**IN THE SUPREME COURT OF THE STATE OF WASHINGTON**

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| CERTIFICATION FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT<br>IN<br>JARED PECK,<br>Plaintiff,<br><br>and<br><br>JAMES BOWDEN, a Washington resident, individually and on behalf of all the members of the class of persons similarly situated,<br>Plaintiff-Appellant,<br><br>v.<br><br>AT&T MOBILITY, a Delaware limited liability company doing business as Cingular Wireless, AKA Cingular Wireless, LLC; NEW CINGULAR WIRELESS Services, Inc., a Delaware corporation doing business as AT&T Wireless; NEW CINGULAR WIRELESS SERVICES PURCHASING COMPANY LP, a Delaware limited partnership doing business as Cingular Wireless; NEW CINGULAR WIRELESS PCS LLC, a Delaware limited liability company doing business as Cingular Wireless,<br>Defendants-Appellees. | ) | No. 85581-1<br><br>En Banc<br><br>Filed April 26, 2012 |

C. JOHNSON, J. —This certified question from the Ninth Circuit Court of

Appeals centers on whether under RCW 82.04.500, a seller may, upon disclosure, recoup its business and occupation (B&O) tax by collecting a surcharge to recover gross receipts taxes in addition to its monthly service fee. We hold that, regardless of disclosure, RCW 82.04.500 prevents a business from recouping the B&O tax as an added charge to its sales price.

## FACTS

James Bowden purchased three cellular telephones and a monthly cellular service plan for each telephone at a Cingular kiosk. As part of the purchase process, he signed a one-page Wireless Service Agreement (Agreement) for each plan. The Agreement included the cost for the monthly service fee and optional plan features such as text messaging. At the bottom of the Agreement was the following provision:

> REGULATORY COST RECOVERY FEE Cingular also imposes the following charges: a Regulatory Cost Recovery Fee of up to $1.25 to help defray its costs incurred in complying with obligations and charges imposed by State and Federal telecom regulation, *a gross receipts surcharge*, and State and Federal Universal Service charges. The Regulatory Cost Recovery Fee is not a tax or a government required charge.

Appellant's Br., App. (emphasis added).

The Agreement also incorporated the "Terms of Service," which were

outlined in a separate brochure that Bowden received at the time of purchase. The Terms of Service included that, in addition to the rate plan, Cingular's charges would include "applicable taxes and governmental fees, whether assessed directly upon you or upon Cingular." Appellee's Supplemental Excerpts of Record (ASER) at 68. Cingular's web site also had information about the gross receipts surcharge. ASER at 132-41.

Cingular's monthly service fee did not include Washington's B&O tax. The B&O tax, however, was listed as a "State B and O Surcharge" on Bowden's monthly bills, for which he was charged various amounts for each of the phones, ranging from $.05 to $.44 per month. 2 Appellant's Excerpts of Record (AER) at 137. During deposition, Cingular's senior tax manager testified that Cingular charged the B&O tax surcharge to its customers as a separate line item and that it was "very much like a transactional tax, which you would think that was a sales tax." 2 AER at 129. It is undisputed that Cingular properly disclosed the surcharge, and Bowden accepted the plan and the B&O tax surcharge without objecting to the inclusion of the surcharge or attempting to make adjustments to the terms or price of the plan.

This suit was originally filed in state court by Jared Peck who alleged similar facts and claims. Cingular removed the case to federal court. The federal district court dismissed Peck's claims, but the Ninth Circuit Court of Appeals reversed and remanded the case to state court. Bowden joined the suit and sought class certification. Peck took a voluntary dismissal. Cingular again removed the case to federal court and moved for summary judgment. The federal district court granted Cingular's motion. Bowden appealed the summary judgment order to the Ninth Circuit. Due to potential conflict with our decision in *Nelson v. Appleway Chevrolet, Inc.*, 160 Wn.2d 173, 157 P.3d 847 (2007), and the Court of Appeals decision in *Johnson v. Camp Automotive, Inc.*, 148 Wn. App. 181, 199 P.3d 491 (2009), the Ninth Circuit certified this question to us. *Peck v. AT&T Mobility*, 632 F.3d 1123 (9th Cir. 2011).

CERTIFIED QUESTION

Under RCW 82.04.500, may a seller recoup its business and occupation taxes where, prior to the sale of a monthly service contract, the seller discloses that in addition to the monthly service fee, it collects a surcharge to cover gross receipts taxes?

## ANALYSIS

Washington State charges the B&O tax on all business "for the act or privilege of engaging in business activities" in the state, which is measured against the value of products, gross proceeds of sales, or gross income of a business. RCW 82.04.220(1). The tax is levied directly on businesses as part of operating overhead:

> It is not the intention of this chapter that the taxes herein levied upon persons engaging in business be construed as taxes upon the purchasers or customers, but that such taxes shall be levied upon, and collectible from, the person engaging in the business activities herein designated and that such taxes shall constitute a part of the operating overhead of such persons.

RCW 82.04.500.

We addressed whether RCW 82.04.500 permits a business to pass the B&O tax through to its customers in *Nelson*, concluding that a seller was not permitted to pass the tax through as an added charge to the final purchase price. Due to the facts presented in *Nelson*, and the Court of Appeals' application of *Nelson* to its *Johnson* decision, the parties here disagree on whether the B&O tax may be passed through if disclosed. Cingular contends that under *Nelson*, the statute permits a seller to charge a B&O surcharge to its customers as long as the charge is disclosed to the customer prior to the sale of the service contract. The Ninth Circuit appears to also

share a similar interpretation. *See Peck v. Cingular Wireless, LLC*, 535 F.3d 1053, 1058 (9th Cir. 2008) (holding that RCW 82.04.500 is not preempted by federal law prohibiting state regulation of "rates" under the Federal Communications Act, 47 U.S.C. § 332(c)(3)(A), because the statute regulates disclosure). On the other hand, Bowden argues that under *Nelson*, the statute does not permit an added charge for the B&O tax regardless of disclosure. Because of these conflicting interpretations, we take a closer look at *Nelson* and *Johnson*, reconciling any potential conflict between the decisions and clarifying any confusion.

In *Nelson*, the superior court granted summary judgment in favor of the customers, concluding the seller's collection of the B&O tax from customers violated RCW 82.04.500. The Court of Appeals affirmed, and the seller petitioned for our review. There, the seller and purchaser negotiated a sales price for a car. The seller charged several fees and taxes in addition to the agreed sales price, including an added charge for the B&O tax. The seller disclosed it was passing the B&O tax through four times in the contract, though our opinion noted that the purchaser paid the tax under protest. The purchaser initialed a line acknowledging he understood that the B&O tax was being passed through as overhead and that he

was paying the sales tax on the sales price and B&O tax amounts. In reaching our conclusion, we noted that like any overhead, such as rent, insurance, and other office expenses, RCW 82.04.500 permits businesses to pass the B&O tax through to its customers as overhead, but prevents businesses from directly imposing the tax on its customers. Like any overhead cost, we explained that the B&O tax, if passed through, must be factored into, that is, included in, the sales price. But in *Nelson*, the seller added the tax to the final price like it did a sales tax, which violated RCW 82.04.500. Therefore, we affirmed the Court of Appeals and held that the seller improperly charged the purchaser the B&O tax on top of the final price. *Nelson*, 160 Wn.2d at 178-82, 184-85.

Despite reaching the opposite conclusion, the Court of Appeals decision in *Johnson* is consistent with *Nelson.* In *Johnson*, the Court of Appeals concluded that the car seller properly passed the B&O tax through to its customer. There, during negotiations for a car, the B&O tax amount was disclosed on a "writeback" used to facilitate negotiations. The writeback also included a statement that the seller understood the "above figures have been negotiated." *Johnson*, 148 Wn. App. at 183 (emphasis omitted). The purchasers initialed the writeback and

finalized the sale. During summary judgment, the seller submitted unopposed declarations establishing that the purchase price included a B&O tax that was disclosed and negotiated. Given this, the Court of Appeals held that *Nelson* was distinguishable because in *Johnson*, the purchaser negotiated with the seller about the B&O tax before reaching the agreed price. *Johnson*, 148 Wn. App. at 183-85. Implicit in the Court of Appeals' conclusion is that the B&O tax was factored into the sales price. Therefore, because in *Johnson* the B&O tax was included in, not added to, the sales price, *Johnson* is consistent with *Nelson.*

Cingular contends that under *Nelson*, so long as a B&O surcharge is disclosed before a transaction is finalized, the seller can properly recoup its B&O taxes as an added-on charge under RCW 82.04.050. To support its argument, Cingular primarily points to our discussion in *Nelson*, where we state:

> [I]t is lawful for [the seller] to disclose a B&O charge to Nelson *during* the course of negotiating a purchase price or later identify any claimed element of overhead. However, [the seller] may not add a B&O charge as one of several fees and taxes *after* [the seller] and Nelson negotiated and agreed upon a final purchase price.

*Nelson*, 160 Wn.2d at 181. Thus, Cingular argues that because it disclosed the B&O surcharge to Bowden prior to purchase—in the Agreement, in the Terms of Service,

and on its web site—under *Nelson*, it properly passed the B&O tax through.

The above selection, however, cannot be read in isolation. When read in context, that portion of our *Nelson* decision shows disclosure was not central to our holding, but rather shows we were addressing the seller's claims about disclosure. The selection is found at the end of a paragraph in *Nelson*. In that paragraph, we began with the seller's claim that the Court of Appeals' decision meant a seller "could add on the tax as long as it did not disclose or itemize it to the customer," meaning, sellers "remain[ed] free to pass through the B&O tax to consumers . . . *but only so long as they bury the pass-through*." *Nelson*, 160 Wn.2d at 181 (boldface omitted) (second alteration in original). Then, in response, we explained that the Court of Appeals decision could not stand for that proposition because the court (1) explicitly found the add-on was improper and (2) did not prohibit disclosure. Rather, we noted the Court of Appeals stated that "'the seller *can* disclose the B&O overhead charge to the purchaser, but it must be done while setting the final purchase price. The process here involved the negotiation of a price; hence, the information should have been disclosed as part of that process.'" *Nelson*, 160 Wn.2d at 181 (quoting *Nelson v. Appleway Chevrolet, Inc.*, 129 Wn. App. 927,

945, 121 P.3d 95 (2005) (emphasis added)). The above selection is found at this point in the paragraph. Explaining what the Court of Appeals meant, we clarified that it was lawful for the seller to disclose the B&O charge during negotiations, meaning that the price being negotiated included a B&O charge; it was also lawful for the seller to identify, after negotiations, that the purchase price included a B&O charge as an overhead cost. However, we explained the seller could not add the B&O charge on the agreed-to purchase price. *Nelson*, 160 Wn.2d at 181. Put simply, whether disclosed or not, the seller could properly pass the B&O tax through as an overhead line itemization, but not as an added charge.

Moreover, any confusion in that paragraph is clarified later in *Nelson* where we address the seller's argument that the Court of Appeals decision violated its First Amendment right to free speech. Responding to that argument, we expressly state that RCW 82.04.500 was silent about disclosure. As mentioned, we explained that a business is free to disclose to its customer that the sales price *included* the B&O tax, whether it was during the course of or even after negotiations. *Nelson*, 160 Wn.2d at 184. Therefore, putting Cingular's selection of *Nelson* into its proper context shows that neither disclosure nor the timing of disclosure was essential to

our holding.

Rather, the crux of *Nelson* is that under RCW 82.04.500, a business cannot add on the B&O tax to the sales price. This makes sense given that the legislature specifically stated "It is not the intention . . . that the taxes herein levied upon persons engaging in business be construed as taxes upon the purchasers or customers." RCW 82.04.500. Allowing the tax to be added on to a sales price would equate the B&O tax with the distinctly different sales tax, which are imposed on a purchaser but collected from the seller. If businesses were allowed to add the tax (here, the tax was described as a "surcharge") onto a sales price, consumers would effectively be taxed twice, making the B&O levy on businesses illusory and rendering RCW 82.04.500 meaningless.

When a business adds on fees to its sales price or in the fine print, it gives the appearance that the added charges have nothing to do with the price of its product or service. The B&O tax, however, has everything to do with a business's products or services as it is a levy for operating a business in Washington. RCW 82.04.220. Moreover, RCW 82.04.500 provides that persons engaging in business must treat the tax as operating overhead costs. Operating costs include, for example, labor,

office supplies, rent, and utilities. These are costs that businesses factor into or include in its sales price; it would be odd for a business, and likely not a wise business practice, to add on separate charges for each of those operating costs. Likewise, under RCW 82.04.500, the B&O tax is to be treated no differently. This is precisely why the tax must be factored in as overhead when a business is establishing its sales price and determining its profit margin. Although in the end businesses may charge the entire B&O tax amount to its customers as overhead, at least it will be reflected in a sales price that consumers can compare against competitors. But as we explained in *Nelson*, while a seller can increase its final price by the amount of the B&O tax, it cannot necessarily receive whatever price it sets because the market determines fair market value. *Nelson*, 160 Wn.2d at 180 n.5.

Here, Cingular's monthly service fee, the sales price of its service contract, did not include the B&O surcharge. Rather, on the Agreement, the surcharge was listed separately under the "Regulatory Recovery Fee" provision and described as a gross receipts surcharge. Additionally, Cingular's billing statements listed the surcharge separately like it was a sales tax, and both the sales tax and the B&O

surcharge were added on to the service fee. Indeed, Cingular's senior tax manager testified that the surcharge was "very much like a transactional tax, which you would think that was a sales tax." AER at 129. Under RCW 82.04.500, it is irrelevant that the surcharge was disclosed to Bowden prior to purchase, that the actual amount of the surcharge was not disclosed because it varied each month, or that Bowden did not object or make an attempt to adjust or negotiate the terms or price of the plan. Although in both *Nelson* and *Johnson* the seller disclosed the actual amount of the B&O tax unlike Cingular in this case, this factual difference is of no consequence. Like in *Nelson* where the tax was added to the sales price, here, Cingular's surcharge was also added on to its monthly service fee. This practice is not permitted under RCW 82.04.500.

## CONCLUSION

We answer no. Under RCW 82.04.500, even if disclosed, a seller is prohibited from recouping its B&O taxes by collecting a surcharge in addition to its monthly service fee.

AUTHOR:
Justice Charles W. Johnson

WE CONCUR:

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| | Justice James M. Johnson |
| | Justice Debra L. Stephens |
| Justice Tom Chambers | Justice Charles K. Wiggins |
| Justice Susan Owens | Gerry L. Alexander, Justice Pro Tem. |
| Justice Mary E. Fairhurst | |