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No. 44195-1-II

COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON

SPACE AGE FUELS, INC.,

Appellant,

v.

STATE OF WASHINGTON,

Respondent.

PETITION FOR REVIEW

Scott L. Jensen, WSBA #17526
Jay A. Boelter, WSBA #11676
Brownstein | Rask
1200 S.W. Main St.
Portland, OR 97205
(503) 221-1772

Philip A. Talmadge, WSBA #6973
Talmadge/Fitzpatrick
18010 Southcenter Parkway
Tukwila, WA 98188
(206) 574-6661

Attorneys for Appellant

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A. IDENTITY OF PETITIONER

Appellant Space Age Fuels, Inc. ("Space Age") hereby respectfully seeks review by the Supreme Court of the published Court of Appeals decision identified in Part B.

B. COURT OF APPEALS DECISION

The Court of Appeals filed its opinion on December 31, 2013. A copy of the slip opinion is in the Appendix at pages A-1 through A-11.

C. ISSUE PRESENTED FOR REVIEW

Under the Commerce Clause of the United States Constitution a state may only impose a tax on an out-of-state business if that business has substantial nexus with the taxing state. Substantial nexus is created when the out-of-state business engages in substantial activities in the taxing state that are significantly associated with the company's ability to establish and maintain a market for sales in the state. Does delivery of product by an out-of-state business in its own trucks to Washington customers, standing alone, create substantial nexus?

D. STATEMENT OF THE CASE

1. Background/Introduction.

The relevant factual and procedural history of this case is set forth in the Court of Appeals decision.[1] This matter arises out of the State of Washington's ("the State") assessment of significant Business and Occupations ("B&O") tax, together with interest and penalties, against Space Age. The State assessed these taxes on sales of non-branded fuel sold by Space Age, an Oregon company, to wholesale customers in Washington. The State assessed these taxes even though Space Age does not own or lease any real property in Washington, CP13, does not have any bank accounts in Washington, CP 14, does not have any employees or representatives in Washington, CP 15, does not have any contracts with any person or entity in Washington, CP 22, does not solicit any sales from Washington customers, CP 376, 380, makes no effort to secure new

[1] Certain of the facts stated in the Court of Appeals' decision are not relevant for Commerce Clause analysis. The court remarked that Space Age marks up its fuel prices to account for delivery costs, thereby making a profit. As explained below, delivery is not an activity that is significantly associated with Space Age's ability to establish and maintain a market for sales in Washington, and delivery does not create substantial nexus. Consequently, it is legally irrelevant whether or not Space Age makes a profit on its deliveries. Likewise, it is irrelevant for Commerce Clause analysis whether the sale "occurs" in Oregon when the customer places its order or in Washington when the fuel is delivered.

customers for its fuel in Washington, CP 54, and does not provide its customers or any potential customers with Space Age displays, brochures, product samples, or similar items. CP 22.

All of Space Age's sales to Washington customers are made over the telephone, at Space Age's office in Oregon. CP 54. In response to customer inquiries for price information, Space Age provides quotes by fax, telephone, or e-mail. CP 54; 380. Space Age's ability to make wholesale sales is driven solely by price. CP 54.

Space Age's sole activity in Washington is delivering fuel, in its own trucks, to Washington customers who had already decided to purchase that fuel based solely on its price. Those trucks return each day to Oregon.

2. The Decision of the Court of Appeals.

On December 31, 2013, Division II of the Court of Appeals ("Division II") issued a published opinion affirming the decision of the trial court. A-1 to A-11. Division II held that Space Age's deliveries alone were sufficient to create the requisite substantial nexus. A-6.

E. ARGUMENT WHY REVIEW SHOULD BE GRANTED

The Court is familiar with the criteria governing the acceptance of review of a Court of Appeals opinion. Here, the Court of Appeals decision satisfies three of these standards: RAP 13.4(b)(1), (3) and (4).

1. The Court of Appeals Decision Involves a Significant Question of Law Under the United States Constitution

This petition for review raises the question as to the scope of the State's power, under the Commerce Clause, to tax out-of-state businesses with limited connections to Washington. The Court of Appeals held that Washington may constitutionally tax an out-of-state business whose *only* activity in Washington was delivering a product to Washington customers, a product that the customers had already decided to purchase based solely on cost. In ruling that "delivery alone" is sufficient to create the requisite substantial nexus, Division II has expanded the limits of the State's power beyond what has been accepted by the United States Supreme Court and by this Court. Not only has Division II collapsed the minimum contacts analysis of the Due Process Clause with the substantial nexus analysis required by the Commerce Clause, it offers businesses no guidance on when they will subject themselves to taxation by Washington. Under Division II's analysis, seemingly any transaction in Washington by an out-

of-state business will satisfy the substantial nexus required by the Commerce Clause. As the petition raises a significant issue of law under the United States Constitution, review is appropriate under RAP 13.4(b)(3).

a. The Commerce Clause Prohibits Washington from Imposing a Tax on an Out-of-State Business that Lacks a Substantial Nexus with Washington

The Commerce Clause of the United States Constitution, U.S. Const. Art I, § 8, cl. 3, prohibits state actions that unduly burden interstate commerce. *Quill Corp. v. North Dakota*, 504 U.S. 298, 312, 112 S. Ct. 1904, 119 L. Ed. 2d 91 (1992). In the area of state taxation, for a tax imposed against an out-of-state entity to withstand a Commerce Clause challenge, the tax must, *inter alia*, be "applied to an activity with a substantial nexus with the taxing State." *Id.* at 311, quoting *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279, 97 S. Ct. 1076, 51 L. Ed. 2d 326 (1977). *Accord Lamtec Corp. v. Department of Revenue*, 170 Wn. 2d 838, 844, 246 P.3d 788, 791-92, *cert. denied*, ___ U.S. ___, 132 S. Ct. 95 (2011) (for a state to tax an out-of-state corporation the tax must meet the four-part *Complete Auto* test).

b. For Substantial Nexus to Exist, the Taxpayer must Engage in Substantial Activities in the Taxing State that are Significantly Associated with the Taxpayer's Ability to Establish and Maintain a Market for Sales in the Taxing State

In determining whether or not the requisite substantial nexus exists, "the crucial factor is whether the activities performed in [the taxing] state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales." *Tyler Pipe Industries, Inc. v. Washington State Department of Revenue*, 483 U.S. 232, 250, 107 S. Ct. 2810, 97 L. Ed. 2d 199 (1987), quoting *Tyler Pipe Industries, Inc. v. State Department of Revenue*, 105 Wn. 2d 318, 323, 715 P.2d 123, 126 (1986). *Tyler Pipe's* reference to the establishment of a market *for sales* is absent from Division II's opinion. The court did not explain how deliveries furthered a market for sales of fuel by Space Age in Washington.

Importantly, "substantial nexus" under the Commerce Clause is a different concept than the connection required between the taxpayer and the State under the Due Process Clause. The connection required by the Due Process Clause is simply "some minimum connection between a state and the person, property or transaction it seeks to tax." *Quill*, 504 U.S. at 306, 308. The "minimum contacts" required by the Due Process Clause is

thus a distinct, and lesser, standard than the "substantial nexus" required by the Commerce Clause. *Id.* at 3135 ("a corporation may have the 'minimum contacts' with a taxing State as required by the Due Process Clause, and yet lack the 'substantial nexus' with that State as required by the Commerce Clause").

c. The *Lamtec* Decision

This Court analyzed a claim that imposition of the B&O tax on an out-of-state taxpayer violated the Commerce Clause in *Lamtec*, *supra.* In that case, the taxpayer was a manufacturer of insulation and vapor barriers. *Lamtec*, 170 Wn. 2d at 840-41. The taxpayer manufactured its products in New Jersey, and sold them nationwide. *Id.* Its customers placed orders over the telephone. *Id.* at 841. The taxpayer did not have any offices or agents permanently in Washington. *Id.* at 840-41. It did, however, on two or three occasions per year, send three sales employees to visit major customers in Washington. *Id.* at 840. The employees made between 50 and 70 visits to Washington customers during the seven year period at issue. *Id.* The taxpayer estimated that the total amount of time spent in Washington by the employees each year was seven to 11 days. Brief of Respondent DOR, 2008 WL 8014770, at *4.

The employees did not solicit sales directly during these visits. *Lamtec*, 170 Wn. 2d at 841. During these visits the employees sometimes left brochures and product samples with the customers. Brief of Respondent DOR, 2008 WL 8014770, at *4. The employees answered customer concerns, addressed issues relating to the use of Lamtec's products, and participated in telephone calls to Lamtec's technical or customer service departments. *Id.*

According to the State, the taxpayer "admitted that it was engaging in efforts to maintain Lamtec's market in Washington" and "Lamtec considered the physical, in-person visits by its sales representatives significant to its business model and marketing program and would not even consider abandoning the visits." Brief of Respondent DOR, 2008 WL 8014770, at *5.

On that record, this Court held that the taxpayer had the requisite substantial nexus to allow the State to constitutionally impose the B&O tax:

> [t]o the extent that there is a physical presence requirement [to establish substantial nexus], it can be satisfied by the presence of activities within the state. * * * The activities must be substantial and must be associated with the company's ability to establish and maintain the company's market within the state. *The contacts by Lamtec's sales representatives were designed to maintain its*

> *relationship with its customers and to maintain its market within Washington State.* Nor were the activities slight or incidental to some other purpose or activity. We hold that *Lamtec's practice of sending sales representatives to meet with its customers within Washington was significantly associated with its ability to establish and maintain its market.*

Lamtec, 170 Wn. 2d at 851 (emphasis added).

d. The Court of Appeals Misapplied the Test for Determining Whether or Not Substantial Nexus Exists

In its published opinion, Division II misapplied the test for determining whether or not substantial nexus exists. As an initial matter, the court twice cited *Lamtec* for the proposition that physical presence creates the requisite substantial nexus: "A company's physical presence in Washington can establish a substantial nexus," A-5; "[b]ut Space Age fails to account for *Lamtec's* statement that a company's physical presence can establish a substantial nexus." A-10. The court thus suggests that physical presence alone can create substantial nexus, regardless of the nature of that presence. But this is not what this Court said in *Lamtec*. Instead, the Court held that "to the extent there is a physical presence requirement, it can be satisfied by the presence of activities within the state." *Lamtec*, 170 Wn. 2d at 850-51. Moreover, and most significantly, "[t]he activities must be substantial and must be associated the company's ability to establish

and maintain the company's market within the state." *Id.* at 851. Consequently, where a company's activities in the State are the basis for substantial nexus, those activities must be "substantial" and they must be "associated the company's ability to establish and maintain the company's market within the state." *Id.* at 851.

Division II compounded the error in its analysis by treating Space Age's purported physical presence and Space Age's deliveries as if they were two different things. First, the court stated that "Space Age's regular deliveries establish its physical presence in Washington." A-6. Then, it stated that "[b]oth Space Age's physical presence in Washington and its delivery activities are significantly associated with its ability to establish and maintain a market in Washington for its sales" (emphasis added). *Id.*[2]

But Space Age has no "physical presence" in Washington other than the delivery of fuel.[3] Under *Lamtec*, for Space Age's activities in Washington (*i.e.*, the delivery of fuel), to create the requisite substantial nexus those activities "must be substantial and must be associated with the

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[2] Division II did not explain why this is so.

[3] To the extent that Division II suggests that "sticking the tank" and/or pumping fuel from trucks into tanks is something distinct from delivery, such suggestion is wrong, as those tasks are simply part of the delivery process.

company's ability to establish and maintain the company's market within the state." *Lamtec*, 170 Wn. 2d at 851. In responding to Space Age's argument that delivery alone is not an activity significantly associated with Space Age's ability to establish and maintain its market in Washington, the court fell back on the conclusion that "Space Age fails to account for *Lamtec's* statement that a company's physical presence can establish a substantial nexus." A-10. Division II thus confused the mere fact that Space Age employees delivered fuel in Washington with the critical inquiry of whether those deliveries were significantly associated with Space Age's ability to establish and maintain its market in Washington.[4] The court was wrong to suggest that simply because Space Age makes deliveries in Washington, it has a physical presence in Washington, thereby necessarily creating substantial nexus.

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[4] In this regard, the Court of Appeals has essentially conflated the Commerce Clause with the Due Process Clause. As noted above, unlike the Commerce Clause, which requires substantial nexus, the Commerce Clause requires only "minimum contacts" between the taxpayer and the taxing state, and "substantial nexus" is more than "minimum contacts." *Quill*, *supra*, 504 U.S. at 313. The fact that Space Age employees delivered fuel in Washington is sufficient to establish "minimum contacts" under the Due Process Clause, but is insufficient to establish "substantial nexus" under the Commerce Clause.

On the "crucial factor" of whether Space Age's activities in Washington were substantial and significantly associated with Space Age's ability to establish and maintain a market in Washington, Division II made only the conclusory statements that "[b]oth Space Age's physical presence in Washington and its delivery activities are significantly associated with its ability to establish and maintain a market in Washington for its sales," and "Space Age ignores the extent to which its deliveries make possible 'the realization and continuance' of sales to its customers." A-10, quoting *Standard Pressed Steel Co. v. Washington Department of Revenue*, 419 U.S. 560, 562, 95 S. Ct. 706, 42 L. Ed. 2d 719 (1975).

The court did not, however, offer any basis for those two conclusory statements, leaving Space Age, and other similarly-situated entities, to guess at why deliveries meet this test, and what other activities may or may not meet this test. United States Supreme Court precedent, as well as a decision from Washington's Board of Tax Appeals,[5] recognize that delivery alone is not a nexus-creating event. In *Quill* the out-of-state taxpayer was a mail order company that had no outlets or sales

[5] Washington courts recognize the Board's special expertise on tax issues. *See Lamtec*, 170 Wn. 2d at 846; *Seattle Filmworks, Inc. v. State of Washington Department of Revenue*, 106 Wn. App. 448, 459, 24 P.3d 460 (2001).

representatives in North Dakota. It solicited business through catalogs and flyers, advertisements in national magazines, and telephone calls. It made annual sales of over $1 million to more than 3,000 customers in North Dakota. The merchandise was delivered by common carrier or through the United States mail. The Court held that while North Dakota's attempt to impose the tax in question on Quill passed muster under the Due Process Clause, it failed to pass muster under the Commerce Clause. The fact that products were shipped into North Dakota was not sufficient to create substantial nexus.

In *Sage V Foods, LLC v. State of Washington Department of Revenue*, 2012 WL 4794242 (Wa. Bd. Tax App. 2012), Sage was a California company. It sold rice flour and other rice-based products to approximately 20 Washington customers. These sales ranged from $1.8 million to $4.6 million per year. Most of the products were delivered to the customers in "PD" railcars that Sage leased. The DOR argued, as it does here, that the regular deliveries of Sage's products into Washington created substantial nexus. Applying the *Tyler Pipe* standard, the Board of Tax Appeals disagreed with DOR, declining to "equate the mere continuing delivery of [Sage's] product in the desired condition using the

new PD cars with 'substantial activities' in furtherance of the establishment and maintenance of the company's market within the state." *Id.* at *7. The Board noted that the delivery activity "could have just as easily been accomplished * * * by having the customer itself lease the PD cars." *Id.* The Board also found it noteworthy that Sage's "market was established prior to any contact or delivery of product." *Id.* The Board thus concluded that "Sage's use of leased rail cars for delivery was not 'significantly associated with [Sage's] ability to establish and maintain a market in this state for the sales," and that "the nexus necessary to support the imposition on Sage of the B&O wholesaling tax and litter tax has not been established." *Id.* at 9.

Sage is consistent with *Tyler Pipe*, *Standard Pressed Steel*, and *Lamtec*, all of which found substantial nexus based on contacts by the taxpayer's employees or representatives that were designed to ensure that customers would purchase, and continue to purchase, products from the taxpayer. In *Tyler Pipe* the individual whose activity created substantial nexus was an "in-state sales representative"; in *Standard Pressed Steel* the individual was an employee "whose primary duty was to consult with Boeing regarding its anticipated needs and requirements" for the taxpayer's

products; in *Lamtec* the individuals were employee "sales representatives." Space Age submits, as it argued before Division II, that activities "significantly associated with [its] ability to establish and maintain a market" in Washington for sales means activities designed to generate *initial and future sales* of products, and not simply delivery of a product that the customer has already decided to purchase for reasons unrelated to Space Age's activities in the taxing state, in this case price.

While Division II rejected Space Age's argument, it offered no explanation for why it was doing so, and it offered no defining test for determining when an activity is "significantly associated with the taxpayer's ability to establish and maintain a market in this state for sales." The Court of Appeals decision means that there is no principled limitation on substantial nexus under the Commerce Clause. The decision thus involves a significant issue under the United States Constitution, and review is appropriate under RAP 13.4(b)(3).

2. The Court of Appeals Decision Involves an Issue of Substantial Public Interest

The constitutional issue raised by Space Age's petition for review is not merely academic. The question of the extent of the state's taxing power under the Commerce Clause is an issue of substantial public interest

because it has a very real impact on decisions made by real world businesses operating in the national economy.[6] Whether or not a particular transaction is subject to taxation is a significant factor that a business must consider in determining whether or not to enter into that transaction in the first place. This issue is particularly significant for many e-commerce and border businesses in Oregon and Idaho. Illustrative is the Oregon mattress company that was forced out of business when it unwittingly became subject to Washington's B&O tax when it arranged for delivery of mattresses from its Portland metropolitan stores to customers in Clark County.[7]

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[6] This Court has historically exhibited an interest in examining the scope of the state's taxing power under a variety of circumstances. In addition to *Lamtec*, *see e.g. Flight Options, LLC v. State, Department of Revenue*, 172 Wn. 2d 487, 259 P.3d 234 (2011) (addressing whether out-of-state company had a tax situs in Washington and whether Washington could assess apportioned property taxes against that company without violating the Due Process Clause); *City of Seattle v. Rogers Clothing for Men, Inc.*, 114 Wn. 2d 213, 787 P.2d 39 (1990) (addressing whether city's special assessment violated the Equal Protection Clause).

[7] *See* Wendy Culverwell, *Mattress World Sunk by Washington Tax Penalties*, Portland Bus. J., Jan. 4, 2013, http://www/bizjournals.com/portland/news/2012/01/04/mattress-world-sunk-by-washington-tax.html. The article details the fact that DOR has stepped up efforts to seek taxes from so-called "cross-border" businesses, indicating that the issues presented in this case are capable of repetition as to businesses not only in Oregon, but in Idaho and elsewhere.

Division II's decision in this case demonstrates that the Court's decision in *Lamtec* has not put to rest the question of the scope of constitutional nexus under the Commerce Clause. This Court needs to offer definitive principles by which businesses and the DOR can be guided to assess if activities that touch upon Washington may constitutionally be taxed. The petition for review thus raises an issue of substantial public interest, and review is appropriate under RAP 13.4(b)(4).

3. The Court of Appeals Decision is in Conflict with a Decision of the Supreme Court

Finally, review is appropriate under RAP 13.4(b)(1) because the Court of Appeals decision is in conflict with a decision of the Supreme Court, namely *Lamtec*. As explained above, Division II's decision states that a company's physical presence in Washington can create substantial nexus, apparently without regard to the nature of that presence. In *Lamtec*, however, this Court held that "to the extent that there is a physical presence requirement, it can be satisfied by the presence of activities within the state," and that "[t]he activities must be substantial and must be associated with the company's ability to establish and maintain the company's market with the state." *Lamtec*, 170 Wn. 2d at 850-51. To the extent that Division II's decision holds that *any* physical presence in

Washington can establish substantial nexus, regardless of whether or not that physical presence is associated with establishing and maintaining a market in Washington, it conflicts with this court's *Lamtec* decision, and review is appropriate under RAP 13.4(b)(1).

F. CONCLUSION

Division II's published opinion raises a significant issue of law under the United States Constitution, namely whether "delivery alone" by an out-of-state company to customers in Washington amounts to the "substantial nexus" that is required before a State may impose its tax on such company without violating the Commerce Clause. The court's opinion fails to maintain the distinction between the "minimum contacts" required by the Due Process Clause and "substantial nexus" required by the Commerce Clause under United States Supreme Court precedent. If left to stand, Division II's opinion means that there is no principled limitation on substantial nexus under the Commerce Clause. This significant constitutional issue is of substantial public interest in view of expanding e-commerce and cross-border business, and DOR's stepped up

efforts to impose the B&O tax on such businesses. For these reasons, this Court should grant review of Division II's opinion.

DATED this 29th day of January, 2014.

BROWNSTEIN | RASK

Scott L. Jensen, WSBA #17526
Jay A. Boelter, WSBA #11676
Brownstein Rask
1200 S.W. Main St.
Portland, OR 97205
(503) 221-1772

and

TALMADGE/FITZPATRICK

Philip A. Talmadge, WSBA #6973
18010 Southcenter Parkway
Tukwila, WA 98188
Phone: (206) 574-6661

Attorneys for Appellant
Space Age Fuels, Inc.

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

DIVISION II

SPACE AGE FUELS, INC., Appellant, v. STATE OF WASHINGTON, Respondent.	No. 44195-1-II PUBLISHED OPINION

WORSWICK, C.J. — Space Age Fuels, Inc., an Oregon corporation, appeals summary judgment dismissing its claim for a refund of business and occupation tax payments. Space Age argues that the dormant commerce clause[1] prohibits Washington from taxing its activities because they lack a substantial nexus with Washington. We disagree and affirm.

[1] The "dormant" commerce clause is implied by article I, section 8, clause 3 of the United States Constitution. *Quill Corp. v. North Dakota*, 504 U.S. 298, 309, 112 S. Ct. 1904, 119 L. Ed. 2d 91 (1992).

FACTS

Space Age Fuels, Inc. is a retail and wholesale seller of fuel. Space Age is incorporated in Oregon and maintains its principal place of business in Clackamas, Oregon. Although all of its retail fuel stations are in Oregon, approximately 40 of its wholesale customers are in Washington.

Upon a wholesale customer's request, Space Age quotes fuel prices via telephone, fax, or email. Once it receives an order, Space Age delivers fuel to wholesale customers using vehicles it owns and operates.[2]

Because delivery is "another profit center," Space Age marks up its fuel prices to account for delivery costs. Clerk's Papers (CP) at 297. Thus, Space Age charges more for deliveries made at longer distances. Before transferring fuel from its delivery vehicle into a customer's storage tank, a Space Age employee will "stick the tank," i.e., measure its contents to ensure the tank can hold the fuel. When Space Age uses specialized vehicles to pump fuel into aboveground storage tanks for some customers, it charges more for this extra pumping service.

But Space Age's activities in Washington are limited. Space Age makes "no effort to secure new customers for its fuel in Washington" because it believes its wholesale customers base their purchases solely on price. CP at 54. Thus, no Space Age employees have visited Washington to solicit sales or assess a customer's needs. Further, Space Age does not own or lease any real property in Washington, and it has no Washington-based employees or assets. Instead, Washington customers contact Space Age.

[2] Rarely, Space Age delivers fuel by common carrier.

The Washington State Department of Revenue audited Space Age's books and records for the period between January 1, 2004, and June 30, 2007. During that time, Space Age grossed over $48 million from 1,675 recorded sales to wholesale customers in Washington.[3] Between July 1, 2005, and the end of the audit period, Space Age's vehicles drove 141,491 miles on Washington roadways.

The Department determined that Space Age owed $235,834 in unpaid business and occupation (B&O) taxes for its wholesaling activities in Washington during the audit period.[4] The Department also assessed interest and penalties.[5]

Space Age paid the tax assessment and then filed a claim for a refund in superior court, arguing that (1) there was no substantial nexus between Space Age and the State of Washington; and (2) without such a nexus, imposition of the B&O tax violated the dormant commerce clause. On cross motions for summary judgment, the trial court granted the Department's motion, denied Space Age's motion, and dismissed its refund claim.

Space Age sought direct review in our Supreme Court. But our Supreme Court transferred the case to us. Order, *Space Age Fuels, Inc. v. State*, No. 86972-3 (Wash. Oct. 30, 2012).

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[3] The number of actual deliveries "would likely be much higher" than the number of recorded sales because Space Age's books used a single sales entry to record all deliveries to a single customer in a given month. CP at 81.

[4] The B&O tax is imposed on "the act or privilege of engaging in business activities." Former RCW 82.04.220 (1961). After the audit period, the legislature amended RCW 82.04.220 to, inter alia, incorporate the constitutional requirement of a "substantial nexus with this state." LAWS OF 2010, 1st Spec. Sess., ch. 23, § 102; *see also* LAWS OF 2011, 1st Spec. Sess., ch. 20, § 101.

[5] The Department further assessed nominal amounts of unpaid retail sales taxes, retail B&O taxes, and hazardous substance taxes. Space Age has not sought refunds of these amounts.

ANALYSIS

Space Age argues that the trial court erroneously granted the Department's motion for summary judgment because the dormant commerce clause prohibits the Department from taxing Space Age. We disagree.

We review an order granting summary judgment de novo and engage in the same inquiry as the trial court. *TracFone Wireless, Inc. v. Dep't of Revenue*, 170 Wn.2d 273, 280-81, 242 P.3d 810 (2010). Summary judgment is appropriate when there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. CR 56(c). We consider the evidence and draw all reasonable inferences in the light most favorable to the nonmoving party. *Schaaf v. Highfield*, 127 Wn.2d 17, 21, 896 P.2d 665 (1995).

Two clauses of the United States Constitution limit a state's power to tax interstate commerce: (1) the Fourteenth Amendment due process clause and (2) the "dormant" commerce clause implied by article I, section 8, clause 3. *Quill Corp. v. North Dakota*, 504 U.S. 298, 301, 305, 112 S. Ct. 1904, 119 L. Ed. 2d 91 (1992). Under the due process clause, an out-of-state taxpayer must have sufficient minimum contacts with the taxing state such that taxation "does not offend traditional notions of fair play and substantial justice." *Int'l Shoe Co. v. Washington*, 326 U.S. 310, 316, 66 S. Ct. 154, 90 L. Ed. 95 (1945) (internal quotation marks omitted). Space Age does not challenge its tax liability on due process grounds.

Next, the dormant commerce clause prohibits a state from discriminating against or unduly burdening interstate commerce. *Quill*, 504 U.S. at 312. Yet a state may tax interstate commerce if the tax (1) applies to an activity having a substantial nexus with the taxing state, (2) is fairly apportioned, (3) does not discriminate against interstate commerce, and (4) is fairly

related to the services provided by the state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279, 97 S. Ct. 1076, 51 L. Ed. 2d 326 (1977). Space Age contests only the first element: it denies having a substantial nexus with Washington.[6]

Whether an out-of-state company has a substantial nexus with Washington is a question of law reviewed de novo. *See Lamtec Corp. v. Dep't of Revenue*, 170 Wn.2d 838, 842, 246 P.3d 788, *cert. denied*, 132 S. Ct. 95 (2011). Taxes are presumed valid, and the company bears the burden of showing that a substantial nexus does not exist. *Lamtec*, 170 Wn.2d at 843.

A substantial nexus exists when a company's activities in Washington are both substantial and significantly associated with its ability to establish and maintain a market in Washington for its sales. *Tyler Pipe Indus., Inc. v. Wash. Dep't of Revenue*, 483 U.S. 232, 250, 107 S. Ct. 2810, 97 L. Ed. 2d 199 (1987); *Lamtec*, 170 Wn.2d at 851. A company's physical presence in Washington can establish a substantial nexus. *Lamtec*, 170 Wn.2d at 845; *see Nat'l Geographic Soc'y v. Cal. Bd. of Equalization*, 430 U.S. 551, 562, 97 S. Ct. 1386, 51 L. Ed. 2d 631 (1977). Further, periodic visits can create a physical presence in Washington. *Lamtec*, 170 Wn.2d at 846. Thus, a company may have a physical presence in Washington even though it lacks a "brick and mortar address within the state." *Lamtec*, 170 Wn.2d at 851; *see Standard*

[6] Citing *Quill*, 504 U.S. at 313 & n.7, Space Age asserts that the dormant commerce clause's requirement of a substantial nexus is more stringent than the due process clause's minimum contacts requirement. Space Age then calls our attention to *Miller Brothers Co. v. Maryland*, 347 U.S. 340, 74 S. Ct. 535, 98 L. Ed. 744 (1954), a case in which taxation of an out-of-state company violated due process. In *Miller Brothers*, a Delaware company's occasional delivery of products to Maryland customers via its own vehicles did not establish minimum contacts with Maryland. 347 U.S. at 345. But given more recent developments in the law of minimum contacts, "the continued authority of *Miller Brothers* is in considerable doubt." *Brown's Furniture, Inc. v. Wagner*, 171 Ill. 2d 410, 426, 665 N.E.2d 795, *cert. denied*, 519 U.S. 866 (1996); *see Quill*, 504 U.S. at 307-08 (quoting *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 476, 105 S. Ct. 2174, 85 L. Ed. 2d 528 (1985)).

Pressed Steel Co. v. Wash. Dep't of Revenue, 419 U.S. 560, 562, 95 S. Ct. 706, 42 L. Ed. 2d 719 (1975).

Space Age's regular deliveries establish its physical presence in Washington. *See Lamtec*, 170 Wn.2d at 845-46. These deliveries are substantial because Space Age's recorded sales to Washington customers occurred, on average, more than once per day during the audit period. In addition, Space Age's vehicles drove extensively on Washington roads while delivering over $48 million of fuel to Washington customers.

Further, Space Age conducts substantial activities in Washington because, as a wholesale fuel distributor, Space Age sells *both* the commodity of fuel *and* the service of delivery to customers in Washington. The commodity sales occur in Washington when Space Age employees stick the tank and transfer fuel into its Washington customers' storage tanks. *See* RCW 82.04.040(1). Space Age charges more to make deliveries at longer distances, and it also charges more to pump fuel into aboveground tanks when necessary.

Both Space Age's physical presence in Washington and its delivery activities are significantly associated with its ability to establish and maintain a market in Washington for its sales. *Tyler Pipe*, 483 U.S. at 250. Because a substantial nexus exists, the Department's B&O tax assessment did not violate the dormant commerce clause.[7] *Complete Auto*, 430 U.S. at 279.

Arguing to the contrary, Space Age contends that delivery alone cannot establish a substantial nexus. In support of this contention, Space Age relies on (1) the example given in an

[7] We reject Space Age's assertion that this analysis "fails to acknowledge the difference between Due Process Clause analysis and Commerce Clause analysis." Reply Br. of Appellant at 17. We do not base our decision on whether Space Age has purposefully directed its activities at Washington residents so as to establish minimum contacts with this state. *See Quill*, 504 U.S. at 308.

interpretive rule published by the Department, (2) Space Age's own assertion that nexus-creating activities are activities designed to generate sales, and (3) the reasoning supporting the bright-line test applied in *Quill*, 504 U.S. 298.

A. *The Department's Interpretive Rule*

Arguing that delivery alone cannot establish a substantial nexus, Space Age asserts that the Department took the same view when promulgating an interpretive rule, WAC 458-20-193(11).[8] But this assertion lacks relevance to the issue before us for three reasons.

First, an interpretive rule such as WAC 458-20-193(11) is "not binding on the courts at all."[9] *Ass'n of Wash. Bus. v. Dep't of Revenue*, 155 Wn.2d 430, 447, 120 P.3d 46 (2005). Second, we give no deference to an agency's interpretative rule unless it reasonably interprets an ambiguous statute that the legislature has charged the agency with administering and enforcing. *Edelman v. State ex rel. Pub. Disclosure Comm'n*, 152 Wn.2d 584, 590, 99 P.3d 386 (2004). Even if WAC 458-20-193(11) interpreted the dormant commerce clause—and it does not do so—we would not defer to its interpretation because the Department does not administer or enforce the commerce clause of the United States Constitution.

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[8] WAC 458-20-193(11)(a) provides:

> Company A is located in California. It sells machine parts at retail and wholesale. Company B is located in Washington and it purchases machine parts for its own use from Company A. Company A uses its own vehicles to deliver the machine parts to its customers in Washington for receipt in this state. The sale is subject to the retail sales and B&O tax if the seller has nexus, or use tax if nexus is not present.

[9] WAC 458-20-193(11) is an interpretive rule because (1) its violation does not subject a person to a penalty and (2) it merely "sets forth the agency's interpretation of statutory provisions it administers." RCW 34.05.328(5)(c)(ii).

Third, WAC 458-20-193(11) illustrates only *what* taxes apply and *who* must pay them in interstate transactions. In the example of WAC 458-20-193(11)(a), an out-of-state seller uses its own vehicles to deliver products to an in-state buyer. The *seller* pays Washington *sales and B&O taxes* "if the seller has nexus"; otherwise, the in-state *buyer* pays Washington *use taxes*.[10] WAC 458-20-193(11)(a). Thus WAC 458-20-193(11)(a) shows merely that a substantial nexus is necessary to tax an out-of-state seller; it does not attempt to show whether a substantial nexus exists given a particular set of facts. We do not consider this provision further.

B. *Activity Designed To Generate Sales*

Space Age next contends that a substantial nexus can exist *only* by virtue of an activity that is "designed to generate sales." Br. of Appellant at 22. Space Age then attempts to distinguish its activities from the nexus-creating activities in *Tyler Pipe*, *Standard Pressed Steel*, and *Lamtec*. We disagree because generating sales is not the touchstone of all nexus-creating activity. As stated above, a substantial nexus exists when a company's activities in Washington "are significantly associated with [its] ability to establish and maintain a market in this state for the sales." *Tyler Pipe*, 483 U.S. at 250 (internal quotation marks omitted).

In *Lamtec*, an out-of-state company sent agents to Washington about two or three times per year to meet with major customers. 170 Wn.2d at 841. The agents shared information about the company's insulation and vapor barrier products, but they did not solicit sales directly. 170 Wn.2d at 840-41. Nonetheless, our Supreme Court held that the agents' visits created a substantial nexus because the visits were significantly associated with the company's ability to

[10] Sales and B&O taxes are paid to the Department by the seller. *See* RCW 82.04.220; RCW 82.08.050. In contrast, use taxes are paid by the buyer. *See* RCW 82.12.020.

establish and maintain a market for its products in Washington. 170 Wn.2d at 851. Whether the agents' visits generated sales was not determinative.

Likewise in *Standard Pressed Steel*, a Pennsylvania company sold nuts and bolts to Washington customers, principally Boeing. 419 U.S. at 561. The company had a single Washington employee, and the employee operated out of his home. 419 U.S. at 561. The employee, along with a group of engineers who periodically traveled to Washington, consulted with Boeing about its needs and addressed any difficulties with the company's nuts and bolts. 419 U.S. at 561. However, the employee did not take Boeing's orders, accept its payments, or deliver nuts and bolts. 419 U.S. at 561. Yet the Court held that a B&O tax assessment did not violate the dormant commerce clause because the company's Washington employee "made possible the realization and continuance of valuable contractual relations" between the company and its Washington customers. 419 U.S. at 562.

Lamtec and *Standard Pressed Steel* take a broader view of establishing and maintaining a market than Space Age's narrow emphasis on generating sales would allow. Attempting to distinguish these cases as well as *Tyler Pipe*, Space Age appears to argue that (1) business relationships are essential to generating sales and (2) Space Age has no business relationship with any of its 40 Washington customers, each of whom buys fuel on the exclusive basis of its

price.[11] But Space Age fails to account for *Lamtec*'s statement that a company's physical presence can establish a substantial nexus. 170 Wn.2d at 845. Moreover, Space Age ignores the extent to which its deliveries make possible "the realization and continuance" of sales to its customers. *Standard Pressed Steel*, 419 U.S. at 562. Space Age's argument is unpersuasive.

C. *The Quill Bright-Line Test*

Lastly, Space Age argues that its deliveries did not create a nexus under the reasoning of *Quill*, 504 U.S. 298. We disagree.

In *Quill*, the United States Supreme Court reaffirmed its prior holding that "a vendor whose only contacts with the taxing State are by mail or common carrier lacks the 'substantial nexus' required by the Commerce Clause." 504 U.S. at 311, 317 (citing *Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill.*, 386 U.S. 753, 87 S. Ct. 1389, 18 L. Ed. 2d 505 (1967), *overruled on other grounds by Quill*, 504 U.S. at 308). Thus *Quill* preserved the "safe harbor" protecting the mail-order industry from state sales taxes since *Bellas Hess*. 504 U.S. at 315-16.

Space Age asserts that it would fall within this safe harbor if it had made its deliveries by common carrier. It then argues, "Given the Commerce Clause's structural concerns about the effects of state regulation on the national economy, there is no reason for the constitutionality of the tax to turn on the method by which the fuel is delivered." Br. of Appellant at 25. But this

[11] Unlike the companies selling specialized products in *Tyler Pipe*, *Standard Pressed Steel*, and *Lamtec*, Space Age sells a commodity: a commercial good (namely fuel) for which the quality does not vary from one source to another. Thus it is plausible that business relationships, advertising, and branding do not generate Space Age's sales. But Space Age's president stated that delivery is "another profit center," i.e., a service for which Space Age charges its customers. CP at 297. That statement belies Space Age's factual assertion that its customers make purchases based *solely* on price. In other words, Space Age's wholesale customers buy its fuel partly because Space Age delivers it to them.

argument contradicts *Quill*. *Quill* fully considered the commerce clause's structural concerns and maintained a bright-line rule.[12] 504 U.S. at 312, 315. That rule is unavailing to Space Age because it delivered fuel in its own vehicles, not by common carrier.[13]

Similarly unavailing is the Board of Tax Appeals's recent decision finding no substantial nexus in *Sage V Foods, LLC v. Dep't of Revenue*, No. 11-704, 2012 WL 4794242 (Wash. Bd. of Tax Appeals Aug. 31, 2012). In *Sage*, an out-of-state company engaged a common carrier to deliver its food product to Washington customers, using rail cars leased by the out-of-state company. *Sage*, 2012 WL 4794242 at *7-8. But unlike the company in *Sage*, Space Age did not deliver its fuel by common carrier.

Each of Space Age's arguments fails. Because Space Age has a substantial nexus with Washington, the Department's B&O tax assessment did not violate the dormant commerce clause.

Affirmed.

Worswick, C.J.

We concur:

Hunt, J.

Johanson, J.

[12] *Quill* recognized, "Like other bright-line tests, the *Bellas Hess* rule appears artificial at its edges . . . . This artificiality, however, is more than offset by the benefits of a clear rule." 504 U.S. at 315.

[13] Because Space Age does not come within the safe harbor of *Quill* and *Bellas Hess*, we do not address the Department's assertion that the safe harbor protects a company *only* from sales and use taxes, and not from *all* taxes including the B&O tax. *See Lamtec*, 170 Wn.2d at 848-49.

DECLARATION OF SERVICE

On said day below I mailed and deposited in the U.S. Mail a true and accurate copy of the Petition for Review in Court of Appeals Cause No. 44195-1-II to the following parties:

Philip A. Talmadge
Talmadge Fitzpatrick,
18010 Southcenter Parkway
Tukwila, WA 98188

Charles Zalesky
Assistant Attorney General
David M. Hankins
Special Counsel
Revenue Division
P.O. Box 40123
Olympia, WA 98504-0123

Original E-Filed With

Washington Court of Appeals
950 Broadway
Ste 300, MS TB-06
Tacoma, WA 98402

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

Dated January 29, 2014, at Portland, Oregon.

Lynette Dawan

Lynette Dawan, Legal Assistant
Brownstein | Rask