

NO. 50057-4-II

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

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STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Appellant,

v.

WAREHOUSE DEMO SERVICES, INC.,

Respondent.

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**REPLY BRIEF OF APPELLANT**

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ROBERT W. FERGUSON  
Attorney General

Charles Zalesky, WSBA No. 37777  
Kelly Owings, WSBA No. 44665  
Assistant Attorneys General  
Revenue Division, OID No. 91027  
P.O. Box 40123  
Olympia, WA 98504-0123  
(360) 753-5528

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## I. INTRODUCTION

Warehouse Demo seeks a broad and imaginative construction of RCW 82.04.290(2)(b). The company asserts that the statutory phrase “the value of” means “cash payments,” “furnished” means a two-step “purchase and reimbursement” payment method, and the statute itself is “not a tax exemption.” In addition, Warehouse Demo tries to distance itself from its prior written admission that it was not acting as an agent, and falsely claims that evidence of “control” over its demonstration activities can be gleaned from testimony of its co-owner, Brett Ellis. None of these contentions has any merit.

The statute at issue—RCW 82.04.290(2)(b)—is a narrowly tailored tax exemption. It provides that *the value of* promotional supplies and materials *furnished to an agent* by his or her principal to be used for informational, educational, or promotional purposes is not to be included as part of the agent’s remuneration or commission for purposes of the state’s business and occupation (B&O) tax. The exemption does not apply to cash payments Warehouse Demo received as reimbursement for demonstration products that it purchased from Costco and used in its demonstration business. Moreover, the record before the Board of Tax Appeals was consistent with Warehouse Demo’s earlier admission that it was not an agent, and Mr. Ellis never testified that Costco vendors instructed the

company on how to perform a demonstration. Warehouse Demo simply relies on legally and factually incorrect arguments in its efforts to salvage a B&O tax refund that the Board of Tax Appeals erroneously granted to it.

The Board's decision granting Warehouse Demo's tax refund erroneously interprets and applies the law and should be set aside.

## II. ARGUMENT

### A. **The Board Of Tax Appeals Erroneously Construed And Applied The "Promotional Materials Furnished To An Agent" Tax Exemption.**

It is established law in Washington that amounts received as reimbursement for costs of doing business are includable as gross income unless expressly exempted from the tax by the Legislature. *Pullman Co. v. State*, 65 Wn.2d 860, 867, 400 P.2d 91 (1965). Following this established law, Warehouse Demo reported all amounts it received from its customers as gross income on its Washington B&O tax returns, including amounts it billed and received as reimbursement for the cost of demonstration products it purchased from Costco. The tax Warehouse Demo paid on the reimbursement payments is presumed to be correct, and Warehouse Demo carries the burden of establishing that the payments were exempt and should be refunded. *Avnet, Inc. v. Dep't of Revenue*, 187 Wn.2d 44, 49, 384 P.3d 571 (2016).

Warehouse Demo relies on RCW 82.04.290(2)(b) as authority for excluding the reimbursement amounts from its gross income. By its plain terms, that statute excludes from the “service and other” B&O tax classification the value of promotional supplies and materials furnished to an agent by his or her principal to be used for informational, educational, or promotional purposes. Although the statute is narrowly tailored and uses plain terms, the Board of Tax Appeals nonetheless concluded that it was broad enough to encompass the reimbursement payments Warehouse Demo received from its customers. The Board’s construction and application of the “promotional materials furnished to an agent” B&O tax exemption was erroneous and should be set aside. RCW 34.05.570(3)(d).

**1. The portion of RCW 82.04.290 at issue in this appeal is a narrowly tailored tax exemption.**

The B&O tax applies broadly to “virtually all business activity carried on within the state.” *Avnet*, 187 Wn.2d at 50-51 (quoting *Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971)). Conversely, exemptions and deductions are construed and applied narrowly. *Avnet*, 187 Wn.2d at 49-50. Warehouse Demo attempts to avoid this longstanding principle by arguing that the B&O tax exemption for “promotional materials furnished to an agent” in RCW 82.04.290(2)(b) is not really a tax exemption at all; it is a tax imposing statute. Resp. Br. at 10. The

argument is illogical on its face. RCW 82.04.290(2)(b) excludes from the “service and other” B&O tax classification the value of materials and supplies furnished to an agent to be used for a qualifying informational, educational, promotional activity. This is a quintessential tax exemption, carving out from a general tax provision a subclass of transactions that are excluded from the tax. Even the Board of Tax Appeals, which misconstrued and misapplied the statute, nonetheless recognized that it was a tax exemption provision. AR 018-019 (COL 9-10).

Warehouse Demo asserts that the statutory language at issue here is not a tax exemption because it is included as part of a broader statute that sets out the B&O tax rates for various taxable activities. Resp. Br. at 11.<sup>1</sup> According to Warehouse Demo, there is a legal distinction between an “exception” to a tax imposing statute and a tax “exemption.” *Id.* at 10-11. Warehouse Demo cites no relevant authority for its argument. Moreover, referring to the statutory provision at issue here as a tax “exception” rather than a tax “exemption” has no bearing on the manner in which the provision is construed. *Foster v. Dep’t of Ecology*, 184 Wn.2d

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<sup>1</sup> RCW 82.04.290(1) sets out the B&O tax rate that applies to persons engaging in international investment management services. RCW 82.04.290(2)(a) sets out the rate applicable to those engaged in business activities that are not “taxes explicitly under another section” of the B&O tax code, including most service activities. And RCW 82.04.290(3) sets out the tax rate applicable to persons engaged in providing aerospace product development for others. Warehouse Demo is a service provider and was subject to B&O tax under the rate set out in RCW 82.04.290(2)(a).

465, 473, 362 P.3d 959 (2015) (“statutory exceptions are construed narrowly in order to give effect to the legislative intent underlying the general provision”); *TracFone Wireless, Inc. v. Dep’t of Revenue*, 170 Wn.2d 273, 297, 242 P.3d 810 (2010) (to avoid tax the plain language of the statute requires “some language of exemption or exception”) (internal quotations and citations omitted).

The only authority cited by Warehouse Demo in support of its “tax exceptions are different from tax exemptions” argument is *Agrilink Foods, Inc. v. Dep’t of Revenue*, 153 Wn.2d 392, 103 P.3d 1226 (2005). See Resp. Br. at 11. That case is not helpful to Warehouse Demo for several reasons. First, our Supreme Court in *Agrilink* relied on the plain language of the statute at issue, and the Court’s plain language analysis is on all fours with the Department’s plain language analysis in this appeal. Compare *Agrilink*, 153 Wn.2d at 397 (“where the Legislature uses certain statutory language in one instance, and different language in another, there is a difference in legislative intent”) (quoting *United Parcel Serv., Inc. v. Dep’t of Revenue*, 102 Wn.2d 355, 362, 687 P.2d 186 (1984)) with App. Br. at 17 (“[i]t is well settled that where the Legislature uses certain language in one instance but different, dissimilar language in another, a difference in legislative intent is presumed”) (quoting *Millay v. Cam*, 135 Wn.2d 193, 202, 955 P.2d 791 (1998)).

Second, the statutory construction issue raised in *Agrilink* was whether RCW 82.04.260(4) should be narrowly construed because it provided a preferential tax rate for certain manufacturing activities. *Agrilink*, 153 P.2d at 396.<sup>2</sup> In dicta at the end of the opinion, the Court suggested that all tax imposing statutes, even those that offer a lower tax rate, must be construed in favor of the taxpayer. *Id.* at 399 n.1. However, the Court did not rely on that concept in deciding the case and has not applied that dicta in any case either before or after *Agrilink* was decided.<sup>3</sup>

Finally, the issue in this case does not involve application of a preferential tax rate. Rather, it involves the application of a narrowly tailored tax exemption or, to use Warehouse Demo's preferred term, a narrowly tailored tax "exception." Regardless of what rule of construction might apply to a preferential tax rate, tax exemptions and exceptions are always construed and applied narrowly. *TracFone Wireless*, 170 Wn.2d at 296-97.

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<sup>2</sup> RCW 82.04.260(4) provides that the B&O tax on qualifying manufacturing activity is taxed at the rate of 0.138 percent. The tax rate applicable to most other types of manufacturing is 0.484 percent. *See* RCW 82.04.240.

<sup>3</sup> Roughly one year after *Agrilink* was decided, the Legislature enacted a statute defining the term "tax preference" to include "an exemption, exclusion, or deduction from the base of a state tax . . . [and also] a *preferential state tax rate*." Laws of 2006, ch. 197, § 2 (emphasis added) (codified at RCW 43.136.021). Based on that statute, it is reasonable to surmise that our Supreme Court would construe a statute providing a preferential tax rate in the same narrow manner that it construes tax exemptions, exclusions, deductions and other tax preferences.

**2. The statute does not exempt “amounts received” with respect to demonstration supplies and materials.**

RCW 82.04.290(2)(b) is narrowly tailored. As pointed out at pages 16 through 18 of the Department’s opening brief, in construing the plain language of RCW 82.04.290(2)(b) it is telling that the statute does not exempt “amounts received” with respect to qualifying advertising, demonstration and promotional supplies and materials. Rather, the exemption is limited solely to “[t]he value of” qualifying supplies and materials. The Legislature undoubtedly knows how to exempt from the B&O tax “amounts received” from qualifying business activity. *See* App. Br. at 17-18 n.3 (listing 28 separate B&O tax provisions that exempt “amounts received” or use similar language). But RCW 82.04.290(2)(b) contains no language expressing that intent.

In this important respect, RCW 82.04.290(2)(b) is distinct from other B&O tax exemptions. No other exemption is limited solely to “the value of” qualifying property. As discussed above with respect to *Agrilink*, the express language used in RCW 82.04.290(2)(b) versus the language used in other exemption statutes is important in ascertaining its plain meaning. When the Legislature “uses certain statutory language in one instance, and different language in another, there is a difference in

legislative intent.” *Agrilink*, 153 Wn.2d at 397 (quoting *United Parcel*, 102 Wn.2d at 362).

RCW 82.04.290(2)(b) establishes a narrow, targeted tax exemption that shields sales agents from having the value of promotional supplies and materials “to be used” for a qualified purpose from being included as part of the agents’ “remuneration or commission.” If the Legislature had intended the exemption to apply to *amounts received* with respect to qualifying supplies and materials used in a qualifying activity, it would have used plain language to express that intent. It did not, and the Board of Tax Appeals erred as a matter of law when it expanded the exemption beyond its plain and unambiguous terms.

Warehouse Demo offers no meaningful response to the principle that the use of certain statutory language in one instance and different language in another shows a difference in legislative intent. It relies instead on its claim that RCW 82.04.290(2)(b) is not a tax exemption. *See* Resp. Br. at 12 (arguing that the different language employed in RCW 82.04.4266, RCW 82.04.4268, and 82.04.4269 “is not as helpful as the Department suggests” because “RCW 82.04.290(2)(b) is not an exemption”). But this principle of statutory construction is not limited to tax exemptions. *See Millay*, 135 Wn.2d at 202 (principle applied in construing a statute pertaining to the procedure for redeeming foreclosed

real property). Here, the express language used in RCW 82.04.290(2)(b) is materially different from numerous other statutes that exempt “amounts received” from the measure of the B&O tax. Warehouse Demo’s characterization of RCW 82.04.290(2)(b) as “not an exemption” does not explain why the Legislature excluded the phrase “amounts received” when enacting the statute.

Additionally, Warehouse Demo’s reliance on the term “gross proceeds of sale” in RCW 82.04.290(1) is unavailing. *See* Resp. Br. at 12. It is not clear why Warehouse Demo has grounded its argument on RCW 82.04.290(1). That subsection of RCW 82.04.290 establishes a preferential tax rate for businesses providing international investment management services and is not at issue in this appeal. Warehouse Demo likely meant to cite RCW 82.04.290(2)(a), which sets out the B&O tax rate applicable to its demonstration service activities. Under that subsection, the measure of the tax is the “gross income of the business,” not the gross proceeds of sales. *See* RCW 82.04.080 (definition of “gross income of the business”). In any event, all of the amounts Warehouse Demo received from its demonstration activities, including reimbursements it received for the cost of demonstration products it purchased from Costco, were correctly reported by Warehouse Demo on its Washington B&O tax returns as

“gross income of the business.” AR 030 (COL 6).<sup>4</sup> This case turns on whether Warehouse Demo can establish that the amounts at issue are excluded from its gross income under the plain language of RCW 82.04.290(2)(b). As explained above, the express language of the statute simply does not support Warehouse Demo’s claim or the Board of Tax Appeals’ application of the statute. Consequently, the Board’s erroneous decision to grant Warehouse Demo’s refund claim should be set aside. RCW 34.05.570(3)(d).

**3. The phrase “the value of” cannot be fairly interpreted to mean “cash” payments.**

Echoing the same shaky logic the Board of Tax Appeals employed, Warehouse Demo argues that RCW 82.04.290(2)(b) can be interpreted to apply to the amounts it received as reimbursement for the cost of demonstration products it purchased from Costco simply by broadly construing the phrase “the value of” to mean “cash.” Resp. Br. at 12-13. The theory Warehouse Demo offers, after correcting its citation error, is that (1) the service and other B&O tax is measured by “gross income of the business,” (2) “gross income of the business” is defined in RCW

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<sup>4</sup> Warehouse Demo argued to the Board of Tax Appeals that the reimbursement amounts it received from its customers were not “gross income of the business.” AR 723. The Board rejected the argument. *See* AR 025 (brief answer to issue 1). Warehouse Demo did not appeal. And even if the company had appealed from that ruling, no Washington case law supports the claim. *See, e.g., Pullman Co.*, 65 Wn.2d at 867 (amounts received as reimbursement for the actual cost of work performed is gross income of the business even though the reimbursement payments “yield[ed] no profit”).

82.04.080 as “the value proceeding or accruing by reason of the business engaged in,” (3) “value proceeding or accruing” is defined in RCW 82.04.090 as “consideration, whether money, credits, rights, or other property expressed in terms of money,” (4) therefore “‘value’ means the same thing as money (cash).” *Id.* at 12.

The Department has previously addressed this argument. *See App. Br.* at 18-20. The connection between the phrase “value proceeding and accruing” and the phrase “the value of” advertising, demonstration, and promotional supplies and materials is exceedingly thin and ignores the context in which these terms are used. The Legislature broadly defined the phrase “value proceeding and accruing” in order to ensure that the B&O tax applies to all forms of compensation or consideration, including reimbursement payments. *Engine Rebuilders, Inc. v. State*, 66 Wn.2d 147, 150, 401 P.2d 628 (1965); *Pullman Co.*, 65 Wn.2d at 867. By contrast, the term “the value of,” when read in the context of RCW 82.04.290(2)(b), is intentionally narrow. The Legislature did not exempt all “value” that happens to qualify as gross income of the business. Rather, only the value of specified supplies and materials are exempt. Read in context, “the value of” qualifying supplies and materials cannot fairly be construed to mean the amount of “cash” received by the sales agent with respect to demonstration supplies and materials it purchased from a third party.

Moreover, Warehouse Demo's theory requires persons reading the statute to go through several steps to reach the conclusion it advocates. It would have been much simpler for the Legislature to expressly provide that the exemption covers the value of qualifying supplies and materials *and* "amounts received" with respect to qualifying supplies and materials. It is highly unlikely that the Legislature intended to require a person reading and attempting to apply the statute to go through all of the steps framed by Warehouse Demo in order to properly understand its meaning.

**4. The phrase "furnished to an agent" cannot be fairly interpreted to mean "reimbursement payments received by an agent."**

Warehouse Demo also contends that the term "furnished to an agent" can be construed broadly enough to fit its two-step "purchase and reimbursement" method of obtaining demonstration products. Resp. Br. at 15. As support, Warehouse Demo points out that both the Board of Tax Appeals and the trial court agreed. *Id.* at 16.

In an appeal under the Administrative Procedure Act, the appellate court typically gives no deference to the decision or legal conclusions of the trial court. *Verizon Nw., Inc. v. Employment Sec. Dep't*, 164 Wn.2d 909, 915, 194 P.3d 255 (2008). Moreover, in this case the trial court judge based his decision on his own "commonsense" understanding of the term "furnished," deliberately avoiding the dictionary definition of the term.

VRP at 32. The commonsense understanding of a single judge is not especially persuasive, particularly when the judge admitted that he did not consult or consider basic rules of statutory construction. *Id.*

As to the Board of Tax Appeals, that adjudicative agency simply misconstrued the statute. “When determining a statute’s plain meaning, [courts] consider ‘the ordinary meaning of words, basic rules of grammar, and the statutory context to conclude what the legislature has provided for in the statute and related statutes.’” *Darkenwald v. Emp’t Sec. Dep’t*, 183 Wn.2d 237, 245, 350 P.3d 647 (2015) (quoting *In re Forfeiture of One 1970 Chevrolet Chevelle*, 166 Wn.2d 834, 838-39, 215 P.3d 166 (2009)).

The ordinary meaning of “furnished” is “provided with essentials : EQUIPPED.” *Webster’s Third New Int’l Dictionary* 924 (unabridged ed. 2002). Additionally, as pointed out in the Department’s opening brief, “furnished” is not synonymous with “purchased.” App. Br. at 24-25. In order to construe the statute in favor of Warehouse Demo, the term “furnished” must be given an extraordinary or unusual construction, rather than its ordinary meaning. No rule of construction supports the practice of searching for the most unusual meaning of a term to ascertain legislative intent.

When the term “furnished to an agent” is read in context and its words are accorded their ordinary meaning, the tax exemption at issue

here cannot be fairly interpreted to apply to demonstration products that Warehouse Demo purchased from Costco. The Board's conclusion of law to the contrary was incorrect and should be rejected.

**5. Warehouse Demo “bears the same tax burden” that applies to any business that charges its customers for materials and supplies purchased from a third party.**

Warehouse Demo next argues that a broad construction of RCW 82.04.290(2)(b) is necessary to achieve parity between a business that demonstrates products that are actually furnished to it by its principal or supplier and a business like Warehouse Demo that demonstrates products it purchases from a third party. Resp. Br. at 16-17. The argument is meritless and ignores a crucial fact. Warehouse Demo has made the business decision to charge its customers for the cost of the food and other consumer products it purchases from Costco. Warehouse Demo was not required to charge its customers for these costs of doing business. But having done so, just like any other business, it is subject to B&O tax on the amounts it receives unless an express exemption or deduction applies. *See Pullman Co.*, 65 Wn.2d at 867.

The two-step “purchase and reimbursement” business model employed by Warehouse Demo is materially different from the business model contemplated by RCW 82.04.290(2)(b) where the sales agent is being furnished with supplies and materials at no cost. In the business

model contemplated by the statute, an agent that is furnished with supplies and materials to be used to demonstrate, promote, or advertise its client's products or services is not required to include the value of the property as part of his or her "remuneration or commission." Warehouse Demo does not fit this business model, and there is nothing unfair about rejecting its efforts to enlarge the exemption to fit its circumstances. *Cf., Forbes v. City of Seattle*, 113 Wn.2d 929, 944-45, 785 P.2d 431 (1990) (the Legislature has broad authority to create different taxing classifications).

Moreover, Warehouse Demo's plea for a broad reading of the statute that ignores the "consequence" flowing from its two-step purchase and reimbursement business model is primarily a policy argument. The Washington Legislature establishes the tax policy of this State. In 1963 the Legislature enacted a narrow tax exemption that applies to the value of promotional supplies and materials furnished to an agent to be used in a qualifying activity. That exemption, on its face, does not apply to reimbursement payments received after the demonstration activity is completed. If Warehouse Demo believes the State should establish a different policy, its remedy lies with the Legislature, not the courts.

**B. Warehouse Demo Was Not Acting As An Agent Of The Costco Vendors Who Hired It To Perform Product Demonstrations.**

“An agency relationship generally arises when two parties consent that one shall act under the control of the other.” *Washington Imaging Services, LLC v. Dep’t of Revenue*, 171 Wn.2d 548, 562, 252 P.3d 885 (2011) (quoting *Rho Co., Inc. v. Dep’t of Revenue*, 113 Wn.2d 561, 570, 782 P.2d 986 (1989)). “The two elements of an agency are mutual consent and control by the principal of the agent.” *Uni-Com Northwest, Ltd. v. Argus Publishing Co.*, 47 Wn. App. 787, 796, 737 P.2d 304 (1987). The burden of establishing a principal-agency relationship in this appeal falls upon Warehouse Demo, the party asserting its existence. *Hewson Constr., Inc. v. Reintree Corp.*, 101 Wn.2d 819, 823, 685 P.2d 1062 (1984).

**1. The evidence in the record shows a “buyer-seller” relationship, which is how Warehouse Demo initially explained its relationship with the Costco vendors.**

The element of control is crucial and “must exist to prove agency.” *Uni-Com Northwest*, 47 Wn. App. at 796. Absent evidence of control, the relationship is one of a buyer and seller, for example, not a principal and agent. *Id.* at 797.

When Warehouse Demo filed its tax refund petition with the Department of Revenue, it expressly disavowed any agency relationship. AR 579. Instead, it described its business activities as a typical seller of services:

WDS is engaged in the business of demonstrating vendor products at Costco Wholesale . . . locations. For example, a vendor that supplies Costco with certain food products to sell will engage WDS to provide demonstration services of those products at Costco. WDS demonstrators are skilled in communication and sales. Each WDS demonstrator has a food and beverage service worker's permit so that WDS can legally perform these demonstration services for the vendors.

AR 576. The company made no claim that its customers exerted some control over its demonstration business activities. And, as previously noted, the company expressly disavowed any agency relationship.

Everything Warehouse Demo told the Department was consistent with a buyer-seller relationship. There is no dispute that, in some cases, the buyer of Warehouse Demo's services would pick the product to be demonstrated and the location of the demonstrations. *See* Tr. at 23-24 (about one-half of Warehouse Demo's business was initiated through direct contact with the customer, with the other half initiated by Costco). But the same is true in many buyer-seller relationships. A homeowner who hires a contractor to paint her home will most often tell the contractor the location of the home, the date the work should start, and the color of the paint to use. Insisting on these logistical details does not convert the relationship into an agency. Likewise, the fact that Costco vendors often make basic logistical decisions—the “when what and where” decisions—does not convert the relationship into an agency.

Warehouse Demo also argues that its statement that it was “not an agent of . . . the product vendors” was a limited admission, applying only to the agency required to satisfy Department “Rule 111.” Resp. Br. at 27 (referring to WAC 458-20-111).<sup>5</sup> But that is not what Warehouse Demo actually stated in its refund petition. *See* AR 579 (“WDS is not an agent of, nor do they have a contract with, the product vendors, thus an agency/Rule 111 analysis is not warranted”). More importantly, Rule 111 does not require some specialized form of agency. To the contrary, that Rule looks to the common law to determine agency. *Washington Imaging*, 171 Wn.2d at 561-62. Warehouse Demo’s attempt to distance itself from its prior admission of no agency is hollow and should be rejected.

**2. Warehouse Demo misstates the facts in the record pertaining to demonstration instructions.**

Aside from the “when what and where” logistical decisions that vendors made with respect to “about half” of Warehouse Demo’s business, *see* Tr. at 23-24, the only other “evidence” of control cited by Warehouse Demo is a misstatement of testimony offered at the BTA hearing. At five separate points in its Respondent’s Brief, Warehouse Demo claims that it performed product demonstrations pursuant to

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<sup>5</sup> WAC 458-20-111 allows a taxpayer to exclude from taxable gross income amounts received when acting solely as an agent for a client, which the agent must pay on the client’s behalf to third parties. These amounts are sometimes described as “pass-through” payments.

“vendor’s . . . instructions.” *See* Br. of Resp. at 18, 19, 23, 26, and 28.

Warehouse Demo made the same statement of fact to the trial court. *See* CP 92 (referring to the demo instructions as “the vendor’s demo instructions”). But the actual testimony Warehouse Demo cites to in the record does not support its statement of fact. *See* Tr. at 58. Warehouse Demo simply misstates the sworn testimony offered by Bruce Ellis, part owner and CFO of the company.

During cross examination, Mr. Ellis was asked to explain to the Board how Warehouse Demo would prepare a sausage patty, which was one of the products it demonstrated for Tyson Foods. *Id.* Mr. Ellis stated that he did not know. Tr. at 58, ln. 15. He continued: “Well, again, I could speculate. I just -- you know, there were demo instructions for every demo, and they said what to do with it, how to prepare it. I can’t tell you how this particular event was executed.” *Id.* at ls. 17-20.

Mr. Ellis did not specify who provided or received these “demo instructions.” And no evidence supports Warehouse Demo’s bald claim that it was the product vendor that instructed Warehouse Demo on how to prepare a product for demonstration. To the contrary, Warehouse Demo holds itself out as employing “thoroughly trained” demonstrators that have “[f]ull-time, on-site demo supervision.” AR 631. Mr. Ellis testified that the company’s on-site demo managers oversee the demonstrations. Tr. at 29.

Additionally, the company's agreement with Costco expressly stated that Warehouse Demo was responsible for the "mode, manner, methods and means" used in the performance of demonstrations, and was "solely responsible for the direction of persons conducting Demos under [the] Agreement." AR 675. In short, there is simply no evidence supporting Warehouse Demo's claim that demonstration instructions were provided by the product vendors.<sup>6</sup>

Because there is no evidence of control, Warehouse Demo has not met its burden of establishing an agency relationship. Consequently, its belated claim that it was an agent for purposes of RCW 82.04.290(2)(b) fails as a matter of law. *See Blodgett v. Olympic Savings & Loan Ass'n*, 32 Wn. App. 116, 128, 646 P.2d 139 (1982) (where building owner exercised no control over contractor's remodeling work, trial court should have concluded that contractor was not an agent as a matter of law).

**3. Department tax determinations do not establish an agency relationship under the facts in this appeal.**

Finally, Warehouse Demo argues that two published tax determination issued by the Department establish that an agency

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<sup>6</sup> Warehouse Demo contends that it is fair to "speculate that a product vendor would want" to control the manner in which demonstrations were conducted in order "to minimize product liability risks." Resp. Br. at 26 n. 8. But it is just as likely, perhaps more likely, that Warehouse Demo's customers would eschew any agency relationship out of concern that they could be held liable for Warehouse Demo's actions under the doctrine of respondeat superior. In any event, Warehouse Demo bears the burden of proving the existence of an agency relationship, and speculation as to what its customers might "want" is insufficient to carry that burden.

relationship exists between Warehouse Demo and its customers because, like the facts discussed in the two determinations, its in-state promotional activities “helped these vendors establish or maintain a market for their products sold in Costco’s Washington stores.” Resp. Br. at 31. The argument is nonsense. When the Department issues published tax determinations, it is acting in a quasi-judicial role. It weighs evidences, makes findings of fact, and applies those findings to legal principles to arrive at a conclusion. The fact that the Department may have found an agency relationship with respect to a particular taxpayer based on particular facts does not mean that Warehouse Demo is an agent based on the facts here.

Moreover, the two determinations cited by Warehouse Demo involve issues of whether out-of-state taxpayers had sufficient “nexus” with Washington for our taxes to apply to their in-state activities. It is well established that nexus can be established through the actions of non-agents. *See Tyler Pipe Indus. v. Washington Dep’t of Revenue*, 483 U.S. 232, 250, 107 S. Ct. 2810, 97 L. Ed. 2d 199 (1987) (instate activities of an independent sales representative were sufficient to establish nexus where the activities helped establish and maintain a market for the taxpayer’s goods). In short, an agency relationship is not required to establish nexus. Consequently, Warehouse Demo’s willingness to concede that each of its

customers has tax nexus with Washington is not evidence of an agency relationship.

If Warehouse Demo is looking for guidance from the Department regarding agency law, it should look to WAC 458-20-159. That administrative rule explains that the person claiming to be acting as an agent or broker in promoting sales or making purchases “will have such claim recognized only when the contract or agreement between such persons clearly establishes the relationship of principal and agent . . . .” Warehouse Demo has not clearly established an agency relationship here. Consequently, it is not entitled to the tax exemption for “promotional materials furnished to an agent” both as a matter of common law and under published Department guidance.

**C. The Sparse Legislative History Is Not Useful And Does Not Control Over The Plain Language Of The Statute.**

In the event that the Court concludes that RCW 82.04.290(2)(b) is ambiguous, it would be permissible to “look to legislative history for assistance in discerning legislative intent.” *State v. Evans*, 177 Wn.2d 186, 193-94, 298 P.3d 724 (2013). However, with respect to the exemption at issue here, there is virtually no legislative history detailing its purpose.

The “promotional materials furnished to an agent” B&O tax exemption was added to RCW 82.04.290 in 1963 as part of Senate Bill 54.

*See* Laws of 1963, Ex. Sess., ch. 28. That bill made several amendments to Washington's tax laws. *See id.* The only substantive discussion of the bill recorded in the Senate Journal took place on April 3, 1963. *See* Senate Journal, 38th Leg., Ex. Sess., at 198 (Wash. 1963). Most of that discussion pertained to other sections of the bill. *Id.* at 198-205. The only comment concerning the section amending RCW 82.04.290 was from Senator Gallagher explaining why he voted against the bill:

The undersigned Senator voted "nay" on Engrossed Senate Bill No. 54 because it was clearly stated on the floor of the Senate that the purpose of section 2 amending RCW 84.04.290 [sic] was to permit distillery representatives the right to deduct the value of samples purchased by them in furtherance of their business. I have no objection to such deductions but feel that the exemption more properly belongs in another section of the law. . . .

*Id.* at 205.

Apparently, although by no means clear, Senator Gallagher viewed the bill as "stated on the floor of the Senate" as exempting the "purchase" of samples used by distillery representatives in furtherance of their business. Whether that was indeed his understanding of the bill, or whether he simply misspoke, cannot be conclusively determined from the legislative history. But what is conclusively reflected by the legislative history is that the bill as originally proposed used the term "furnished," not the term "purchased." *See Printed Bills of the 38th Legislature, Ex. Sess., Senate Bill No. 54 at 2*

(Wash. 1963). Consequently, it is unlikely that other Senators who read the bill would have concluded that it applied to materials “purchased” by a qualifying agent. That reading is simply incompatible with the actual words used in the bill. Moreover, as discussed in the Department’s opening brief, there would never be a circumstance where a sales agent would recognize gross income as a result of a “purchase” of supplies and materials. *See* Br. of App. at 23-24. Consequently, there would have been no reason for the Legislature to enact an exemption to cover the value of such purchases.

The much more likely purpose of section 2 of Senate Bill 54 was to prevent the value of qualifying supplies and materials from being considered part of the compensation or commission earned by a sales agent in the course of his or her business. The B&O tax applies broadly, and gross income of a business generally includes all consideration received regardless of its form. *Engine Rebuilders*, 66 Wn.2d at 151. Thus, it is conceivable that the Legislature was concerned that materials and supplies “furnished to” an agent could be treated as taxable gross income. It follows that the sponsor of the bill sought to clarify that, while the B&O tax applies broadly, it does not apply to the value of advertising and promotional supplies and materials that are furnished to an agent involved in advertising and promotion for its principal.

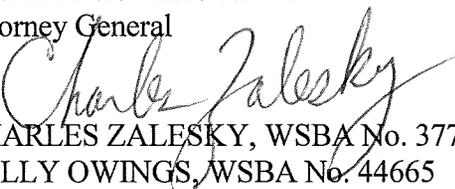
In any event, the statement of a single Senator who voted against the bill does not undermine the plain language of the statute or conclusively establish legislative intent. *See Spokane County Health Dist. v. Brockett*, 120 Wn.2d 140, 154-55, 839 P.2d 324 (1992) (“a legislator’s comments from the floor are not necessarily indicative of legislative intent”). Senator Gallagher was not the drafter or sponsor of Senate Bill 54, and there is no reason to believe he had any special insight into its purpose. He either misspoke or misunderstood the purpose of the bill.

### III. CONCLUSION

The Board of Tax Appeals’ construction and application of the “promotional materials furnished to an agent” B&O tax exemption is not supported by the plain language of the statute or by the evidence in the administrative record. Accordingly, this Court should reverse and reinstate the Department of Revenue’s denial of Warehouse Demo’s refund claim.

RESPECTFULLY SUBMITTED this 12<sup>th</sup> day of July, 2017.

ROBERT W. FERGUSON  
Attorney General

  
CHARLES ZALESKY, WSBA No. 37777  
KELLY OWINGS, WSBA No. 44665  
Assistant Attorneys General  
Attorneys for Appellant

**PROOF OF SERVICE**

I certify that I served a copy of this document, via electronic mail, per agreement, on the following:

Garry G. Fujita  
Eisenhower Carlson, PLLC  
1200 Wells Fargo Plaza 1201  
Tacoma, WA 98102  
gfujita@eisenhowerlaw.com  
crochelle@eisenhowerlaw.com

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

DATED this 12<sup>th</sup> day of July, 2017, at Tumwater, WA.

  
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Candy Zilinskas, Legal Assistant

**ATTORNEY GENERAL'S OFFICE - REVENUE & FINANCE DIVISION**

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