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## I. INTRODUCTION

RCW 82.04.423 provides a business and occupation (B&O) tax exemption to direct sellers.<sup>1</sup> The exemption is for certain out-of-state sellers that sell consumer products in Washington exclusively to or through representatives using direct sale activities such as in-home parties or door-to-door solicitations. It is modeled on federal legislation that applies to representatives of sellers who market consumer products in the home or at other non-permanent retail locations such as booths at fairs and exhibitions, rather than in permanent retail establishments.

Appellant Dot Foods, Inc. (Dot), the nation's leading food redistributor, seeks the benefit of the direct seller's exemption. But the exemption is available only to sellers whose consumer products are sold "in the home or otherwise than in a permanent retail establishment." The exemption is not available to sellers, like Dot, whose products are sold in a permanent retail establishment. In addition, the direct seller's exemption is available only to sellers who exclusively sell or solicit the sale of consumer products to or through a direct seller's representative. It is not available to sellers, like Dot, whose representative solicits sales of non-consumer products. Furthermore, only natural persons can qualify as a

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<sup>1</sup> A copy of RCW 82.04.423 is appended to this brief at A-1.

direct seller's representative. The exemption is not available to sellers, like Dot, whose representative is a corporation.

For each of the reasons discussed in the above paragraph, Dot does not qualify for the direct seller's exemption. Dot further argues, however, that even if it does not qualify for the exemption, it nonetheless should receive a refund of all taxes assessed by respondent Department of Revenue (Department) after January 1, 2000, and all taxes subsequently paid by Dot, in reliance on the Department's pre-2000 interpretation of RCW 82.04.423.<sup>2</sup> Dot claims it is entitled to rely on the Department's pre-2000 interpretation of RCW 82.04.423 because the Department failed to comply with the procedural requirements of the Administrative Procedure Act (APA) by not informing taxpayers that it intended to radically change its policy when it revised WAC 458-20-246. Not only did Dot fail to raise this claim in the trial court, but it also is barred by RCW 34.05.375, which imposes a two-year time limit for commencing an action contesting the validity of a rule on procedural grounds. Dot's argument based on RCW 34.05.328 therefore cannot be considered.

This Court should affirm the trial court's order granting summary judgment to the Department.

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<sup>2</sup> Effective December 31, 1999, the Department revised WAC 458-20-246, the administrative rule interpreting the direct seller's exemption. A copy of the amended rule is appended to this brief at A-2 through A-4. A copy of the prior version of the rule is appended to this brief at A-5.

## II. RESTATEMENT OF THE ISSUES

1. RCW 82.04.423 provides a business and occupation tax exemption for out-of-state sellers making sales in Washington exclusively to or through a “direct seller’s representative.” A “direct seller’s representative” is a “person who buys consumer products . . . for resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment, or who sells, or solicits the sale of, consumer products in the home or otherwise than in a permanent retail establishment.” RCW 82.04.423(2) (emphasis added). Dot’s products are sold at retail in permanent retail establishments. Does Dot qualify for the direct seller’s exemption even though its products are not sold “in the home or otherwise than in a permanent retail establishment”?

2. Dot’s sales representative in Washington solicits sales of non-consumer products in addition to consumer products. Does Dot qualify for the direct seller’s exemption even though its representative solicits sales of non-consumer products?

3. Dot’s sales representative is a corporation. Does Dot qualify for the direct seller’s exemption even though its sales representative is not a natural person?

4. Dot argues for the first time on appeal that the Department failed to comply with the procedural requirements of RCW 34.05.328

when it amended WAC 458-20-246 in 1999. An action contesting the validity of a rule for the agency's failure to comply with the procedural requirements of the APA must be commenced within two years after the effective date of the rule. RCW 34.05.375. The effective date of revised WAC 458-20-246 was December 31, 1999. Dot filed this refund action in May 2005. Dot first claimed that WAC 458-20-246 was not adopted in substantial compliance with RCW 34.05.328 in its Brief of Appellant, filed in March 2007. Should this Court refuse to consider Dot's argument based on RCW 34.05.328 because (a) Dot failed to raise it in the trial court and (b) RCW 34.05.375 precludes its consideration?

### III. STATEMENT OF THE CASE

Dot, an Illinois corporation, sells food and related products. CP at 87, ¶¶ 1-2. Most of the food products Dot sells are consumer products. CP at 87, ¶ 2.<sup>3</sup> The related products include both consumer and non-consumer products. CP at 87, ¶ 2.<sup>4</sup> Dot represents itself as "the nation's leading food redistributor." CP at 118.

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<sup>3</sup> For example, Dot sells dry foods and products such as cornstarch and spaghetti sauces (CP at 119-20), refrigerated foods such as dill pickles and butter (CP at 135), and frozen foods such as stuffed chicken entrees and processed frozen vegetables (CP at 137). Dot sells products to convenience stores such as Tang, Pop Tarts, and Pampers (CP at 147-48), and to retail wholesalers such as New York Style Bagel Chips and meats (CP at 151). It also sells ingredients such as cocoa powders and chocolate flavors (CP at 154).

<sup>4</sup> The non-consumer products sold by Dot include janitorial and sanitation items (CP at 161), professional weight fry pans, sauce pans, stock pots, roaster pans, and bake pans (CP at 164), cash register rolls (CP at 149), urinal screens, changing stations, condiment pumps and servers, chef hats and hairnets (CP 164-66).

During the tax periods at issue, Dot solicited sales in Washington through Dot Transportation, Inc. (DTI), a wholly-owned subsidiary. CP at 87-88, ¶¶ 4, 10. Neither Dot nor DTI made sales in Washington from a permanent retail establishment. CP at 88, ¶ 5. Rather, DTI's salesmen solicited sales by making in-person calls on foodservice distributors, meat packers, and dairies located in this state. CP at 88, ¶ 10.

Many of the products sold by Dot eventually are resold to consumers in permanent retail establishments such as convenience stores. See CP at 146. Other products sold by Dot are used as ingredients in products sold in permanent retail establishments such as grocery stores. CP at 88, ¶ 6. And other products sold by Dot are non-consumer products used in permanent retail establishments. See CP at 164-66.

In July 1997, an attorney representing an unidentified taxpayer wrote the Department to request a ruling that the taxpayer's sales into Washington qualified for the direct seller's exemption under RCW 82.04.423. CP at 107-12. The attorney represented that the "products for which the taxpayer's direct seller's representative will solicit orders are 'consumer products.' These products are food and related products (such as fuel for warming food) of the type sold for personal use." CP at 108. The attorney subsequently identified Dot as the taxpayer. CP at 104.

On October 23, 1997, the Department issued a letter ruling to Dot stating that it qualified for the direct seller's exemption. CP at 93-94. The letter ruling explained, however, that it was based on the facts represented by Dot. CP at 94 ("This ruling is binding upon both Dot Foods, Inc. and the Department of Revenue under the facts presented."). It also listed several subsequent events that would render the ruling no longer binding:

[This ruling] will remain binding until: the facts change; the law (either by statute or court decision) changes; the applicable rule(s) change; the Department of Revenue publicly announces a change in the policy upon which this ruling is based; or Dot Foods, Inc. is notified in writing that this ruling is not valid.

CP at 94.

In late 1999, the Department revised WAC 458-20-246, the administrative rule interpreting RCW 82.04.423. In contrast to the prior version of WAC 458-20-246, the revised rule provided a detailed explanation of the direct seller's exemption. Among other things, the revised rule set forth the Department's interpretation that the exemption may not be taken if the retail sale of the consumer product occurs in a permanent retail establishment: "The direct seller may take the exemption only if the retail sale of the consumer product takes place either in the home or otherwise than in a permanent retail establishment." WAC 458-20-246(4)(b)(i)(B). The revised rule's effective date was December 31, 1999. CP at 196.

Shortly after the revised rule's effective date, the Department issued a one-page Special Notice for Direct Sellers, dated February 1, 2000. CP at 96. The notice informed taxpayers the Department had "updated WAC 458-20-246, Rule 246, which implements RCW 82.04.423, the business and occupation tax exemption for sales to or through direct sellers' representatives." CP at 96. The Department mailed a copy of the notice to Dot and Dot received it. CP at 89, ¶ 12.

The Special Notice for Direct Sellers told taxpayers the Department had revised WAC 458-20-246 to provide guidance regarding the requirements of the direct seller's exemption, including the requirement that the retail sale of the consumer product must not occur in a permanent retail establishment:

The purpose of the rule revision is to provide guidance to taxpayers regarding the requirements of the statute. The rule reiterates the express requirements of the statute, including, among others, the limitation that sales of consumer products sold in permanent retail establishments are not eligible for the direct sellers' business and occupation tax exemption. This is because the law states that the sale of consumer products must be "in the home or otherwise than in a permanent retail establishment." If a consumer product is sold by **anyone** in a permanent retail establishment, the direct sellers' exemption is not available to the direct seller.

CP at 96 (bold lettering in original).

The notice also notified taxpayers such as Dot that “[a]s of January 1, 2000, any reporting instructions directed specifically to individual taxpayers that are inconsistent with the revised rule have no effect.” CP at 96. The notice further informed taxpayers that the Department had rescinded four published determinations that had been supplanted by the revised rule. CP at 96.<sup>5</sup>

Notwithstanding the changes to WAC 458-20-246, and the Special Notice for Direct Sellers that it received, Dot continued to take the direct seller’s exemption for tax periods after December 31, 1999. CP at 91-92, ¶ 20. Several years later, the Department audited Dot for tax periods January 1, 2000, through December 31, 2003. The Department concluded that Dot had erroneously taken the exemption and, in late 2004, issued a B&O tax assessment in the amount of \$707,848, plus statutory interest and penalties. CP at 90, ¶ 13, 98, 101.<sup>6</sup>

After receiving the assessment, beginning with the fourth quarter of 2004, Dot began reporting and paying its B&O tax without taking the direct seller’s exemption. CP at 90, ¶ 15. A few months later, Dot filed an excise tax refund action under RCW 82.32.180, seeking a refund of its

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<sup>5</sup> Dot cites one the rescinded published determinations listed in the Special Notice to Direct Sellers, 3 WTD 357 (1987), in its opening appellate brief. Br. of Appellant at 9.

<sup>6</sup> Dot eventually paid the assessment, including additional statutory interest, in June 2006. CP at 90, ¶ 16.

fourth quarter 2004 B&O tax payment. CP at 5-10. In an amended complaint, Dot added refund claims with respect to the assessment it paid in June 2006 and for B&O taxes it paid for periods from February 2005 through April 2006. CP at 22-31, 90, ¶ 17.

Dot moved for summary judgment, arguing that DTI was a “direct seller’s representative” under RCW 82.04.423(2) because “Dot *does not sell to a direct seller representative who buys for resale* – a ‘Clause one’ situation. Rather, Dot’s representative *solicits* sales on a commission basis – a ‘Clause two’ scenario.” CP at 43 (italics in original). Dot also argued, in the alternative, that its reliance on the October 1997 letter ruling it received from the Department was “clearly justified and eminently reasonable” until 2004 when it received the tax assessment issued by the Department. CP at 57.

The Department responded that summary judgment should be granted to it, not Dot. CP at 168. The Department argued that Dot did not qualify for the direct seller’s exemption because it sold non-consumer products through DTI:

Since at least 2000, DTI has solicited the sale of non-consumer products for Dot Foods. With regard to those non-consumer products, DTI was not a “direct seller’s representative.” Since at least 2000, therefore, Dot Foods cannot prove that its sales in this state were made “exclusively to or through a direct seller’s representative.”

CP at 178 (footnotes omitted; underlining in original). The Department also argued that Dot did not qualify for the exemption because its products are sold at retail in permanent retail establishments. CP at 179-84.

In addition, the Department argued that Dot did not qualify for the exemption because its sales representative was not a natural person as the context of RCW 82.04.423(2) requires. CP at 185-86. Lastly, the Department argued that Dot's reliance on the October 1997 letter ruling was not reasonable after December 31, 1999, at the latest. CP at 187-89.

The trial court granted summary judgment to the Department. CP at 327-30. The Honorable Richard D. Hicks concluded that the direct seller's exemption does not apply to exempt "redistributors like Dot Foods whose products end up down the line in permanent retail establishments." RP at 11.<sup>7</sup> The trial court also concluded that Dot's sale of non-consumer products disqualified it from the exemption: "I cannot agree with Dot Foods that I should treat the small amount of non-consumable [sic] products as *de minimis* when the legislature has used the term 'consumer products' even if we find the exclusivity provision in a different paragraph of the exact same statute." RP at 8. Finally, Judge Hicks concluded that Dot could not rely on the 1997 letter ruling "which was not only

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<sup>7</sup> A copy of the transcript of the trial court's oral ruling is appended to this brief at A-6 through A-20.

specifically signaled to be put at risk by Dot being sent the notice, but the rule itself was changed.” RP at 12.<sup>8</sup>

Dot appealed. CP at 331-38.

#### IV. ARGUMENT

##### A. **The B&O Tax Applies To Virtually All Business Activities In Washington, And The Taxpayer Bears The Burden Of Establishing Its Eligibility For A B&O Tax Exemption.**

Several general principles should be kept in mind when a taxpayer seeks the benefit of a B&O tax exemption. First, the intent of the Legislature is to “impose the business and occupation tax upon virtually all business activities carried on within the state,” Time Oil Co. v. State, 79 Wn.2d 143, 146, 483 P.2d 628 (1971), and to ‘leave practically no business and commerce free of tax.’ Budget Rent-A-Car of Washington-Oregon, Inc. v. Department of Revenue, 81 Wn.2d 171, 175, 500 P.2d 764 (1972).” Simpson Inv. Co. v. Dep’t of Revenue, 141 Wn.2d 139, 149, 3 P.3d 741 (2000).

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<sup>8</sup> Regarding the Department’s argument that only a natural person can qualify as a “direct seller’s representative,” Judge Hicks commented that looking at the statute as a whole, its history, how the statute came into being, and how both versions of the rule have dealt “with all this, I don’t think Mr. Comfort is being unreasonable when he points out that it’s a fair interpretation to say that the legislature must have intended that we’re talking about flesh and blood taxpayers here and not any other business form, corporate or otherwise.” RP at 7-8. Nonetheless, he concluded that a corporation may qualify as a “direct seller’s representative” because the word “person” is “used throughout Title 82, and it always means taxable entities without them necessarily having to be ‘flesh and blood[;]’ . . . [T]he word ‘person,’ unless it’s somehow distinguished by the legislature, has to have the same meaning throughout the whole taxing statutes.” RP at 7-8.

Second, a “tax exemption presupposes a taxable status and the burden is on the taxpayer to establish eligibility for the benefit.” In re Sehome Park Care Ctr., Inc., 127 Wn.2d 774, 778, 903 P.2d 443 (1995). Similarly, under RCW 82.32.180, the statute authorizing excise tax refund actions, “the burden shall rest upon the taxpayer to prove that the tax as paid by the taxpayer is incorrect, either in whole or in part, and to establish the correct amount of tax.” See also Ford Motor Co. v. City of Seattle, \_\_\_ Wn.2d \_\_\_, \_\_\_ P.3d \_\_\_ (2007) (No. 77167-7, slip op. at 6 (April 12, 2007)).

Third, tax exemptions are to be construed narrowly. Evergreen-Washelli Mem’l Park Co. v. Dep’t of Revenue, 89 Wn.2d 660, 663, 574 P.2d 735 (1978) (“It may be possible to construe the exemption statute broadly yet rationally to conclude that [the taxpayer] is entitled to the exemption. However, we cannot construe statutory exemptions from taxing laws broadly.”); Sehome Park, 127 Wn.2d at 778 (ambiguity in an exemption statute is construed in favor of taxation). The meaning of an unambiguous statute, of course, is derived from the statutory language alone. Agrilink Foods, Inc. v. Dep’t of Revenue, 153 Wn.2d 392, 396, 103 P.3d 1226 (2005).

**B. The Direct Seller's Exemption Is Modeled On Federal Legislation Applying To Persons Who Market Consumer Products Through In-Home Parties And Door-To-Door.**

The Legislature enacted RCW 82.04.423, the direct seller's exemption, in 1983. Laws of 1983, ch. 66, § 5. Subsection (1) of the statute provides a B&O tax exemption to:

any person in respect to gross income derived from the business of making sales at wholesale or retail if such person:

(a) Does not own or lease real property within this state; and

(b) Does not regularly maintain a stock of tangible personal property in this state for sale in the ordinary course of business; and

(c) Is not a corporation incorporated under the laws of this state; and

(d) Makes sales in this state exclusively to or through a direct seller's representative.

RCW 82.04.423(1) (emphasis added). Only requirement (d), whether Dot "makes sales in this state exclusively to or through a direct seller's representative," is disputed.<sup>9</sup>

Subsection (2) of the statute defines what a "direct seller's representative" is:

For purposes of this section, the term "direct seller's representative" means a person who buys consumer products

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<sup>9</sup> The Department has conceded that Dot satisfies requirements (a), (b), and (c). CP at 91, ¶ 19.

on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment, or who sells, or solicits the sale of, consumer products in the home or otherwise than in a permanent retail establishment; and

(a) Substantially all of the remuneration paid to such person, whether or not paid in cash, for the performance of services described in this subsection is directly related to sales or other output, including the performance of services, rather than the number of hours worked; and

(b) The services performed by the person are performed pursuant to a written contract between such person and the person for whom the services are performed and such contract provides that the person will not be treated as an employee with respect to such purposes for federal tax purposes.

RCW 82.04.423(2) (emphasis added).

The statutory language defining a direct seller's representative is derived from a 1982 federal law designating certain persons performing services as direct sellers as non-employees for purposes of federal employment taxes. See 26 U.S.C. § 3508; see also WAC 458-20-246(2) (referring to the federal Tax Equity and Fiscal Responsibility Act of 1982, Pub. Law 97-248, and 26 U.S.C. § 3508).<sup>10</sup>

According to an Internal Revenue Service publication, “[d]irect selling provides important benefits . . . to consumers who enjoy an alternative to shopping centers, department stores or the like . . .” CP at

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<sup>10</sup> A copy of Pub. Law 97-248, § 269, codified at 26 U.S.C. § 3508 (1982), is appended to this brief at A-21 through A-22.

198. This is because direct sellers market their company's consumer products person to person and not in permanent retail establishments:

Direct selling companies market their products through person to person contact away from a fixed retail location through a network of independent sellers. Frequently these sales presentations are in the home, in the form of a sales "party," or through door to door solicitations, presentations, or sometimes, as part of a get-together – one person to one person. In any case, these approaches all are considered direct sales. In addition, direct selling provides a channel of distribution for companies with innovative or distinctive products not readily available in traditional retail stores, or who cannot afford to compete with the enormous advertising and promotion costs associated with gaining space on retail shelves.

CP at 198-99. Some well-known companies marketing consumer products through direct selling include Mary Kay, Avon, Pampered Chef, Longaberger, and Creative Memories. CP at 201-02. Each of these companies sells consumers products through in-home parties or through door-to-door salespersons, not in permanent retail establishments.

Given that the statutory definition of a "direct seller's representative" is modeled on federal legislation applying to persons who market consumer products through activities like in-home parties and door-to-door sales solicitations, and not in permanent retail establishments, the Legislature presumably enacted the direct seller's exemption to benefit sellers that use representatives to sell their consumer

products through in-home parties and door-to-door sales solicitations, and not in permanent retail establishments. The Legislature surely did not intend the exemption to apply to sellers like Dot whose products are sold at retail in permanent retail establishments.

**C. Dot Is Not A Direct Seller Because Its Products Are Sold At Retail In Permanent Retail Establishments.**

RCW 82.04.423 has been the subject of one reported appellate decision issued by this Court in 2001. Stroh Brewery Co. v. Dep't of Revenue, 104 Wn. App. 235, 15 P.3d 692, review denied, 144 Wn.2d 1002 (2001). Stroh, a wholesaler, produced beer and other alcoholic beverages that it sold to Washington distributors for resale to restaurants, grocery stores, and other retail outlets. Even though its products eventually were resold in permanent retail establishments, Stroh contended its distributors qualified as direct seller's representatives because the distributors did not resell Stroh's products in their own permanent retail establishments. Stroh Brewery, 104 Wn. App. at 238. This Court disagreed:

We hold that, in order for a direct seller who sells to wholesalers to qualify for the exemption, neither the "buyer," which is the direct seller's representative, nor "any other person" may resell the direct seller's products in a permanent retail establishment.

. . . And fairly and consistently interpreted, the exemption does not apply if either the direct seller's representative or anyone else sells the direct seller's products in a permanent retail establishment.

. . . When a direct seller sells through a wholesaler, the seller can qualify for the B&O tax exemption in RCW 82.04.423 only if its products are never sold in a permanent retail establishment. . . .

Stroh Brewery, 104 Wn. App. at 241, 242, 243.

Dot makes essentially the same argument as Stroh. Dot argues that it qualifies for the direct seller's exemption because DTI does not solicit the sale of Dot's products in permanent retail establishments. Br. of Appellant at 15-26. Judge Hicks disagreed, correctly concluding that the exemption does not apply to exempt "redistributors like Dot Foods whose products end up down the line in permanent retail establishments." RP at 11.

Because Dot's products are sold at retail in permanent retail establishments (CP at 88, ¶ 6), it cannot qualify for the direct seller's exemption.

The fundamental object of the court in construing a statute is to ascertain and carry out the Legislature's intent. Dep't of Ecology v. Campbell & Gwinn, L.L.C., 146 Wn.2d 1, 9, 43 P.3d 4 (2002). To determine legislative intent, including whether a statute's meaning is plain, the "act must be construed as a whole, and effect should be given to all the language used." State v. Fontanilla, 128 Wn.2d 492, 498, 909 P.2d 1294 (1996); see also Campbell & Gwinn, 146 Wn.2d at 9-12. Dot's argument

fails to construe RCW 82.04.423 as a whole or give effect to all the language used in the statute.

When RCW 82.04.423 is construed as a whole and effect is given to all the language used, it is plain the Legislature intended to limit the direct seller's exemption to those direct sellers whose consumer products are never sold at retail in a permanent retail establishment. RCW 82.04.423(1) exempts from B&O tax "gross income derived from the business of making sales at wholesale or retail if such person: . . . (d) Makes sales in this state exclusively to or through a direct seller's representative." (Emphasis added). This same structure – making sales at wholesale or retail -- is paralleled in subsection (1)(d). Making sales to a "direct seller's representative" refers to making wholesale sales to a "direct seller's representative" who resells in the home or otherwise or otherwise than in a permanent retail establishment. And making sales through a "direct seller's representative" refers to making retail sales through a "direct seller's representative" in the home or otherwise than in a permanent retail establishment.

In the wholesaling part – i.e., making sales to a direct seller's representative – the phrase "for resale" is coupled with "by the buyer or any other person" so that the exemption for wholesaling direct sellers is limited to those sellers whose consumer products are never sold at retail in permanent retail establishments. The retailing part – i.e., making sales

through a direct seller’s representative – does not include the “by the buyer or any other person” language. But that language is unnecessary to ensure that the consumer products are never sold at retail in a permanent retail establishment. This is because a retail sale is the final sale. Thus, the limitation that the direct seller’s representative either sells or solicits sales “in the home or otherwise than in a permanent retail establishment” limits the retail exemption to those direct sellers whose products are never sold in permanent retail establishments.

The Department’s reading of RCW 82.04.423 finds support in Stroh Brewery, in which this Court implicitly adopted it as the correct one. In Stroh Brewery, the Department made the same argument it makes here – that RCW 82.04.423(2) addresses two types of sales, wholesale sales and retail sales:

The Department argues that the statute defines two categories of direct seller’s representative: wholesalers and retailers. According to the Department, the phrase “a person who buys consumer products on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person . . .” defines a wholesaler direct seller’s representative. The second phrase “who sells, or solicits the sale of, consumer products in the home or otherwise than in a permanent retail establishment” defines a retailer direct seller’s representative. Stroh concedes this reading of the statute is reasonable.

Stroh Brewery, 104 Wn. App. at 240.

Because it made wholesale sales, the Department argued that Stroh must qualify for the direct seller's exemption under the wholesaling part of the definition in RCW 82.04.423(2). This Court accepted the Department's interpretation and solely applied the wholesaling part of RCW 82.04.423(2) to determine that Stroh's distributors did not qualify as direct seller's representatives. Stroh Brewery, 104 Wn. App. at 240-42.

Here, like Stroh, Dot makes wholesale sales. CP at 88, ¶ 6. Consequently, also like Stroh, it must qualify for the direct seller's exemption under the wholesaling part of RCW 82.04.423(2). And because its products, like Stroh's, are sold in permanent retail establishments, Dot cannot qualify for the exemption.

Dot attempts to distinguish Stroh Brewery on the basis that it sells its products through DTI and "does not sell its products to a direct seller's representative for resale." Br. of Appellant at 18 (emphasis added). But that distinction does not matter: "When a direct seller sells through a wholesaler, the seller can qualify for the B&O tax exemption in RCW 82.04.423 only if its products are never sold in a permanent retail establishment." Stroh Brewery, 104 Wn. App. at 243. Dot sells through wholesalers and its products are sold in permanent retail establishments. Dot, therefore, cannot qualify for the direct seller's exemption.

Dot inaccurately describes the Department's position (and the trial court's ruling). See Br. of Appellant at 20 ("the trial court adopted the Department's improper reading of RCW 82.04.423(2) by adding the 'any other person' language of the first clause to the definition of direct seller's representative that does not appear in the second clause of subsection (2).") The Department's interpretation does not improperly add the "any other person" language from the "first clause" of subsection (2) into "second clause" of subsection (2). Instead, the Department's position, as it was in Stroh Brewery, is that subsection (2) contains a part addressing wholesale sales and a part addressing retail sales. Because Dot is a wholesaler and does not make retail sales, the part addressing retail sales does not apply to it.

Moreover, to apply the retailing part of RCW 82.04.423(2) to Dot, and thereby permit Dot to take the direct seller's exemption even though its products are sold in permanent retail establishments, would render meaningless the statute's twice-stated limitation that qualifying sales be "in the home or otherwise than in a permanent retail establishment." Statutes, however, "must be interpreted and construed so that all the language used is given effect, with no portion rendered meaningless or superfluous." Prison Legal News, Inc. v. Dep't of Corr., 154 Wn.2d 628, 645, 115 P.3d 316 (2005).

Dot's proposed construction also is illogical. It simply is not plausible that the Legislature, in the first part of RCW 82.04.423(2), would expressly exclude from the direct seller's exemption wholesalers whose products are ever sold in a permanent retail establishment, but then in the very same sentence nullify that choice by granting the exemption to wholesalers whose products are sold in a permanent retail establishment. See Oregon Dep't of Revenue v. ACF Indus., Inc., 510 U.S. 332, 343, 114 S. Ct. 843, 127 L. Ed. 2d 165 (1994) ("It would be illogical to conclude that Congress, having allowed the States to grant property tax exemptions in subsections (b)(1)-(3) [of former 49 U.S.C. § 11503], would turn around and nullify its own choice in subsection (b)(4).").

In contrast to Dot's interpretation, the Department's interpretation properly gives meaning to all the language in RCW 82.04.423, including the limitation that qualifying sales be "in the home or otherwise than in a permanent retail establishment." It is undisputed that Dot's products are sold in permanent retail establishments. CP at 88, ¶ 6. That fact alone forecloses Dot's claim to the direct seller's exemption. This Court should reject Dot's flawed interpretation and should affirm the trial court, which properly granted summary judgment to the Department.

**D. Dot Is Not A Direct Seller Because DTI Solicits Sales Of Non-Consumer Products In Addition To Consumer Products For Dot.**

The trial court concluded that Dot's sales of non-consumer products make it ineligible for the direct seller's exemption. See RP at 8. Dot argues that its sales of non-consumer products do not disqualify it from the exemption. Br. of Appellant at 26-29.<sup>11</sup> The trial court is right and Dot is wrong.

According to Dot, it sells "food products exclusively through DTI in the state of Washington, and DTI solicits the sale of consumer products for Dot Foods. That is all the statute requires." Br. of Appellant at 29 (emphasis added). But Dot's interpretation fails to read RCW 82.04.423 as a whole and to give effect to all of the statute's language.

The direct seller's exemption is available only to direct sellers who make "sales in this state exclusively to or through a direct seller's representative." RCW 82.04.423(1)(d) (emphasis added). In turn, a direct seller's representative is a person who buys consumer products for resale or who sells or solicits the sale of consumer products, in the home or otherwise than in a permanent retail establishment. RCW 82.04.423(2). Reading subsections (1)(d) and (2) together, and giving effect to all the language

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<sup>11</sup> Dot does not dispute that it sells non-consumer products, but merely argues that such sales constitute less than one percent of its total sales. Br. of Appellant at 5, 29.

used, it is plain that a representative who buys any non-consumer products for resale or who sells or solicits the sale of any non-consumer products does not qualify as a direct seller's representative.

DTI has solicited sales of non-consumer products in Washington for Dot since at least 2000. CP at 87-88, ¶¶ 2, 4, 10. When it solicited those sales, it was not a direct seller's representative. Therefore, Dot is not a direct seller because it did not make "sales in this state exclusively to or through a direct seller's representative." RCW 82.04.423(1)(d) (emphasis added).

Rather than reading the direct seller's exemption as a whole, Dot focuses on bits and pieces of the statute and construes those bits and pieces as if they were entirely unrelated. See, for example, Br. of Appellant at 27 ("Subsection (1) does not refer to consumer products at all."; "Subsection (2) contains no exclusivity requirement."). Because Dot improperly restricts its focus, it proposes an absurd interpretation that renders meaningless several of the words and phrases used in the statute. A couple of hypothetical examples demonstrate the flaws in Dot's reading of the exemption.

- *Example 1:* Assume Company A uses Sales Representative X to sell \$100,000,000 of non-consumer products and \$50 of consumer products in Washington and further assume that the other statutory requirements are met. Under the construction urged by Dot, Company A would qualify for the

direct seller's exemption because it solicits sales exclusively through Sales Representative X, and Sales Representative X solicits the sale of consumer products. See Br. of Appellant at 29 (“[A]ll the statute requires” is that “[Company A] sells its [ ] products exclusively through [Sales Representative X] in the state of Washington, and [Sales Representative X] solicits the sale of consumer products for [Company A].” But construing RCW 82.04.423 to allow Company A to take the exemption would be absurd, given that its principal business is selling non-consumer products and its sales of consumer products are nominal.<sup>12</sup> The requirement in subsection (1)(d) that the seller make “sales in this state exclusively to or through a direct seller’s representative,” and the multiple use of the term “consumer products” in subsection (2) in the definition of a direct seller’s representative are rendered meaningless if selling a nominal amount of consumer products through a representative is all that is necessary to qualify for the exemption. “An interpretation that produces ‘absurd consequences’ must be rejected, since such results would belie legislative intent.” Troxell v. Rainier Pub. Sch. Dist. No. 307, 154 Wn.2d 345, 350, 111 P.3d 1173 (2005).

- Example 2: Assume the same facts as Example 1. Further assume that another company, Company B, sells both consumer products and non-consumer products in Washington. Company B sells \$100,000,000 of

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<sup>12</sup> \$50/\$100,000,050 (or less than .00005% of its total sales).

consumer products through Sales Representative Y and \$50 of non-consumer products through Sales Representative Z. Sales Representative Y solely solicits sales of consumer products and Sales Representative Z solely solicits sales of non-consumer products. Company A, as explained in Example 1 above, would qualify for the direct seller's exemption even though less than .00005% of its sales are consumer products.<sup>13</sup> But under Dot's proposed construction, Company B would not qualify for the exemption even though 99.99995% of its sales are consumer products<sup>14</sup> because Sales Representative Z does not "solicit the sale of consumer products for [Company B]." See Br. of Appellant at 26-28 ("The statute's exclusivity requirement relates only to the method of selling within the state of Washington, not the type of product sold. . . . Dot Foods meets the requirement of RCW 82.04.423(1)(d) because all of its sales are *exclusively through* a direct seller's representative.") (Emphasis in original).

If Dot's proposed construction were applied, the company selling consumer products (for the most part) would not qualify for the direct seller's exemption while the company selling non-consumer products (for the most part) would qualify. Not only would that result be absurd, but it also would render meaningless the statute's requirement that the seller exclusively make sales to or through a person who buys consumer products

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<sup>13</sup> See footnote 12.

<sup>14</sup>  $\$100,000,000/\$100,000,050=0.9999995$ .

for resale or who sells or solicits the sale of consumer products, in the home or otherwise than in a permanent retail establishment. See Prison Legal News, 154 Wn.2d at 645 (requiring statutes to be construed so that no statutory language is rendered meaningless).

The Department's interpretation of RCW 82.04.423, in contrast to Dot's, does not produce absurd consequences and gives effect to all the statutory language. If a direct seller exclusively sells consumer products to or through a direct seller's representative, it qualifies for the direct seller's exemption. If a seller does not exclusively sell consumer products to or through a direct seller's representative, it cannot qualify for the exemption. There is nothing absurd about that result. The Department's interpretation also gives effect to the requirement that the seller exclusively makes sales to or through a direct seller's representative as well as to the statutory description of a direct seller's representative as a person who buys consumer products for resale or who sells or solicits the sale of consumer products, in the home or otherwise than in a permanent retail establishment.

Finally, Dot relies on AgriLink Foods, Inc. v. Dep't of Revenue, 153 Wn.2d 392, 103 P.3d 1226 (2005), and Lone Star Indus., Inc. v. Dep't of Revenue, 97 Wn.2d 630, 647 P.2d 1013 (1982), to argue that its sales of non-consumer products do not disqualify it from the direct seller's exemption for consumer products. Br. of Appellant at 28-29. Dot's

reliance on AgriLink and Lone Star plainly is misplaced. Neither one remotely supports Dot's proposition that the Legislature did not mean "exclusively" when it used the word "exclusively" in RCW 82.04.423(1)(d). In fact, neither RCW 82.04.260 nor RCW 82.04.050, the tax statutes addressed in those cases, even contain the word "exclusively."

Furthermore, that AgriLink may have paid B&O taxes under more than one classification, as Dot argues, would not be surprising. Br. of Appellant, at 28. RCW 82.04.440(1) expressly requires that "[e]very person engaged in activities which are within the purview of the provisions of two or more sections RCW 82.04.240 to 82.04.298, inclusive, shall be taxable under each paragraph applicable to the activities engaged in."

The trial court correctly concluded that RCW 82.04.423 does not contain a de minimis exception. Thus, the trial court also correctly concluded that Dot's sales of non-consumer products disqualify it from the exemption. RP at 8-9.

**E. Dot Is Not A Direct Seller Because DTI Is Not A Natural Person As RCW 82.04.423(2) Requires.**

Another reason Dot does not qualify for the direct seller's exemption is that DTI is a corporation (CP at 87, ¶ 2) and only natural persons can qualify as direct seller's representatives. That the Legislature

did not intend a corporation to qualify as a direct seller's representative is made apparent by the additional requirements in RCW 82.04.423(2)(a) and (b) that it used to define a direct seller's representative. Applying these requirements to entities other than natural persons does not make sense.

RCW 82.04.423(2)(a) requires that "substantially all of the remuneration paid to [the direct seller's representative], whether or not paid in cash, for the performance of services described in this subsection is directly related to sales or other output, including the performance of services, rather than the number of hours worked . . . ." And RCW 82.04.423(2)(b) requires that the services performed by the "direct seller's representative" must be pursuant to a written contract providing "that the person will not be treated as an employee with respect to such purposes for federal tax purposes." These two requirements strongly imply that a direct seller's representative must be a natural person.

First, the requirement in subsection (2)(a) that the direct seller's representative not be paid based on "the number of hours worked" makes sense when applied to a natural person. It does not make sense when applied to a corporation. Corporations do not work; only their employees do. Thus, the Legislature must have been thinking about a natural person when it

included this requirement in the statutory definition of a direct seller's representative.

Second, the requirement in subsection (2)(b) that the “contract provides that the person will not be treated as an employee with respect to such purposes for federal tax purposes” similarly makes no sense when applied to a corporation. A corporation obviously cannot be an employee. Only a natural person can. Again, therefore, the Legislature must have been thinking about a natural person when it included this requirement in the statutory definition of a direct seller's representative.<sup>15</sup>

In response, Dot may argue, as it did in the trial court, that DTI qualifies as a direct seller's representative because DTI is a “person” under RCW 82.04.030 (defining “person” to include a “corporation”). CP at 224-25. But that response would ignore RCW 82.04.010 which provides: “Unless the context clearly requires otherwise, the definitions set forth in the sections preceding RCW 82.04.220 apply throughout this chapter.” (Emphasis added). Here, the context of RCW 82.04.423(2) clearly requires otherwise. When RCW 82.04.423(2) is read as a whole, it

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<sup>15</sup> It is rational to conclude that the Legislature only intended natural persons to qualify as direct seller's representatives, given that the direct seller's exemption is based on federal statutory language which obviously applies only to individuals (natural persons) selling or soliciting the sale of consumer products. Congress enacted the federal legislation to designate certain individuals as non-employees for purposes of federal employment taxes. Such legislation simply has no application with respect to corporations.

becomes clear the Legislature intended only natural persons to qualify as direct seller's representatives.

Dot may also argue, as it did in the trial court, that the word "person" in subsection (2) of the statute must have the same meaning as "person" in subsection (1), under which a qualifying direct seller can be a corporation. CP at 225. This Court should decline to adopt such a rigid approach to statutory construction. Rules of construction "are not statements of law. They are rules in aid of construing legislation and an aid in the process of determining legislative intent." Johnson v. Cont'l West, Inc., 99 Wn.2d 555, 559, 663 P.2d 482 (1983). Indeed, the United States Supreme Court recently explained that a word may have different shades of meaning even when it is used in the same statute:

Although we presume that the same term has the same meaning when it occurs here and there in a single statute, the Court of Appeals mischaracterized that presumption as "effectively irrebuttable." 411 F.3d, at 550. We also understand that "[m]ost words have different shades of meaning and consequently may be variously construed, not only when they occur in different statutes, but when used more than once in the same statute, or even in the same section." Atlantic Cleaners & Dyers, Inc. v. United States, 286 U.S. 427, 433 (1932). Thus, the "natural presumption that identical words used in different parts of the same act are intended to have the same meaning . . . is not rigid and readily yields whenever there is such variation in the connection in which the words are used as reasonably to

warrant the conclusion that they were employed in different parts of the act with different intent.” Ibid. . . .

Envtl. Def. v. Duke Energy Corp., 549 U.S. \_\_\_, 127 S. Ct. 1423, 1432, \_\_\_ L. Ed. 2d \_\_\_ (2007).

The trial court appeared to agree with the Department’s argument that the Legislature intended only natural persons to qualify as direct seller’s representatives. RP at 8 (“[I]t’s a fair interpretation to say that the legislature must have intended that we’re talking about flesh and blood taxpayers here and not any other business form, corporate or otherwise.”). Nonetheless, the trial court concluded that the definition of “person” in RCW 82.04.030 controls. RP at 7-8. To that limited extent, Judge Hicks erred. The fact that DTI is a corporation is another reason Dot is not a direct seller.

**F. Dot’s Argument Based On RCW 34.05.328 Should Not Be Considered Because Dot Failed To Raise It In The Trial Court And, In Any Event, It Is Barred By RCW 34.05.375.**

On appeal, Dot claims for the first time that the Department’s amendments to WAC 458-20-246 in 1999 were “significant” and the Department failed to comply with the procedural requirements imposed by RCW 34.05.328 with respect to “significant legislative rules.” Br. of Appellant at 29-35. Dot should not be permitted to raise this argument for

the first time on appeal. RAP 2.5(a); State v. Riley, 121 Wn.2d 22, 31, 846 P.2d 1365 (1993).

Moreover, Dot's argument is barred by RCW 34.05.375. That statute limits the period within which to challenge a rule on procedural grounds to two years: "No action based upon this section [referring to RCW 34.05.310 through 34.05.395] may be maintained to contest the validity of any rule unless it is commenced within two years after the effective date of the rule." RCW 34.05.375. The effective date of the amendments to WAC 458-20-246 was December 31, 1999. CP at 196. The time period during which to file an action challenging the amended rule thus lapsed more than four years ago, long before Dot filed its opening appellate brief in March 2007 and even long before it filed this refund action in May 2005. Consequently, this Court cannot consider Dot's argument based on the rule-making requirements of the APA.

Dot's argument also is barred by RCW 82.32.180, the statute authorizing refund actions. RCW 82.32.180 requires a taxpayer, at the time it files its action seeking a refund, to set forth "the reason why the tax should be reduced or abated." With respect to this argument based on RCW 34.05.328, Dot did not comply with RCW 82.32.180. Neither the complaint nor the amended complaint it filed in superior court mentions the APA, let alone its rule-making requirements. See CP at 5-10, 22-31.

Since Dot failed to set forth the APA in either its superior court complaint or amended complaint as a reason why its B&O taxes should be reduced or rebated, it cannot obtain a refund based on that reason.

Furthermore, even if this Court were to consider Dot's argument based on RCW 34.05.328, it has no merit. For example, Dot argues that the Department's amendments to WAC 458-20-246 in 1999 were substantive, and not merely interpretative, "because the Department has treated its new rule as subjecting taxpayers to a 'penalty or sanction' for its violation." Br. of Appellant at 31. To support this claim Dot cites to the Department's audit of Dot in which the auditor stated that the revised rule "has the same effect as the Revenue Act itself (RCW 82.32.300)." Br. of Appellant at 31 (citing CP at 78). Dot's argument is mistaken for at least two reasons.

First, the auditor's statements asserted more than four years after WAC 458-20-246 was revised plainly have no bearing whatsoever on whether the revisions to the rule were substantive or merely interpretative. The validity of a rule is determined at the time it is adopted, not on statements made years later by an agency employee.

Second, the Department did not penalize or sanction Dot for violating WAC 458-20-246. Rather, the Department based its assessment on RCW 82.04.423. CP at 78-80 (repeatedly citing and discussing RCW

82.04.423). And even if the Department's auditor had not repeatedly cited RCW 82.04.423, that would not matter. As the Supreme Court explained in Ass'n of Wash. Bus. v. Dep't of Revenue, 155 Wn.2d 430, 447, 120 P.3d 46 (2005): "If the public violates an interpretative rule that accurately reflects the underlying statute, the public may be sanctioned and punished, not by authority of the rule, but by authority of the statute. This is the nature of interpretative rules." (Emphasis in original). For the reasons stated earlier in this brief, Dot does not qualify for the direct seller's exemption. RCW 82.04.423, therefore, fully supports the Department's assessment against Dot.

In addition, Dot seems to suggest that an agency's authority to change an erroneous interpretation of a statute is extremely limited and the agency bears the burden to justify its changed interpretation. See Br. of Appellant, at 23-24. Dot misconstrues the law. The burden is on the party asserting a rule's invalidity. RCW 34.05.570(a). See also Seven Seas, Inc. v. United States, 873 F.2d 225, 227 (9th Cir. 1989) ("Our courts have never held that any agency cannot change its collective mind on a legal issue."); Mesa Verde Const. Co. v. Northern Cal. Dist. Council of Laborers, 861 F.2d 1124, 1134 (9th Cir.1988) (en banc) (NRLB "is free to change its interpretation of the law if its interpretation is reasonable and not precluded by Supreme Court precedent."); Dep't of Ecology v.

Theodoratus, 135 Wn.2d 582, 957 P.2d 1241 (1998) (where Department of Ecology originally acted ultra vires in measuring a water right, it did not act arbitrarily and capriciously in abandoning unlawful practice and switching to new practice).

Finally, the reliance argument Dot makes in its opening appellate brief is based entirely on the claim that the Department failed to comply with the APA's rule-making requirements. Br. of Appellant at 34 (“Because the Department’s notice failed to meet the requirements of the APA, Dot Foods may continue to rely on the Department’s previous interpretation of RCW 82.04.423.”).<sup>16</sup> In the trial court, Dot asserted entirely different reasons to argue it reasonably relied on the 1997 letter ruling that it received from the Department. CP 54-57, 226-28. In response, the Department explained why those reasons were “utterly without merit.” CP at 187-89.

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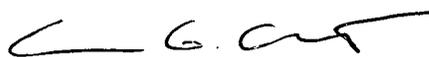
<sup>16</sup> See also Br. of Appellant at 4 (Issue Statement 3): “Was the Department entitled to reverse its construction of the statute by issuing an ‘interpretative’ rule that departed radically from its original rule, promulgated 15 years earlier, and to then rely on its new interpretation to assess B&O taxes against Dot Foods, without engaging in the additional notice requirements mandated by the APA where an agency significantly amends its policy?” (Emphasis added).

**V. CONCLUSION**

The trial court correctly granted summary judgment to the Department. This Court should affirm the trial court's summary judgment order.

RESPECTFULLY SUBMITTED this 16<sup>th</sup> day of April, 2007.

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# APPENDIX

A-1	RCW 82.04.423
A-2 through A-4	WAC 458-20-246 (effective 12/31/99)
A-5	Former WAC 458-20-246 (filed 11/30/84)
A-6 through A-20	Ruling By The Honorable Richard D. Hicks (12/6/06)
A-21 through A-22	26 U.S.C. § 3508 (1982)

**RCW 82.04.423**

**Exemptions — Sales by certain out-of-state persons to or through direct seller's representatives.**

(1) This chapter shall not apply to any person in respect to gross income derived from the business of making sales at wholesale or retail if such person:

(a) Does not own or lease real property within this state; and

(b) Does not regularly maintain a stock of tangible personal property in this state for sale in the ordinary course of business; and

(c) Is not a corporation incorporated under the laws of this state; and

(d) Makes sales in this state exclusively to or through a direct seller's representative.

(2) For purposes of this section, the term "direct seller's representative" means a person who buys consumer products on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment, or who sells, or solicits the sale of, consumer products in the home or otherwise than in a permanent retail establishment; and

(a) Substantially all of the remuneration paid to such person, whether or not paid in cash, for the performance of services described in this subsection is directly related to sales or other output, including the performance of services, rather than the number of hours worked; and

(b) The services performed by the person are performed pursuant to a written contract between such person and the person for whom the services are performed and such contract provides that the person will not be treated as an employee with respect to such purposes for federal tax purposes.

(3) Nothing in this section shall be construed to imply that a person exempt from tax under this section was engaged in a business activity taxable under this chapter prior to the enactment of this section.

[1983 1st ex.s. c 66 § 5.]

**Notes:**

**Reviser's note:** The effective date of 1983 1st ex.s. c 66 is August 23, 1983.

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458-20-245 << 458-20-246 >> 458-20-247

## WAC 458-20-246

### Sales to or through a direct seller's representative.

(1) **Introduction.** RCW 82.04.423 provides an exemption from the business and occupation (B&O) tax on wholesale and retail sales by a person who does not own or lease real property in the state, is not incorporated in the state, does not maintain inventory in this state, and makes sales in this state exclusively to or through a "direct seller's representative." This rule explains the statutory elements that must be satisfied in order to be eligible to take this exemption.

(2) **Background.** The statutory language describing the direct seller's representative is substantially the same language as contained in the federal Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982, PL 97-248. See 26 USC 3508. The federal law designates types of statutory nonemployees for social security tax purposes. The purpose of the direct seller provision in the federal tax law is to provide that a direct seller's representative is not an employee of the direct seller, thereby relieving the direct seller of a tax duty. Under the federal law, the direct seller is a business that sells its products using a representative who either purchases from the direct seller and resells the product or sells for or solicits sales on behalf of the direct seller. Retail sales are limited to those occurring in the home or in a temporary retail establishment, such as a vendor booth at a fair.

The 1983 Washington state legislature used the same criteria to delineate, for state tax purposes, the necessary relationship between a direct seller and a direct seller's representative.

(3) **The direct seller's exemption.** The exemption provided by RCW 82.04.423 is limited to the B&O tax on wholesaling or retailing imposed in chapter 82.04 RCW (Business and occupation tax). A direct seller is subject to other Washington state tax obligations, including, but not limited to, the sales tax under chapter 82.08 RCW, the use tax under chapter 82.12 RCW, and the litter tax imposed by chapter 82.19 RCW.

(4) **Who may take the exemption.** The B&O tax exemption may be taken by a person (the direct seller) selling a consumer product using the services of a representative who sells or solicits the sale of the product as outlined in statute. There are ten elements in the statute that must be present in order for a person to qualify for the exemption for Washington sales. The person must satisfy each element to be eligible for the exemption. The taxpayer must retain sufficient records and documentation to substantiate that each of the ten required elements has been satisfied. RCW 82.32.070.

(a) The four statutory elements describing the direct seller. RCW 82.04.423 provides that a direct seller:

(i) Cannot own or lease real property within this state. For example, if the direct seller's representative is selling vitamins door to door for the direct seller, but the direct seller owns or leases a coffee roasting factory in the state, the direct seller is not eligible for this exemption; and

(ii) Cannot regularly maintain a stock of tangible personal property in this state for sale in the ordinary course of business. This provision does not, however, prohibit the direct seller from holding title to the consumer product in the state. For instance, the direct seller owns the consumer products sold by the direct seller's representative when the representative is making retail sales for the direct seller. However, the personal property must not be a stock of goods in the state that is for sale in the ordinary course of business. The phrase "sale in the ordinary course of business" means sales that are arm's length and that are routine and reasonably expected to occur from time to time; and

(iii) Is not a corporation incorporated under the laws of this state; and

(iv) Makes sales in this state exclusively to or through a direct seller's representative. This provision of the statute describes how sales by the direct seller may be made. To be eligible for the exemption, all sales by the direct seller in this state must be made to or through a direct seller's representative. The direct seller may not claim any B&O tax exemption under RCW 82.04.423 if it has made sales in this state using means other than a direct seller's representative. This requirement does not, however, limit the methods the direct seller's representative may use to sell these products. For example, the representative can use the mail or the internet, if all other conditions of the exemption are met. The direct seller's use of mail order or internet, separate from the representative's use, may or may not be found to be "sales in this state" depending on the facts of the situation. If the direct seller's use of methods other than to or through a direct seller's representative constitutes "sales in this state," the exemption is lost. Additionally, a direct seller does not become ineligible for the exemption due to action by the direct seller's representative that is in violation of the statute, such as selling a product to a permanent retail establishment, if the department finds by a review of the facts that the ineligible sales are irregular, prohibited by the direct seller, and rare.

If a seller uses a direct seller's representative to sell "consumer products" in Washington, and also has a branch office, local outlet, or other local place of business, or is represented by any other type of selling employee, selling agent,

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or selling representative, no portion of the sales are exempt from B&O tax under RCW 82.04.423. For example, a person who uses representatives to sell consumer products door to door and who also sells consumer products through retail outlets is not eligible for the exemption. The phrase "sales exclusively to ... a direct seller's representative" describes wholesale sales made by the direct seller to a representative. The phrase "sales exclusively ... through a direct seller's representative" describes retail sales made by the direct seller to the consumer. The B&O tax exemption provided by RCW 82.04.423 is limited to these types of wholesale and retail sales.

(b) The six statutory elements describing the direct seller's representative. RCW 82.04.423 provides the following elements that relate to the direct seller's representative:

(i) How the sale is made. A direct seller's representative is "a person who buys consumer products on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment, or who sells, or solicits the sale of, consumer products in the home or otherwise than in a permanent retail establishment." The direct seller sells the product using the services of a representative in one of two ways, which are described by two clauses in the statute. The first clause ("a person who buys ... for resale" from the direct seller) describes a wholesale sale by the direct seller. The second clause (a person who "sells or solicits the sale" for the direct seller) describes a retail sale by the direct seller.

(A) A transaction is on a "buy-sell basis" if the direct seller's representative performing the selling or soliciting services is entitled to retain part or all of the difference between the price at which the direct seller's representative purchases the product and the price at which the direct seller's representative sells the product. The part retained is remuneration from the direct seller for the selling or soliciting services performed by the representative. A transaction is on a "deposit-commission basis" if the direct seller's representative performing the selling or soliciting services is entitled to retain part or all of a purchase deposit paid in connection with the transaction. The part retained is remuneration from the direct seller for the selling or soliciting services performed by the representative.

(B) The location where the retail sale of the consumer product may take place is specifically delineated by the terms of the statute. The direct seller may take the exemption only if the retail sale of the consumer product takes place either in the home or otherwise than in a permanent retail establishment. The resale of the products sold by the direct seller at wholesale is restricted by the statute through the following language: "For resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment." This restrictive phrase requires the product be sold at retail either in the home or in a nonpermanent retail establishment. Regardless of to whom the representative sells, the retail sale of the product must take place either in the buyer's home or in a location that is not a permanent retail establishment. Examples of permanent retail establishments are grocery stores, hardware stores, newsstands, restaurants, department stores, and drug stores. Also considered as permanent retail establishments are amusement parks and sports arenas, as well as vendor areas and vendor carts in these facilities if the vendors are operating under an agreement to do business on a regular basis. Persons selling at temporary venues, such as a county fair or a trade show, are not considered to be selling at a permanent retail establishment.

(ii) What product the direct seller must be selling. The direct seller must be selling a consumer product, the sale of which meets the definition of "sale at retail," used for personal, family, household, or other nonbusiness purposes. "Consumer product" includes, but is not limited to, cosmetics, cleaners and soaps, nutritional supplements and vitamins, food products, clothing, and household goods, purchased for use or consumption. The term does not include commercial equipment, industrial use products, and the like, including component parts. However, if a consumer product also has a business use, it remains a "consumer product," notwithstanding that the same type of product might be distributed by other unrelated persons to be used for commercial, industrial, or manufacturing purposes. For example, desktop computers are used extensively in the home as well as in businesses, yet they are a consumer product when sold for nonbusiness purposes.

(iii) How the person is paid. The statute requires that "substantially all of the remuneration paid to such person, whether or not paid in cash, for the performance of services described in this subsection is directly related to sales or other output, including the performance of services, rather than the number of hours worked." The remuneration must be for the performance of sales and solicitation services and it must be based on measurable output. Remuneration based on hours does not qualify. A fixed salary or fixed compensation, without regard to the amount of services rendered, does not qualify.

Remuneration need not be in cash, and it may be the consumer product itself or other property, such as a car.

(iv) How the contract is memorialized. The services by the person must be performed pursuant to a written contract between the representative and the direct seller. The requirement that the contract be in writing is a specific statutory condition of RCW 82.04.423.

(v) What the contract must contain. The sale and solicitation services must be the subject of the contract. The contract must provide that the representative will not be treated as an employee of the direct seller for federal tax purposes.

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(vi) The status of the representative. A person satisfying the requirements of the statute should also be a statutory nonemployee under federal law, since the requirements of RCW 82.04.423 and 26 U.S.C. 3508 are the same. The direct seller must maintain proof the representative is a statutory nonemployee.

(5) **Tax liability of the direct seller's representative.** The statute provides no tax exemption with regard to the "direct seller's representative." The direct seller's representative is subject to the service and other activities B&O tax on commission compensation earned for services described in RCW 82.04.423. Likewise, a direct seller's representative who buys consumer products for resale and does in fact resell the products is subject to either the wholesaling or retailing B&O tax upon the gross proceeds of these sales. Retail sales tax must be collected and remitted to the department on retail sales unless specifically exempt by law. For example, certain food products are statutorily exempt from retail sales tax (see WAC 458-20-244).

(a) Subject to the agreement of the representatives, the direct seller may elect to remit the B&O taxes of the representatives and collect and remit retail sales tax as agents of the representatives through an agreement with the department. The direct seller's representative should obtain a tax registration endorsement with the department unless otherwise exempt under RCW 82.32.045. (See also WAC 458-20-101 on tax registration.)

(b) Every person who engages in this state in the business of acting as a direct seller's representative for unregistered principals, and who receives compensation by reason of sales of consumer products of such principals for use in this state, is required to collect the use tax from purchasers, and remit the same to the department of revenue, in the manner and to the extent set forth in WAC 458-20-221. (Collection of use tax by retailers and selling agents.)

(6) **The retail sales and/or use tax reporting responsibilities of the direct seller.** A direct seller is required to collect and remit the tax imposed by chapter 82.08 RCW (Retail sales tax) or 82.12 RCW (Use tax) if the seller regularly solicits or makes retail sales of "consumer products" in this state through a "direct seller's representative" even though the sales are exempt from B&O tax pursuant to RCW 82.04.423.

[Statutory Authority: RCW 82.32.300, 99-24-007, § 458-20-246, filed 11/19/99, effective 12/31/99; 84-24-028 (Order 84-3), § 458-20-246, filed 11/30/84.]

A-4

**WAC 458-20-246 Sales to or through a direct seller's representative.** Under RCW 82.04.423, the business and occupation tax does not apply to any out-of-state person in respect to the gross income derived from the business of making sales in this state of "consumer products" at wholesale or retail to or through a "direct seller's representative," subject to certain requirements explained more fully below. The effective date of this exemption is August 23, 1983. For an outline of the tax liability of persons making sales of goods which originate in other states to customers in Washington, other than sales to or through a "direct seller's representative," see WAC 458-20-193B.

#### DEFINITIONS

For purposes of the exemption explained herein, the following definitions shall apply:

The term "consumer product" means any article of tangible personal property, or component part thereof, of the type sold for personal use or enjoyment. The term includes only those kinds of items of tangible personal property which are customarily sold at stores, shops, and retail outlets open to the public in general. It includes such things as home furnishings, clothing, personal effects, household goods, food products, and similar items purchased for personal use or consumption. The term does not include commercial equipment, manufacturing items, industrial use products, and the like, including component parts thereof. However, if a product is primarily used for personal use or enjoyment, it remains a "consumer product" within this definition notwithstanding that a portion of the product's distribution is for commercial, industrial, or manufacturing purposes.

A "direct seller's representative" is a person who (a) buys "consumer products" on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person, in the home or other than in a permanent retail establishment or (b) sells or solicits the sale of "consumer products" in the home or other than in a permanent retail establishment. In order to be considered a "direct seller's representative" a person must also show that:

1. Substantially all of the remuneration paid, whether or not paid in cash, for the performance of services is directly related to sales or other output, including the performance of services, rather than the number of hours worked; and
2. The services performed are performed pursuant to a written contract between such person and the person for whom the services are performed and such contract provides that the person will not be treated as an employee with respect to such services for federal tax purposes.

#### BUSINESS AND OCCUPATION TAX

**WHOLESALE AND RETAILING.** The business and occupation tax does not apply to an out-of-state seller making wholesale or retail sales to or through a "direct seller's representative." The out-of-state seller must show that it is represented in this state by a "direct seller's representative," as defined above. In addition, the out-of-state seller must also show that it:

1. Does not own or lease real property within this state;
2. Does not regularly maintain a stock of tangible personal property in this state for sale in the ordinary course of business;
3. Is not a corporation incorporated under the laws of this state; and
4. Makes sales in this state exclusively to or through a "direct seller's representative."

Thus, a representative who solicits sales of "consumer products" in this state, other than in a permanent retail establishment, and also meets the other requirements of the law as set forth above, qualifies as a "direct seller's representative." If the out-of-state seller and the in-state representative can factually establish compliance with all of the above listed requirements, the out-of-state seller is exempt from business and occupation tax.

The exemption is available only where an out-of-state seller is present in this state and represented exclusively by a "direct seller's representative." If an out-of-state seller makes wholesale or retail sales of "consumer products" in Washington to or through a "direct seller's representative" and also has a branch office, local outlet, or other local place of business, or is represented by any other employee, agent, or other representative, no portion of the sales are exempt from business and occupation tax.

The business and occupation tax likewise applies to the gross income of a "direct seller's representative" who buys "consumer products" for resale and does in fact resell the products. The measure of the business and occupation tax is the gross proceeds of sales.

**SERVICE.** The law provides no similar business and occupation tax exemption with regard to the compensation paid to the "direct seller's representative." Thus, the representative will remain subject to the business and occupation tax on all commissions or other compensation earned.

#### SALES AND USE TAX

An out-of-state vendor is required to pay or collect and remit the tax imposed by chapter 82.08 or 82.12 RCW if the vendor regularly solicits or makes retail sales of "consumer products" in this state through a "direct seller's representative," as defined above, even though such sales are exempt from business and occupation tax pursuant to RCW 82.04.423.

Every person who engages in this state in the business of acting as a "direct seller's representative" for unregistered principals, and who receives compensation by reason of sales of "consumer products" of such principals for use in this state, is required to collect the use tax from purchasers, and remit the same to the department of revenue, in the manner and to the extent set forth in WAC 458-20-221. [Statutory Authority: RCW 82.32-.300, 84-24-028 (Order 84-3), § 458-20-246, filed 11/30/84.]

A-5

IN THE SUPERIOR COURT OF THE STATE OF WASHINGTON  
IN AND FOR THE COUNTY OF THURSTON

---

DOT FOODS, INC.,                    )  
  )  
      Petitioner,                    )  
  )  
              vs.                    ) SUPERIOR COURT NO. 05-2-00990-7  
  )  
WASHINGTON STATE                )  
DEPARTMENT OF REVENUE,         )  
  )  
              Respondent.         )

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RULING BY THE HONORABLE RICHARD D. HICKS, DEPARTMENT 4

---

December 6, 2006  
2000 Lakeridge Drive SW  
Olympia, Washington

**COPY**

Court Reporter  
Ralph H. Beswick, CCR  
Certificate No. 2023  
1603 Evergreen Pk Ln SW  
Olympia, Washington

A P P E A R A N C E S

For the Petitioner:            Jacquelyn Beatty  
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   1201 Third Avenue, Suite 2900  
   Seattle, WA 98101

Donald Tracy

For the Respondent:           Cameron Comfort  
   Assistant Attorney General  
   PO Box 40123  
   Olympia, WA 98504-0123

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1  
2 THE COURT: All right. I am going to rule,  
3 but I don't have any written notes because my time  
4 was a little truncated, but I don't see any benefit  
5 to anybody to draw this out on the one hand and for  
6 me to craft a written decision, and secondly, I know  
7 from being here a long time that my written decision  
8 carries absolutely no weight with the Court of  
9 Appeals. They don't give any discretion to what the  
10 trial judge does at all here. I'm not offended by  
11 that. By law they don't have to give any weight to  
12 my decision. They'll bring their own expertise to  
13 bear on it, and I've many times either been upheld  
14 and a few times reversed without having my arguments  
15 ever addressed by the Court of Appeals or the *ratio*  
16 *decidendi* of how I made the decision addressed by  
17 them. So for those two reasons, I think it's in  
18 everyone's best interest for me to go ahead and rule.

19 First, before I make somebody unhappy, I want to  
20 thank all three attorneys for their civility and  
21 professionalism. There's a lot of money at stake  
22 here, over a million dollars, and all counsel were  
23 not only professional, but also civil and respectful  
24 to each other and to the court, and I thank you for  
25 that. It's a hotly contested issue with a lot of

1 zeros at stake, and it's too bad the public isn't  
2 here to see how a case can be very competently argued  
3 by all sides without slipping down into *ad hominem*  
4 arguments or too much hyperbole and so on.

5 Well, I think there's something to what all of you  
6 have to say. In a ruling with cross-motions for  
7 summary judgment, I have to first take Dot's motion  
8 for summary judgment and take the factual inferences  
9 -- or the facts and reasonable inferences from them  
10 in the light most favorable to the Department, and  
11 then in ruling on the Department's motion for summary  
12 judgment I have to take the facts in the light most  
13 favorable to Dot Foods, including any reasonable  
14 inferences therefrom.

15 And also because we're dealing with an exemption  
16 as opposed to the application of the tax, like in for  
17 instance *Agrilink Foods*, 153 Wn.2d 392, where Judge  
18 Strophy I think had before him -- and the court  
19 speaks at page 396 and 397 about doubtful application  
20 of a tax being construed in favor of a taxpayer.  
21 Here we're dealing with the construction of an  
22 exemption to the tax, and so therefore it's a narrow  
23 construction, not construed in favor of the  
24 taxpayers, but construed narrowly and in favor of the  
25 tax unless the exemption is clearly and fairly

1 applicable here.

2 So the burden of proof here, no matter who has the  
3 burden of coming forward with the evidence, is on Dot  
4 Foods to show that they qualify for the exemption.

5 Maybe because I've been here a long time, I think  
6 Ms. Beatty, Ms. Knight, and I don't know that  
7 Mr. Comfort or -- everybody's name -- is it Mr. Tracy?

8 MR. TRACY: Yes.

9 THE COURT: -- would necessarily disagree  
10 that the genesis of this kind of a case goes back  
11 twenty or thirty years, two or three decades, to this  
12 problem that continues to arise over and over again,  
13 in particular in Washington, but also other states in  
14 which they don't have income taxes, but they rely on  
15 excise taxes like the B&O tax in order to have  
16 revenue in order to support the government. And I  
17 think that's in part what's behind this letter, which  
18 is one of the exhibits from 1983, immediately prior  
19 to the adoption of the statute, from then Director  
20 Don Burrows at the Department of Revenue to then  
21 Governor John Spellman about the uncertainty  
22 regarding jurisdiction to impose the B&O tax on  
23 certain types of activities. That's now two or three  
24 decades old, but there was a great deal of not only  
25 discussion, but United States Supreme Court cases,

1 some of them from the State of Washington, that were  
2 wrestling with this problem trying to find some  
3 formulaic solution to equalize taxes between states  
4 that tax income and states that do not, like  
5 Washington. These kind of issues also come up in  
6 Dormant Commerce Cause cases such as the Stevedoring  
7 Cases for instance, which John Piper argued by the  
8 way.

9 Now, I also agree with all counsel that the *Stroh*  
10 case is not on all fours with what I have in front of  
11 me, partly because it didn't need to address it  
12 because of the concessions *Stroh* made, and partly  
13 because they didn't reach all the issues or arguments  
14 that are being advanced here. But the *Stroh* case,  
15 even though not dispositive of the issues in front of  
16 me, is a strong wind sock for which way the wind is  
17 blowing and how the Court of Appeals, at least in  
18 Division II, looks at this, and I think analytically  
19 *Stroh* supports the argument the Department is making  
20 here. And the argument that was made in the *Stroh*  
21 case, even if it isn't determinative -- partly  
22 because *Stroh* conceded the way the statute was being  
23 read so the Court of Appeals didn't have to really  
24 address that, and partly with the principle of ruling  
25 conservatively -- is controlling in principle. And

1 at the same time they only had to address the  
 2 wholesaling function by a manufacturer, and as  
 3 Mr. Tracy points out here, we're talking about a  
 4 solicitation as opposed to wholesaling. So Stroh  
 5 didn't really get into what the taxpayers here are  
 6 calling a "clause two analysis." I'm not sure I  
 7 agree with that terminology necessarily, but I do  
 8 understand, I think, how it's being used.

9 I also should say that I really don't agree, and I  
 10 think the Department is on shaky ground when they try  
 11 to make this flesh and blood distinction regarding  
 12 the word "person." Because that's a word that's used  
 13 throughout Title 82, and it always means taxable  
 14 entities without them necessarily having to be "flesh  
 15 and blood." And so to use the word in a different  
 16 way in this one section of the statute without  
 17 specifically identifying it I think is a weak reed to  
 18 rely on and would get the Department in trouble.

19 Having said that, if you step back and look at the  
 20 whole statute instead of parsing it out like we  
 21 lawyers tend to do, and when you look at the history  
 22 as to how this came into being, in part relying upon  
 23 how retail door-to-door sellers were handled under  
 24 the federal internal revenue code, and apparently  
 25 some of that thinking went into adopting this back in

1 1983, and we follow that up with how the rule, both  
 2 the prior rule and even the revised rule, deals with  
 3 all this, I don't think Mr. Comfort is being  
 4 unreasonable when he points out that it's a fair  
 5 interpretation to say that the legislature must have  
 6 intended that we're talking about flesh and blood  
 7 taxpayers here and not any other business form,  
 8 corporate or otherwise.

9 But I more agree with Dot Foods that the  
 10 Department can't do that by rule. The legislature  
 11 maybe could do that by statute, although I even would  
 12 question that under the privileges and immunities  
 13 clause, which we're not going to get into here, but I  
 14 think that the word "person," unless it's somehow  
 15 distinguished by the legislature, has to have the  
 16 same meaning throughout the whole taxing statutes.

17 But, having given Dot Foods their due in that  
 18 regard, I cannot agree with Dot Foods that I should  
 19 treat the small amount of non-consumable products as  
 20 *de minimis* when the legislature has used the term  
 21 "consumer products" even if we find the exclusivity  
 22 provision in a different paragraph of the exact same  
 23 statute.

24 As long as Mr. Tracy told us that he had a father  
 25 in a small business, I'll tell you my father had a

1 small oyster farm, and when I came home from law  
2 school once -- I used to help him go and deliver to  
3 supermarkets -- and one day we were driving up I-5,  
4 and he had a pickup truck like your father, and in  
5 the back of it was a cold box, and I'd be riding with  
6 him, and we got up to the weigh station, and he  
7 pulled off along with all the big semi-trucks. And I  
8 said, "What are you doing? We're just driving a  
9 pickup truck. Why don't we just get on up to  
10 Tacoma?" And he said, "Cork," -- that's what he  
11 called me -- "the sign didn't say big trucks stop and  
12 little trucks go through; it said, 'trucks stop.'"  
13 So I understood then that "exclusively" can mean  
14 exclusively in this regard based on my personal  
15 experience, and I think the Department, unless the  
16 legislature makes some flexibility for a *de*  
17 *minimis*-type argument, is correct on that.

18 Now, I've seen cases where during negotiation with  
19 a taxpayer -- I recently had such a case involving an  
20 oil refinery in Anacortes where through some  
21 negotiation a taxpayer was able to negotiate a  
22 somewhat favorable result based upon a *de minimis*  
23 result of how some otherwise taxable gases were  
24 captured and re-used inside the refinery. And I  
25 suppose we give some discretion to the executive

1 branch of government through state agencies when  
2 something is in a gray area and it's difficult to  
3 draw what we call a black and white line when things  
4 are looked at very closely. But the legislature  
5 hasn't specifically addressed "*de minimis*" here, and  
6 there's no case that I think anybody can point to  
7 that says close enough is good enough.

8 So in looking at this I think the Department is  
9 right that the fact that there's non-consumer  
10 products -- even though according to the affidavit  
11 that supplements the agreed statement of facts it's  
12 one-half of one percent -- that still the exclusivity  
13 provision applies. And although it's a somewhat  
14 seductive argument by Mr. Tracy that there can be  
15 inclusion by silence because paragraph two of the  
16 statute defines a direct seller's representative as  
17 meaning somebody who deals with consumer products and  
18 is silent as to non-consumer products, I think the  
19 Department's application of the rule here, which is  
20 known by the legislature and recognized in such cases  
21 as the *Stroh* case, then I have to give some  
22 deference, and I think other courts have to give some  
23 deference to the Department's interpretation that it  
24 doesn't apply to individuals or persons, taxpayers  
25 who solicit for sale or resale "non-consumer"

1 products.

2 I also found a little bit confusing that the  
3 Department says that some Dot Foods products are sold  
4 at retail, but I think here when I hear Mr. Tracy say  
5 that they don't do any retail sales, what the  
6 Department means here is what Mr. Tracy says is down  
7 the chain or down the line, but I think that's what  
8 the legislature had in mind here when trying to  
9 figure out how to deal with jobbers or brokers, was  
10 that this little exemption that was opened up wasn't  
11 intended to exempt manufacturers like Stroh's or even  
12 redistributors like Dot Foods whose products end up  
13 down the line in permanent retail establishments. I  
14 think the legislature's intent comes through pretty  
15 clear there.

16 Insofar as the private-letter ruling is concerned,  
17 I think Dot Foods, based upon how they presented the  
18 case to the Department of Revenue and got a favorable  
19 ruling for many years, is disappointed to find either  
20 a change of policy, which I think some of the  
21 material concedes there was, or at least a different  
22 interpretation. But the *Stroh* court also dealt with  
23 this, and Stroh's case wasn't as strong as Dot Foods'  
24 case insofar as the change of policy. But the *Stroh*  
25 court concedes that even if the policy had been

1 changed or the interpretation had been changed, that  
2 the real test is what did the legislature intend with  
3 the statute. And I made a reference in oral  
4 argument, and I think it's in the footnotes of one of  
5 the briefs, to the *Hansen Baking Company* case, which  
6 is a case in the state of Washington that deals with  
7 a taxpayer being given erroneous information and to  
8 what extent it can be relied upon here.

9 But the private-letter ruling that was given to  
10 Dot specifically gave any number of ways in which the  
11 ruling would be put at risk, and two or three of them  
12 were met here. So I don't think Dot Foods can rely  
13 on the private-letter ruling which was not only  
14 specifically signaled to be at risk by Dot being sent  
15 notice, but the rule itself was changed.

16 So I think there is probably something else that I  
17 would have wanted to say if I had notes and made this  
18 out. I do understand, as an aside here, that someone  
19 in the redistribution business probably works on a  
20 very small margin, and even though they might be the  
21 largest redistributor in the United States, a million  
22 dollars in taxes is a lot of money. And I very much  
23 appreciate the way Mr. Tracy presented himself here,  
24 which is somewhat patronizing and I guess I apologize  
25 for that aspect of it. But Ms. Beatty and

1 Mr. Comfort were equal in both their competence and  
2 civility, so I do again, as I started to at the  
3 beginning, thank all of you.

4 But I think that Division II of the Court of  
5 Appeals will find that this is the right foot that  
6 comes down to bring the feet together with the left  
7 foot that came down in the *Stroh's* case, and that  
8 they'll rule consistent with the way they did in  
9 *Stroh's*, and I think properly so, or I would myself  
10 rule differently, and I would therefore grant the  
11 Department's motion.

12 Since I don't have to make findings of fact or  
13 conclusions of law for a summary judgment, I'd be  
14 happy just to sign an abbreviated order if either  
15 side has one ready so you can get on your way up the  
16 street to the Court of Appeals, or if you want to  
17 note this for presentation, that too is okay.

18 MR. COMFORT: Your Honor --

19 THE COURT: We'll take a brief recess.

20 MR. COMFORT: Your Honor, I didn't prepare an  
21 order just because there was enough issues that I  
22 didn't know how you would rule, but I think what I'll  
23 do is just prepare a very brief order, send it over  
24 to Ms. Beatty, and I'm sure we can hopefully agree.

25 THE COURT: If everybody signs off on it, you

1 can send it down *ex parte* and nobody has to make the  
2 trip down.

3 MR. COMFORT: And that way we won't have to  
4 note it up for presentation.

5 (A recess was taken.)  
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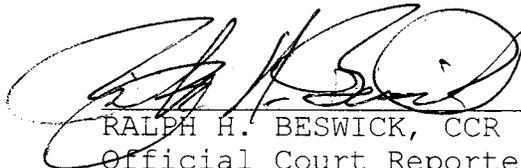
CERTIFICATE OF REPORTER

STATE OF WASHINGTON )  
 ) ss.  
COUNTY OF THURSTON )

I, RALPH H. BESWICK, CCR, Official Reporter of the Superior Court of the State of Washington in and for the County of Thurston do hereby certify:

That I was authorized to and did stenographically report the foregoing proceedings held in the above-entitled matter as designated by Counsel to be included in the transcript and that the transcript is a true and complete record of my stenographic notes.

Dated this 18th day of December, 2006.



RALPH H. BESWICK, CCR  
Official Court Reporter  
Certificate No. 2023

## Subtitle E—Employment Taxes

### PART I—IN GENERAL

#### SEC. 269. TREATMENT OF REAL ESTATE AGENTS AND DIRECT SELLERS.

(a) GENERAL RULE.—Chapter 25 of the Internal Revenue Code of 1954 is amended by adding at the end thereof the following new section:

#### “SEC. 3508. TREATMENT OF REAL ESTATE AGENTS AND DIRECT SELLERS.

26 USC 3508.

(a) GENERAL RULE.—For purposes of this title, in the case of services performed as a qualified real estate agent or as a direct seller—

“(1) the individual performing such services shall not be treated as an employee, and

“(2) the person for whom such services are performed shall not be treated as an employer.

(b) DEFINITIONS.—For purposes of this section—

“(1) QUALIFIED REAL ESTATE AGENT.—The term ‘qualified real estate agent’ means any individual who is a sales person if—

“(A) such individual is a licensed real estate agent,

“(B) substantially all of the remuneration (whether or not paid in cash) for the services performed by such individual as a real estate agent is directly related to sales or other output (including the performance of services) rather than to the number of hours worked, and

“(C) the services performed by the individual are performed pursuant to a written contract between such individual and the person for whom the services are performed and such contract provides that the individual will not be

treated as an employee with respect to such services for Federal tax purposes.

“(2) DIRECT SELLER.—The term ‘direct seller’ means any person if—

“(A) such person—

“(i) is engaged in the trade or business of selling (or soliciting the sale of) consumer products to any buyer on a buy-sell basis, a deposit-commission basis, or any similar basis which the Secretary prescribes by regulations, for resale (by the buyer or any other person) in the home or otherwise than in a permanent retail establishment, or

“(ii) is engaged in the trade or business of selling (or soliciting the sale of) consumer products in the home or otherwise than in a permanent retail establishment,

“(B) substantially all the remuneration (whether or not paid in cash) for the performance of the services described in subparagraph (A) is directly related to sales or other output (including the performance of services) rather than to the number of hours worked, and

“(C) the services performed by the person are performed pursuant to a written contract between such person and the person for whom the services are performed, and such contract provides that the person will not be treated as an employee with respect to such services for Federal tax purposes.

“(3) COORDINATION WITH RETIREMENT PLANS FOR SELF-EMPLOYED.—This section shall not apply for purposes of subtitle A to the extent that the individual is treated as an employee under section 401(c)(1) (relating to self-employed individuals).”

(b) AMENDMENT OF SOCIAL SECURITY ACT.—Section 210 of the Social Security Act is amended by adding at the end thereof the following new subsection.

42 USC 410.

A-21

"Treatment of Real Estate Agents and Direct Sellers

Ante, p. 551.

"(p) Notwithstanding any other provision of this title, the rules of section 3508 of the Internal Revenue Code of 1954 shall apply for purposes of this title."

(c) INDEFINITE EXTENSION OF PROVISIONS RELATING TO EMPLOYMENT STATUS FOR EMPLOYMENT TAXES.—

26 USC 3401  
note.

26 USC 530.

(1) TERMINATION OF CERTAIN EMPLOYMENT TAX LIABILITY.—

(A) Subparagraph (A) of section 530(a)(1) of the Revenue Act of 1978 (relating to termination of certain employment tax liability for periods before July 1, 1982) is amended by striking out "ending before July 1, 1982".

(B) Paragraph (3) of section 530(a) of such Act is amended by striking out "and before July 1, 1982."

(C) The subsection heading of subsection (a) of section 530 of such Act is amended by striking out "FOR PERIODS BEFORE JULY 1, 1982".

(2) PROHIBITION AGAINST REGULATIONS AND RULINGS ON EMPLOYMENT STATUS.—Subsection (b) of section 530 of such Act is amended—

(A) by striking out "July 1, 1982 (or, if earlier," and

(B) by striking out "taxes)" and inserting in lieu thereof "taxes".

(3) CERTAIN REGULATIONS, ETC., PERMITTED.—Nothing in section 530 of the Revenue Act of 1978 shall be construed to prohibit the implementation of the amendments made by this section.

26 USC 3508  
note.  
26 USC 280.

(d) CLERICAL AMENDMENT.—The table of sections for chapter 25 of such Code is amended by adding at the end thereof the following item:

Sec. 3508. Treatment of real estate agents and direct sellers."

(e) EFFECTIVE DATES.—

26 USC 3508  
note.

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to services performed after December 31, 1982.

(2) SUBSECTION (c).—The amendments made by subsection (c) shall take effect on July 1, 1982.

COURT OF APPEALS  
DIVISION II

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STATE OF WASHINGTON  
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DEPUTY

NO. 35733-0-II

**COURT OF APPEALS, DIVISION II  
OF THE STATE OF WASHINGTON**

DOT FOODS, INC.,

Appellant,

v.

DEPARTMENT OF REVENUE,  
STATE OF WASHINGTON,

Respondent.

DECLARATION OF  
SERVICE

I, Carrie A. Parker, 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 April 16, 2007, I provided a true and correct copy of BRIEF OF RESPONDENT and this DECLARATION OF SERVICE to be served via U.S. mail (through Consolidated Mail Services), with proper postage affixed to:

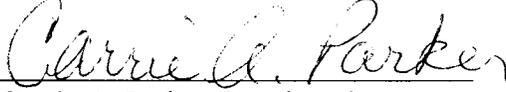
Jacquelyn A. Beatty  
Karr Tuttle Campbell  
1201 Third Avenue, Suite 2900  
Seattle, WA 98101-3028

and

Howard M. Goodfriend  
Edwards Sieh Smith & Goodfriend PS  
1109 First Avenue, Suite 500  
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 16<sup>th</sup> day of April, 2007, in Olympia, Washington.

  
Carrie A. Parker, Legal Assistant