Cite as 6 WTD 217 (1988)

BEFORE THE DIRECTOR
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Refund of	)	F I N A L D E T E R M I N A T I O N
	)	No. 86-29A
. . .	)	Registration No. . . . Tax Assessment No. . . .

[1] **RULE 193B:** B&O TAX -- WHOLESALING -- INTERSTATE COMMERCE -- NEXUS -- SIGNIFICANT SERVICES -- SOLICITING -- AMOUNT OF TIME. The examples of nexus listed in Rule 193B are not an exhaustive list of nexus nor are the examples mutually exclusive for purposes of illustrating the presence of nexus. Where a taxpayer may not meet the criteria of example (5) does not eliminate nexus if the activity fits another example or if the activity serves to establish or maintain a market, which is the legal principle that the examples are intended to illustrate. Accord: Det. No. 87-286, 4 WTD 51 (1987).

[2] **RULE 193B:** B&O TAX -- WHOLESALING -- INTERSTATE COMMERCE -- NEXUS -- SOLICITING -- NON-RESIDENT EMPLOYEE. Whether an out of state business solicits through a resident or non-resident employee is immaterial for purposes of establishing nexus. It is the holding that subsequent U.S. Supreme Court decisions have significantly limited McLeod, Commissioner of Revenue v. J. E. Dilworth Co. et al to its facts.

[3] **RULE 100, RCW 82.04.4286 AND RCW 82.32.060:** B&0 TAX -- EXEMPTION -- MULTIPLE ACTIVITIES -- REFUNDS -- UNCONSTITUTIONAL TAX -- RETROACTIVITY. The Washington Supreme Court in National Can Corporation v. Department of Revenue and Tyler Pipe Industries, Inc. v. Department of Revenue, 109 Wn.2d 878, cert. denied, 56 U.S.L.W. 3828 (1988) held that the U.S. Supreme Court decision in Tyler Pipe, which invalidated the multiple activities exemption of the B&O tax, applied prospectively only. The Department will follow that finding. Accord: Det. No. 87-215A, ___ WTD ___ (1988).

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

NATURE OF ACTION:

The taxpayer petitions from Det. No. 86-29 which denied the taxpayer's claim for refund. The issue arose out of an assessment of Wholesaling B&O tax which was paid in full on September 7, 1984 and thus, this proceeding is a refund request.

A brief note with respect to the background in this appeal is in order. This matter was originally filed for the Director's review February 10, 1986, however, since the taxpayer claimed relief under Armco, Inc. v. Hardesty, 467 U.S. 638, 81 L. Ed. 2d 540, 104 S. Ct. 2620 (1984) (*Armco*) (which caused significant uncertainty with respect to the status of Washington law) the Director withheld issuing a decision until the status of the B & O tax was determined. The U.S. Supreme court in Tyler Pipe Indust., Inc. v. Dep't of Revenue, ___ U.S. ___, 97 L. Ed. 2d 199, 107 S. Ct. 2810 (1987) struck down the multiple activities statute (RCW 82.04.440); however, the Washington State Supreme Court in Nat'l Can Corp. v. Dep't of Revenue, 109 Wn.2d 878, ___ P.2d ___, cert. denied, 56 U.S.L.W. 3828 (1988) denied all refunds. All uncertainty has now been eliminated with respect to this taxpayer and the Director now renders his decision.

TAXPAYER'S EXCEPTIONS:

Fujita, A.D. -- The taxpayer appeals the Determination for three reasons. First, the taxpayer claims that its non-resident salesperson spends less than one percent of his time in Washington and therefore does meet the test for nexus in WAC 458-20-193B (Rule 193B). Second, the taxpayer argues that the legal authority cited by the administrative law judge involved taxpayers who had resident agents but nevertheless claimed a lack of nexus. In this case, the salesperson is a non-resident and therefore, the authority is distinguishable. Lastly, in the alternative, the taxpayer claims that *Armco, supra,* obliterated the B & O tax liability this taxpayer might have to this state.

DISCUSSION:

Rule 193B provides in relevant part:

> RETAILING, WHOLESALING. Sales to persons in this state are taxable when the property is shipped from points outside this state to the buyer in this state and the seller carries on or has carried on in this state any local activity which is significantly associated with the seller's ability to establish or maintain a market in this state for the sales. If a person carries on

significant activity in this state and conducts no other business in this state except the business of making sales, this person has the distinct burden of establishing that the instate activities are not significantly associated in any way with the sales into this state. The characterization or nature of the activity performed in this state is immaterial so long as it is significantly associated in any way with the seller's ability to establish or maintain a market for its products in this state. The essential question is whether the instate services enable the seller to make the sales.

Applying the foregoing principles to sales of property shipped from a point outside this state to the purchaser in this state, the following activities are examples of sufficient nexus for application of the business and occupation tax:

(1) The seller's branch office, local outlet or other place of business in this state is utilized in any way, such as in receiving the order, franchise or credit investigation, or distribution of the goods.

(2) The order for the goods is given in this state to an agent or other representative connected with the seller's branch office, local outlet, or other place of business.

(3) The order for the goods is solicited in this state by an agent or other representative of the seller.

(4) The delivery of the goods is made by a local outlet or from a local stock of goods of the seller in this state.

(5) Where an out-of-state seller, either directly or by an agent or other representative, performs significant services in relation to establishment or[1] maintenance of sales into the state, the business tax is applicable, even though (a) the seller may not have formal sales offices in Washington or (b) the agent or representative may not be formally characterized as a "salesman."

(6) Where an out-of-state seller either directly or by an agent or other representative in this state installs its products in this state as a condition of the sale, the installation services shall be deemed significant

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[1] The word "or" replaced the word "and" in the 1983 revision of the rule.

> services for establishing or[2] maintaining a market in this state for such installed products and the gross proceeds from the sale and installation are subject to business tax.
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> Under the foregoing principles, sales transactions in which the property is shipped directly from a point outside the state to the purchaser in this state are exempt only if there is and there has been no participation whatsoever in this state by the seller's branch office, local outlet, or other local place of business, or by an agent or other representative of the seller. A franchise or credit investigation of a prospective purchaser and/or recommendation or approval by a local office upon which subsequent transactions are based is such a utilization of the local office as to render such subsequent transactions taxable. (Emphasis provided.)

The taxpayer refers specifically in its petition to paragraph (5) and argues that the amount of activity present in this case does not meet the criteria therein stated. In a recent nexus case, the Interpretation and Appeals Division had the opportunity to discuss the examples listed in Rule 193B, to wit, the judge stated:

> Although the taxpayer claims that because its activities are not included in the examples given in Rule 193B they cannot be held to establish local nexus, we are constrained to point out that its activities are included in example (5). Even were they not spelled out in one of the examples, it must be noted that the examples given are not an exclusive listing of activities which might give rise to taxability. The operative phrases in the rule (highlighted above) make it clear that any in-state activity (unless otherwise specifically exempt) that serves to "enable" the Washington sales of an out-of-state taxpayer are sufficient to render those sales taxable under the Washington business and occupation tax.

Det. No. 87-286, 4 WTD 51 (1987).

[1] The taxpayer was arguing, in that case, that none of the examples of Rule 193B described its activities. In this matter, this taxpayer is arguing that since it does not meet the criteria of paragraph (5), there is no nexus. With respect to both arguments, as the judge stated, the examples are nothing more than examples; they are not read to be as exhaustive nor, we now add, are they intended to be mutually exclusive. The examples merely

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[2] Id.

illustrate that the described activities enable the seller to make the sale.

In this matter, we need not reach the question as to whether this taxpayer is within Rule 193B(5), because we believe that this taxpayer cannot escape the example of paragraph (3). In paragraph (3), the taxpayer has sufficient nexus if the sales are solicited by an agent or other representative of the seller.

This taxpayer has an out-of-state sales representative who came to this state, solicited and sold on behalf of his employer. There is ample evidence that the facts of example (3) are present in this case and thus, we hold that there is sufficient nexus with respect to the sales that are made by the non-resident salesman. This is not a case where the state is attempting to tax more activity than what the salesperson performed in this state. The audit record reflects that the Department has dissociated non-related sales and has not sought to include the dissociated amounts from the measure of the tax. See Norton Company v. Illinois Department of Revenue, 340 U.S. 534 (1951).

[2] Next, the taxpayer draws a line between itself and the reported cases on nexus. It distinguishes the prevailing authority from itself, because in the cited cases, there were resident agents soliciting and making sales into this state whereas in the taxpayer's situation, there was no resident representative.

While the taxpayer has not cited McLeod, Commissioner of Revenue v. J. E. Dilworth Co. et al, 322 U.S. 327 (1944) (*McLeod*), this is the best authority upon which we think this taxpayer can rely for its proposition. In the past, taxpayers have argued that this case supports the proposition that a business tax cannot be imposed on the non-resident business if the only contact with the state is through a non-resident salesperson.

J. E. Dilworth Co., a Tennessee manufacturer, had no places of business in Arkansas. Orders for goods came through solicitation in Arkansas by salesmen domiciled in Tennessee, by mail, or by telephone. All orders were approved and goods were shipped from Tennessee, with title passing to the purchaser upon delivery to the carrier. A closely divided Court (four Justices dissenting) in a 1944 decision held that the commerce clause prohibited Arkansas from requiring Dilworth to collect and remit retail sales tax on these sales.

At issue here is the application of a gross receipts business and occupation tax rather than a retail sales tax, and so the question is this: Would the Supreme Court sitting today extend the *McLeod* case rationale to Washington's gross receipts business and occupation tax?

In the forty years since *McLeod* was decided, the Supreme Court has effected sweeping changes of the law in this area. For example, in a 1964 decision upholding the Washington business and occupation tax against claimed violations of the Due Process Clause and Commerce Clause, the Court attached no significance to the fact that two divisions of General Motors had no places of business within this state. The court noted that resident employees working out of their homes "performed substantial services . . . with relation to the establishment and maintenance of sales." General Motors Corp. v. Washington, 377 U.S. 436, 447 (1964) (*General Motors*). "Despite their label as 'homes' they served the corporation just as effectively as 'offices.'" Id.

However, the same can be said of nonresident employees who physically enter the state to solicit orders and otherwise promote sales. Consequently, the residency of persons physically present within the taxing state on the taxpayer's behalf does not appear to be a matter of constitutional significance under the rationale used in *General Motors*. In other words, *General Motors* represents a serious erosion of *McLeod*, the significance of which did not go unnoticed by Justice Goldberg who wrote:

> It is difficult, for example to distinguish between the in-state activities of the representatives here involved and the in-state activities of solicitors or traveling salesmen--activities which this Court has held are insufficient to constitute a basis for imposing a tax on interstate sales. . . . [Citing *McLeod* and other authority]. Surely the distinction cannot rest on the fact that the solicitors or salesmen make hotels or motels their "offices" whereas in the present case the sales representatives made their homes their "offices."

Id. at 456, Justice Goldberg dissenting.

Thus, where a taxpayer's employees physically enter a state to solicit orders and otherwise promote sales into the state, it is doubtful that the Supreme Court would deny that state the right to tax those sales merely because those employees happened to reside outside the state, *McLeod* notwithstanding.

Furthermore, *McLeod* was decided in an era when any direct tax (as distinguished from an indirect tax) on interstate commerce was regarded as unconstitutional. See Puget Sound Stevedoring Co. v. State Tax Commission, 302 U.S. 90 (1937), and Joseph v. Carter & Weekes Stevedoring Co., 330 U.S. 422 (1947). Under the analysis currently employed, even a direct tax on interstate commerce is permissible so long as: (1) it applies to an activity with a substantial nexus with the state; (2) it is fairly apportioned; (3) it does not discriminate against interstate commerce; and (4) it is fairly related to services provided by the state. Washington

Revenue Department v. Stevedoring Associates, 435 U.S. 734 (1978). See also Complete Auto Transit Co. v. Brady, 430 U.S. 274 (1977).

We therefore believe that *McLeod* has deteriorated to the point that it can no longer be argued that it presents a distinction and we conclude that it does not matter whether the sales are made by non-resident employees. Its application, to the extent of any viability, is limited to its facts. We so hold.

[3] Finally, this petition asks for relief under *Armco*, which was the basis for recent litigation in this state, Tyler Pipe Indust., Inc. v. Dep't of Revenue, ___ U.S. ____, 97 L.Ed.2d 199, 107 S.Ct. 2810 (1987). The U. S. Supreme Court invalidated the multiple activities exemption, RCW 82.04.440, and remanded the case to the Washington Supreme Court to decide the issue of remedy.

On January 28, 1988, the Washington Supreme Court issued its opinion in Nat'l Can Corp. v. Dep't of Revenue, 109 Wn.2d 878, ___ P.2d ___ (1988). The Court ruled that the U. S. Supreme Court's decision in Tyler Pipe should be applied only prospectively from the date the opinion was issued, June 23, 1987. Thus, taxpayers were properly subject to Washington's B&O tax for periods prior to this date and no refunds were granted. We therefore deny a refund based upon the decision in *Armco*, and its Washington State progeny.

DECISION AND DISPOSITION:

The taxpayer's petition for refund is hereby denied.

DATED this 22nd day of July 1988.