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NO. 77690-3

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**SUPREME COURT OF THE STATE OF WASHINGTON**

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UNITED STATES TOBACCO SALES AND MARKETING COMPANY  
INC.,

Petitioner,

v.

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Respondent.

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**ANSWER TO PETITION FOR REVIEW**

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## I. IDENTITY OF RESPONDENT

Respondent is the State of Washington, Department of Revenue (Department).

## II. ISSUES PRESENTED FOR REVIEW

1. The trial court found that the fair market value for Tobacco Manufacturing's sales of smokeless tobacco products in 1992 to Tobacco Sales was \$.82 per can. Neither party presented any evidence or testimony in support of that price. Did the Court of Appeals err in concluding that substantial evidence did not support the trial court's finding?
2. Did Tobacco Sales fail to meet its burden under RCW 82.32.180 to prove that it is entitled to a tax refund and the amount of the refund?

## III. STATEMENT OF THE CASE

Washington State imposes an excise tax on the "sale, use, consumption, handling, or distribution of all tobacco products in this state[.]"<sup>1</sup> "Tobacco products" are all types of chewing and smoking tobacco, snuff, and cigars, but the term does not include cigarettes.<sup>2</sup> The tax is commonly known as the Other Tobacco Products (OTP) tax.

Prior to the 2005 legislative session, the OTP tax was measured by the "wholesale sales price" of tobacco products brought into the state.<sup>3</sup>

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<sup>1</sup> Former RCW 82.26.020(1) (1993). Under the statute's current version, which the Legislature amended in 2005, the tax is imposed on the "sale, handling, or distribution of all tobacco products in this state[.]" RCW 82.26.020(1) (2005).

<sup>2</sup> Former RCW 82.26.010(1) (1993). The statutory definition of "Tobacco products" remains the same today as in 1993. *See* RCW 82.26.020(1) (2005).

<sup>3</sup> Former RCW 82.26.020(1) (1993). In 2005, the Legislature changed the rate and also the measurement of the OTP tax from "wholesale sales price" to "taxable sales price," and added statutory definitions for "actual price" and "affiliated" entities such as

The “wholesale sales price” meant “the established price for which a manufacturer sells a tobacco product to a distributor, exclusive of any discount or other reduction[.]”<sup>4</sup> The OTP tax is imposed at the time the tobacco product is delivered into the state: “Taxes under this section shall be imposed at the time the distributor (a) brings, or causes to be brought, into this state from without the state tobacco products for sale . . .”<sup>5</sup>

Prior to 1990, United States Tobacco Company performed all functions relating to the manufacturing, sale, and marketing of its smokeless tobacco products.<sup>6</sup> In 1990, United States Tobacco Company formed two wholly owned subsidiaries: United States Tobacco Sales and Marketing Company Inc. (Tobacco Sales) and United States Tobacco Manufacturing Company Inc. (Tobacco Manufacturing).<sup>7</sup> Tobacco Manufacturing manufactures smokeless tobacco products, primarily the brand names Copenhagen and Skoal, which are sold only to Tobacco Sales.<sup>8</sup> Tobacco Sales engages in the business of marketing and selling the smokeless tobacco products that it obtains from Tobacco Manufacturing.<sup>9</sup> Tobacco Sales advertises and distributes its smokeless

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U.S. Tobacco. *See* Laws of 2005, ch. 180, § 2 (codified at RCW 82.26.010(12), (13), (18)(a)(i)-(vi), (20) and (21)).

<sup>4</sup> Former RCW 82.26.010(7) (1995).

<sup>5</sup> Former RCW 82.26.020(2) (1993); RCW 82.26.020(2) (2005).

<sup>6</sup> CP at 128, 133.

<sup>7</sup> CP at 127-28, 131-32.

<sup>8</sup> CP at 128, 133; RP Vol. 1 at 100, ll. 13-16; RP Vol. 1 at 209, ll. 9-12.

<sup>9</sup> CP at 129, 133.

tobacco product samples to adult consumers at promotional events such as rodeos, auto races, and fishing tournaments.<sup>10</sup>

Senior management at Tobacco Sales determined the price charged for its smokeless tobacco products to distributors.<sup>11</sup> The price for the smokeless tobacco products sold by Tobacco Manufacturing to Tobacco Sales, commonly referred to as the transfer price, was based upon a formula.<sup>12</sup> Tobacco Manufacturing's 1992 transfer price to Tobacco Sales for smokeless tobacco products was \$.625 per can.<sup>13</sup> Tobacco Sales' 1992 selling price to unaffiliated distributors averaged \$1.43 per can.<sup>14</sup> Tobacco Sales sells its smokeless tobacco products at prices higher than the prices at which it purchases them from Tobacco Manufacturing.<sup>15</sup>

In 1996, the Department audited Tobacco Sales and determined that for the distribution of samples only Tobacco Sales was the taxable "distributor" and that the correct measure of the OTP tax was Tobacco Sales' selling price to distributors and not the transfer price from its affiliate, Tobacco Manufacturing.<sup>16</sup> Therefore, for the samples of smokeless tobacco products Tobacco Sales distributed in Washington in

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<sup>10</sup> CP at 130, 134.

<sup>11</sup> *Id.*

<sup>12</sup> *Id.*

<sup>13</sup> CP at 130, 134.

<sup>14</sup> CP at 130, 134; see also Ex. 4, 5, 6.

<sup>15</sup> *Id.*

<sup>16</sup> *U.S. Tobacco Sales & Mktg. Co. Inc., v. Dep't of Revenue*, 128 Wn. App. 426, 429, 115 P. 3d 1080 (2005)

1992, the Department calculated OTP tax based on Tobacco Sales' selling price to unaffiliated distributors (\$1.43 per can).<sup>17</sup> In 1997, Tobacco Sales filed an action seeking a refund of OTP taxes for the year 1992 for samples it distributed in this state.<sup>18</sup>

Tobacco Sales and the Department filed cross motions for summary judgment before the Thurston County Superior Court. The parent company had engaged an accounting firm, Ernst & Young, in 1995 to prepare a transfer price study under Section 482 of the Internal Revenue Code to determine transfer prices for a wide range of inter-company transactions. The study concluded that Tobacco Manufacturing's 1992 transfer price to Tobacco Sales for smokeless tobacco products was \$.625 per can.<sup>19</sup> Tobacco Sales offered the transfer price study to the trial court.<sup>20</sup>

The trial court concluded that the \$.625 per can transfer price from Tobacco Manufacturing to Tobacco Sales was a discounted price under the OTP statute and entered an order denying Tobacco Sales' summary judgment motion and granting summary judgment to the Department. Tobacco Sales appealed.

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<sup>17</sup> CP at 134.

<sup>18</sup> CP at 120.

<sup>19</sup> CP at 130, 134.

<sup>20</sup> *U.S. Tobacco Sales & Mktg. Co. Inc., v. Dep't of Revenue*, 96 Wn. App. 932, 942, 982 P.2d 652 (1999); *see also* RP Vol. 1 at 46, ll. 15-23.

In *U.S. Tobacco Sales & Mktg. Co. Inc., v. Dep't of Revenue*, 96 Wn. App. 932, 982 P.2d 652 (1999) (*Tobacco Sales I*), the Court of Appeals reversed the grant of summary judgment to the Department and affirmed the denial of summary judgment to Tobacco Sales. The Court evaluated the OTP tax statutory definitions and determined that they were unambiguous.<sup>21</sup> In evaluating the term “wholesale sales price,” which was defined as an “established price exclusive of any discount or other reduction,”<sup>22</sup> the Court concluded that an “‘established price’ from a manufacturer must be a generally available, stable, fixed price, such as a list price or invoice price.”<sup>23</sup> The Court further concluded that a manufacturer’s “‘established price’ would be available to all customers and would represent the fair market value of the products.”<sup>24</sup>

The Court then defined “fair market value” to mean “the amount a willing buyer would pay a seller who is willing but not obligated to sell.”<sup>25</sup> Since the case involved affiliated companies, the Court held: “In the case of affiliated companies, which, in effect, are obligated to buy and sell from

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<sup>21</sup> *Tobacco Sales I*, 96 Wn. App. at 938.

<sup>22</sup> Former RCW 82.26.010(7) (1995) (“‘Wholesale sales price’ means the established price for which a manufacturer sells a tobacco product to a distributor, exclusive of any discount or other reduction.”).

<sup>23</sup> *Tobacco Sales I*, 96 Wn. App. at 938.

<sup>24</sup> *Id.* at 940.

<sup>25</sup> *Id.* (citations omitted).

each other, the ‘established price’ must be based upon fair market value rather than the manufacturer’s price to its affiliate.”<sup>26</sup>

The Court directed the trial court to make a factual determination as to whether Tobacco Manufacturing’s price to Tobacco Sales was a fair market price or whether it was a discounted price,<sup>27</sup> remanding the matter to the trial court for further proceedings consistent with its opinion.<sup>28</sup>

On remand, the trial court held a three-day bench trial.<sup>29</sup> Tobacco Sales engaged the same accounting firm to conduct another transfer price study, because the original transfer price study related to 1995 and not 1992.<sup>30</sup> In 2000, for purposes of the litigation, the accounting firm completed the second study for sales between Tobacco Manufacturing and Tobacco Sales in 1992.<sup>31</sup> Additionally, Tobacco Sales engaged the services of an appraiser, Mr. Robert Reilly of Willamette Management Associates, to provide a fair market value opinion.<sup>32</sup>

The second study indicated that the transfer price for 1992 was in the range between \$.68 and \$.72 per can, and the appraiser testified that he

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<sup>26</sup> *Id.*

<sup>27</sup> *Id.* at 941-42.

<sup>28</sup> *Id.* at 944.

<sup>29</sup> RP Vol. 1 at 1. Prior to the bench trial, both parties again moved for summary judgment, but the trial court denied the motions and set the matter for hearing. CP at \_\_\_.

<sup>30</sup> RP Vol. 1 at 25, ll. 2-7; RP Vol. 1 at 87, ll. 6-9.

<sup>31</sup> Trial Exhibit 1 (attached as Exhibit II, Ernst & Young, and LLP Transfer Pricing Report July 2000).

<sup>32</sup> RP Vol. 1 at 25, ll. 8-11.

agreed with the study.<sup>33</sup> Furthermore, both the accounting firm and the appraiser concluded that based upon the company's formula the actual inter-company transfer price between the two affiliated companies for the tax year 1992 was \$.73 per can.<sup>34</sup>

The trial court found that the 1992 transfer price of \$.68 to \$.72 from Tobacco Manufacturing to Tobacco Sales based upon the 2000 transfer price study and the transfer price of \$.625 from the original transfer price study were discounted prices compared to the fair market value price.<sup>35</sup> The trial court further concluded that both prices failed to represent the fair market value of the smokeless tobacco products sold by Tobacco Manufacturing to Tobacco Sales.<sup>36</sup> The trial court concluded as a matter of law that the transfer prices did not reflect fair market value because Tobacco Manufacturing would not willingly sell to an unaffiliated buyer at that price.<sup>37</sup>

The trial court, nevertheless, derived a 1992 "fair market value" for Tobacco Manufacturing's sales of smokeless tobacco products to Tobacco Sales of \$.82 per can.<sup>38</sup> Neither party presented any evidence or testimony supporting that price. Instead, the trial court calculated the price simply

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<sup>33</sup> RP Vol. 1 at 55, ll. 1-3; Ex. 1, pg. 23.

<sup>34</sup> RP Vol. 1 at 147, ll. 5-7; *See also* Trial Exhibit 1, pg. 23.

<sup>35</sup> *Id.*

<sup>36</sup> *Id.*

<sup>37</sup> CP at 135; RP Vol. 1 at 452-53, ll. 20-25, 1-5.

<sup>38</sup> CP at 134.

by “taking the middle price of \$.70 per can” and re-allocating the residual profit split from the transfer price study offered by Tobacco Sales and adding this additional amount to arrive at the fair market value of \$.82 per can, without regard to whether Tobacco Manufacturing would sell its product to an unaffiliated company at that price.<sup>39</sup> The trial court then ordered a refund based upon its calculation of OTP tax being due on \$.82 per can.<sup>40</sup>

The Department appealed and Tobacco Sales cross appealed. The Court of Appeals issued a published decision again reversing the trial court and remanding the matter. *U.S. Tobacco Sales & Mktg. Co. Inc., v. Dep’t of Revenue*, 128 Wn. App. 426, 115 P. 3d 1080 (2005) (Tobacco Sales II) (*Tobacco Sales II*). In *Tobacco Sales II*, the Court concluded that substantial evidence did not support the “trial court’s finding of \$.82 as the fair market value[.]”<sup>41</sup> The Court also rejected the Department’s argument that the correct measure of the OTP tax was Tobacco Sales’ selling price of \$1.43 per can.<sup>42</sup> The Court likewise rejected Tobacco Sales’ evidence, stating: “But as discussed in *U.S. Tobacco I*, the internal transfer price between the two subsidiaries does not establish fair market value, i.e., what a willing buyer would pay a willing seller in an arm’s length

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<sup>39</sup> RP Vol. 3 at 456, ll. 12-17; 457, ll. 4-7.

<sup>40</sup> CP at 135.

<sup>41</sup> *Tobacco Sales II*, 128 Wn. App. at 436.

<sup>42</sup> *Id.* at 431.

transaction in a free market.”<sup>43</sup> The Court found that language in the studies offered at trial and the testimony offered by Tobacco Sales continued to reflect a price that was not a fair market value price between two unaffiliated companies.<sup>44</sup> Therefore, the Court remanded the case and directed the parties to present evidence “of the price a *completely unaffiliated entity* would have had to pay to purchase OTP from Tobacco Manufacturing in 1992.”<sup>45</sup>

#### **IV. REASONS WHY REVIEW SHOULD BE DENIED**

Under RAP 13.4(b), this Court will accept a petition for discretionary review of a Court of Appeals decision only if (1) the Court of Appeals decision conflicts with a decision of this Court, (2) the Court of Appeals decision conflicts with a decision of another division of the Court of Appeals, (3) the petition presents a significant federal or state constitutional question, or (4) the petition presents an issue of substantial public interest that should be determined by this Court. Tobacco Sales never mentions RAP 13.4(b) in its discretionary review petition. Nor does the petition contain any direct argument addressing why review should be

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<sup>43</sup> *Id.* at 435-36.

<sup>44</sup> *Id.* at 437.

<sup>45</sup> *Id.* at 438 (emphasis in original).

accepted under the criteria in RAP 13.4(b). That alone should be reason enough to deny review.<sup>46</sup>

Nevertheless, certain arguments in the petition might be read to imply that review should be accepted under RAP 13.4(b)(1)-(4). Those factors will be addressed in the context of Tobacco Sales' arguments in its petition.

**A. RAP 13.4(b)(1): The Court of Appeals Decision Is Not In Conflict With Any Decision Of This Court.**

Tobacco Sales fails to demonstrate how the decision of the Court of Appeals conflicts with any decisions of this Court. It argues that the Court of Appeals' decision in *Tobacco Sales II* to remand the case to determine the price a "completely unaffiliated entity would have had to pay to purchase OTP from Tobacco Manufacturing in 1992" conflicts with *McUne v. Fuqua*, 42 Wn.2d 65, 74, 253 P.2d 632 (1953), because "a remand for taking new evidence is improper when the proposed evidence would be inadmissible."<sup>47</sup> This creative argument fails to present a true conflict.

The fair market value standard requires a willing buyer and willing seller. Tobacco Sales contends the evidence required on remand will be

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<sup>46</sup> See RAP 13.4(c)(7) (requiring that petitions set forth "[a] direct and concise statement of the reason why review should be accepted under one or more of the tests established in section (b), with argument.").

<sup>47</sup> Pet. for Review at 12.

speculative because Tobacco Manufacturing is not a willing seller:  
“Tobacco Manufacturing did not sell OTP to unaffiliated entities in 1992 because it maintained an exclusive marketing arrangement with Tobacco Sales. . . . Tobacco Manufacturing was not willing to sell to distributors other than Tobacco Sales because it maximized the value of its brands by maintaining an exclusive marketing arrangement.”<sup>48</sup> But as the Court of Appeals noted: “Tobacco Sales’s [sic] experts testified that there are several ways to measure the fair market value of goods which have only been sold between affiliated entities.”<sup>49</sup> The Court of Appeals’ remand, directing the parties to produce evidence “of the price a *completely unaffiliated entity* would have had to pay to purchase OTP from Tobacco Manufacturing in 1992[,]”<sup>50</sup> simply requires the parties to produce evidence of the type that always is required to determine fair market value in the absence of an actual sale.

Contrary to Tobacco Sales’ argument, the Court of Appeals is not remanding the case to take additional evidence “because it would prefer the parties had presented more or different evidence.”<sup>51</sup> Rather, as the Court of Appeals specifically indicated: “The record does not contain substantial evidence supporting the trial court’s finding that the fair market

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<sup>48</sup> *Id.* at 10 and 11 (emphasis in original).

<sup>49</sup> *Tobacco Sales II*, at 432.

<sup>50</sup> *Id.* at 438.

<sup>51</sup> Pet. for Review at 18.

value of OTP sold in 1992 by Tobacco Manufacturing was \$.82 per can.”<sup>52</sup>

In sum, remanding the matter to the trial court to determine the correct price to measure the OTP tax does not conflict with this Court’s prior precedent. Tobacco Sales, therefore, fails to show any conflict that would warrant review under RAP 13.4(b)(1).

**B. RAP 13.4(b)(2): The Court Of Appeals Decision Is Not In Conflict With Another Decision Of The Court Of Appeals.**

Nor is review warranted under RAP 13.4(b)(2). No plausible argument is contained in Tobacco Sales’ petition remotely asserting that the Court of Appeals’ decision conflicts with another decision of the Court of Appeals.

**C. RAP 13.4(b)(3): The Petition Does Not Present A Significant Federal or State Constitutional Issue.**

Tobacco Sales’ petition also does not present a significant federal or state constitutional issue. At most, the petition demonstrates that the trial court and the Court of Appeals disagree as to whether substantial evidence supports the trial court’s finding of \$.82 per can. Further, this Court has already upheld the constitutionality of the OTP tax in *Galvin v. State Tax Comm’n*, 56 Wn. 2d 738, 355 P. 2d 362 (1961). Hence, that issue is not presented by Tobacco Sales’ petition.

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<sup>52</sup> *Tobacco Sales II*, at 437.

**D. RAP 13.4(b)(4): The Petition Does Not Present An Issue Of Substantial Public Importance That Should Be Decided By This Court.**

Tobacco Sales also fails to establish that the issue it raises involving the former measure of the OTP tax is of such substantial public importance that this Court must decide it. The opposite, in fact, is true. First, the Legislature amended the OTP statute in 2005 such that the issue presented by Tobacco Sales is moot in the future. The Legislature amended the statute to remove as the measure of the tax the “wholesale sales price” and substituted in its stead “taxable sales price.”<sup>53</sup>

Additionally, the 2005 act reflects that the Legislature specifically intends to treat the sales of OTP between affiliated companies differently than sales of OTP between unaffiliated companies:

It is the further intent and purpose of this chapter that the distributor who first possesses the tobacco product in this state shall be the distributor liable for the tax and that in most instances the tax will be based on the actual price that the distributor paid for the tobacco product, *unless the distributor is affiliated with the seller.*

Laws of 2005, ch. 180, § 1 (codified as RCW 82.26.030) (emphases added).

Consistent with the Department’s interpretation in measuring the OTP tax between two affiliated companies, the Legislature clarified that

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<sup>53</sup> Laws of 2005, ch. 180 § 3. *See also* Laws of 2005, ch. 180, § 2 (defining “taxable sales price”) (codified as RCW 82.26.010(18)(a)(i)-(vi)).

the measure of the tax would be the actual price charged to unaffiliated entities, including a default provision that measures the tax on the actual price charged regardless of an entities' affiliated or unaffiliated status:

- (ii) In the case of a taxpayer that purchases tobacco products from an *affiliated manufacturer*, affiliated distributor, or other affiliated person, and that sells those tobacco products to unaffiliated distributors, unaffiliated retailers, or ultimate consumers, *the actual price for which that taxpayer sells those tobacco products to unaffiliated distributors, unaffiliated retailers, or ultimate consumers;*
- (iii) In the case of a taxpayer that sells tobacco products only to affiliated distributors or affiliated retailers, the price, determined as nearly as possible according to the actual price, that other distributors sell similar tobacco products of like quality and character to unaffiliated distributors, unaffiliated retailers, or ultimate consumers;
- ...
- (vi) In any case where (a)(i) through (v) of this subsection do not apply, the price determined as nearly as possible according to the actual price, that the taxpayer or other distributors sell the same tobacco products or similar tobacco products of like quality and character to unaffiliated distributors, unaffiliated retailers, or ultimate consumers.

Laws of 2005, ch. 180, § 2 (codified as RCW 82.26.010(18)(a)(ii), (iii) and (vi)) (emphases added).

The statutory amendments made in 2005 should resolve any potential legal issues in the future with respect to the issues raised in

Tobacco Sales' petition. The petition thus fails to raise an issue of substantial public importance that justifies review by this Court.

Second, review under RAP 13.4(b) would be inappropriate for another reason. The core issue presented by this case is whether substantial evidence supports the trial court's finding of \$.82 per can. The Court of Appeals determined that the trial court's finding was not supported by substantial evidence. Given Tobacco Sales' cross appeal, it clearly agrees that substantial evidence does not support the trial court's finding. That substantial evidence fails to support the trial court's finding of \$.82 per can certainly is not of such importance that review by this Court is warranted.

In addition, Tobacco Sales bore the burden of proving it was entitled to a refund.<sup>54</sup> But Tobacco Sales did not assign error to the trial court's finding that Tobacco Manufacturing's 1992 selling price was not a fair market value price:

Neither Tobacco Sales' nor Tobacco Manufacturer's 1992 selling price represents the fair market value of the smokeless tobacco products sold by Tobacco Manufacturing to Tobacco Sales. Tobacco Manufacturing's selling price was a discounted price as compared to the fair market value price (\$.82) for those sales.

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<sup>54</sup> RCW 82.32.180(1) ("At trial, 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 the tax.").

CP at 135. Unchallenged findings are verities on appeal.<sup>55</sup> Tobacco Sales' continuing effort to urge that Tobacco Manufacturing's 1992 selling price represents a fair market value price cannot be squared with the trial court's uncontested finding.

Furthermore, the Court of Appeals perhaps rejected Tobacco Sales evidence because Tobacco Sales offered three different prices to measure the OTP tax. Tobacco Sales offered evidence and continues to assert in its petition before this Court that Tobacco Manufacturing's actual selling price was \$.625 per can.<sup>56</sup> In addition, the 2000 study prepared for litigation concluded that the transfer price for 1992 was \$.68 to \$.72 per can and that should be the measure of the tax.<sup>57</sup> Finally, Tobacco Sales' experts testified that if the transfer price formula for 1992 from the 2000 transfer price study was applied, the actual price would be \$.73 per can.<sup>58</sup> It is no wonder the Court of Appeals remanded the matter to the trial court for further proceedings:

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<sup>55</sup> *In re Contested Election of Schoessler*, 140 Wn.2d 368, 998 P.2d 818 (2000); *New W. Fisheries, Inc. v. Dep't of Revenue*, 106 Wn. App. 370, 375, 22 P.3d 1274 (2001).

<sup>56</sup> Pet. for Review at 8; CP at 130, 134. However, this price cannot be the "actual sales price" because the "wholesale sales price" means the "established price for which a manufacturer sells a tobacco product to a distributor, exclusive of any discount or other reduction." The \$.625 is a discounted price, because Tobacco Manufacturing does not sell its products at this price to any entity except its affiliate, and Tobacco Sales stipulated that it always sells its products at prices higher than the prices which it purchases from Tobacco Manufacturing. CP at 130, 134.

<sup>57</sup> RP Vol. 1 at 55, ll. 1-3; Ex. 1, pg. 23.

<sup>58</sup> RP Vol. 1 at 147, ll. 5-7; *see also* Trial Exhibit 1 at 23.

But certain language from those studies and the testimony from which they were presented suggest that the qualifier “level of trade” included the affiliation between Tobacco Manufacturing and Tobacco Sales. . . . Moreover, although the Ernst & Young study in this appeal came to the conclusion that the 1992 fair market value was between \$.68 and \$ .72 per can, the Ernst & Young study in the first appeal concluded that the \$.625 price was an appropriate arm’s length price for that same year. *U.S. Tobacco I*, 96 Wn. App. at 942. Neither party has clarified this disparity.

*Tobacco Sales II*, 128 Wn. App. at 437 (footnotes omitted).

Under the Court of Appeals decision in *Tobacco Sales I*, which *Tobacco Sales* did not ask this Court to review, *Tobacco Sales* had to prove that the transfer price with its affiliate was a fair market value price -- that is, “what a willing buyer and a willing seller would pay a seller who is willing but not obligated to sell.”<sup>59</sup> But *Tobacco Sales* chose to ignore the Court’s ruling and continues to argue for a different standard:

[T]he appropriate valuation standard is the market price at which a manufacturer would sell OTP to an unaffiliated distributor under the circumstances in which the parties otherwise held the same property interests and performed the same functions as are actually performed by the UST manufacturing and marketing subsidiaries.

Pet. for Review at 4.<sup>60</sup> By choosing to travel down this different path, *Tobacco Sales* failed to prove the fair market value price for a sale between unaffiliated entities as required by the Court in *Tobacco Sales I* (and again in *Tobacco Sales II*). The Court of Appeals’ remand to the trial court simply provides *Tobacco Sales* with yet another opportunity to prove

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<sup>59</sup> *Tobacco Sales I*, 96 Wn. App. at 940.

<sup>60</sup> See also Ex. 1 at 3; RP Vol. 2 at 298.

its case. The remand does not constitute an issue of substantial public import that this Court should decide.

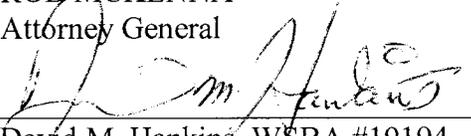
## V. CONCLUSION

Tobacco Sales' petition fails to establish any of the criteria for discretionary review required by RAP 13(b)(1)-(4). Rather, the petition merely demonstrates that both parties have thus far had difficulty proving the fair market value of Tobacco Sales' smokeless product for the purpose of measuring its OTP tax obligation in 1992. As a result of *U.S. Tobacco II*, Tobacco Sales will have yet another opportunity to establish fair market value, with the right to appeal if is not successful before the trial court. That hardly is unfair to Tobacco Sales.

Moreover, the 2005 legislation has eliminated the issue raised by Tobacco Sales as to future periods. Tobacco Sales cannot establish that the issue it raises is one of substantial public interest that should be decided by this Court. The Department requests that this Court deny Tobacco Sales' petition for discretionary review.

RESPECTFULLY SUBMITTED this 7<sup>th</sup> day of November, 2005.

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Assistant Attorney General  
Attorneys for Respondent



Candy Zilinskas

Candy Zilinskas, Legal Assistant  
to David M. Hankins  
(360) 753-5528

SIGNED and SWORN to before me, this 7th day of November,

2005.



Carrie A. Parker

Signature of Notary Public

Carrie A. Parker

Printed Name

NOTARY Public in and for the  
State of Washington, residing at

Olympia

Commission expires 2-9-08