensation for the rendition of services and fees are different types of gross income than interest, it would have mentioned any such non-interest types of income explicitly in RCW 82.04.4292 if it had intended to allow financial businesses to deduct them.

**2. The purpose of the parallel deduction in RCW 82.04.4293 suggests that the phrase “amounts derived from interest” in RCW 82.04.4292 means only interest income.**

RCW 82.04.390 is not the only tax preference with phrasing similar to that in RCW 82.04.4292. When the Legislature amended former RCW 82.04.430 in 1970, it added not only the first mortgage interest deduction now codified as RCW 82.04.4292, but also a parallel deduction for “amounts derived from interest paid on all obligations of the

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<sup>5</sup> See *Securities-Intermountain, Inc. v. United States*, 460 F.2d 261, 261-62 (9th Cir. 1972); *Malcolm MacDowell & Associates, Inc. v. Ecorse-Lincoln Park Bank*, 325 Mich. 591, 592-93, 38 N.W.2d 921 (1949); *John T. Stewart III Trust v. Comm’r*, 63 T.C. 682, 684-85 (1975); *First Pa. Banking & Trust Co. v. Comm’r*, 56 T.C. 677, 678-79 (1971); *Realty Loan Corp. v. Comm’r*, 54 T.C. 1083, 1084-87 (1970), *aff’d*, 478 F.2d 1049 (9th Cir. 1973).

state of Washington, its political subdivisions, and municipal corporations organized pursuant to the laws thereof,” now codified as RCW 82.04.4293. Laws of 1970, 1st Ex. Sess., ch. 101, § 2 (Appendix at A-7 to A-9). This deduction, modeled after common state income tax exemptions or deductions for in-state municipal bonds, is designed to make Washington state municipal bonds more attractive in the bond market.<sup>6</sup>

Given the purpose of RCW 82.04.4293, the Legislature logically would have intended the phrase “amounts derived from interest paid on” such state and local debt obligations to mean only the interest income received on such obligations.<sup>7</sup> In nearly four decades since RCW 82.04.4293 was enacted, no Washington taxpayer appears to have ever contended that this municipal bond interest deduction extends more broadly to non-interest income. If the 1970 Legislature intended “amounts derived from interest” in RCW 82.04.4293 to mean only interest income, then it also must have intended the identical phrase to mean only interest income in RCW 82.04.4292.

**3. Cases interpreting similar language in RCW 82.04.4282 and RCW 82.04.4286 suggest that “amounts derived from interest” in RCW 82.04.4292 means only interest income.**

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<sup>6</sup> See *Dep’t of Revenue of Ky. v. Davis*, \_\_\_ U.S. \_\_\_, 128 S. Ct. 1801, 1805-07, \_\_\_ L. Ed. 2d \_\_\_ (2008) (explaining the purpose and history of such differential tax schemes).

<sup>7</sup> See WAC 458-20-146; WAC 458-28-030.

When the Legislature amended former RCW 82.04.430 in 1970, that section contained two existing subsections beginning with the phrase “amounts derived from.” Former RCW 82.04.430(2) (now RCW 82.04.4282) allowed a deduction for “[a]mounts derived from bona fide initiation fees, dues, contributions, donations, tuition fees, charges made for the operation of privately operated kindergartens, and endowment funds.” Former RCW 82.04.430(6) (now RCW 82.04.4286) allowed a deduction for “[a]mounts derived from business which the state is prohibited from taxing under the Constitution of this state or the Constitution or laws of the United States.” Both of these existing deductions were contained in the original B&O tax statute enacted in 1935.<sup>8</sup> Thus, the phrase “amounts derived from” already had a 35-year history in this statute when it was used in the 1970 act.

The State Tax Commission, the Department’s predecessor agency, long had interpreted the language in RCW 82.04.430(2) to allow deductions only for bona fide initiation fees, dues, contributions, donations, tuition fees, or endowment funds, beginning with the Tax Commission’s first set of rules adopted in 1936. (See Appendix, at A-37 to A-39.)<sup>9</sup> This Court upheld the Tax Commission’s interpretation of

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<sup>8</sup> Laws of 1935, ch. 180, § 12.

<sup>9</sup> The Tax Commission’s rules are on file at the Washington State Archives. *In re Sehome Park Care Ctr.*, 127 Wn.2d 774, 779-80 & nn.1-3, 903 P.2d 443 (1995).

former RCW 82.04.430(2) in *Red Cedar Shingle Bureau v. State*, 62 Wn.2d 341, 346-47, 382 P.2d 503 (1963). This Court held that payments the Bureau's members made to it to support its inspection service, trade promotion and advertising, and lobbying activities could not be deducted under former RCW 82.04.430(2) because the payments were neither "dues" nor "contributions."

Similarly, for several decades, this Court consistently has interpreted the language in RCW 82.04.4286 (formerly RCW 82.04.430(6)) as providing a deduction only for tax amounts that "the state is prohibited from taxing" under the state constitution or federal law.<sup>10</sup>

**4. Cases interpreting similar language in RCW 82.16.050 suggest that the phrase "amounts derived from interest" in RCW 82.04.4292 means only interest income.**

When the Legislature enacted the first mortgage interest deduction in 1970, the public utility tax (a related gross receipts tax imposed on public utilities instead of the B&O tax) also contained a deduction section, RCW 82.16.050, that was structured like former RCW 82.04.430. It similarly provided that "[i]n computing tax there may be deducted from the gross income the following items," followed by several subsections

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<sup>10</sup> See, e.g., *Coast Pac. Trading, Inc. v. Dep't of Revenue*, 105 Wn.2d 912, 918 & n.3, 719 P.2d 541 (1986); *Crown Zellerbach Corp. v. State*, 45 Wn.2d 749, 751, 759-65, 278 P.2d 305 (1954); *E. I. Du Pont de Nemours & Co. v. State*, 44 Wn.2d 339, 341-42, 346-51, 267 P.2d 667 (1954); *Gen. Elec. Co. v. State*, 42 Wn.2d 411, 414-17, 256 P.2d 265 (1953); *id.* at 425-31 (Finley, J., dissenting).

listing allowable deductions.<sup>11</sup> Many of these subsections began with the phrase “amounts derived from,” including RCW 82.16.050(6), a deduction for “[a]mounts derived from business which the state is prohibited from taxing under the Constitution of this state or the Constitution or laws of the United States” worded identically to former RCW 82.04.430(6) (now RCW 82.04.4286) discussed above. As with RCW 82.04.4286, this Court consistently has interpreted the language in RCW 82.16.050(6) as providing a deduction only for tax amounts that “the state is prohibited from taxing” under the state constitution or federal law.<sup>12</sup>

**5. Cases interpreting similar language in the Internal Revenue Code suggest that the phrase “amounts derived from interest” in RCW 82.04.4292 means only interest.**

For many years, the Internal Revenue Service and the federal courts have interpreted similar language (“gross receipts derived from . . . interest,” “gross income . . . derived from . . . interest”) in Internal Revenue Code provisions as meaning only interest income.<sup>13</sup> At the very least, this demonstrates that the servicers’ proposed interpretation of

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<sup>11</sup> See Laws of 1967, 1st Ex. Sess., ch. 149, § 25.

<sup>12</sup> See *Pub. Util. Dist. 2 of Grant Cy. v. State*, 82 Wn.2d 232, 234-42 & n.2, 510 P.2d 206 (1973); *id.* at 243-49 (Finley, J., dissenting); *Wash. Tel. Co. v. State*, 77 Wn.2d 923, 924-30, 468 P.2d 687 (1970); *Columbia River Bridge Co. v. State*, 46 Wn.2d 385, 386-90, 282 P.2d 283 (1955).

<sup>13</sup> See, e.g., *Marshall v. Comm’r*, 510 F.2d 259, 261-64 (10th Cir. 1975); *Noteman v. Welch*, 108 F.2d 206, 207-08, 210-15 (1st Cir. 1939); *Thompson v. Comm’r*, 73 T.C. 878, 887-89 & nn.7-9 (1980); *Buhler Mortgage Co. v. Comm’r*, 51 T.C. 971, 972-76 & n.2 (1969), *aff’d per curiam*, 443 F.2d 1362 (9th Cir. 1971); *W. Acceptance Corp. v. Comm’r*, 46 B.T.A. 828, 831-32 & n.1 (1942).

“amounts derived from interest” in RCW 82.04.4292 cannot be the only reasonable meaning attributable to that statutory phrase.

**B. The Statute’s History and Contemporaneous Administrative Construction Show That the Legislature Intended the Deduction to Apply Only to Interest**

As shown above, statutory phrases such as “amounts derived from interest” do not exist in a vacuum. They cannot be understood as intended by reading them in isolation, apart from the context in which they are used. The history of this statute also is an important part of that context and is a useful tool to ascertain the Legislature’s intent in enacting RCW 82.04.4292.<sup>14</sup>

**1. The deduction currently codified as RCW 82.04.4292 originally was enacted in 1970 as part of a bill designed to raise additional revenue.**

This deduction was enacted in 1970 as a part of an act extending the B&O tax to most financial institutions. Laws of 1970, 1st Ex. Sess., ch. 101, § 2 (Appendix at A-7 to A-9). This 1970 act amended former RCW 82.04.430, adding a new subsection (10) to that section to create the first mortgage interest deduction.

As initially introduced by Representative Murray on January 17, 1970, House Bill 232 simply would have repealed former RCW

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<sup>14</sup> See, e.g., *In re Sehome Park Care Ctr.*, 127 Wn.2d 774, 778, 903 P.2d 443 (1995).

82.04.400.<sup>15</sup> House Journal, 41st Legislature (1970), at 62; CP at 775 (see Appendix at A-11). As reported out of the House Committee on Revenue and Taxation on January 29, 1970, however, Substitute House Bill 232 (SHB 232) contained several additional sections. See House Journal, 41st Legislature (1970), at 172. Section 2 of SHB 232 would have amended former RCW 82.04.430 as follows:

In computing tax there may be deducted from the measure of tax the following items:

(1) Amounts derived by persons, other than those engaged in banking, loan security, or other financial businesses, from investments or the use of money as such, and also amounts derived as dividends by a parent from its subsidiary corporations;

...

(10) By those engaged in banking, loan, security or other financial businesses, amounts derived from interest received on investments primarily secured by first mortgages or trust deeds on nontransient residential properties;

(11) By those engaged in banking, loan, security or other financial businesses, amounts derived from interest paid on all obligations of the state of Washington, its political subdivisions, and municipal corporations organized pursuant to the laws thereof.

CP at 777-780 (see Appendix at A-12 to A-15).<sup>16</sup>

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<sup>15</sup> Former RCW 82.04.400 broadly exempted banks and other financial institutions from chapter 82.04 RCW. Laws of 1970, 1st Ex. Sess., ch. 101, § 4; see Laws of 1969, Ex. Sess., ch. 246, § 1; *Clifford v. State*, 78 Wn.2d 4, 7-8, 469 P.2d 549 (1970). This exemption for banks and other financial institutions had existed since 1937. See Laws of 1937, ch. 227, § 4. The Legislature repealed the exemption within weeks after Congress authorized states to impose nondiscriminatory gross receipts taxes on national banks. See Act of Dec. 24, 1969, Pub. L. No. 91-156, 83 Stat. 434; *Chase Manhattan Bank v. Finance Admin.*, 440 U.S. 447, 448-49, 99 S. Ct. 1201, 59 L. Ed. 2d 445 (1979); *United States v. State Bd. of Equalization*, 639 F.2d 458, 460-61 & n.2 (9th Cir. 1980).

<sup>16</sup> No committee records of the House Committee on Revenue and Taxation from the 1970 session can be found in the Washington State Archives. House standing

2. **The fiscal note the Department prepared for the Legislature assumed that the deduction proposed by the House committee was limited to interest received on investments primarily secured by first mortgages.**

The Department of Revenue prepared a fiscal note for SHB 232 on February 2, 1970. The fiscal note described the substitute bill as follows:

SHB 232 extends the business and occupation tax of 1 percent of gross operating income to those engaged in banking, loan, security, or other financial businesses. *Exempt from the tax are interest on all obligations of the state of Washington, its political subdivisions, and municipal corporations; interest received on investments primarily secured by first mortgages or trust deeds (on nontransient residential properties); and also amounts derived as dividends by a parent from its subsidiary corporations.* For the 16-month period, from March 1, 1970 through June, 1971, approximately \$4.2 million will be collected by the state.

(Italics added.) CP at 822 (see Appendix at A-16). This fiscal note is persuasive evidence that the House committee intended the two new deductions in former RCW 82.04.430(10) and (11) in section 2 of SHB 232 to be limited to interest.<sup>17</sup>

3. **None of the subsequent floor action in the House suggested that the Department's fiscal note erroneously interpreted the intended scope of the deductions in the bill.**

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committees did not routinely tape record committee meetings until 1973, and committee staff did not prepare bill reports for each bill passed out of committee until about 1974. Arthur C. Wang, Comment, *Legislative History in Washington*, 7 U. Puget Sound L. Rev. 571, 572 n.7 (1984). Committee records typically are unavailable before the mid-1970s. *Id.* at 601.

<sup>17</sup> It is appropriate to consider fiscal notes submitted to the Legislature in determining the intended meaning of legislative acts. *See, e.g., Davis v. Dep't of Licensing*, 137 Wn.2d 957, 969-70, 977 P.2d 554 (1999); *Cena v. Dept of Labor & Indus.*, 121 Wn. App. 915, 923, 91 P.3d 903 (2004), *review denied*, 153 Wn.2d 1015 (2005).

The bill came to the House floor on February 12, 1970. House Journal, 41st Legislature (1970), at 503. The House approved a clarifying amendment to section 2 of SHB 232 proposed by Representative Kiskaddon, adding the words “or loans” after “investments” in the new subsection (10) of former RCW 82.04.430. *Id.* The House also approved a floor amendment to section 2 proposed by Representatives Benitz and Haussler, adding a new subsection (12) of former RCW 82.04.430, creating a deduction for interest on agricultural production loans made by production credit associations. *See id.*

Representative Murray spoke in favor of passage of the bill as amended. He explained that the bill was necessary to balance the budget. CP at 766; *see* House Journal, 41st Legislature (1970), at 504. ESHB 232 then passed the House on a 65-33 vote. *Id.*

4. **The Department’s communications with the Senate committee chair in charge of the bill also reflected an understanding that the proposed deduction for first mortgages was limited to interest.**

Shortly after preparing the fiscal note for SHB 232, the Department expressed its opposition to the first mortgage interest deduction in section 2 of the bill in a pair of letters to Senator McCormack, the Chair of the Revenue and Taxation Subcommittee of the Senate Ways and Means Committee. CP at 789-798 (see Appendix at A-

17 to A-26).<sup>18</sup> The letters indicate that the principal proponents of the first mortgage interest deduction were savings and loan associations, which were then experiencing financial difficulties largely due to a shortage of savings deposits. The savings and loan associations argued that a tax on “residential mortgage loans” would drive interest rates higher, affect the amount of mortgage loan money available, and discourage new housing starts. The Department disputed that a tax on “residential mortgage loan interest” would bring about any of those results.

5. **After receiving the fiscal note and these subsequent communications from the Department, the Senate passed the bill without any further amendments and without referring the bill to committee.**

On February 12, 1970, immediately after the House transmitted ESHB 232 to the Senate, Senator McCormack made motions to suspend the rules and place ESHB 232 on final passage without amendment and without referring the bill to his subcommittee. Senate Journal, 41st Legislature (1970), at 545-546. The bill then passed the Senate on a 34-11 vote. *Id.* at 546.

6. **A report the Department prepared shortly after the legislative session again described this provision as a tax preference for first mortgage interest.**

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<sup>18</sup> The letters are contained in a file on ESHB 232 in the records of the Legislative Budget Committee in the Washington State Archives.

In March 1970, shortly after the legislative session ended, the Department of Revenue's Research and Information Division produced a report entitled "1970 Special Session Legislation Involving Tax Exemptions and Credits." The report described ESHB 232 in part as follows:

Effects: Imposes the B&O tax on banks, savings and loan companies, mutual savings banks and similar institutions with the following exemptions:

...

(2) Amounts derived as interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties (homes and apartments but not hotels, motels, or business properties).

...

The original House Bill 232 provided that all financial institutions would be subject to the B&O tax by repealing the statutory exemption granted by RCW 82.04.400. The substitute bill, which came out of the House Revenue and Taxation Committee, added most of the exemptions listed above; others were a result of House floor action. (Attempts to amend the bill in the Senate to provide that first mortgage interest would be phased into the tax base over a four-year period were unsuccessful.)

CP at 824-826 (see Appendix at A-27 to A-29).

- 7. The Department formally interpreted the deduction in 1970 in WAC 458-20-146, interpreting it as a deduction for interest received on investments or loans primarily secured by first mortgages.**

Two months after the first mortgage interest deduction was enacted, the Department of Revenue adopted WAC 458-20-146. The rule interpreted the allowable deductions from gross income for financial

institutions. WAC 458-20-146 limited the deduction ESHB 232 enacted in former RCW 82.04.430(10) to “interest”:

The deductions generally applicable to financial businesses include the following:

...

2. Interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties. (See Rule 166 for definition of “transient.”) (RCW 82.04.430(10)).

CP at 829-830 (see Appendix at A-31 to A-32).

**8. The Legislature affirmed the Department’s interpretation of the deduction in WAC 458-20-146 when it reenacted the deduction in 1971.**

The Legislature amended former RCW 82.04.430 twice during the 1970 session.<sup>19</sup> To correct this double amendment, the Legislature amended and reenacted former RCW 82.04.430 in the 1971 session to incorporate both amendments from the 1970 session. Laws of 1971, ch. 13, § 1. The Legislature reenacted the first mortgage interest deduction as former RCW 82.04.430(11). The bill contained an explanatory note describing each of the reenacted deductions. The note described the reenacted former RCW 82.04.430(11) as “relating to interest received on investments or loans secured by first mortgages or trust deeds on

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<sup>19</sup> Engrossed Senate Bill 13 enacted a new subsection (10) to former RCW 82.04.430 to create a deduction for “[a]mounts derived by a political subdivision of the state of Washington from another political subdivision of the state of Washington as compensation for services which are within the purview of RCW 82.04.290.” Laws of 1970, 1st Ex. Sess., ch. 65, § 5. This deduction now is codified as RCW 82.04.4291.

nontransient residential properties by certain financial businesses.”

(Appendix at A-35 to A-36).

Like legislative intent or purpose sections,<sup>20</sup> titles,<sup>21</sup> and section headings<sup>22</sup> contained in acts of the Legislature, explanatory notes such as this one, although without operative force in themselves, are important guides in understanding the intended effect of the operative statutory provisions.<sup>23</sup> In this instance, the explanatory note also should be regarded as a legislative affirmation of the Department’s interpretation of the first mortgage interest deduction in WAC 458-20-146.

**9. After the Legislature required that the deduction would apply to any local tax on financial institutions measured by gross income, the Department formally interpreted the deduction in 1972 in WAC 458-28-030(2), again interpreting it as a deduction for interest received on investments or loans primarily secured by first mortgages.**

In the 1972 session, the Legislature enacted legislation authorizing cities and towns to impose license fees or taxes on financial institutions.

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<sup>20</sup> See, e.g., *Hartman v. Wash. State Game Comm’n*, 85 Wn.2d 176, 179, 532 P.2d 614 (1975); *Huntworth v. Tanner*, 87 Wash. 670, 675-78, 152 P. 523 (1915).

<sup>21</sup> See, e.g., *Covell v. Seattle*, 127 Wn.2d 874, 887-88, 905 P.2d 324 (1995) (“The title of a legislative act also may be referred to as a source of legislative intent.”); *Shoop v. Kittitas Cy.*, 108 Wn. App. 388, 392, 30 P.3d 529 (2001) (“In contrast to captions generated by the code reviser, the title is a part of the legislative act. The title of a legislative act is a source of legislative intent.”).

<sup>22</sup> See, e.g., *State v. Chhom*, 162 Wn.2d 451, 460 n.3, 173 P.3d 234 (2007) (“In contrast to captions generated by the Washington State Code Reviser, section headings which are adopted as part of a statute may be referred to as a source of legislative intent.”).

<sup>23</sup> See 2A Norman J. Singer & J.D. Shambie Singer, *Statutes and Statutory Construction* § 47:14 (7th ed. 2007) (“Either comments or notes included when the statute is passed or revised are not part of the law, but can be considered a useful guide to the legislative purpose underlying the statutory language.”).

Laws of 1972, ch. 134 (codified as chapter 82.14A RCW). The 1972 act required that the “definitions, deductions and exemptions” in chapter 82.04 RCW would apply to any such local fee or tax, if the fee or tax “is measured by the gross income of the business.” RCW 82.14A.010.

Shortly after the Legislature passed the 1972 act, the Department of Revenue adopted a rule, WAC 458-28-030, listing the deductions from gross income in chapter 82.04 RCW that financial institutions are allowed under RCW 82.14A.010. Like WAC 458-20-146, this rule also interpreted the deduction in RCW 82.04.4292 as limited to “[i]nterest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties.” WAC 458-28-030(2).

**10. The Legislature has acquiesced in the Department’s interpretation of the deduction reflected in the Department’s rules for nearly four decades.**

In 1980, the Legislature repealed former RCW 82.04.430 and recodified the first mortgage interest deduction as RCW 82.04.4292 without changing its meaning.<sup>24</sup> The Legislature has not amended the statute since. The Legislature has never expanded the deduction beyond the Department’s contemporaneous interpretation of it reflected in WAC 458-20-146 and WAC 458-28-030. The Legislature’s long acquiescence

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<sup>24</sup> See Laws of 1980, ch. 37, §§ 1, 12, 81; *Simpson Inv. Co. v. Dep’t of Revenue*, 141 Wn.2d 139, 150 n.8, 3 P.3d 741 (2000) (recognizing limited purpose of the 1980 act).

in the Department's contemporaneous interpretation should be entitled to great weight in deciding this case.<sup>25</sup>

**C. The Principle That Courts Narrowly Construe Tax Deductions Supports the Result Reached By the Court of Appeals**

If this Court still remains uncertain of the Legislature's likely intent in enacting RCW 82.04.4292 after considering the overall statutory context discussed above, it should bear in mind the principle that tax deductions and exemptions are to be narrowly construed.<sup>26</sup> In adopting the B&O tax system, the Legislature intended to impose the tax upon "virtually all" business activities within the state.<sup>27</sup> Moreover, the purpose of the 1970 bill that enacted the first mortgage interest deduction was to raise additional revenue. Therefore, it is reasonable to conclude that the Legislature intended RCW 82.04.4292 to be narrowly confined to interest income received by the owners of first mortgage loans.

The servicers are asking this Court to adopt an expansive interpretation of RCW 82.04.4292 that would upset settled understandings of the meaning of this statute. Adopting the servicers' proposed

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<sup>25</sup> See, e.g., *In re Sehome Park Care Ctr.*, 127 Wn.2d 774, 779-81, 903 P.2d 443 (1995); *Newschwander v. Bd. of Trustees*, 94 Wn.2d 701, 711, 620 P.2d 88 (1980).

<sup>26</sup> See, e.g., *O'Leary v. Dep't of Revenue*, 105 Wn.2d 679, 682, 717 P.2d 273 (1986); *Evergreen-Washelli Memorial Park v. Dep't of Revenue*, 89 Wn.2d 660, 663, 574 P.2d 735 (1978); *Group Health Co-op v. Tax Comm'n*, 72 Wn.2d 422, 429, 433 P.2d 201 (1967).

<sup>27</sup> *Simpson Inv. Co. v. Dep't of Revenue*, 141 Wn.2d 139, 149, 3 P.3d 741 (1999); *Impecoven v. Dep't of Revenue*, 120 Wn.2d 357, 363, 841 P.2d 752 (1992); *Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971).

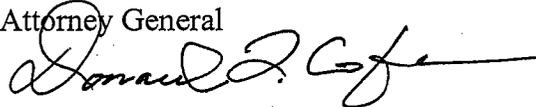
interpretation would likely lead to more litigation over the application of this statute and other similarly phrased deduction and exemption statutes in chapters 82.04 and 82.16 RCW, including RCW 82.04.4282, RCW 82.04.4286, RCW 82.04.4293, and RCW 82.16.050.<sup>28</sup> To avoid these untoward consequences, this Court should join the Court of Appeals in upholding the Department's interpretation of RCW 82.04.4292.

### III. CONCLUSION

The Court of Appeals correctly interpreted RCW 82.04.4292 and correctly applied the statute to the facts in this case. This Court should affirm the judgment of the Court of Appeals.

RESPECTFULLY SUBMITTED this 20th day of June, 2008.

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<sup>28</sup> The Legislature continues to enact such similarly phrased deduction statutes. Most recently, in 2002, the Legislature substantially revised RCW 82.04.4281 in response to this Court's decision in *Simpson Inv. Co. v. Dep't of Revenue*, 141 Wn.2d 139, 3 P.3d 741 (2000), in an effort to "provide certainty and stability for taxpayers and the state." Laws of 2002, ch. 150, § 1. Among other changes, the 2002 act created a new deduction in a revised RCW 82.04.4281(1)(c) for "[a]mounts derived from interest on loans between subsidiary entities and a parent entity or between subsidiaries of a common parent entity[.]" Laws of 2002, ch. 150, § 2. The legislative history of the 2002 act indicates that the Legislature intended "amounts derived from interest" to mean interest. See 2002 Final Legislative Report, 57th Legislature, at 98.

**82.04.080 "Gross income of the business."** "Gross income of the business" means the value proceeding or accruing by reason of the transaction of the business engaged in and includes gross proceeds of sales, compensation for the rendition of services, gains realized from trading in stocks, bonds, or other evidences of indebtedness, interest, discount, rents, royalties, fees, commissions, dividends, and other emoluments however designated, all without any deduction on account of the cost of tangible property sold, the cost of materials used, labor costs; interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses. [1961 c 15 § 82.04.080. Prior: 1955 c 389 § 9; prior: 1949 c 228 § 2, part; 1945 c 249 § 1, part; 1943 c 156 § 2, part; 1941 c 178 § 2, part; 1939 c 225 § 2, part; 1937 c 227 § 2, part; 1935 c 180 § 5, part; Rem. Supp. 1949 § 8370-5, part.]

**82.04.090 "Value proceeding or accruing."** "Value proceeding or accruing" means the consideration, whether money, credits, rights, or other property expressed in terms of money, actually received or accrued. The term shall be applied, in each case, on a cash receipts or accrual basis according to which method of accounting is regularly employed in keeping the books of the taxpayer. However, persons operating grain warehouses licensed under chapter 22.09 RCW may elect to report the value proceeding or accruing from grain warehouse operations on either a cash receipts or accrual basis. The department of revenue may provide by regulation that the value proceeding or accruing from sales on the installment plan under conditional contracts of sale may be reported as of the dates when the payments become due. [2001 c 20 § 1; 1975 1st ex.s. c 278 § 40; 1961 c 15 § 82.04.090. Prior: 1955 c 389 § 10; prior: 1949 c 228 § 2, part; 1945 c 249 § 1, part; 1943 c 156 § 2, part; 1941 c 178 § 2, part; 1939 c 225 § 2, part; 1937 c 227 § 2, part; 1935 c 180 § 5, part; Rem. Supp. 1949 § 8370-5, part.]

**82.04.290 Tax on international investment management services or other business or service activities.** (Effective until July 1, 2003.) (1) Upon every person engaging within this state in the business of providing international investment management services, as to such persons, the amount of tax with respect to such business shall be equal to the gross income or gross proceeds of sales of the business multiplied by a rate of 0.275 percent.

(2) Upon every person engaging within this state in any business activity other than or in addition to those enumerated in RCW 82.04.230, 82.04.240, 82.04.250, 82.04.255, 82.04.260, 82.04.270, 82.04.298, 82.04.2905, 82.04.280, 82.04.2635, 82.04.2907, and 82.04.272, and subsection (1) of this section; as to such persons the amount of tax on account of such activities shall be equal to the gross income of the business multiplied by the rate of 1.5 percent.

This section includes, among others, and without limiting the scope hereof (whether or not title to materials used in the performance of such business passes to another by accession, confusion or other than by outright sale), persons engaged in the business of rendering any type of service which does not constitute a "sale at retail" or a "sale at wholesale." The value of advertising, demonstration, and promotional supplies and materials furnished to an agent by his principal or supplier to be used for informational, educational and promotional purposes shall not be considered a part of the agent's remuneration or commission and shall not be subject to taxation under this section. [2001 1st sp.s. c 9 § 5; (2001 1st sp.s. c 9 § 4 expired July 1, 2001). Prior: 1998 c 343 § 4; 1998 c 331 § 2; 1998 c 312 § 8; 1998 c 308 § 4; 1997 c 7 § 2; 1996 c 1 § 2; 1995 c 229 § 3; 1993 sp.s. c 25 § 203; 1985 c 32 § 3; 1983 2nd ex.s. c 3 § 2; 1983 c 9 § 2; 1983 c 3 § 212; 1971 ex.s. c 281 § 8; 1970 ex.s. c 65 § 4; 1969 ex.s. c 262 § 39; 1967 ex.s. c 149 § 14; 1963 ex.s. c 28 § 2; 1961 c 15 § 82.04.290; prior: 1959 ex.s. c 5 § 5; 1955 c 389 § 49; prior: 1953 c 195 § 2; 1950 ex.s. c 5 § 1, part; 1949 c 228 § 1, part; 1943 c 156 § 1, part; 1941 c 178 § 1, part; 1939 c 225 § 1, part; 1937 c 227 § 1, part; 1935 c 180 § 4, part; Rem. Supp. 1949 § 8370-4, part.]

**82.04.4282 Deductions—Fees, dues, charges.** In computing tax there may be deducted from the measure of tax amounts derived from bona fide (1) initiation fees, (2) dues, (3) contributions, (4) donations, (5) tuition fees, (6) charges made by a nonprofit trade or professional organization for attending or occupying space at a trade show, convention, or educational seminar sponsored by the nonprofit trade or professional organization, which trade show, convention, or educational seminar is not open to the general public, (7) charges made for operation of privately operated kindergartens, and (8) endowment funds. This section shall not be construed to exempt any person, association, or society from tax liability upon selling tangible personal property or upon providing facilities or services for which a special charge is made to members or others. If dues are in exchange for any significant amount of goods or services rendered by the recipient thereof to members without any additional charge to the member, or if the dues are graduated upon the amount of goods or services rendered, the value of such goods or services shall not be considered as a deduction under this section. [1994 c 124 § 3; 1989 c 392 § 1; 1980 c 37 § 3. Formerly RCW 82.04.430(2).]

Intent—1980 c 37: See note following RCW 82.04.4281.

**82.04.4286 Deductions—Nontaxable business.** In computing tax there may be deducted from the measure of tax amounts derived from business which the state is prohibited from taxing under the Constitution of this state or the Constitution or laws of the United States. [1980 c 37 § 7. Formerly RCW 82.04.430(6).]

Intent—1980 c 37: See note following RCW 82.04.4281.

**82.04.4292 Deductions—Interest on investments or loans secured by mortgages or deeds of trust.** In computing tax there may be deducted from the measure of tax by those engaged in banking, loan, security or other financial businesses, amounts derived from interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties. [1980 c 37 § 12. Formerly RCW 82.04.430(11).]

Intent—1980 c 37: See note following RCW 82.04.4281.

**82.04.4293 Deductions—Interest on obligations of the state, its political subdivisions, and municipal corporations.** In computing tax there may be deducted from the measure of tax by those engaged in banking, loan, security or other financial businesses, amounts derived from interest paid on all obligations of the state of Washington, its political subdivisions, and municipal corporations organized pursuant to the laws thereof. [1980 c 37 § 13. Formerly RCW 82.04.430(12).]

Intent—1980 c 37: See note following RCW 82.04.4281.

**82.16.050 Deductions in computing tax.** In computing tax there may be deducted from the gross income the following items:

(1) Amounts derived by municipally owned or operated public service businesses, directly from taxes levied for the support or maintenance thereof: PROVIDED, That this section shall not be construed to exempt service charges which are spread on the property tax rolls and collected as taxes;

(2) Amounts derived from the sale of commodities to persons in the same public service business as the seller, for resale as such within this state. This deduction is allowed only with respect to water distribution, gas distribution or other public service businesses which furnish water, gas or any other commodity in the performance of public service businesses;

(3) Amounts actually paid by a taxpayer to another person taxable under this chapter as the latter's portion of the consideration due for services furnished jointly by both, if the total amount has been credited to and appears in the gross income reported for tax by the former;

(4) The amount of cash discount actually taken by the purchaser or customer;

(5) The amount of credit losses actually sustained by taxpayers whose regular books of accounts are kept upon an accrual basis;

(6) Amounts derived from business which the state is prohibited from taxing under the Constitution of this state or the Constitution or laws of the United States;

(7) Amounts derived from the distribution of water through an irrigation system, for irrigation purposes;

(8) Amounts derived from the transportation of commodities from points of origin in this state to final destination outside this state, or from points of origin outside this state to final destination in this state, with respect to which the carrier grants to the shipper the privilege of stopping the shipment in transit at some point in this state for the purpose of storing, manufacturing, milling, or other processing; and thereafter forwards the same commodity, or its equivalent, in the same or converted form, under a through freight rate from point of origin to final destination; and amounts derived from the transportation of commodities from points of origin in the state to an export elevator, wharf, dock or ship side on tidewater or navigable tributaries thereto from which such commodities are forwarded, without intervening transportation, by vessel, in their original form, to interstate or foreign destinations: PROVIDED, That no deduction will be allowed when the point of origin and the point of delivery to such an export elevator, wharf, dock, or ship side are located within the corporate limits of the same city or town;

(9) Amounts derived from the production, sale, or transfer of electrical energy for resale within or outside the state or for consumption outside the state;

(10) Amounts derived from the distribution of water by a nonprofit water association and used for capital improvements by that nonprofit water association;

(11) Amounts paid by a sewerage collection business taxable under RCW 82.16.020(1)(a) to a person taxable under chapter 82.04 RCW for the treatment or disposal of sewage. [2000 c 245 § 1; 1994 c 124 § 12; 1989 c 302 § 103; 1987 c 207 § 1; 1982 2nd ex.s. c 9 § 3; 1977 ex.s. c 368 § 1; 1967 ex.s. c 149 § 25; 1965 ex.s. c 173 § 22; 1961 c 15 § 82.16.050. Prior: 1959 ex.s. c.3 § 18; 1949 c 228 § 11; 1937 c 227 § 12; 1935 c 180 § 40; Rem. Supp. 1949 § 8370-40.]

plicated transactions, call the nearest district office of the department of revenue for assistance.

[Statutory Authority: RCW 82.32.300, 83-07-032 (Order ET 83-15), § 458-20-145, filed 3/15/83; Order ET 75-1, § 458-20-145, filed 5/2/75; Order ET 70-3, § 458-20-145 (Rule 145), filed 5/29/70, effective 7/1/70.]

**WAC 458-20-146 National and state banks, mutual savings banks, savings and loan associations and other financial institutions.**

#### Business and Occupation Tax

Effective March 1, 1970, the legislature repealed RCW 82.04.400 which exempted from the business and occupation tax the gross income of national banks, states banks, mutual savings banks, savings and loan associations and certain other financial institutions. Accordingly, the gross income of gross sales of such institutions will become subject to the business and occupation tax according to the following general principles.

**Services and other activities.** Generally, the gross income from engaging in financial businesses is subject to the business and occupation tax under the classification service and other activities. Following are examples of the types of income taxable under this classification: Interest earned (including interest on loans made to nonresidents unless the financial institution has a business location in the state of the borrower's residence which rendered the banking service), commissions earned, dividends earned, fees and carrying charges, charges for bookkeeping or data processing, safety deposit box rentals.

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

The law allows certain deductions from gross income to arrive at the taxable amount (the amount upon which the business and occupation tax is computed). Deductible gross income should be included in the gross amount reported and should then be shown as a deduction and explained on the deduction schedules provided on the reverse side of the reporting form. The deductions generally applicable to financial businesses include the following:

- (1) Dividends received by a parent from its subsidiary corporations (RCW 82.04.4281).
- (2) Interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties. (See WAC 458-20-166 for definition of "transient.") (RCW 82.04.4291.)
- (3) Interest received on obligations of the state of Washington, its political subdivisions, and municipal corporations organized pursuant to the laws thereof. (RCW 82.04.4292). A deduction may also be taken for interest received on direct obligations of the federal government, but not for interest

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attributable to loans or other financial obligations on which the federal government is merely a guarantor or insurer.

(4) Gross proceeds from sales or rentals of real estate (RCW 82.04.390). These amounts may be entirely excluded from the gross income reported and need not be shown on the return as a deduction.

**Retailing.** Sales of tangible personal property and certain services are defined as "retail sales" and are subject to the business and occupation tax under the classification retailing. Such sales are also subject to the retail sales tax which the seller must collect and remit to the department of revenue. Transactions taxable as sales at retail are not subject to tax under service and other activities.

Following are examples of transactions subject to the retailing classification of the business and occupation tax and to the retail sales tax: Sales of meals or confections, sales of repossessed merchandise, sales of promotional material, leases of tangible personal property, sales of check registers, coin banks, personalized checks. (Note: When the financial institution is not the seller of these items but simply takes orders as agent for the supplier, the supplier is responsible for reporting as the retail seller. The financial institution has liability for reporting the retail sales tax on sales made as an agent only if the supplier is an out-of-state firm not registered with the department of revenue), escrow fees, casual sales (occasional sales of depreciated assets such as used furniture and office equipment—subject to retail sales tax but deductible from the business and occupation tax; see WAC 458-20-106).

**Resale certificates.** When a financial institution buys tangible personal property for resale to its customers without intervening use, the sales tax is not applicable. In this case the financial institution should give the vendor a resale certificate, containing the number of its certificate of registration and its statement that the articles purchased are for resale in the course of its business activities. Resale certificates can be given in blanket form covering all future purchases. (See also WAC 458-20-102.)

#### Use Tax

The use tax complements the retail sales tax by imposing a tax of like amount on the use of tangible personal property purchased or acquired without payment of the retail sales tax. Thus, when office equipment or supplies are purchased or leased from an unregistered out-of-state vendor who does not collect the Washington state retail sales tax, the use tax must be paid directly to the department of revenue. Space for the reporting of this tax will be found on the regular excise tax return. (For more information, see WAC 458-20-178.)

**When tax liability arises.** Tax should be reported during the reporting period in which the financial institution receives, becomes legally entitled to receive, or in accord with the system of accounting regularly employed enters the consideration as a charge against the client, purchaser or borrower. Financial institutions may prepare returns to the department of revenue reporting income in periods which correspond to accounting methods employed by each institution for its normal accounting purposes in reporting to its supervisory authority.

**Reporting procedures.** Financial institutions subject to the business and occupation tax, retail sales tax, or use tax

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must secure a certificate of registration from the department of revenue and pay a registration fee of \$15.00. Form 2401, application for certificate of registration, is available at all district offices of the department of revenue or may be obtained by writing directly to the Department of Revenue, Olympia, Washington, 98504.

Reporting periods will be assigned by the department on the basis of total tax liability incurred. Most financial institutions will be required to report on a monthly basis, although some smaller institutions may qualify for quarterly reporting. Forms for reporting will be mailed shortly before the close of each reporting period and will be due and payable on or before the 15th day of the month following. No penalties will be charged if the return is postmarked on or before the last day of the month in which the due date falls.

[Statutory Authority: RCW 82.22.300, 83-07-032 (Order ET 83-15), § 458-20-146, filed 3/15/83; Order ET 70-3, § 458-20-146 (Rule 146), filed 5/29/70, effective 7/1/70.]

**WAC 458-20-14601 Financial institutions—Income apportionment. (1) Introduction.**

(a) This section provides tax reporting instructions for financial institutions doing business both inside and outside the state of Washington. Financial businesses that do not meet the definition of "financial institution" in subsection (3)(j) of this section and other businesses taxable under RCW 82.04.290 should refer to WAC 458-20-194 (Doing business inside and outside the state).

(b) Financial institutions engaged in making interstate sales of tangible personal property should also refer to WAC 458-20-193 (Inbound and outbound interstate sales of tangible personal property).

**(2) Apportionment and allocation.**

(a) Except as otherwise specifically provided, a financial institution taxable under RCW 82.04.290 and taxable in another state shall allocate and apportion its apportionable income as provided in this section. All gross income that is not includable in apportionable income shall be allocated pursuant to the provisions of chapter 82.04 RCW. A financial institution organized under the laws of a foreign country, the Commonwealth of Puerto Rico, or a territory or possession of the United States, except such institutions that are exempt under RCW 82.04.315, whose effectively connected income (as defined under the Federal Internal Revenue Code) is taxable both in this state and another state, other than the state in which it is organized, shall allocate and apportion its gross income as provided in this section.

(b) The apportionment percentage is determined by adding the taxpayer's receipts factor (as described in subsection (4) of this section), property factor (as described in subsection (5) of this section), and payroll factor (as described in subsection (6) of this section) together and dividing the sum by three. If one of the factors is missing, the two remaining factors are added together and the sum is divided by two. If two of the factors are missing, the remaining factor is the apportionment percentage. A factor is missing if both its numerator and denominator are zero, but it is not missing merely because its numerator is zero.

(c) Each factor shall be computed according to the method of accounting (cash or accrual basis) used by the taxpayer for Washington state tax purposes for the taxable

period. Persons should refer to WAC 458-20-197 (When tax liability arises) and WAC 458-20-199 (Accounting methods) for further guidance on the requirements of each accounting method. Generally, financial institutions are required to file returns on a monthly basis. To enable financial institutions to more easily comply with the provisions of this section, financial institutions will file returns using factors calculated based on the most recent calendar year for which information is available. A reconciliation shall be filed for each year within thirty days of the time that the taxpayer files its federal income tax returns for that year, but not later than October 30th of the following year. For example, for returns filed for taxable activities occurring during calendar 1998, a taxpayer would use factors calculated based on its 1996 information. A reconciliation would be filed for 1998 using factors based on 1998 information as soon as the information was available to the taxpayer, but not later than thirty days after the time federal income tax returns were due for 1998, or October 30, 1999. In the case of consolidations, mergers, or divestitures, a taxpayer shall make the appropriate adjustments to the factors to reflect its changed operations.

(d) If the allocation and apportionment provisions of this section do not fairly represent the extent of its business activity in this state, the taxpayer may petition for, or the department may require, in respect to all or any part of the taxpayer's business activity:

- (i) Separate accounting;
- (ii) A calculation of tax liability utilizing the cost of doing business method outlined in RCW 82.04.460(1);
- (iii) The exclusion of any one or more of the factors;
- (iv) The inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or
- (v) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's receipts.

(3) **Definitions.** The following definitions apply throughout this section:

(a) **"Apportionable income"** means the gross income of the business taxable under RCW 82.04.290, including income received from activities outside this state if the income would be taxable under RCW 82.04.290 if received from activities in this state, less the exemptions and deductions allowable under chapter 82.04 RCW.

(b) **"Billing address"** means the location indicated in the books and records of the taxpayer on the first day of the taxable period (or on such later date in the taxable period when the customer relationship began) as the address where any notice, statement and/or bill relating to a customer's account is mailed.

(c) **"Borrower or credit card holder located in this state"** means:

- (i) A borrower, other than a credit card holder, that is engaged in a trade or business which maintains its commercial domicile in this state; or
- (ii) A borrower that is not engaged in a trade or business or a credit card holder, whose billing address is in this state.

(d) **"Commercial domicile"** means:

- (i) The headquarters of the trade or business, that is, the place from which the trade or business is principally managed and directed; or

**Chapter 458-28 WAC**  
**TAXATION OF FINANCIAL BUSINESSES BY CITIES**  
**OR TOWNS**

WAC	
458-28-010	Scope of rule.
458-28-020	Gross income defined.
458-28-030	Deductions.
458-28-040	Branch locations, division of income.

**WAC 458-28-010** Scope of rule. Chapter 134, Laws of 1972 ex. sess., authorizes cities and towns to impose a license fee or tax on financial institutions. Financial institutions having business locations in cities and towns which levy a tax upon gross income or gross receipts for the privilege of engaging in business shall divide their gross income for purposes of computing income earned in the cities, towns or unincorporated areas in which such places of business are located in accordance with these rules.

[Order ET 72-1, § 458-28-010, filed 9/29/72.]

**WAC 458-28-020** Gross income defined. "Gross income of the business" means the value proceeding or accruing by reason of the transaction of the business engaged in and includes gross proceeds of sales, compensation for the rendition of services, gains realized from trading in stocks, bonds, or other evidences of indebtedness, interest, discount, rents, royalties, fees, commissions, dividends, and other emoluments however designated, all without any deduction on account of the cost of tangible property sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses.

Other examples of gross income are receipts from carrying charges, service charges, credit cards, safety deposit box rentals, bookkeeping or data processing, overdraft fees, flooring fees, and penalty fees.

[Order ET 72-1, § 458-28-020, filed 9/29/72.]

**WAC 458-28-030** Deductions. In arriving at income taxable to a city or town from activities of a place of business located therein, financial institutions may deduct from gross income:

- (1) Dividends received by a parent from a subsidiary corporation.
- (2) Interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties.
- (3) Interest received on obligations of the State of Washington, its political subdivisions, and municipal corporations. A deduction may also be taken for interest received on direct obligations of the Federal government, but not for interest attributable to loans or other financial obligations on which the Federal government is merely a guarantor or insurer.
- (4) Gross proceeds from the sale or rental of real estate.

[Order ET 72-1, § 458-28-030, filed 9/29/72.]

**WAC 458-28-040** Branch locations, division of income. Financial institutions having more than one place of business shall divide total taxable gross income so as to attribute taxable income to each location in the ratio of total interest earned (whether taxable or not) on loans originated at

(2005 Ed.)

each location during the period covered by the tax return. The location at which a loan is originated is the place of business of the financial institution at which the customer deals with the financial institution to obtain the loan. Financial institutions having time or demand deposits may compute the ratio of total deposits at each location as a basis for approximating gross income of each location, provided the financial institution can demonstrate that the taxable income so computed will not differ by more than \$10,000 in any one calendar year as to any one business location from the amount computed using the ratio of interest earned on loans originated at each location.

[Order ET 72-1, § 458-28-040, filed 9/29/72.]

CHAPTER 101

[Engrossed Substitute House Bill No. 232]  
TAXES--DEDUCTIONS--FINANCIAL INSTITUTIONS--  
SHARES OF STOCK

AN ACT Relating to revenue and taxation; amending section 79, chapter 235, Laws of 1945 and RCW 33.28.040; amending section 82.04.430, chapter 15, Laws of 1961 as last amended by section 11, chapter 173, Laws of 1965 ex. sess. and RCW 82.04.430; adding a new section to chapter 15, Laws of 1961 and to chapter 82.04 RCW; repealing section 82.04.400, chapter 15, Laws of 1961, section 1, chapter 136, Laws of 1963, section 8, chapter 173, Laws of 1965 ex. sess., section 1, chapter 246,

[771]

Laws of 1969 ex. sess., and RCW 82.04.400; repealing sections 84.40.270, 84.40.280, 84.40.290, 84.40.300 and 84.40.310; chapter 15, Laws of 1961 and RCW 84.40.270, 84.40.280, 84.40.290, 84.40.300 and 84.40.310; prescribing an effective date; and declaring an emergency.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

Section 1. Section 79, chapter 235, Laws of 1945 and RCW 33-.28.040 are each amended to read as follows:

The fees herein provided for shall be in lieu of all other corporation fees, licenses, or excises for the privilege of doing business, except for business and occupation taxes imposed pursuant to chapter 82.04 RCW, notwithstanding any other provisions of this section.

Neither an association nor its members shall be taxed upon its savings accounts as property. An association shall be taxable upon its real and tangible personal property.

An association is a mutual institution for savings and neither it nor its property shall be taxed under any law which shall exempt banks or other savings institutions from taxation.

For all purposes of taxation, the assets represented by the contingent fund and other reserves (other than reserves for expenses and specific losses) of an association shall be deemed its only permanent capital and, in computing any tax, whether property, income, or excise, appropriate adjustments shall be made to give effect to the mutual nature of such association.

Sec. 2. Section 82.04.430, chapter 15, Laws of 1961 as last amended by section 11, chapter 173, Laws of 1965 ex. sess., and RCW 82.04.430 are each amended to read as follows:

In computing tax there may be deducted from the measure of tax the following items:

- (1) Amounts derived by persons, other than those engaging in banking, loan; security, or other financial businesses, from investments or the use of money as such, and also amounts derived as divi-

dends by a parent from its subsidiary corporations;

(2) Amounts derived from bona fide initiation fees, dues, contributions, donations, tuition fees, charges made for operation of privately operated kindergartens, and endowment funds. This paragraph shall not be construed to exempt any person, association, or society from tax liability upon selling tangible personal property or upon providing facilities or services for which a special charge is made to members or others. Dues which are for, or graduated upon, the amount of service rendered by the recipient thereof are not permitted as a deduction hereunder;

(3) The amount of cash discount actually taken by the purchaser. This deduction is not allowed in arriving at the taxable amount under the extractive or manufacturing classifications with respect to articles produced or manufactured, the reported values of which, for the purposes of this tax, have been computed according to the provisions of RCW 82.04.450;

(4) The amount of credit losses actually sustained by taxpayers whose regular books of account are kept upon an accrual basis;

(5) So much of the sale price of motor vehicle fuel as constitutes the amount of tax imposed by the state or the United States government upon the sale thereof;

(6) Amounts derived from business which the state is prohibited from taxing under the Constitution of this state or the Constitution or laws of the United States;

(7) Amounts derived by any person as compensation for the receiving, washing, sorting, and packing of fresh perishable horticultural products and the material and supplies used therein when performed for the person exempted in RCW 82.04.330, either as agent or as independent contractor;

(8) Amounts derived as compensation for services rendered or to be rendered to patients by a hospital, as defined in chapter 70.41, devoted to the care of human beings with respect to the prevention or treatment of disease, sickness, or suffering, when such hospital

[773]

is operated by the United States or any of its instrumentalities, or by the state, or any of its political subdivisions;

(9) Amounts derived as compensation for services rendered to patients by a hospital, as defined in chapter 70.41, which is operated as a nonprofit corporation, nursing homes and homes for unwed mothers operated as religious or charitable organizations, but only if no part of the net earnings received by such an institution inures directly or indirectly, to any person other than the institution entitled to deduction hereunder. In no event shall any such deduction be allowed, unless the hospital building is entitled to exemption from taxation under the property tax laws of this state;

(10) By those engaged in banking, loan, security or other financial businesses, amounts derived from interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties;

(11) By those engaged in banking, loan, security or other financial businesses, amounts derived from interest paid on all obligations of the state of Washington, its political subdivisions, and municipal corporations organized pursuant to the laws thereof.

(12) Amounts derived as interest on loans by a lending institution which is owned exclusively by its borrowers or members and which is engaged solely in the business of making loans for agricultural production.

NEW SECTION. Sec. 3. There is added to chapter 15, Laws of 1961 and to chapter 82.04 RCW a new section to read as follows:

This chapter shall not apply to the gross income of credit unions organized under the laws of this state or the United States.

NEW SECTION. Sec. 4. The following acts or parts of acts are each repealed:

(1) Section 82.04.400, chapter 15, Laws of 1961, section 1, chapter 136, Laws of 1963, section 8, chapter 173, Laws of 1965 ex. sess., section 1, chapter 246, Laws of 1969 ex. sess., and RCW 82-

1970 1st ex. sess. (41st Legis. 2nd ex. sess.) Ch. 101, 102

.04.400;

(2) Sections 84.40.270, 84.40.280, 84.40.290, 84.40.300, and 84.40.310, chapter 15, Laws of 1961, and RCW 84.40.270, 84.40.280, 84.40.290, 84.40.300, and 84.40.310.

NEW SECTION. Sec. 5. If any provision of this act, or its application to any person or circumstance is held invalid, the remainder of the act, or the application of the provision to other persons or circumstances is not affected.

NEW SECTION. Sec. 6. This act is necessary for the immediate preservation of the public peace, health and safety, the support of the state government and its existing public institutions, and shall take effect March 1, 1970.

Passed the House February 12, 1970

Passed the Senate February 12, 1970

Approved by the Governor February 20, 1970

Filed in Office of Secretary of State February 24, 1970

HOUSE BILL NO. 232

State of Washington  
41st Legislature  
Second Extraordinary Session

by Representative Murray

Read first time January 17, 1970, and referred to Committee on  
Revenue and Taxation.

1 AN ACT Relating to revenue and taxation; repealing section 82.04.400,  
2 chapter 15, Laws of 1961 as last amended by section 1, chapter  
3 246, Laws of 1969 1st ex. sess. and RCW 82.04.400.

4 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

5 NEW SECTION. Section 1. Section 82.04.400, chapter 15, Laws  
6 of 1961 as last amended by section 1, chapter 246, Laws of 1969 1st  
7 ex. sess. and RCW 82.04.400 are each repealed.

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HB 232

SUBSTITUTE HOUSE BILL NO. 232

State of Washington by Committee on Revenue and  
41st Legislature Taxation  
Second Extraordinary Session

Read first-time January 29, 1970, and passed to second reading.

1 AN ACT Relating to revenue and taxation; amending section 79, chap-  
2 ter 235, Laws of 1945 and RCW 33.28.040; amending section 82-  
3 .04.430, chapter 15, Laws of 1961 as last amended by section 11,  
4 chapter 173, Laws of 1965 ex. sess. and RCW 82.04.430; adding  
5 a new section to chapter 15, Laws of 1961 and to chapter 82-  
6 .04 RCW; repealing section 82.04.400, chapter 15, Laws of 1961,  
7 section 1, chapter 136, Laws of 1963, section 8, chapter 173,  
8 Laws of 1965 ex. sess., section 1, chapter 246, Laws of 1969  
9 ex. sess., and RCW 82.04.400; repealing sections 84.40.270,  
10 84.40.280, 84.40.290, 84.40.300 and 84.40.310, chapter 15,  
11 Laws of 1961 and RCW 84.40.270, 84.40.280, 84.40.290, 84.40-  
12 .300 and 84.40.310; prescribing an effective date; and dec-  
13 laring an emergency.

14 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

15 Section 1. Section 79, chapter 235, Laws of 1945 and RCW 33-  
16 .28.040 are each amended to read as follows:

17 The fees herein provided for shall be in lieu of all other  
18 corporation fees, licenses, or excises for the privilege of doing  
19 business, except for business and occupation taxes imposed pursuant  
20 to chapter 82.04 RCW.

21 Neither an association nor its members shall be taxed upon  
22 its savings accounts as property. An association shall be taxable  
23 upon its real and tangible personal property.

24 An association is a mutual institution for savings and neither  
25 it nor its property shall be taxed under any law which shall exempt  
26 banks or other savings institutions from taxation.

27 For all purposes of taxation, the assets represented by the

1 contingent fund and other reserves (other than reserves for expenses  
2 and specific losses) of an association shall be deemed its only per-  
3 manent capital and, in computing any tax, whether property, income,  
4 or excise, appropriate adjustments shall be made to give effect to  
5 the mutual nature of such association.

6 Sec. 2. Section 82.04.430, chapter 15, Laws of 1961 as last  
7 amended by section 11, chapter 173, Laws of 1965 ex. sess., and RCW  
8 82.04.430 are each amended to read as follows:

9 In computing tax there may be deducted from the measure of  
10 tax the following items:

11 (1) Amounts derived by persons, other than those engaging in  
12 banking, loan, security, or other financial businesses, from invest-  
13 ments or the use of money as such, and also amounts derived as divi-  
14 dends by a parent from its subsidiary corporations;

15 (2) Amounts derived from bona fide initiation fees, dues,  
16 contributions, donations, tuition fees, charges made for operation of  
17 privately operated kindergartens, and endowment funds. This para-  
18 graph shall not be construed to exempt any person, association, or  
19 society from tax liability upon selling tangible personal property  
20 or upon providing facilities or services for which a special charge  
21 is made to members or others. Dues which are for, or graduated upon,  
22 the amount of service rendered by the recipient thereof are not per-  
23 mitted as a deduction hereunder;

24 (3) The amount of cash discount actually taken by the pur-  
25 chaser. This deduction is not allowed in arriving at the taxable  
26 amount under the extractive or manufacturing classifications with re-  
27 spect to articles produced or manufactured, the reported values of  
28 which, for the purposes of this tax, have been computed according to  
29 the provisions of RCW 82.04.450;

30 (4) The amount of credit losses actually sustained by tax-  
31 payers whose regular books of account are kept upon an accrual basis;

32 (5) So much of the sale price of motor vehicle fuel as con-  
33 stitutes the amount of tax imposed by the state or the United States

1 government upon the sale thereof;

2 (6) Amounts derived from business which the state is pro-  
3 hibited from taxing under the Constitution of this state or the Con-  
4 stitution or laws of the United States;

5 (7) Amounts derived by any person as compensation for the  
6 receiving, washing, sorting, and packing of fresh perishable horti-  
7 cultural products and the material and supplies used therein when  
8 performed for the person exempted in RCW 82.04.330, either as agent  
9 or as independent contractor;

10 (8) Amounts derived as compensation for services rendered or  
11 to be rendered to patients by a hospital, as defined in chapter 70.41,  
12 devoted to the care of human beings with respect to the prevention  
13 or treatment of disease, sickness, or suffering, when such hospital  
14 is operated by the United States or any of its instrumentalities, or  
15 by the state, or any of its political subdivisions;

16 (9) Amounts derived as compensation for services rendered to  
17 patients by a hospital, as defined in chapter 70.41, which is oper-  
18 ated as a nonprofit corporation, nursing homes and homes for unwed  
19 mothers operated as religious or charitable organizations, but only  
20 if no part of the net earnings received by such an institution inures  
21 directly or indirectly, to any person other than the institution en-  
22 titled to deduction hereunder. In no event shall any such deduction  
23 be allowed, unless the hospital building is entitled to exemption  
24 from taxation under the property tax laws of this state;

25 (10) By those engaged in banking, loan, security or other  
26 financial businesses, amounts derived from interest received on in-  
27 vestments primarily secured by first mortgages or trust deeds on non-  
28 transient residential properties;

29 (11) By those engaged in banking, loan, security or other  
30 financial businesses, amounts derived from interest paid on all ob-  
31 ligations of the state of Washington, its political subdivisions, and  
32 municipal corporations organized pursuant to the laws thereof.

33 NEW SECTION. Sec. 3. There is added to chapter 15, Laws of

1 1961 and to chapter 82.04 RCW a new section to read as follows:

2 This chapter shall not apply to the gross income of credit  
3 unions organized under the laws of this state or the United States.

4 NEW SECTION. Sec. 4. The following acts or parts of acts are  
5 each repealed:

6 (1) Section 82.04.400, chapter 15, Laws of 1961, section 1,  
7 chapter 136, Laws of 1963, section 8, chapter 173, Laws of 1965 ex.  
8 sess., section 1, chapter 246, Laws of 1969 ex. sess., and RCW 82-  
9 .04.400;

10 (2) Sections 84.40.270, 84.40.280, 84.40.290, 84.40.300, and  
11 84.40.310, chapter 15, Laws of 1961, and RCW 84.40.270, 84.40.280,  
12 84.40.290, 84.40.300, and 84.40.310.

13 NEW SECTION. Sec. 5. If any provision of this act, or its  
14 application to any person or circumstance is held invalid, the re-  
15 mainder of the act, or the application of the provision to other  
16 persons or circumstances is not affected.

17 NEW SECTION. Sec. 6. This act is necessary for the immediate  
18 preservation of the public peace, health and safety, the support of  
19 the state government and its existing public institutions, and shall  
20 take effect March 1, 1970.

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# FISCAL NOTE

To be completed by Agency

Requested by:

Concerning:

Draft   
 Original   
 Amended

13

Request Number

2/2/70

Date Received

2/2/70

Due Date

Revenue

Responding Agency

36 hours

Preparation Time

an Teller, OPP&FM

SHB 232

Bill Number

Responding Agency:

Reviewed by:

Department of Revenue

OPP & FM

LBC

## Estimated Fiscal Impact of Proposed Legislation

A. Revenue Impact by Source and Fund	BIENNIUM IMPACT			Five Year Long Range Impact
	First Year	Second Year	Total	
Business & Occupation	+ \$740,000	+ \$3,510,000	+ \$4,250,000	+ \$16,324,000
TOTAL	+ \$740,000	+ \$3,510,000	+ \$4,250,000	+ \$16,324,000
B. Expenditure Impact by Man Years				
Operating Funds				
Capital Funds				
Other (specify)				
TOTAL				

2. Explanation of Estimate:

SHB 232 extends the business and occupation tax of 1 percent of gross operating income to those engaged in banking, loan, security, or other financial businesses. Exempt from the tax are interest on all obligations of the state of Washington, its political subdivisions, and municipal corporations; interest received on investments primarily secured by first mortgages or trust deeds (on nontransient residential properties); and also amounts derived as dividends by a parent from its subsidiary corporations. For the 16-month period, from March 1, 1970 through June, 1971, approximately \$4.2 million will be collected by the state.

Attachments  YES  NO

N. Scott Sheeran 2/2/70  
 Prepared by Date  
*Wendell R. ...* 2/2/70  
 Released by Date



STATE OF WASHINGTON  
DEPARTMENT OF REVENUE

OLYMPIA 98501

February 3, 1970

TO: Mike McCormack, Chairman, Senate Sub-Committee, Taxation and Revenue  
FROM: George Kinnear, Director, Department of Revenue  
SUBJECT: Proposed Exemptions To Bank Tax, Substitute House Bill 232

We have reviewed the business and occupation tax exemptions proposed in Substitute House Bill 232, especially the exemption in Section 2, Paragraph 10, which sponsors claim is necessary to avert an undesirable effect on residential mortgage loans and the building industry.

Based on its study, the Department of Revenue opposes the exemption contained in Section 2, Paragraph 10, sheltering residential mortgage loans, but agrees with the exemptions in Section 2, Paragraph 1 (subsidiaries) and Section 2, Paragraph 11 (state and municipal bonds).

None of the facts we have found, including the latest building and financial market analyses, support the allegations that a business and occupation tax on residential mortgage loans will drive interest rates higher, affect the amount of mortgage loan money available, or discourage new housing starts. These are matters almost entirely controlled by the current federal fiscal policies, and would not be affected by this type of state legislation.

In fact, the opposite to those reasons may be argued, that Substitute HB 232, without a preferential exemption such as that proposed, will favor a better economic climate in the state. In company with other revenue proposals, it will act to relieve the intolerable tax pressures on property and other revenue sources.

A Proposal for Phasing the Application of B&O Tax to Residential Mortgages

While opposing SHB 232 in its present form, the Department of Revenue concurs that the transition into this new taxing area should be made without an abrupt impact on the lending institutions.

For that reason the Department of Revenue proposes that the tax rate on residential mortgage loans be phased on a four-year scale starting with 22/100 percent in March, 1970, and reaching the 1 percent maximum in January, 1973:

March, 1970	.0022
January, 1971	.0044
January, 1972	.007
January, 1973	.01

(A phasing of the tax was suggested first by industry representatives.)

### Effect on Anticipated Revenues of the Department's Proposal

This schedule will increase anticipated revenues approximately \$800,000 over those proposed in SHB 232. The tax on other types of loans charged by financial institutions would be left at 1 percent starting March, 1970.

If the schedule the Department of Revenue proposes is not adopted, SHB 232 would reduce tax revenues \$2.8 million this biennium as a result of this one exemption.

### The B&O Tax Would Not Adversely Affect the Housing Market

Arguments that the business and occupation tax would depress the building market are unfounded. The potential impact of the tax on housing, measured in dollars, clearly is minimal relative to the total housing needs of the State of Washington.

These needs are estimated to be at least 30,000 new units a year, at a minimum cost of \$540 million. To this must be added low-cost housing amounting to another 10,000 units a year.

These points are critical:

- A gradual easing of the money situation is forecast in 1970 with a significant upswing in building starts nationally after mid-1970.
- Basically, it is economic improvements such as reduced interest rates or increase earnings which will bring about a revitalization of the lending and building markets.
- The amount of B&O taxes that would fall upon savings institutions, when divided among all of them, would be extremely light.
- The chief effect of the exemption in Section 2 (10), SHB 232, will be to enable financial institutions to retain profits, not to materially abet new housing starts.

### The Effect on Uniformity of Taxation

The Department of Revenue's proposal will lessen the impact on the lending institutions and, most important, assure the uniformity essential to such taxes.

Not only does the granting of exemptions result in an unequal distribution of the tax burden, but it also reduces the amount of revenue available to the governing body through reduction of the tax base. Legal exemptions from tax are generally harmful to the community as a whole and create limitations without forcing increased rates. It is undesirable in our opinion to use exemptions as an instrument of either social or industrial policy.

The changes proposed by the Department of Revenue would satisfy the uniformity criterion in these ways:

The special rates would apply to only a certain type of loan -- thus, all financial institutions would be in an equal tax status regarding whatever type of loan they choose to invest in; the initial rate of .0022 would be the lowest state rate that is broadly applied; if the tax package is approved, the rate would be uniform among all payers of B&O taxes; upon the end of phasing, all financial revenues would be taxed uniformly at the 1 percent rate.

Will the B&O Tax Make Residential Loans Harder To Obtain?

The answer is no.

Numerous authorities agree that the savings and loan associations are suffering from a lack of cash inflow, that they are not obtaining deposits sufficient to meet loan demands. It is this, rather than the number of low interest rate mortgages they hold, that is their dilemma. The recent action of the Federal Reserve Board authorizing an increase in passbook account interest rates was intended to alleviate this, and such moves are the only effective means of eliminating the problem.

From President Nixon on down, the country's entire fiscal psychology is under intense study by its regulating bodies to determine how more lending funds can be made available without sidetracking the anti-inflation campaign. A state B&O tax on bank interest, especially one phased to spreadeagle economic conditions over four years' time, cannot affect this struggle in an entirely different arena.

How Will the B&O Tax Affect the Small Associations?

A small savings association that is not well-managed could be distressed by minor additions in overhead of any kind. However, the Department of Revenue believes that the loan industry, working with the federal government, would never permit an association to fail for this reason.

Dramatic support for this opinion was the Lytton case last year in California. When Lytton Savings and Loan, one of the country's largest, went to the wall, other members of the industry promptly bought up its business and continued it without a dollar of loss.

With savings and loan association portfolios averaging around 6 1/2 percent in loan values, their outlook is very promising once the federal controls on money are eased. In the present highly competitive loan market, there is no likelihood that the B&O tax proposed would be used to raise an already stiff interest level. The money is available; somebody is going to make a loan at current interest rates and profit by it.

Business Outlook

Business forecasters expect some early easing of money restrictions and an upswing in housing starts by mid-1970. The editors of Fortune Magazine, in their January, 1970 Roundup, stated:

"A recovery in housing must wait on easier credit conditions and a readjustment in interest rates sufficient to attract funds back into mortgage channels. Starts should be rising in the spring, generating more activity thereafter. Once under way, the recovery could be rapid."



STATE OF WASHINGTON  
DEPARTMENT OF REVENUE  
OLYMPIA 98501

February 4, 1970

TO: Mike McCormack, Chairman, Senate Sub-Committee, Taxation and Revenue

FROM: George Kinnear, Director, Department of Revenue

SUBJECT: SHB 232 -- Appendix to the Department of Revenue Position  
Statement of February 3, 1970

Yesterday we sent you the Department's position statement opposing the provision in Section 2 (10) of SHB 232 exempting residential mortgage loan interest from the business and occupation tax. A number of contemporary sources were cited in that statement, and in order that members of your committee can draw on these in greater detail we have prepared an appendix which is herewith transmitted.

Please call on us for any further supporting data you may need.

GK:mb

DEPARTMENT OF REVENUE POSITION STATEMENT ON SHB 232 (The Bank Tax)

Appendix

- Exhibit 1. Business Roundup, Fortune Magazine, January, 1970
- Exhibit 2. Value Line Investment Survey, January 9, 1970
- Exhibit 3. Value Line Investment Survey, November 21, 1970
- Exhibit 4. Comment on Tax Exemption by State Supreme Court,  
December 31, 1969
- Exhibit 5. Prediction of Lower Interest Rates by Treasury  
Secretary Kennedy, 2/4/70

APPENDIX

The editors of Fortune Magazine, in their Business Roundup (January, 1970) predict an upswing in housing after mid-year and a return to normalcy of the growth of money supply and bank credit. They emphasize that easier credit and lower interest rates are prerequisites to the recovery.

Exhibit 1

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CREDIT

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"A number of Federal Reserve Bank members have lately made pronouncements that restraint will be needed for some time yet, but within a context of restraint, the Fed will soon find room for moderating its grip. This does not portend another reversal to a policy of downright ease, of course, but a shift back by the end of spring to normal rates of monetary growth."

"How much rates drop back, and how soon, can prove critical in determining how quickly funds flow back into the mortgage market."

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HOUSING

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"A recovery in housing must wait on easier credit conditions and a readjustment in interest rates sufficient to attract funds back into mortgage channels. Starts should be rising in the spring, generating more activity thereafter. Once under way, the recovery could be rapid, making up lost ground by mid-1971."

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SPENDING

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"Thus the economy will be undergoing in any case a readjustment not only in the curve of output but in the composition of demand -- away from business and defense spending and toward more consumption and more construction of housing and public facilities."

"The decline of business spending will ease financial strains, and permit another sharp recovery in housing activity, starting after midyear."

APPENDIX

"Savings and loan associations are suffering from a lack of cash inflow. It is this, rather than the number of low interest rate mortgages they hold, that is their dilemma."

Exhibit 2

From The Value Line Investment Survey, Jan. 9, 1970

THE BEST OF  
TWO WORLDS

"Savings and loan associations are a conduit through which money is passed from savers to borrowers. On the one end, interest paid to depositors is regulated and cannot exceed prescribed limits. On the other end, lending charges have been climbing, with borrowers recently willing to pay 9 percent and more for mortgage money. This combination has resulted in the widest spread in history between the cost of borrowing and the rate of return on lending.

"Money from amortization and prepayment of existing loans (generally older, low interest bearing ones) is funneled into these new high yielding mortgages. In this way the average yield on loan portfolios has climbed steadily upward."

INVESTMENT  
OUTLOOK

"We view a decline of one percentage point or slightly more in overall interest rates as a good possibility by mid-1970. If interest rates should dip much more for a sustained period of time, then deposits of savings and loans could once again begin to grow; healthy earnings gains would be generated."

APPENDIX

"None of the latest building and financial market analyses support the contention that a business tax on residential mortgage loan interest will push interest rates higher, reduce the amount of mortgage loan money or discourage building."

Exhibit 3

From The Value Line Investment Survey, Nov. 21, 1969

THE RECESSIONS'  
SILVER LINING

"If the tight money policy being pursued by the Federal Reserve Board is successful in slowing the economy and taming inflation, the home building industry will be a key beneficiary in time. If general economic activity slows and the unemployment rate rises, credit and manpower now being used in other ways will become available to the building industry.

"As the economy cools, money market interest rates recede and savings institutions are able to attract a larger share of the savings stream.

"The mortgage interest rate structure tends to be more rigid than most other long-term interest rates. This hurts the building industry during periods of climbing money market yields, but helps it when money rates are falling.

"Aside from an end of the war in Vietnam, the best thing that could happen for the housing industry would be a recession in the U. S. economy."

THE REAL BRAKES  
ON BUILDING

"While scarcity of credit is the main impediment to housing, steeply rising land and construction costs are also a serious adverse factor. The inflation in the cost of building reflects a combination of factors, including archaic building codes, restrictive zoning regulations and monopoly labor practices."

OUTLOOK

"As soon as the demand for funds softens as the economy cools, more resources will become available for construction. Our current view is that enough of a slowdown in industrial activity will occur in the first half of 1970 to permit an upturn in residential construction by the third quarter."

APPENDIX

"Exemptions as an instrument of taxing policy are generally harmful."

Exhibit 4

WHAT THE STATE  
SUPREME COURT SAYS

"Not only does the granting of exemptions result in an unequal distribution of the tax burden, but it also reduces the amount of revenue available to the governing body through reduction of the tax base."

(Washington State Supreme Court,  
in Pacific Northwest Conference  
of the Free Methodist Church vs.  
Snohomish County Assessor, Dec.  
31, 1969.)

Exhibit 5

Prediction of lower interest rates by Treasury Secretary Kennedy,  
Wall Street Journal, 2/4/70

## Treasury Chief Says Interest Rate Drops Likely Earlier 'Than Most People Realize'

A WALL STREET JOURNAL News Roundup

Treasury Secretary Kennedy predicted that interest-rate declines, resulting from a more stable economy, "may be closer to hand than most people realize."

He didn't specify when rates may begin to drop. The Nixon Administration has clearly indicated it expects interest rates to drop this year, and some of the figures in the new Federal budget are based on that assumption.

Mr. Kennedy told a savings bond sales meeting in New York that interest rates will drop "to a more reasonable level" when "the inflationary psychology is broken and the business community and the public in general begins to look forward to greater stability." That "happy day," he added, may be nearer than is generally expected.

Mr. Kennedy's statement caused the blue-chip Dow Jones industrial average to advance 14.26 points in less than half an hour. (For details, please see "Abreast of the Market," page 27.)

The Treasury Secretary said the Administration's anti-inflation battle "clearly is beginning to make headway." An economic slowdown is taking place, he said, "without the dislocation of a sudden, jarring move into reverse."

But Mr. Kennedy cautioned that the Administration "will continue our policies of restraint" until the economy's "basic health and stability" is restored.

### Johnson Aide Backs View

Support for Mr. Kennedy's interest-rate comments came, coincidentally, from former Johnson Administration economist Otto Eckstein, a Harvard professor and consultant. The Federal Reserve Board "will be free to make its first visible move toward accommodating economic growth between now and April 1," he said, "if unemployment does move up and if the rate of increase of prices shows a substantial improvement."

Addressing the Washington Society of In-

vestment Analysts and the National Economists Club, Mr. Eckstein added that the very low unemployment rate of recent months appears to be "a statistical aberration" and that the February consumer price climb "perhaps" will become less rapid. This year, he forecast, is "likely to see the end of the 20-year uptrend of interest rates," but the downward trek "will take a long time."

The Nixon Administration "will deserve much credit" if it can keep its budget tight, he said, and agreed generally with the Administration's outlook on the economy. If the official forecasts do prove faulty, he added, it would probably be that the slowdown in business becomes "a little worse."

### A Pessimistic Note

A much more pessimistic note was struck at a meeting in Washington of the U.S. Savings and Loan League's legislative committee, however. The only thing wrong with the Nixon Administration's economic policy is that "it won't work unless it is carried on so long and to such an extent that the country will face a serious and prolonged depression," contended Chairman Henry A. Bubb of Capitol Federal Savings & Loan Association, Topeka.

Mr. Bubb, long an active Republican, urged President Nixon to promptly apply controls to business and consumer credit and to "call for a voluntary wage and price freeze for six months." A banking act passed by Congress on Dec. 23 gave the President broad power to limit "any or all extensions of the credit," a power he said he wouldn't use. The Federal Reserve Board, which would administer any such controls on Presidential request, published details of the law in its latest monthly bulletin.

1970 SPECIAL SESSION LEGISLATION  
INVOLVING TAX EXEMPTIONS AND CREDITS

CONTENTS

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Revenue Impact: Loss to the state General Fund (gain to local funds) could amount to \$135,000 annually if both cities elect to use the full amount available to them under the act.

Senate House Bill 232

Effects: Imposes the B & O tax on banks, savings and loan companies, mutual savings banks and similar institutions with the following exemptions:

- (1) Amounts derived as dividends by a parent from its subsidiary corporation.
- (2) Amounts derived as interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties (homes and apartments but not hotels, motels, or business properties).
- (3) Amounts derived as interest on all obligations of the state of Washington, its political subdivisions, and municipal corporations organized pursuant to the laws thereof.
- (4) Amounts derived as interest on loans by a lending institution which is owned exclusively by its borrowers or members and which is engaged solely in the business of making loans for agricultural production.
- (5) The gross income of credit unions organized under the laws of this state or the United States.

Background: States have been limited in the manner in which they can tax national banks by an 1819 U.S. Supreme Court decision. Since Washington was unable to apply the B & O tax to national banks, a statutory exemption was granted to cover all financial institutions. A recent U.S. Supreme Court decision, which reaffirmed the 1819 decision, prompted action by Congress to specifically allow states to tax national banks. (This authority was not extended to cover the taxation of federally chartered credit unions, however.)

The original House Bill 232 provided that all financial institutions would be subject to the B & O tax by repealing the statutory exemption granted by RCW 82.04.400. The substitute bill, which came out of the House Revenue and Taxation Committee, added most of the exemptions listed above; others were a result of House floor action. (Attempts to amend the bill in the Senate to provide that first mortgage interest would be phased into the tax base over a four-year period were unsuccessful.)

Revenue Impact: The original Senate Bill 232 would have produced about \$6 million annually - the exemptions enumerated above will reduce the anticipated revenue to \$3.4 million per year.

The following table shows the effect of each exemption:

	<u>Annual Income</u>	<u>1969-1971 Biennium</u>
Anticipated revenue under original House Bill 232.....	\$6,000,000	\$7,500,000
Exemptions		
(1) Subsidiary corporation dividends....	N.A.	N.A.
(2) First mortgage interest.....	(2,240,000)	(2,800,000)
(3) Interest on state and municipal obligations.....	(360,000)	(450,000)
(4) Interest on loans made by agricultural co-operatives.....	(20,000)	(25,000)
(5) Credit union loan interest.....	<u>----*</u>	<u>----*</u>
	\$3,380,000	\$4,225,000

\*The Department of Revenue estimated that the B & O tax on interest from loans made by state chartered credit unions would amount to about \$224,000 per year. Since these institutions could readily become federally chartered and thus not subject to the state tax, this figure was not included in the original total estimates made by Department personnel.

State of Washington  
Department of Revenue  
Research and Information Division  
March, 1970

DANIEL J. EVANS, Governor



# **R**ULES relating to the **REVENUE ACT OF 1935**

COVERING

- RETAIL SALES TAX
- USE TAX
- BUSINESS & OCCUPATION TAX
- PUBLIC UTILITY TAX
- MECHANICAL DEVICES TAX
- CONVEYANCE TAX
- CIGARETTE TAX
- TOBACCO PRODUCTS TAX

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STATE OF WASHINGTON  
DEPARTMENT OF REVENUE

GEORGE KINNEAR, Director  
R. A. LOTZENHISER, Deputy Director

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INTERPRETATION AND APPEALS DIVISION

JAMES R. STANFORD, Assistant Director

S. ED TVEDEN, Chief Examiner

June 1, 1970



3. Same as example 2 except the Sumner resident sends a catalog mail order directly to the Portland warehouse rather than going through the Tacoma catalog store. The vendor will collect Sumner's local use tax along with the state use tax.

The above explanation is intended to cover only the most frequently encountered situations. For more intricate or complicated transaction, call the nearest district office of the Department of Revenue for assistance.

Effective April 1, 1970.

WAC 458-20-146 (Rule 146) NATIONAL AND STATE BANKS, MUTUAL SAVINGS BANKS, SAVINGS AND LOAN ASSOCIATIONS AND OTHER FINANCIAL INSTITUTIONS

BUSINESS AND OCCUPATION TAX

Effective March 1, 1970, the legislature repealed RCW 82.04.400 which exempted from the business and occupation tax the gross income of national banks, states banks, mutual savings banks, savings and loan associations and certain other financial institutions. Accordingly, the gross income or gross sales of such institutions will become subject to the business and occupation tax according to the following general principles.

**SERVICES AND OTHER ACTIVITIES.** Generally, the gross income from engaging in financial businesses is subject to the business and occupation tax under the classification Service and Other Activities. Following are examples of the types of income taxable under this classification: Interest earned (including interest on loans made to nonresidents unless the financial institution has a business location in the state of the borrower's residence which rendered the banking service), commissions earned, dividends earned, fees and carrying charges, charges for bookkeeping or data processing, safety deposit box rentals.

The term "gross income" is defined in the law as follows:

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

The law allows certain deductions from gross income to arrive at the taxable amount (the amount upon which the business and occupation tax is computed). Deductible gross income should be included in the gross amount shown in Column 2 of Form 2406, Excise Tax Return, should then be shown as a deduction in Column 3, and explained on the deduction schedules provided on the reverse side of the form. The deductions generally applicable to financial businesses include the following:

1. Dividends received by a parent from its subsidiary corporations (RCW 82.04.430(1)).
2. Interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties. (See Rule 166 for definition of "transient.") (RCW 82.04.430(10)).
3. Interest received on obligations of the State of Washington, its political subdivisions, and municipal corporations organized pursuant to the laws thereof. (RCW 82.04.430(11)). A deduction may also be taken for interest received on direct obligations of the Federal government, but not for interest attributable to loans or other financial obligations on which the Federal government is merely a guarantor or insurer.

4. Gross proceeds from sales or rentals of real estate (RCW 82.04.390). These amounts may be entirely excluded from the gross income reported and need not be shown on the return as a deduction.

**RETAILING.** Sales of tangible personal property and certain services are defined as "retail sales" and are subject to the business and occupation tax under the classification Retailing. Such sales are also subject to the retail sales tax which the seller must collect and remit to the Department of Revenue. Transactions taxable as sales at retail are not subject to tax under Service and Other Activities.

Following are examples of transactions subject to the Retailing classification of the business and occupation tax and to the retail sales tax: Sales of meals or confections, sales of repossessed merchandise, sales of promotional material, leases of tangible personal property, sales of check registers, coin banks, personalized checks. (Note: When the financial institution is not the seller of these items but simply takes orders as agent for the supplier, the supplier is responsible for reporting as the retail seller. The financial institution has liability for reporting the retail sales tax on sales made as an agent only if the supplier is an out-of-state firm not registered with the Department of Revenue), escrow fees, casual sales (occasional sales of depreciated assets such as used furniture and office equipment—subject to retail sales tax but deductible from the business and occupation tax; see Rule 106.)

**RESALE CERTIFICATES.** When a financial institution buys tangible personal property for resale to its customers without intervening use, the sales tax is not applicable. In this case the financial institution should give the vendor a resale certificate containing the number of its certificate of registration and its statement that the articles purchased are for resale in the course of its business activities. Resale certificates can be given in blanket form covering all future purchases. (See also Rule 102.)

#### USE TAX

The use tax complements the retail sales tax by imposing a tax of like amount on the use of tangible personal property purchased or acquired without payment of the retail sales tax. Thus, when office equipment or supplies are purchased or leased from an unregistered out-of-state vendor who does not collect the Washington state retail sales tax, the use tax must be paid directly to the Department of Revenue. Space for the reporting of this tax will be found on Form 2406, Excise Tax Return. (For more information, see Rule 178.)

**WHEN TAX LIABILITY ARISES.** Tax should be reported during the reporting period in which the financial institution receives, becomes legally entitled to receive, or in accord with the system of accounting regularly employed enters the consideration as a charge against the client, purchaser or borrower. Financial institutions may prepare returns to the Department of Revenue reporting income in periods which correspond to accounting methods employed by each institution for its normal accounting purposes in reporting to its supervisory authority.

**REPORTING PROCEDURES.** Financial institutions subject to the business and occupation tax, retail sales tax, or use tax must secure a certificate of registration from the Department of Revenue and pay a registration fee of \$1.00. Form 2401, Application for Certificate of Registration, is available at all district offices of the Department of Revenue or may be obtained by writing directly to the Department of Revenue, Olympia, Washington, 98501.

Reporting periods will be assigned by the department on the basis of total tax liability incurred. Most financial institutions will be required to report on a monthly basis, although some smaller institutions may qualify for quarterly reporting. Forms for reporting will be mailed shortly before the close of each reporting period and will be due and payable on or before the 15th day of the month following. No penalties will be charged if the return is postmarked on or before the last day of the month in which the due date falls.

Effective March 1, 1970.

CHAPTER 13  
[House Bill No. 99]  
REVENUE AND TAXATION--  
CODE CORRECTIONS

AN ACT Relating to revenue and taxation; amending and reenacting section 82.04.430, chapter 15, Laws of 1961 as last amended by section 5, chapter 65, Laws of 1970 ex. sess. and by section 2, chapter 101, Laws of 1970 ex. sess., and RCW 82.04.430; and declaring an emergency.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

Section 1. Section 82.04.430, chapter 15, Laws of 1961 as last amended by section 5, chapter 65, Laws of 1970 ex. sess. and by

section 2, chapter 101, Laws of 1970 ex. sess., and RCW 82.04.430 are each amended and reenacted to read as follows:

In computing tax there may be deducted from the measure of tax the following items:

(1) Amounts derived by persons, other than those engaging in banking, loan, security, or other financial businesses, from investments or the use of money as such, and also amounts derived as dividends by a parent from its subsidiary corporations;

(2) Amounts derived from bona fide initiation fees, dues, contributions, donations, tuition fees, charges made for operation of privately operated kindergartens, and endowment funds. This paragraph shall not be construed to exempt any person, association, or society from tax liability upon selling tangible personal property or upon providing facilities or services for which a special charge is made to members or others. Dues which are for, or graduated upon, the amount of service rendered by the recipient thereof are not permitted as a deduction hereunder;

(3) The amount of cash discount actually taken by the purchaser. This deduction is not allowed in arriving at the taxable amount under the extractive or manufacturing classifications with respect to articles produced or manufactured, the reported values of which, for the purposes of this tax, have been computed according to the provisions of RCW 82.04.450;

(4) The amount of credit losses actually sustained by taxpayers whose regular books of account are kept upon an accrual basis;

(5) So much of the sale price of motor vehicle fuel as constitutes the amount of tax imposed by the state or the United States government upon the sale thereof;

(6) Amounts derived from business which the state is prohibited from taxing under the Constitution of this state or the Constitution or laws of the United States;

(7) Amounts derived by any person as compensation for the receiving, washing, sorting, and packing of fresh perishable horticultural products and the material and supplies used therein when performed for the person exempted in RCW 82.04.330, either as agent or as independent contractor;

(8) Amounts derived as compensation for services rendered or to be rendered to patients by a hospital, as defined in chapter 70.41, devoted to the care of human beings with respect to the prevention or treatment of disease, sickness, or suffering, when such hospital is operated by the United States or any of its instrumentalities, or by the state, or any of its political subdivisions;

(9) Amounts derived as compensation for services rendered to

patients by a hospital, as defined in chapter 70.41, which is operated as a nonprofit corporation, nursing homes and homes for unwed mothers operated as religious or charitable organizations, but only if no part of the net earnings received by such an institution inures directly or indirectly, to any person other than the institution entitled to deduction hereunder. In no event shall any such deduction be allowed, unless the hospital building is entitled to exemption from taxation under the property tax laws of this state;

(10) Amounts derived by a political subdivision of the state of Washington from another political subdivision of the state of Washington as compensation for services which are within the purview of RCW 82.04.290 (-);

(11) By those engaged in banking, loan, security or other financial businesses, amounts derived from interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties;

(12) By those engaged in banking, loan, security or other financial businesses, amounts derived from interest paid on all obligations of the state of Washington, its political subdivisions, and municipal corporations organized pursuant to the laws thereof (-);

(13) Amounts derived as interest on loans by a lending institution which is owned exclusively by its borrowers or members and which is engaged solely in the business of making loans for agricultural production.

**NEW SECTION.** Sec. 2. This act is necessary for the immediate preservation of the public peace, health and safety, the support of the state government and its existing public institutions, and shall take effect immediately.

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EXPLANATORY NOTE

RCW 82.04.430 was twice amended during the 1970 extraordinary session.

Section 5, chapter 65, Laws of 1970 ex. sess. added subsection (10) relating to amounts derived as compensation for services from one political subdivision of the state by another political subdivision.

Section 2, chapter 101, Laws of 1970 ex. sess. added to subsection (1) "and also amounts derived as dividends by a parent from its subsidiary corporations". Three subsections were also added, herein renumbered as: (11) relating to interest received on investments or loans secured by first

mortgages or trust deeds on nontransient residential properties by certain financial businesses; (12) relating to interest received by certain financial businesses on obligations of the state, its political subdivisions, or municipal corporations; and (13) relating to interest derived on loans by institutions engaged solely in making loans for agricultural production.

As these amendments appear to be in different respects, the purpose of this bill is to give effect to each by reenacting the section with the amendments incorporated therein.

Passed the House January 29, 1971.

Passed the Senate February 17, 1971.

Approved by the Governor February 26, 1971.

Filed in Office of Secretary of State February 27, 1971.

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# Rules and Regulations

RELATING TO

The Revenue Act of 1935

Chapter 180, Laws of 1935

OF THE

State of Washington



Issued by the Excise Tax Division of the Tax Commission  
of the State of Washington

Commissioners

H. H. HENNEFORD, Chairman  
T. M. JENNER                      T. S. HEDGES

Counsel --- Excise Tax Division  
DONALD H. WEBSTER

Revised April 1, 1936

1320  
STATE PRINTING PLANT  
OLYMPIA

Sales by supply houses of articles of equipment, such as kitchen utensils, fountain fixtures, booths and the like to restaurants, soda fountains, beer parlors, etc., are retail sales upon which the Retail Sales Tax must be collected by the supply houses. In the same category are sales of napkins, whether linen or paper, toothpicks, matches and the like.

**BONA FIDE INITIATION FEES, DUES, CONTRIBUTIONS, DONATIONS, TUITION FEES AND ENDOWMENT FUNDS—DEDUCTIONS**

**Rule 117.**

In computing tax liability, amounts derived from bona fide initiation fees, dues, contributions, donations, tuition fees and endowment funds may be deducted from the measure of tax under the Business and Occupation Tax. This deduction is to be strictly construed and such amounts may only be deducted provided,

- (1) they are bona fide, and
- (2) they have been included in the "Gross Amount" reported under the classification with respect to which the deduction is sought, and
- (3) they have not been otherwise deducted through inclusion in the amount of an allowable deduction taken under such classification for another reason, and
- (4) they do not exceed the limitations hereinafter set forth.

Amounts which may be deducted as initiation fees include only amounts actually required to be paid by a person to a club or similar organization for the sole privilege of joining such club or similar organization.

Amounts which may be deducted as dues include only amounts which a member must pay toward the support of a club or similar organization in order to retain his membership therein and does not include amounts which are for or graduated upon services rendered to a member of such club or organization.

The term "tuition fees" refers only to fees charged by an educational institution and, in addition to instruction fees, includes library, laboratory, health and other special fees and amounts charged for room and board when the property or service for which such charges are made is furnished exclusively to the students or faculty of such institution.

An "educational institution," which may deduct "tuition fees," includes any institution created or generally accredited as such by the state and offering to students an educational program of a general academic nature. Such institutions include the following:

(a) The common schools, the state normal schools, the University of Washington, the State College of Washington and such other schools which are or may be established by law and maintained at public expense as part of the "uniform school system" provided for in Remington's Revised Statutes, section 4518, et seq.;

(b) Parochial schools and private schools accredited to schools of the "uniform school system" by the State Board of Education or the State Department of Education;

(c) Schools whose students and credentials are accepted without examination by the schools referred to in (a) and (b) above.

A business college, dancing school, music school or any trade or specialty school generally is not an "educational institution" within the meaning of

that term as defined above and, therefore, is not permitted the deduction for "tuition fees," which are taxable under the classification "Service and Other Business Activities" at the rate of  $\frac{1}{2}$  of 1%.

The right to deduct bona fide initiation fees, dues, contributions, donations, tuition fees and endowment funds does not exempt any person, association or society from tax liability upon selling tangible personal property or upon providing facilities or services for which a special charge is made to members or others.

#### SALES OF CONTAINERS, WRAPPING AND PACKING MATERIALS AND RELATED PRODUCTS

##### Rule 118.

When used in this rule, the term "containers" includes all containers, boxes, wrapping and packing materials, bags, twines, wrapping papers, gummed tapes, cellophane, bottles, drums, cartons, sacks or other packing, packaging, containing and wrapping materials in which tangible personal property may be contained.

Sales of containers to persons for use in connection with rendering services, or for personal or other uses, are sales for consumption and the Retail Sales Tax must be collected thereon. For example, the sale of paper boxes to a laundry is subject to tax because laundries use such boxes in connection with rendering services and do not sell property contained therein.

Sales of containers to persons who resell the containers in the regular course of business are not subject to the Retail Sales Tax. Included in this class are sales of envelopes to a stationer and sales of boxes and packing materials to persons packing fruit for others.

Sales of containers to persons who sell tangible personal property contained in such containers are sales for resale and not subject to the Retail Sales Tax if title to the containers passes to other persons along with the property sold and contained therein. For example, sales of wrapping paper and boxes to a department store, cans to a cannery, or beer bottles to a brewery, are sales for resale because the department store, cannery and brewery resell goods contained therein.

Sales of containers to persons who sell tangible personal property in the containers, but retain title to such containers which are to be returned for reuse, are sales for consumption, and the Retail Sales Tax must be collected thereon. This class may include such containers as wooden or metal bottle cases, barrels, hogsheads, gas tanks, carboys, drums, bags, milk bottles and many others when title remains in the seller and when they are customarily returned to and reused by him in making other deliveries. In such cases, if a charge is made against, or deposit is required from, the customer for the container, with the understanding that such charge will be cancelled or deposit rebated when the container is returned, such amounts will be considered as security for the use and the return of the container, and there is no resale of the container.

#### LABELS, TAGS AND NAMEPLATES

##### Rule 119.

Sales of labels, tags or name plates to persons for use in connection with rendering services, for personal or business use, or which do not become an inseparable part of products sold, are sales for consumption and the Retail

NO. 80544-0

**SUPREME COURT  
STATE OF WASHINGTON**

HOMESTREET, INC., et al.,

Petitioners,

v.

STATE OF WASHINGTON,  
DEPARTMENT OF REVENUE,

Respondent.

DECLARATION OF  
SERVICE

CLERK

RECEIVED  
SUPREME COURT  
STATE OF WASHINGTON  
2008 JUN 20 P 4: 30  
BY RONALD R. CARPENTER

I, KRISTIN D. JENSEN, state and declare as follows:

I am a citizen of the United States of America and over 18 years of age and not a party to this action. On June 20, 2008 I provided a true and correct copy of Supplemental Brief of Respondent Department of Revenue and this Declaration of Service to be served via U.S. mail (through Consolidated Mail Services), with proper postage affixed to:

ROBERT L. MAHON  
SCOTT EDWARDS  
GREGG BARTON  
PERKINS COIE LLP  
1201 THIRD AVENUE, SUITE 4800  
SEATTLE, WA 98101

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

Executed this 20<sup>th</sup> day of June, 2008, at Olympia, Washington.



KRISTIN D. JENSEN, Legal Assistant