ROBERT G. HUTCHINS - LEGAL BULLETINS

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In 2004, a unit of Appleway Chevrolet, Inc., a Spokane car dealer, sold a used Volkswagen Cabriolet to one Herbert Nelson. The stated price for the car was $16,822. Appleway added both sales tax and a proportionate business and occupation ("B&O") tax to that price. The latter tax was $79.23 and the fact that it was being added was disclosed in the sale documents. Nelson's wife also initialed an acknowledgement that the Nelsons were aware both of the total amount they were required to pay and of the fact that $79.23 of the total reimbursed Appleway's B&O tax.

Subsequently, the Nelsons brought a class action lawsuit against Appleway on behalf of themselves and all other Appleway customers who had reimbursed the B&O tax. The Nelsons sought a judicial declaration that Appleway's collection of this tax was illegal, plus an injunction against future collections and a judgment for damages.

The case immediately became a cause celebre. In addition to counsel to the parties, a legion of outside attorneys appeared on behalf of various auto industry participants and the Association of Washington Business and filed amicus curiae ("friend of the court") briefs supporting Appleway.

Nevertheless, on April 26, 2007, in a 6 to 3 decision, the Washington Supreme Court ruled in favor of the Nelsons. Much of the majority opinion is concerned with procedural issues, but in the end the majority reached the following conclusion: Because the relevant statute expressly imposes the B&O tax on Appleway, and not its customers, it follows that Appleway is *prohibited* from collecting that tax by *adding* it to the final sale price. Put differently, Appleway could *include* the B&O tax in the *asking* price for its cars, but it could not add the tax at the end of each sale transaction after the "final" price had been "negotiated," even if the tax was fully disclosed.[1]

That tour de force can be understood only in a wider context. The Washington legislature recognizes that business sellers can be assessed for delinquent taxes much more conveniently than buyers. Accordingly, while Washington's retail sales tax is imposed nominally on buyers, sellers have an affirmative duty to collect it as agents of the state and to pay it to the Department of Revenue on a quarterly basis. Their failure to do so is a gross misdemeanor.[2]

By contrast, the B&O tax is imposed directly on the sellers themselves. The statute provides: "It is not the intention …that the (B&O) taxes …be construed as taxes upon …purchasers or customers, but that such taxes be levied upon, and collectible from, the person engaging in … business…and…shall constitute a part of the operating overhead of such persons." [3]

The majority opinion characterized the statute as "unambiguous" and noted that "overhead" is a common term referring to the cost of doing business, as though it followed somehow that Appleway could not add its B&O tax to the sale price. The inconsistency between allowing

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[1] See, *Herbert Nelson, et al v. Appleway Chevrolet, Inc. et al,* available at **www.courts.wa.gov/opinions**. The dissenting opinion is published separately on the same webpage.

[2] See, RCW 82.08.050(1) and (2).

[3] See, RCW 82.04.500

Appleway to include the B&O tax in its asking price while prohibiting Appleway from adding the tax to the "final" price at the end of the transaction was explained thus: "…Appleway cannot necessarily receive whatever price it sets; the market determines the fair market value, not the costs of doing business….The $16,822 negotiated between Appleway and Nelson is presumably that market price; Appleway cannot then add its B&O tax liability on top of this final price."[4]

The majority's rationale is shaky at best. There is an "efficient" market for publicly traded securities that takes account of all current information available about them and establishes a reliable benchmark for their presumed "value," but no similar market exists for used Volkswagen Cabriolets. It strains credulity to assume that used car buyers accept a "final" price that reflects a "market value" and agree to consummate their purchase before being apprised of dealer preparation fees, taxes and any other additional charges. Indeed Herbert Nelson conceded he knew he could still "walk away" from his transaction after the B&O tax was disclosed to him.[5]

The dissenting opinion declared that, if the legislature really meant to prohibit Appleway from collecting the B&O tax, the prohibition would apply no matter when the tax was added. The fact that the tax is labeled "overhead" does not suggest such a prohibition. Appleway's obligations to pay rent, wages and the like are also "overhead," yet nothing prevents Appleway from including those items in the price of its cars and identifying them as discrete elements of its pricing method. It cannot possibly matter to the parties whether the B&O tax, as an item of overhead, is identified at the beginning of the sale transaction or at the end of it. (I would add that it doesn't matter whether the tax is identified at all. Buyers are concerned with the all-in cost, not its components.)

There could be another explanation. Although the Nelsons did not claim they had been deceived, the majority may simply have balked at the spectacle of Appleway invoicing the B&O tax as though it were equivalent to the sales tax, i.e. an obligation the buyer was *required* to pay that Appleway was collecting as an agent of the state. In any case, the statute merely expresses the legislature's intent not to impose the B&O tax on customers as is the case with the sales tax. A rational basis for that distinction is not hard to find. Fundamental fairness dictates that taxes be imposed on persons who consciously engage in the taxed activity. Appleway chose to enter the car business. Its customers choose to buy its cars. The tax burden is apportioned accordingly.

We may not have heard the end of this. Appleway is part of a corporate group that operates dealerships and supporting facilities for a number of automobile manufacturers. The cost of refunding the B&O tax to all customers, of all dealerships, for all years, could be devastating. Other interested parties have already joined the controversy and the case has constitutional implications. It would not surprise me to see this dispute reach the United States Supreme Court.

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[4] See, opinion, page 5.

[5] See, dissenting opinion at page 6.