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

PHARMACY CORPORATION OF AMERICA, a California corporation,

Appellant,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Respondent.

BRIEF OF RESPONDENT

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TABLE OF CONTENTS

I.	INTRODUCTION.....	1
II.	RESTATEMENT OF THE ISSUE	2
III.	STATEMENT OF THE CASE.....	3
	A. PharMerica’s Business in Washington	3
	1. PharMerica’s business relationship with facilities	3
	2. PharMerica’s business relationship with patients.....	4
	3. PharMerica billed according to the patient’s financial arrangements.....	6
	B. Proceedings Below.....	8
IV.	ARGUMENT	11
	A. Overview of B&O Taxation of Business Activities	12
	B. A Business That Engages in Multiple Business Activities is Taxed Separately on Each Activity	13
	C. As a Matter of Law, the Preferential Tax Classification in RCW 82.04.272 Applies Only to Prescription Drug Sales Made to Persons Selling at Retail or Health Care Providers	14
	1. Under the plain language of the statute, the buyer is the person who paid the monetary consideration for the prescription drug.....	17
	2. PharMerica is selling to the patient because the transactions at issue between the patient and PharMerica meet both elements of a sale	21

3.	Concluding the facility is not the buyer is consistent with the language of the contracts and course of performance between PharMerica and the patients.....	22
4.	Health care providers are not the buyer for the additional reason that the patient has the primary or sole legal obligation to pay for the drug.....	24
5.	The Court should also reject PharMerica’s argument that the element of valuable consideration is met by a promise that another will pay	26
D.	The Buyer Requirement in RCW 82.04.272 is Not Ambiguous, so Resort to Legislative History or Other Aids is Unnecessary.....	28
V.	CONCLUSION	31

TABLE OF AUTHORITIES

Cases

<i>AARO Med. Supplies, Inc. v. Dep't of Revenue</i> , 132 Wn. App. 709, 132 P.3d 1143 (2006).....	24, 25, 26
<i>Aventis Pharm., Inc. v. State</i> , 5 Wn. App. 2d 637, 428 P.3d 389 (2018).....	15, 16, 29, 30
<i>Butcher v. Garrett-Enumclaw</i> , 20 Wn. App. 361, 581 P.2d 1352 (1978).....	18
<i>Drury the Tailor v. Jenner</i> , 12 Wn.2d 508, 122 P.2d 493 (1942).....	13
<i>Gandy v. State</i> , 57 Wn.2d 690, 359 P.2d 302 (1961).....	20, 21
<i>HomeStreet Inc. v. Dep't of Revenue</i> , 166 Wn.2d 444, 210 P.3d 297 (2009).....	29
<i>Impecoven v. Dep't of Revenue</i> , 120 Wn.2d 357, 841 P.2d 752 (1992).....	13
<i>Inland Empire Dairy Ass'n v. Dep't of Revenue</i> , 14 Wn. App. 592, 544 P.2d 52 (1975).....	19, 20, 21
<i>Lake v. Woodcreek Homeowners Ass'n</i> , 169 Wn.2d 516, 243 P.3d 1283 (2010).....	29
<i>P.E. Sys., LLC v. CPI Corp.</i> , 176 Wn.2d 198, 289 P.3d 638 (2012).....	28
<i>Ralph v. State Dep't of Nat. Res.</i> , 182 Wn.2d 242, 343 P.3d 342 (2014).....	19
<i>Sandeman v. Sayres</i> , 50 Wn.2d 539, 314 P.2d 428 (1957).....	28

<i>Steven Klein, Inc. v. Dep't of Revenue</i> , 183 Wn.2d 889, 357 P.3d 59 (2015).....	12, 13, 28
<i>Supply Laundry Co. v. Jenner</i> , 178 Wash. 72, 34 P.2d 363 (1934)	13
<i>United States v. Hoffman</i> , 154 Wn.2d 730, 116 P.3d 999 (2005).....	17

Statutes

Laws of 1998, ch. 343, § 1.....	15
RCW 82.04.040	1, 18, 28
RCW 82.04.040(1).....	17, 19, 29
RCW 82.04.050	13
RCW 82.04.050(1)(a)	16
RCW 82.04.220	12, 27
RCW 82.04.220(1).....	12
RCW 82.04.240	12
RCW 82.04.250	1, 13, 14, 16
RCW 82.04.270	12
RCW 82.04.272	passim
RCW 82.04.272(1).....	2, 16
RCW 82.04.272(2)(b)	2, 15, 18
RCW 82.04.280	12
RCW 82.04.290	12

RCW 82.04.290(2)(a) 13, 14
RCW 82.04.4297 8

Other Authorities

DOR Excise Tax Advisory 3180 (2013)..... 11, 17, 30
Engrossed Substitute H.B. 2933, 55th Leg. Sess., ch. 343 (Wash.
1998) 28
Restatement (Third) Of Agency § 1.01 (2006)..... 20

I. INTRODUCTION

Appellant Pharmacy Corporation of America (PharMerica) requests that over \$57 million of its receipts from selling drugs be reclassified from the retailing Business and Occupation (B&O) tax classification (RCW 82.04.250) to the preferential “warehousing and reselling prescription drugs” B&O tax classification (RCW 82.04.272). For this income to be taxed under the preferential tax classification, RCW 82.04.272 requires, among other things, that the taxpayer sell the drugs to a buyer who is a retailer or health care provider. Accordingly, this case turns on properly identifying whom PharMerica is reselling its drugs to: individual patients or health care providers.

As a matter of law, the term “sale” is defined in RCW 82.04.040, and means a transfer of ownership, title, or possession of property for valuable consideration. Accordingly, the buyer is the person who provided the consideration for the drug in exchange for ownership, title, or possession of the drug. This appeal involves only those sales where patients paid for their own drugs, either directly (Private Pay Resident) or indirectly through a third party (Third Party Payors). None of the approximately \$57 million in payments at issue in this case were made by a long-term health care facility. Therefore, for these sales, PharMerica did not sell to a retailer or health care provider as required in RCW 82.04.272.

The trial court properly granted the Department of Revenue (DOR)'s motion for summary judgment and dismissed PharMerica's complaint seeking to reclassify these sales and obtain a refund. This Court should affirm the trial court's ruling.

II. RESTATEMENT OF THE ISSUE

PharMerica is engaged in the business of buying prescription medications and reselling them. For some of its drug sales, PharMerica received payments from the patient, either directly (a "Private Pay Resident"), or through the patient's coverage under a private insurance plan or government plan (collectively "Third-Party Payors"). PharMerica classified these payments under the retailing B&O classification on its tax returns. Its refund action seeks to reclassify these payments to the more favorable B&O classification in RCW 82.04.272(1) for entities that "buy[] drugs ... from a manufacturer or another wholesaler, and resell[] the drugs to ... hospitals, clinics, health care providers, or other providers of health care services[.]" RCW 82.04.272(2)(b). The issue presented is:

Were the amounts paid to PharMerica for drugs delivered to facilities but paid for by Private Pay Residents and Third Party Payors properly taxed under the retailing classification because the sales do not fall within the rate provided in RCW 82.04.272(1)?

III. STATEMENT OF THE CASE

A. PharMerica's Business in Washington

PharMerica is a for-profit medical supply company, licensed in Washington as a pharmacy. CP 147. During the tax period (January 1, 2008 through June 30, 2012), PharMerica provided pharmacy services and sold prescription drugs, non-prescription drugs, syringes, tubing, and other supplies. CP 104, 138.

PharMerica provided products and services to facilities in Washington—institutions such as nursing homes, assisted living communities, and rehabilitation centers (facilities) that provide health care services to residents and long-term patients. CP 20-21, 104, 245.

PharMerica also provided products and services directly to residents and long-term patients (patients) who lived or stayed at these facilities. CP 20, 104, 147.

1. PharMerica's business relationship with facilities

PharMerica entered into pharmacy service agreements with the facilities. CP 103-14. Therein, PharMerica agreed to provide to the facility pharmacy-related services, prescription drugs, medical devices, and other health care related products. CP 104 (¶ 1(a)). The schedules attached to the pharmacy services agreements explain how PharMerica calculated the charges for prescription drugs sold to the facility. CP 106. Under these

agreements, PharMerica would charge the facility for the products and services. *See* CP 104 (§ 4(a)) (“charges to facilities”).

Facilities purchased prescription drugs from PharMerica for several reasons. In some instances, they purchased drugs for specific patients with a prescription. CP 161-62. The facility would resell the drug to the patient by seeking reimbursement from the patient or the patient’s insurance, or by receiving a *per diem* payment covering the patient’s drug and health care costs from a private or government health plan. CP 152, 161-62. In other instances, facilities purchased commonly needed drugs to have in stock, which they later prescribed and sold to their patients, for example, during an emergency. CP 20-21, 56, 152; *see* CP 106 (stock product pricing). Both types of sales to the facilities are not part of PharMerica’s refund action. CP 3-4 (concerns only private pay patient and third party payors sales); CP 177-78 (Department’s final determination granted PharMerica’s claims for amounts paid by the facility and denied PharMerica’s claims for amounts paid by patients or patient’s insurance).

2. PharMerica’s business relationship with patients

PharMerica and the facilities also agreed that PharMerica would be the “preferred provider” for providing patients of the facility with pharmacy products and services. *See* CP 104 (§ 1(b)) (“subject to applicable laws relating to patient choice”). Patients would “authorize”

PharMerica to be their pharmacy while staying at the facility. CP 104 (§§ 4(b), (c)). The facilities would communicate billing instructions for each patient to PharMerica, which PharMerica called the patient's "financial plan." CP 57. PharMerica created an account for each patient in its database that tracked these instructions. CP 56-57, 66.

PharMerica used two categories, "Private Pay Residents" and "Third Party Payors," to describe the patients to whom PharMerica billed directly for products or services. CP 21, CP 80-81. A "Third Party Payor" was a patient who had "coverage for pharmacy benefits through a third party that was accepted by" PharMerica. CP 104 (§ 4(b)). For Third Party Payors, PharMerica would "directly bill the third party" (such as private insurance or Medicare) that covered the patient's pharmacy benefits. *Id.* PharMerica entered into separate agreements with third parties. CP 115-120. These third party agreements provided different terms of billing, payment, refunds, and pricing than the pharmacy services agreement. *Compare*, CP 106 (facility pricing) *with* CP 119 (third party pricing).

A "Private Pay Resident" was a patient who was not eligible for coverage "under a third party program accepted by" PharMerica. CP 104 (§ 4(c)). For these patients, PharMerica would "directly bill the Private Pay Resident or his [or her] legally responsible representative." *Id.* If the Private Pay Resident failed to pay any amount due to PharMerica within

PharMerica's "standard payment terms for Private Pay Residents," then PharMerica would suspend providing services and products to the resident unless the facility agreed to be responsible for services and products for the Private Pay Resident. *Id.* If the facility agreed to be responsible, then PharMerica would treat the purchase as a facility charge. *Id.*

Patient invoices provided some of PharMerica's "standard payment terms." CP 121-25. The private-pay invoice instructed the patient to provide payment upon receipt. CP 121. The schedules attached to the pharmacy services agreement also provided the pricing terms for Private Pay Residents. *See* CP 106 (¶ 3 (a)-(c)) (Pricing).

3. PharMerica billed according to the patient's financial arrangements

When medications were prescribed to the patient, or needed to be refilled, the facility would order the drugs from PharMerica for the patient. CP 246, 262. PharMerica would then either charge the facility (if it was going to resell the drug to the patient), or bill the patient for the prescribed drug according to the patient's financial plans. *See* CP 20-21, 56-63, 67-70, 161-63. The drugs were delivered to the facilities where the patients were staying or resided. The facilities' care professionals administered the drugs to the patients as prescribed.

When PharMerica charged a facility for the drug, it would send a statement listing the drugs purchased by the facility for specific patients as well as drugs purchased for house use. CP 20-21, 56, CP 104 (¶ 4 (a)). For patients who were Third Party Payors, PharMerica electronically or manually billed the third party. CP 80-81. The third party approved the claim for payment based on the payment and pricing terms between it and PharMerica, and then remitted payment. CP, 80, 119.

For Private Pay Residents, PharMerica sent an invoice to the patient or authorized representative, indicating the balance due for medications dispensed to the patient. CP 63-64, 80-81; *see* CP 121 (sample invoice). Payments were due on receipt and the patient paid PharMerica online, by check, or by credit card. CP 121-25. If the patient did not pay, PharMerica utilized an in-house collection staff to request payment approximately 30 to 40 days after the statement date. CP 81.

In many instances, a patient's financial plan provided that PharMerica would bill the drug to multiple third parties and the patient directly. PharMerica's database system provided a billing hierarchy to identify the priority in which PharMerica would seek payment. CP 58-63. For example, a primary category provided that PharMerica would bill a specific insurance company first for a portion of the drugs cost. CP 59-60. A secondary category provided that another insurance would cover all or a

portion of the remaining payment. CP 60-61. And a tertiary category provided that PharMerica would invoice the remaining balance directly to a specific family member of the patient. CP 61-62, 67-68.

Because of this hierarchy, the individual or entity that ultimately would pay was not always known at the time the drug was ordered for the patient. CP 60-61, 226-27. However, PharMerica's records identified the gross receipts from its drug sales by the amount of payment and category of payor. CP 128, 161-62.

B. Proceedings Below

On its Washington State B&O tax returns for January 1, 2008 through June 30, 2012, PharMerica reported over \$98 million in gross revenues under the "retailing" B&O tax classification and over \$1 million in gross revenues under the "service and other activities" B&O tax classification. CP 138. Based on this reporting, PharMerica paid \$461,220 in retailing B&O taxes. CP 138, 141-42.

In August 2012, PharMerica filed two tax refund claims. Only one of these claims remains an issue in this appeal.¹ CP 132-34. For that remaining claim, PharMerica sought to reclassify \$84 million of its sales

¹ PharMerica also sought a refund for \$46,804 in taxes paid for approximately \$9 million of its drug payments made by Medicare, Medicaid, CHAMPS, and Tricare, which PharMerica claimed were wholly exempt from taxation under RCW 82.04.4297. CP 135. The trial court also granted summary judgment with respect to this second claim, but PharMerica has not appealed this claim. *See* App. Brief at 12, n.5.

revenues from the retailing B&O classification to the preferential “warehousing and reselling prescription drugs” B&O classification. CP 132-34. PharMerica requested a refund of \$281,740 in retailing B&O taxes paid, reflecting the tax rate difference between these two classifications. CP 133-34.

The Department’s audit division reviewed PharMerica’s refund request, partially allowed the reclassification of two types of facility charges, and issued a tax credit. CP 127, 137, 144. Dissatisfied, PharMerica sought administrative review of the auditor’s decision. CP 144-47. The Department’s appeals division reviewed the matter, and in a written determination, partially denied PharMerica’s request. CP 146-58.

Specifically, the appeals division held that a sale qualified for the lower tax rate only where the facility either “(1) absorbed the drug’s cost in the resident’s care (such as when the facility, under Medicaid or Medicare A, was paid only *per diem* amounts), or (2) paid for the drugs and then, in turn, charged residents’ insurance for them.” CP 154. The appeals division denied PharMerica’s claim where PharMerica billed either Private Pay Residents “or other ‘legally responsible representatives or third parties’ directly” because these sales “were not to a hospital, clinic, health care provider, or other provider of health [services].” CP

154, 177. The appeals division remanded the refund application back to the audit division to perform adjustments. CP 155.

On remand, the audit division performed additional adjustments. PharMerica's accounting firm provided books that contained numerous entries showing amounts paid by different sales categories. CP 160-62. The accounting firm identified 30 sales categories that were paid by facilities. *Id.* The auditor totaled the amounts from these categories, approximately \$27 million, and reclassified these receipts from retailing to the lower tax classification. CP 161-62. The audit division then calculated an additional tax credit of \$90,524 and issued a refund. CP 170-74.

The Department's adjustments did not include any amount categorized as a "Private Pay Resident" or "Third Party Payor." This represented approximately \$57 million of PharMerica's gross income for the tax period. PharMerica sought reconsideration of the Department's decision on these sales categories being eligible for reclassification, which the Department denied. CP 176-83.

PharMerica subsequently filed a tax refund action with regard to the taxes on the \$57 million of gross income in Thurston County Superior Court. CP 1-9. It later amended its complaint. *See* CP 19-27. The Department moved for summary judgment on PharMerica's refund claims, arguing that a drug sale qualifies for the rate in RCW 82.04.272 if the

buyer is a health care facility, and that the buyers here were the patients because they paid for the drugs. CP 28-43. PharMerica responded (CP 263-82) and moved for summary judgment in response. CP 281.

On August 17, 2018, the trial court granted the Department's summary judgment motion and denied PharMerica's motion. CP 343-45. PharMerica timely filed an appeal, claiming errors only with respect to its refund claim under RCW 82.04.272. App. Brief at 2-3, 12, n.5.

IV. ARGUMENT

The PharMerica sales at issue, though ordered by, delivered to, and administered by the facilities, do not qualify for the preferential tax rate in RCW 82.04.272 because they were not sold to the facilities. RCW 82.04.272 applies when the drugs are resold to "persons selling at retail or to hospitals, clinics, health care providers, or other providers of health care services." There is no genuine issue of material fact that all of prescription drug sales at issue were paid for by patients, either as Private Pay Residents or by Third-Party Payors. As a matter of law, only a person who paid the consideration for the prescription drug, or who arranged by insurance contract to have it paid for on their behalf, can constitute the buyer for purposes of applying RCW 82.04.272 and the "buyer requirements" under the DOR Excise Tax Advisory 3180 (2013) interpreting this statute. There is no dispute that the facilities are neither

paying nor the insurer. Accordingly, the trial court correctly granted the Department's motion for summary judgment and dismissed PharMerica's tax refund claims. This Court should affirm.

A. Overview of B&O Taxation of Business Activities

Washington imposes the business and occupation (B&O) tax on the "act or privilege of engaging in business activities." RCW 82.04.220(1). Taxpayers calculate the amount of tax due for each business activity by multiplying the applicable tax rate by the value of products, the gross proceeds of sales, or the gross income of the business, depending on the business activity. RCW 82.04.220. Accordingly, the first step for imposing the B&O tax is to identify the statutory classifications that apply to the taxpayer's business activities. *See Steven Klein, Inc. v. Dep't of Revenue*, 183 Wn.2d 889, 896-97, 357 P.3d 59 (2015). This in turn determines the appropriate measure and rate for calculating the amount of tax due for engaging in that particular business activity. *See id.* The B&O tax classifications, include, among many others: manufacturing (RCW 82.04.240); retailing (RCW 82.04.250), wholesaling (RCW 82.04.270); printing or publishing newspapers, magazines, and periodicals (RCW 82.04.280); and "service and other activities" (RCW 82.04.290).

B. A Business That Engages in Multiple Business Activities is Taxed Separately on Each Activity

Taxpayers can also engage in multiple business activities. When a taxpayer engages in more than one type of business activity, each business activity is separate, and each activity is taxed according to its classification. *See Impehoven v. Dep't of Revenue*, 120 Wn.2d 357, 363-64, 841 P.2d 752 (1992) (discussing *Drury the Tailor v. Jenner*, 12 Wn.2d 508, 510, 515, 122 P.2d 493 (1942); *Supply Laundry Co. v. Jenner*, 178 Wash. 72, 79, 34 P.2d 363 (1934)).

An example of a business engaging in multiple business activities is a car dealership that sells cars to consumers. *Steven Klein, Inc.*, 183 Wn.2d at 891. When the dealership sells a car to a consumer, it is making a retail sale (RCW 82.04.050). The amount of tax due for a person engaging in a retailing business is calculated by multiplying the gross proceeds of all of the business's retail (car) sales during the tax period by the retailing rate of .471 percent (RCW 82.04.250). The same car dealership also receives "dealer cash" payments from the manufacturer for selling particular car models. *Steven Klein, Inc.*, 183 Wn.2d at 891-92. That business activity is not a retail sale, and does not fall within any other classification, so it is considered a "service and other" activity. *Id.*, at 898-99; *see* RCW 82.04.290(2)(a). The amount of tax due for a person

engaging in service or other business is calculated by multiplying the gross income from the service or other activity by the tax rate of 1.5 percent. RCW 82.04.290(2)(a). Thus, the dealership is engaged in two separate but related business activities: selling cars and dealer cash. The income attributed to each activity is separately taxed.

Here, there is no dispute that PharMerica engaged in multiple types of business activities. CP 132-34, 138. The sales at issue in this appeal involve only a portion of PharMerica's business activities: sales of prescription drugs for which the patient or a third party paid PharMerica.

C. As a Matter of Law, the Preferential Tax Classification in RCW 82.04.272 Applies Only to Prescription Drug Sales Made to Persons Selling at Retail or Health Care Providers

PharMerica's income from Private Pay Residents and Third Party Payors is subject to the retailing B&O classification (RCW 82.04.250), not the "warehousing and reselling of prescription drugs" classification (RCW 82.04.272) because these individual sales do not meet the buyer requirement. CP 132.² The Legislature enacted RCW 82.04.272 in 1998 as a preferential tax classification for persons engaged in the business of "warehousing and reselling drugs for human use pursuant to a

² A retailing tax of .471 percent is due on the gross income from retailing prescription drugs, and the lower rate of .138 percent is due on the gross income from "warehousing and reselling drugs for human use pursuant to a prescription." RCW 82.04.250; RCW 82.04.272.

prescription.” Laws of 1998, ch. 343, § 1. The Legislature defined the activity of “warehousing and reselling drugs for human use pursuant to a prescription” as:

[T]he buying of drugs for human use pursuant to a prescription from a manufacturer or another wholesaler, and *reselling* of the drugs *to* persons selling at retail or to hospitals, clinics, health care providers, or other providers of health care services, by a wholesaler or retailer

RCW 82.04.272(2)(b) (emphasis added). This Court recently held that to be engaged in the business activity of “warehousing and reselling drugs for human use pursuant to a prescription” under the statute, the taxpayer must meet six requirements. *Aventis Pharm., Inc. v. State*, 5 Wn. App. 2d 637, 644, 428 P.3d 389 (2018). The person must: (1) buy drugs for human use pursuant to a prescription, (2) from a manufacturer or another wholesaler, (3) *resell either to persons* selling at retail or *to health care providers*, (4) be a wholesaler or retailer, (5) be registered with the Drug Enforcement Agency, and (6) be licensed by the pharmacy quality assurance commission. *Id.* (Emphasis added.)

The Department’s Excise Tax Advisory (ETA) 3180 (2013) also discusses the requirements to qualify for preferential tax rate under RCW 82.04.272. The ETA described the requirements applicable to a “buyer” and “seller.” CP 187-88. The buyer requirement refers to the requirement

that the drugs be resold to certain persons. To satisfy the buyer requirements, the seller must resell the drug “*directly to a buyer*” who is:

- A retailer with a pharmacy facility license or non-residential pharmacy license . . . ; or
- A hospital, clinic, health care provider, or other provider of health care services.

CP 188 (emphasis added).

If the taxpayer meets all the statutory requirements, it is eligible to receive the preferential rate. However, it can only apply this rate to individual sales that meet all six requirements. *See Aventis Pharm., Inc.*, 5 Wn. App. 2d at 645 (rejecting taxpayers’ argument that a drug wholesaler is taxed under RCW 82.04.272(1) for all of its sales regardless of whether individual transactions meet all six requirements).

Accordingly, if an otherwise eligible taxpayer, like PharMerica, directly sells the drug to a buyer who is not a pharmacy retailer or a health care provider, then the taxpayer is not warehousing and reselling prescription drugs, and the amounts received from those sales are not subject to the lower prescription drug warehousing tax rate. RCW 82.04.272(1). Instead, if the buyer is a patient (i.e., someone who does not intend to resell the drug), then the sale does not meet the statute and is considered a “retail sale” subject to the retailing tax rate. RCW 82.04.050(1)(a); RCW 82.04.250.

The Department correctly taxed PharMerica, and the superior court properly dismissed the case on summary judgment. For the sales in question, the buyers are not retailers or a health care provider. The buyers are the persons who paid the consideration for the drug or arranged to have a third party pay on their behalf. Accordingly, there is no genuine issue of material fact that the buyers were not health care facilities as required for application of the preferred rate.

1. Under the plain language of the statute, the buyer is the person who paid the monetary consideration for the prescription drug

The buyer is a person who pays the consideration for the drug or arranges to have a third party, like an insurer, pay the seller on his or her behalf. This is evident by the Legislature's definition of a "sale" and the common meaning of buyer. The Legislature defined the term "sale" in RCW 82.04.040(1) as including "any transfer of the ownership of, title to, or possession of property for a valuable consideration." When the Legislature defines a term, courts will use that definition in determining the plain meaning of a statute. *See United States v. Hoffman*, 154 Wn.2d 730, 741, 116 P.3d 999 (2005).

It is appropriate to apply the definition of "sale" to B&O tax classifications like RCW 82.04.272, as the terms "sell," "resell," or "reselling" are verb forms of the word "sale." The addition of "re" denotes

the subsequent sale of the same item. RCW 82.04.272(2)(b) describes the activity of one person reselling a drug to another person. These two persons are commonly understood to be the buyer and seller.

The word “buyer” is also synonymous with “purchaser,” which PharMerica concedes is commonly understood to mean “one who acquires property for a consideration (as of money).” App. Brief at 19. It most commonly refers to the person who paid the purchase price of the good, the monetary or other form of consideration. *See, e.g., Butcher v. Garrett-Enumclaw*, 20 Wn. App. 361, 376, 581 P.2d 1352 (1978) (buyer of portable sawmill was the person paying the purchase price). The Department has also used these terms in a similar manner in ETA.

Nonetheless, PharMerica argues that a person who orders and receives delivery of a drug on behalf of a patient, and who administers that drug to the patient, but who does not pay the purchase price or obtain ownership of that drug, is the buyer. PharMerica’s interpretation is flawed for several reasons. First, PharMerica cites no authority that a buyer is the person who ordered the drug, or that ordering is part of the meaning of “buyer” or “sale.” The term “order” does not appear in the statutory definition of “sale” in RCW 82.04.040, or elsewhere in the business activity definition of RCW 82.04.272(2)(b). Nor does the common definition of “buyer” use the term “order.” Nor is the term administer part

of the definition of “buyer” or “sale.” At best, ordering and administering a drug reveals the facility acts as an agent for the patient, the real buyer.

Nor is delivery to the facility from PharMerica significant here. Transferring possession of a good (i.e., delivery) is part of the definition of “sale” in RCW 82.04.040(1), because it is one of three alternative ways to meet the first element of “sale” (alternatively, the buyer can receive title or ownership). *See* RCW 82.04.040(1)(a). However, that term must be read in context and in light of case law. *See Ralph v. State Dep’t of Nat. Res.*, 182 Wn.2d 242, 248, 343 P.3d 342 (2014). Delivery of the good alone, without providing valuable consideration, does not constitute a sale for B&O tax purposes. *See Inland Empire Dairy Ass’n v. Dep’t of Revenue*, 14 Wn. App. 592, 595, 544 P.2d 52 (1975). If PharMerica is correct, then any person who possessed the drug—the delivery driver, the postal worker, or the administering health care professional—could claim to be the buyer; this is an unreasonable and absurd interpretation.

In *Inland Empire Dairy*, the court explained that both the elements of (1) transfer of ownership, title to, or possession; and (2) valuable consideration must be present to constitute a sale for B&O tax purposes. *Inland Empire Dairy Ass’n*, 14 Wn. App. at 595. In that case, a dairy transferred possession of the milk containers (containing milk) to a customer. *Id.* The dairy imposed a separate charge to the customer for the

container at the end of the month, but only if the container was not returned. *Id.* at 593. There was no dispute that the dairy owed the B&O tax when its customer paid for an unreturned container charge. *Id.* For containers that were returned, the court stated that there had been no sale because there had been no valuable consideration for the transfer of the container. *Id.* at 594. Specifically, a sale occurred “[o]nly then was there valuable consideration flowing from the customer to the dairy for the transfer.” *Id.* See also, *Gandy v. State*, 57 Wn.2d 690, 694, 359 P.2d 302 (1961) (The requirement of a valuable consideration for B&O tax purposes is necessary for a sale and “is at least as important as the transfer”).

While it is true that a health care facility ordered, received, and dispensed these drugs to each resident patient, these facts alone do not establish that the facility is the buyer for these particular sales. Rather, these facts merely confirm that the residential health care facility is the patient’s agent while the patient stays at the facility and receives care. The agent is not the buyer; the patient who pays (or arranges for payment) is. An agent is acting on the principal (buyer’s) behalf. See Restatement (Third) Of Agency § 1.01 (2006) (defining agent). The pharmacy service agreements show there is no material fact, either. They show that the patient “authorizes” the facility to order drugs from PharMerica for the

patient and have the drugs delivered and administered to the patient at the facility's location where the patient is receiving care. *See* CP 104 (§4 (b)).

Once “ordering” and “delivery” are shown to be immaterial, PharMerica has no basis for claiming that health care facilities are the buyers in those sales. The undisputed fact that the facility does not provide any monetary consideration to PharMerica means the facility and PharMerica are not engaged in a sale, and thus the Facility is not the buyer, i.e., person to whom the drug is sold.

PharMerica argues applying *Inland Empire Dairy* and *Gandy* in this manner means “there would be no taxable sale in the first place.” App. Brief at 20. What it means is there would be no sale between PharMerica and the facility if the facility did not pay. But PharMerica's argument assumes that transactions between PharMerica and the individual patient do not meet both elements of a sale. In fact they do.

2. PharMerica is selling to the patient because the transactions at issue between the patient and PharMerica meet both elements of a sale

When PharMerica's customers are Private Pay Residents or patients with Third Party Payors, as a matter of law the sale is being made to the patients, not the health care provider as required for PharMerica to meet the lower tax rate. The first element of “sale” is met because there is a transfer of possession, title, or ownership to the patient. The patient

receives actual possession of the drug when the drug is administered to him or her. The patient, not the facility, has all the indicia of ownership for the drug—he or she can take it, or dispose of it as allowed by law. The patient’s ownership is also evident from the fact that the patient does not pay the facility to obtain the drug and the facility cannot deny the patient the drug because the patient did not pay the facility for it. In contrast, the facility has no indicia of being the purchaser or owner of the drug. For example, the facility cannot administer the drug to another patient or sell it without being liable to the patient for the value of the drug.

PharMerica already concedes the second element is met because the category of refund is defined by sales where the patient (or the patient’s insurance providers) paid PharMerica the monetary consideration for the drug. CP 23 (drugs that are ... paid for by Private Pay Residents and Third Party Payors). There is no dispute the patient made the monetary payment for the drugs, either directly or through one or more third parties who covered the patient’s drug costs, or both. CP 272.

3. Concluding the facility is not the buyer is consistent with the language of the contracts and course of performance between PharMerica and the patients

The conclusion that the facility is not the buyer, because the patient is the buyer, is also consistent with how the pharmacy services agreement, third party agreement, and PharMerica’s standard payment terms identify

the buyer for these types of sales. These agreements identify selling products and services directly to patients as separate types of sales from PharMerica's "charges to facilities." See CP 104 (compare ¶ (4)(a), with ¶¶ 4(b) and (4)(c)).

The pharmacy services agreement also explains that patients individually "authorize" PharMerica to be their pharmacy provider. Sales to patients who are Private Pay Residents are governed by PharMerica's standard payment terms. CP 104; see, e.g., CP 121-25. And sales to patients for whom PharMerica accepts third party payments are governed by separate agreements. CP 104 (¶ (4)(b)); see, e.g., CP 115-20.

The course of performance also mirrors these distinctions in the contracts. PharMerica's sales to facilities are billed differently from PharMerica's sales to patients. See CP 80-81 (describing the differences in how PharMerica bills and collects payments from the three categories). PharMerica bills patients directly for private pay sales and bills third party providers in accordance with its separate agreements with them. CP 104. A written contract is not required to establish a contractual relationship between the patient and PharMerica for PharMerica to be selling to them. Additionally, there is nothing about how PharMerica is setup or licensed that prohibits it from selling directly to individuals. CP 147. There is only one type of pharmacy license in Washington. *Id.* Although a pharmacy

may specify its practice setting to be “long-term care,” which PharMerica has done, it may still sell to anyone, individuals included. *Id.* Accordingly, concluding the patient is the buyer is consistent with PharMerica’s contracts, performances, and licenses. Ample undisputed evidence establishes that PharMerica, though a long-term care pharmacy, contractually and actually sells drugs to individual patients at retail.

4. Health care providers are not the buyer for the additional reason that the patient has the primary or sole legal obligation to pay for the drug

PharMerica points to the *AARO Medical Supplies* case for the proposition that, the “buyer” is the person who is “*legally obligated* to pay the seller in any transaction.” App. Brief at 22. However, this case supports the Department’s position that the patient is the buyer.

In *AARO Medical Supplies*, a medical device seller agreed to accept payment by the federal government (government insurer) rather than from the Medicare beneficiary who received and used the products. *AARO Med. Supplies, Inc. v. Dep’t of Revenue*, 132 Wn. App. 709, 715, 132 P.3d 1143 (2006). The taxpayer argued the federal government, not the Medicare beneficiary, was the buyer for purposes of applying the retail sales tax. *Id.* at 716. The Court explained that the term “buyer” used in the sales tax statutes “is the party legally obligated to pay the seller.” *AARO Med. Supplies, Inc.*, 132 Wn. App. at 718. The Court held that Medicare

beneficiaries, not the federal government, were the buyers of the seller's medical products, even when the federal government paid the sellers for these products on the beneficiaries' behalf. *Id.*, 132 Wn. App. at 712-13.

In this case, the patients have the primary legal obligation to pay for the drug. For Private Pay Residents, the monetary consideration is due upon receipt of the invoice from PharMerica pursuant to its standard payment terms. CP 104. When the patient is a Third Party Payor, PharMerica, like the seller in *AARO Medical Supplies*, accepts the payment from a third party insurer, who makes it on behalf of the patient, the covered beneficiary. So, even though the patient does not pay PharMerica directly, it has the primary obligation to pay, like the beneficiary in *AARO Medical Supplies*.

In contrast, the facilities do not have the primary legal obligation to pay for patients. CP 104. In fact, there are only two situations where a facility incurs a legal obligation to pay for sales made directly to patients. First, where the facility "was wrong" or "too late" in providing billing instructions and that error caused PharMerica to "submit" the purchase "under the applicable payor's procedures." CP 104, ¶ 3(h). If the right information had been provided in time, the facility would have no legal obligation to pay. CP 102. The second scenario is where the patient failed to pay for the drug and the facility entered into a subsequent agreement to

pay for it (CP 104, ¶ (4)(a)(2), (c)). In this instance, the patient has the primary legal obligation to pay, and the facility has no obligation unless it agrees to incur the obligation for it. *Id.* But none of the transactions at issue here are payments where the facility actually paid monetary consideration. The Department has already allowed the reclassification for any sales in which the facility gave the wrong information or subsequently agreed to pay for a patient. *See* CP 161 (categories: “facility agreed to pay” and “facility responsible” were sales directly to the facility and eligible for lower rate). Accordingly, none of the sales at issue are sales where the facility actually had a legal obligation to pay for the patient, and thus *AARO* provides no support for PharMerica’s position.

5. The Court should also reject PharMerica’s argument that the element of valuable consideration is met by a promise that another will pay

While a promise of future performance can, in some instances, constitute consideration for a contract, the Court should reject PharMerica’s argument that the “element of valuable consideration is satisfied by the Facility’s promise that PharMerica will receive payment for the drugs, either from the Facility’s residents, or a third-party payor.” App. Brief at 19. PharMerica’s promise does not satisfy the element of valuable consideration for B&O tax purposes for the following reasons.

First, in the B&O tax context, “valuable consideration” means the actual monetary consideration, i.e., purchase price, is paid in exchange for the drug. This is because the B&O tax is measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be. RCW 82.04.220. In all cases, whether it is the sale of the product or some other business activity transaction, value must proceed or accrue from the transaction for there to be a taxable transaction. *See id.*, RCW 82.04.070 (gross proceeds of sale), RCW 82.04.080 (gross income of business). “Value proceeding or accruing” means “the consideration, whether money, credits, rights, or other property expressed in *terms of money, actually received or accrued.*” RCW 82.04.090 (emphasis added).

Thus for the activity to be taxed, it must have some actual value. The promise of someone else’s future payment for the good is not actual value received or accrued. Rather, those payments from the patients, either directly or indirectly, constituted the value used in the measure of taxes PharMerica reported for this period. And that actual gross income or proceeds is what PharMerica seeks to reclassify. If the promise of future payment had value, that value is different from the receipts actually paid and sought to be reclassified by PharMerica.

Second, PharMerica’s argument sheds no light on how the B&O tax would apply to the receipt of two different considerations. If this promise had actual value, then that activity would be classified and taxed as a separate business activity with a separate source of income. *See Steven Klein, Inc.*, 183 Wn.2d at 898-900 (proceeds from the sale of cars to consumers is taxed at the retailing rate and dealer cash received from the manufacturer is taxed at the service and other rate).

Finally, the promise of someone else’s future payment for the good is not actual or adequate consideration, even when applying contract law. Agreements to agree are illusory promises and unenforceable. *P.E. Sys., LLC v. CPI Corp.*, 176 Wn.2d 198, 208, 289 P.3d 638 (2012); *see Sandeman v. Sayres*, 50 Wn.2d 539, 541, 314 P.2d 428 (1957) (an illusory promise is insufficient consideration to support enforcement of a return promise). Accordingly, a promise that someone else would pay is not “valuable,” which is a required element of the statutory definition of a sale. *See* RCW 82.04.040.

D. The Buyer Requirement in RCW 82.04.272 is Not Ambiguous, so Resort to Legislative History or Other Aids is Unnecessary

PharMerica argues that if the statute is ambiguous, it should be construed in its favor based on the statutory history of Engrossed Substitute H.B. 2933, 55th Leg. Sess., ch. 343 (Wash. 1998) and the rule

that ambiguous statutes imposing a tax are construed against the Department. App. Brief at 24-27. The Court should reject this argument. First, RCW 82.04.272 is not ambiguous because it identifies the requisite buyer requirements. “A statute is not ambiguous merely because different interpretations are conceivable.” *Aventis Pharm., Inc.*, 5 Wn. App. 2d at 642 (citing *HomeStreet Inc. v. Dep’t of Revenue*, 166 Wn.2d 444, 452, 210 P.3d 297 (2009)). PharMerica agrees that the person to whom the drug is sold refers to the buyer. PharMerica’s position that the buyer is a person who does not pay the valuable consideration for the sale, or incurs the primary legal obligation to pay, is unreasonable and inconsistent with the definition of a sale in RCW 82.04.040(1), and the common meaning of making a sale to a person.

PharMerica’s interpretation is also unreasonable because it requires the Court to add terms that are not present, like ordering and administration, and ignore terms that are, such as the payment of valuable consideration. *See Lake v. Woodcreek Homeowners Ass’n*, 169 Wn.2d 516, 526, 243 P.3d 1283 (2010) (court should not add words where the legislature has chosen not to include them, and must construe statutes such that all of the language is given effect). Since there is no ambiguity, it is unnecessary to turn to the legislative history or apply the strict construction in favor of the taxpayer.

Even if the Court were to consider the legislative history, nothing suggests the Legislature intended to apply a lower rate to all business activities by any in-state drug wholesalers. The legislative purpose of providing “assistance” to in-state wholesalers does not support the all or nothing approach to applying B&O tax provided by PharMerica.

Finally, this is not an absurd result as PharMerica argues. In the case of RCW 82.04.272, the plain language shows the Legislature intended only to exempt certain types of business activities of in-state wholesalers. PharMerica’s policy argument for a larger exemption should be directed to the legislature, since the statutory requirements are not ambiguous. Moreover, this conclusion is consistent with *Aventis*, which found that RCW 82.04.272 was unambiguous in its requirements, rejected a broader conception of the statute that would have expanded the classification to all prescription drug wholesales as unpersuasive, and found the Department’s ETA explaining the statute to be “persuasive, and consistent with applicable statutes and rules.” *Aventis Pharm., Inc.*, 5 Wn. App. 2d at 645, 647-48, 649.

In summary, the statute’s meaning is plain, so there is no need to turn to statutory aides to interpret the statute. Regardless, they do not support PharMerica’s interpretation that the classification broadly applies to all of its drug sales, regardless of who pays.

V. CONCLUSION

For the foregoing reasons, the trial court correctly granted summary judgment in favor of the Department and correctly denied PharMerica's motion for summary judgment. This Court should affirm.

RESPECTFULLY SUBMITTED this 7th day of February, 2019.

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DATED this 7th day of February, 2019, at Tumwater, WA.



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