

No. 48807-8-II

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

Washington Restaurant Association, a Washington non-profit organization;
Northwest Grocery Association, a non-profit organization;
and Costco Wholesale Corporation, a Washington corporation,

Appellants/Cross-Respondents,

v.

Washington State Liquor and Cannabis Board, a state agency;
Chris Marr, Sharon Foster, and Ruthann Kurose, in their official
capacities as members of the Washington State Liquor and Cannabis
Board,

Respondents,

and

Association of Washington Spirits & Wine Distributors,

Intervenor-Respondent/Cross-Appellant.

REPLY BRIEF OF APPELLANTS/CROSS-RESPONDENTS

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I. INTRODUCTION

This case presents fundamental questions about how an agency may exercise its authority. Administrative agencies, "being 'creatures of statute,' possess only such powers and authority as are expressly granted by statute or necessarily implied therein." *Taylor v. Morris*, 88 Wn.2d 586, 588 (1977). Courts serve a "vital function" when reviewing agency action, ensuring agencies remain "within the bounds" of their delegated authority and remain "democratically accountable." *City of Burlington v. Liquor Control Bd.*, 187 Wn. App. 853, 875, *review denied*, 184 Wn.2d 1014 (2015).¹

Counsel for the Board argues that the 10 Percent Rule should be upheld without regard to the reason the agency adopted the rule, and despite the fact the agency imposed the fee without exercising its expertise, relying instead on a misconception of what Initiative 1183 required. Affirmance on a different basis would require the Court to substitute its judgment as to the need, benefit, and appropriateness of the fee even though the agency itself never made such a determination. The Administrative Procedure Act specifically prohibits such discretion.

Similarly, the Board defends the Sell-and-Deliver Rule by invoking reasons that do not appear anywhere in the agency record or the

¹ Quoting William R. Andersen, *The 1988 Washington Administrative Procedure Act—An Introduction*, 64 Wash. L. Rev. 781, 820 (1989).

concise explanatory statement. It is not enough for an agency to point to general authority to regulate activities in a broad area; the decision whether and how to regulate must still satisfy the APA's standards to ensure the agency is acting appropriately. Such concerns are not academic. Here, what little insight the agency has given into the origin of the Sell-and-Deliver Rule reveals only that one set of stakeholders lobbied to restrict its competitors, which can hardly be a sufficient rationale.

This appeal also challenges the scope of the Board's authority in the wake of Initiative 1183. As is clear from its rulemaking and briefing, the Board continues to insist it has broad powers to supplement Title 66 and impose rules to create what it deems an "orderly" economic market—despite the Initiative's pointed elimination of such powers and purposes. The appropriate deference is to the People and the legislative delegation of power to the agency. Deference requires the Board to be limited to rules that promote approved regulatory functions, such as public safety. None of the rules at issue here promote those goals, and each exceeds the Board's authority.

II. ARGUMENT

At issue are three rules the Washington Liquor and Cannabis Board enacted in 2012. Petitioners challenge the 10 Percent Rule and the Sell-and-Deliver Rule as being beyond the Board's statutory authority and

arbitrary and capricious, with each ground constituting a separate basis for invalidation under RCW 34.05.570(2)(c). The intervenor (the Association of Washington Spirits and Wine Distributors) appeals the Superior Court's invalidation of WAC 314-02-103(2) and WAC 314-02-106(1)(c) (together, the "Per Day Rule"), even though the Board, after living without the Per Day Rule for years, decided to abandon the effort to keep it. This brief includes Appellants' opposition to that appeal.

A. The 10 Percent Rule Is Invalid Because It Exceeds the Board's Authority

A rule is invalid if it exceeds an agency's statutory authority. RCW 34.05.570(2)(c). Here, the Board enacted the 10 Percent Rule to impose a revenue-based license fee (the "Self-Distribution Fee") on entities, such as spirits certificate of approval holders, exercising limited self-distribution rights.² At the time of adoption, the Board's rationale for the rule followed this reasoning: (1) spirits distributors were required to pay a 10 percent fee on spirits sales (under RCW 66.24.055(3)(a))³; (2) the Initiative required "all applicable laws" governing spirits distributors to govern distillers when acting in an ancillary function as distributors of their own product (under RCW 66.24.640); and therefore (3) the Board

² As in the Opening Brief, Appellants will use the term "distiller" to refer to the various licensees that exercise this limited self-distribution right for spirits.

³ This fee drops to five percent of a spirits distributors' revenue after the first 27 months of licensure. RCW 66.24.055(3)(a)(ii). The Self-Distribution Fee includes the same cliff. WAC 314-23-030(3)(c).

was obligated to impose the same fee on distillers when they engaged in self-distribution. Appendix D (concise explanatory statement at LCB00001035); *see also* CP 971 (Board's briefing before the trial court at 21); RP at 63-67 (hearing before trial court).

The Supreme Court rejected that reasoning in *Association of Washington Spirits & Wine Distributors v. Liquor Control Board*, when interpreting the nearly identical RCW 66.24.055(3)(c). The Court found a specific fee provision trumped the general provision found in RCW 66.24.640.⁴ 182 Wn.2d 342, 356-57 (2015); *see* Appellants' Opening Br. 21-22.

After the Board enacted the rule, and after the Superior Court issued its decision below, counsel for the Board disclaimed the Board's reasoning and now acknowledges the Initiative does not require the Self-Distribution Fee. Board's Br. at 22 ("I-1183 did not specifically impose fees on licensed distillers who choose to distribute their product directly to licensed liquor retailers, or on persons obtaining a certificate of approval to import spirits into Washington to distribute them to license liquor retailers"); *see Ass'n of Wash. Spirits & Wine Distribs.*, 182 Wn.2d at 353

⁴ The Board urges this Court to largely disregard the opinion in *Association of Washington Spirits & Wine Distributors*. Board's Br. at 32-34. While the Supreme Court did decline to explicitly rule on the validity of the WAC 314-23-030, which was not before it, the Supreme Court's analysis of RCW 66.24.055 and of the Board's reasoning controls the analysis here. *See* Appellants' Opening Br. at 21-24.

(recognizing Board abandoned prior reasoning supporting the Self-Distribution Fee).

The Board's lawyers now rely exclusively on alleged general authority to impose license fees. Board's Br. at 18-23; *Ass'n of Wash. Spirits & Wine Distribs.*, 182 Wn.2d at 354 n.4 ("The Board now argues, contrary to its assertions [to the Superior Court in this case], that its broad regulatory authority to impose licensing fees justifies imposing a 10 percent fee on certificate of approval holders.").

The Court should reject this new argument.

1. With the agency's basis for the Self-Distribution Fee held invalid, the rule is invalid.

The Court must evaluate agency action based on the agency's reasoning and record at the time of the action. RCW 34.05.570(1)(b); *see Musselman v. Dep't of Soc. & Health Servs.*, 132 Wn. App. 841, 853 (2006) (refusing to consider challenge to the validity of rule when the agency's record was not before the court because the court needs the "information the agency considered contemporaneously with the adoption of the rule"). Any other approach allows a court to replace its own discretion for that of an agency—an approach specifically prohibited by the APA: "[T]he court shall limit its function to assuring that the agency has exercised its discretion in accordance with law, and shall not itself

undertake to exercise the discretion that the legislature has placed in the agency." RCW 34.05.574(1); *see* Appellants' Opening Br. at 24-27.

This principle (the "*Chenery* principle") is "fundamental" and a "bedrock" under federal administrative law, rooted in part in the constitutional limitations on legislative delegations of power to agencies. Kevin M. Stack, *The Constitutional Foundations of Chenery*, 116 Yale L.J. 952, 955 (2007). "At its core, the *Chenery* principle directs judicial scrutiny toward what the agency has said on behalf of its action, not simply toward the permissibility or rationality of its ultimate decision." *Id.* at 956. In short, a court "may not supply a reasoned basis for the agency's action that the agency itself has not given." *Motor Vehicle Mfrs. Ass'n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (citation omitted) (applying the *Chenery* principle to agency rulemaking). The *Chenery* principle "promotes agency accountability," ensuring that "the grounds for agency policy have been embraced by the most politically responsive and public actors within the agency." Stack, *The Constitutional Foundations of Chenery*, 116 Yale L.J. at 993.

The Board does not address why the *Chenery* principle would not apply here. (Nor does the Association.) The Board points only to the ability of an appellate court to uphold a trial court on a ground not adopted below if the record has been sufficiently developed to fairly consider the

ground.⁵ Board's Br. at 27 (citing RAP 2.5). That principle does not apply under the Administrative Procedures Act. The appellate court applies the standards of the APA directly to the agency record before it, without evaluating the trial court's decision. *State Hosp. Ass'n v. Dep't of Health*, 183 Wn.2d 590, 595 (2015). Having now agreed that it was not compelled by law to impose the Self-Distribution Fee, the Board must actually fulfill the APA's standards in pursuing an alternative approach and then have the Court review that actual, not hypothetical, process and record.⁶

The Board also relies on *Department of Social Health & Services v. Nix*, 162 Wn. App. 902 (2011). Board's Br. at 29. Nix argued that the agency position departed from the agency's prior interpretation of its rule, making the action arbitrary and capricious, but the reasoning for the agency action being challenged itself never wavered. *Nix*, 162 Wn. App. at 913-14. An agency may take action that contradicts a prior

⁵ The Board cites *Nast v. Michels*, 107 Wn.2d 300, 308 (1986), for the same principle. Board's Br. at 27. *Nast* was not decided under the APA and did not involve a challenge to agency action.

⁶ The approach suggested by the Board might be valid if the current situation were reversed—that is, if I-1183 in fact required the Self-Distribution Fee as a matter of law, but the Board had adopted it discretionarily. Thus, in *Haining v. Department of Social and Health Services*, 19 Wn. App. 929 (1978), both sides conceded at argument that an agency rule required the challenged action, which had been adopted under a different rationale. Finding remand to be a "useless formality," the court sustained the agency order on the basis of the agency rule rather than the agency's reason. *Id.* at 931.

interpretation of a rule (subject to review by a court for such a change being arbitrary and capricious); the *Nix* court merely held the change in position was not, in that instance, arbitrary and capricious. *Nix* does not stand for the proposition that Washington has rejected the sound principles articulated by the *Chenery* court and its progeny, which require a court to judge agency action solely on the basis the agency itself relied on, rather than post-hoc rationalizations.⁷

A nearly identical fact pattern gave rise to the *Chenery* principle. In the first *Chenery* decision, the Securities and Exchange Commission promulgated a prohibition on certain stock trades, relying on principles of fiduciary duty law. *SEC v. Chenery Corp.*, 318 U.S. 80, 93 (1943). The Supreme Court concluded the SEC's erred in its interpretation of fiduciary duty law. *Id.* at 92. The Court refused to entertain alternative justifications for the rule, such as the agency's independent authority to promulgate the rule, because "an administrative order cannot be upheld unless the grounds upon which the agency acted in exercising its powers were those upon which its action can be sustained." *Id.* at 95. With the

⁷ RCW 34.05.001 directs Washington courts to interpret Washington's APA consistently with decisions applying the federal act. The Washington Supreme Court favorably cited *Chenery* and embraced its principles in *Lightfoot v. MacDonald*, 86 Wn.2d 331, 336-37 (1976), although no Washington court has applied the *Chenery* doctrine in an APA case.

agency action "based upon a determination of law," the action "may not stand if the agency has misconceived the law." *Id.* at 94.

The same reasoning applies here. The parties agree the original justification for the 10 Percent Rule was based on the Board's interpretation of the Initiative—and that reasoning was incorrect. With the rule based on a misconception of the law, the rule is invalid.

2. The Board does not have the general or specific authority to impose this kind of license fee.

Even if the Court considers the Board's new justification for the Self-Distribution Fee, the conclusion remains the same. The Board does not have the authority to impose this kind of a fee—one whose purpose is to "maximize the State's revenue," rather than merely defraying the costs of the agency's regulatory functions. An agency has only those powers granted or necessarily implied by statute, and "this is especially true where the public treasury will be directly affected." *Properties Four, Inc. v. State*, 125 Wn. App. 108, 117 (2005) (voiding a contract entered into by agency to purchase land).

The Board does not really dispute that the Self-Distribution Fee addresses neither public safety nor costs incurred by the agency for regulating the practice of self-distribution. *See* Appellants' Opening Br. at 35-36. As the Board told the Washington Supreme Court, the agency

sought to "maximize the State's revenue" by imposing these fees. *Ass'n of Spirits & Wine Distribs.*, 182 Wn.2d at 354. Such authority does not fit into the discrete regulatory tasks the Legislature and the People have delegated to the Board, and the Board has no general authority to "maximize" revenue by imposing what amounts to a tax on business. *See Dep't of Revenue v. Bi-Mor, Inc.*, 171 Wn. App. 197, 206 (2012) (invalidating an agency rule that imposed "more tax liability than the legislature authorized" under the plain language of the statute).

First, the Board's lawyers rely on the agency's historically broad powers to "fill in the interstices of statutes," arguing such authority allows the Board to supplement the Initiative with an additional fee on distillers without limiting it to the additional cost of regulating self-distribution. Board's Br. at 19; *accord* Ass'n Br. at 24. Such a broad claim assumes too much; the People limited the agency's powers, and the Board has never enjoyed the power to essentially tax business to "maximize the State's revenue." *See Ass'n of Spirits & Wine Distribs.*, 182 Wn.2d at 354 (acknowledging true purpose for the rule).

Appellants' Opening Brief addressed the narrowed scope of the Board's historical authority after I-1183's revisions to RCW 66.08.030, which the Board largely ignores in its response. Appellants' Opening Br. at 32-36. The Board also appears oblivious to People's purpose in

enacting the Initiative. That purpose supports the conclusion the Board's powers were intentionally diminished with the Initiative. When construing a statute, the declaration of purpose serves as "an important guide" to understanding the breadth of authority the Legislature has delegated to the agency. *Hartman v. Game Comm'n*, 85 Wn.2d 176, 179 (1975).

The general purpose of Title 66 is "for the protection of the welfare, health, peace, morals, and safety of the people of the state." RCW 66.08.010. The ability to "maximize the State's revenue" is not part of that general purpose. Indeed, the People made clear the Board's historical powers had led to "outdated, inefficient, and costly" regulations inhibiting competition and benefit to consumers. I-1183, §101(1). The goal was to reorient the Board away from controlling the economics of the market and to focus on "the more appropriate" purpose of promoting public safety. *Id.*, § 101(2)(b). The Initiative even eliminated the promotion of "orderly marketing" as a policy goal for the state in regulating liquor. *Id.* §124.

Courts defer to the more recent enactment or expression of purpose. *Tunstall ex rel. Tunstall v. Bergeson*, 141 Wn.2d 201, 211 (2000). The most recent enactment here, I-1183, eliminated the Board's authority to "supply any deficiency" in Title 66, and the People announced

its purpose was to limit the Board's power to participate in Washington's liquor marketplace. That should control over a historical expression of "broad" authority.

Second, the Board's lawyers seize on a subsection of a different statute, RCW 66.08.050(8), to assert the Board retains "expansive powers," Board's Br. at 36, but they read this provision out of context. Principles of statutory construction require the grant of authority in RCW 66.08.050(8) to be read as encompassing authority to act in areas similar to the enumerated powers—and setting license fees solely to maximize revenue for the State is not one of those powers.⁸

Under the rule of *ejusdem generis*, "specific terms modify or restrict the application of general terms where both are used in sequence." *City of Seattle v. Dep't of Labor & Indus.*, 136 Wn.2d 693, 699 (1998). The duties listed in RCW 66.08.050 relate to administrative tasks necessary to execute the Board's function. The necessary contracts must be executed, RCW 66.08.050(2), necessary fees paid, *id.* at (3), and necessary bonds issued, *id.* at (4). The Board may regulate the packaging used for liquor, RCW 66.08.050(1), act to prevent the illegal trafficking of liquor, *id.* at (7), and allocate grants to promote alcohol and marijuana

⁸ The Board points to "21 broad topics" for which the Board is authorized to adopt rules under RCW 66.08.030. Board's Br. at 20-21. The Board does not allege, however, that the power to impose the Self-Distribution Fee fits into any of the enumerated topics.

awareness, *id.* at (6). The Board may also perform services for the state lottery commission. RCW 66.08.050(5). These specific acts necessarily limit the more general term that follows in the last enumerated power for the Board, which reads in relevant part:

Perform all other matters and things, whether similar to the foregoing or not, to carry out the provisions of this title, and *has full power to do each and every act necessary to the conduct of its regulatory functions*, including all supplies procurement, preparation and approval of forms, and every other undertaking necessary to perform its regulatory functions whatsoever, subject only to audit by the state auditor.

RCW 66.08.050(8) (emphasis added). First, the agency's authority extends to carrying out only "the provisions of this title," not to create new provisions. Second, the extent of the authority granted here is the "power to do each and every act necessary to the conduct of its regulatory function," not, as the Board alleges, "perform all acts" it deems beneficial. The list of enumerated powers preceding this subsection do not support the Board's broad reading to encompass setting revenue-raising fees.

Finally, the list of enumerated powers following this alleged grant of "full power" also informs the scope of that grant: "supplies procurement," preparing forms, and other undertakings "necessary to perform its regulatory functions." RCW 66.08.050(8). Only a limited

interpretation is consistent with the lists of specific, administrative tasks that precede and follow the general term.

The Board's vision of its authority for the Self-Distribution Fee is also inconsistent with how the Legislature has treated this fee. In 2013, the Legislature amended RCW 66.24.055 to extend the period of time spirits distributors had to pay 10 percent from 24 months, up to 27 months—and it took a two-thirds majority to enact that change because the Initiative had not been on the books for two years. *See* Laws of 2013, 2nd. Sp. Session, ch. 12. It cannot hold true the Legislature needed a supermajority to impose a three-month obligation to pay 10 percent on spirits distributors, but the agency could freely obligate self-distributors to pay a ten percent fee.

Finally, apparently realizing it needs a specific grant of authority, the Board points to RCW 66.08.030(4), which allows the Board to "prescrib[e] the fees payable in respect of permits and licenses issued under this title for which no fees are prescribed in this title, and prescribing the fees for anything done or permitted to be done under the regulations." Board's Br. at 21. As discussed above, that language is plainly intended to allow fees to cover license processing and enforcement costs, not general revenue creation. Such costs are presumably addressed by the annual fees imposed by rule on distillers for their certificates to

exercise the self-distribution right. WAC 314-23-030(2)(a), (3) (imposing annual license fees). Appellants are not challenging these annual fees. And as discussed in the Opening Brief, regardless of the scope of this specific authority, the Board always lacks the authority to modify or amend I-1183 by rulemaking. *See* Appellants' Opening Br. at 28-32 (setting forth reasons the Self-Distribution Fee is inconsistent with the Initiative).

B. The 10 Percent Rule Is Arbitrary and Capricious

The 10 Percent Rule is invalid for a second, independent reason: it is arbitrary and capricious. RCW 34.05.570(2)(c). Action that is "willful and unreasoning and taken without regard to the attending facts or circumstances" must be invalidated. *Rios v. Dep't of Labor & Indus.*, 145 Wn.2d 483, 501 (2002) (citation omitted). The Board's arbitrary approach is evident by its acknowledgement the original basis for the Self-Distribution Fee was based on a misreading of the Initiative.

As discussed in the opening brief, an inconsistency in the agency's interpretation or application of a statute supports a finding of arbitrary and capricious action. Appellants' Opening Br. at 36-37. This doctrine is also well-established under the federal Administrative Procedure Act and was reaffirmed by the United States Supreme Court just last term. While agencies may change their interpretation of a law or their own regulation,

the agency must still "show there are good reasons for the new policy." *Encino Motorcars LLC v. Navarro*, 136 S.Ct. 2117, 2126 (2016). Such "inconsistencies in agency policy is a reason for holding an interpretation to be an arbitrary and capricious change from agency practice." *Id.* (citing *Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 981 (2005)).

Here, the Board adopted inconsistent positions when it promulgated the rule. It read RCW 66.24.055(3)(a), which imposes the spirits distribution fee, to be an "applicable law" that included self-distributing distillers, but read RCW 66.24.055(3)(c), which imposed liability for the \$150 million start-up fee on spirits distributors, to exclude self-distributing distillers. *See Ass'n of Wash. Spirits & Wine Distribs.*, 182 Wn.2d at 354 (discussing Board's "conflicting positions"). At the time of the rulemaking, the agency acknowledged the inconsistency, but its reason was specious: an alleged difference between the words "each spirits distributor licensee" and "all persons holding distributor licenses." Appendix D (concise explanatory statement at LCB00001035); CP 971 (Board's lower court briefing); *see also* Appellants' Opening Br. at 23-24 (discussing the asserted difference in the language).

When the appellate court tested this reasoning, the Board largely conceded it was nonsensical and acknowledged the real reason for the

inconsistent positions was a desire to "maximize" revenue for the State.

Ass'n of Wash. Spirits & Wine Distribs., 182 Wn.2d at 354.

Counsel for the Board now insists the purposes of Subsection 3(a) and 3(c) are different, therefore justifying different interpretations.

Board's Br. at 23-25. But again, the brief does not cite to any portion of the agency record and does not argue the Board did in fact consider the different purposes of the rule—only that the Board *could have* based its inconsistent positions based on the different purposes. The court, however, must decide whether a rule is arbitrary and capricious "as of the time the agency took the action adopting the rule." *Wash. Indep. Tel. Ass'n v. Wash. Utils. & Transp. Comm'n*, 148 Wn.2d 887, 906 (2003).

Even accepting the inconsistency in the Board's treatment of the Initiative, the Self-Distribution Fee is "willful and unreasoning and taken without regard to the attending facts or circumstances." *Id.* Here, the Board did not exercise any discretion or expertise to determine the Self-Distribution Fee was a reasonable rule. The Board imposed the rule because it felt the Initiative required it. Had the Board not felt constrained to impose the fee based on its misreading, it may well have chosen to impose a different percentage fee, or none at all, on the self-distributing distillers who provide a small amount of competition to the distributors

who control more than 95 percent of the distribution market in Washington.

Because the Board did not exercise any discretion or make any choice, the Court cannot uphold the Ten Percent Rule as a result of a reasoned process.

C. The Sell-and-Deliver Rule Is Arbitrary and Capricious

The Sell-and-Deliver Rule is arbitrary and capricious for similar reasons. In determining whether agency action is arbitrary and capricious, "the court must scrutinize the record to determine if the result was reached through a process of reason," and in doing so "ask[s] whether the decision was rational at the *time* it was made." *Rios*, 145 Wn.2d at 501. The record of the agency's process here lacks any relevant substance, and the Court has nothing on which it can scrutinize, much less affirm, the Board's decision-making process. *See* Appellants' Opening Br. at 13-14; *id.* at 39-44.

Counsel for the Board and the Association now attempt to supply reasons the Sell-and-Deliver Rule might be useful, without evidence the Board in fact relied on these reasons. Board's Br. at 34-35 (discussing strengthening the three-tier system, for unspecified reasons, and asserting an unexplained improvement to the efficient collection of taxes); Ass'n Br. at 10 (hypothesizing a need to prevent "unscrupulous" activities). Neither

brief cites to the agency record to show that the Board considered any of these reasons. And thus there is no record that the concerns now raised by the lawyers are actual problems or ones meaningfully addressed by the challenged rule. The briefing is nothing more than lawyer conjecture. *See Encino Motorcars*, 136 S.Ct. at 2127 ("It is not the role of the courts to speculate on reasons that might have supported an agency's decision."); *Somer*, 28 Wn. App. at 272 (stating "agency action cannot be sustained on post hoc rationalizations supplied during judicial review").

Even a cursory analysis of the concerns now articulated by the Board's lawyers shows they are overblown. The Sell-and-Deliver Rule does not "preserve" the three-tier structure by ensuring distributors remain involved. *But see* Board's Br. at 34-35.

As this graphic illustrates, distributors were part of the transaction under the practice prohibited by the rule, and are part of the transaction after:

Before the Sell-and-Deliver Rule



After the Sell-and-Deliver Rule



It is unclear how the "and-Deliver" aspect of Rule improves product tracking or tax collections given record-keeping by all three involved tiers, and the Board's brief provides no details. All the rule really requires is the product to be physically stored (even momentarily) at a distributor's warehouse. This adds costs passed on to retailers, profit for distributors, and an additional opportunity for product tampering or diversion. What it does not alter are the taxes for the State. More significantly, the Board made no record of the extent of any problem or whether its proposed solution would address any such problem without unduly burdening small businesses, as required under RCW 19.85.

The Board's lawyers express concern about a distributor acting "merely as a freight hauler." Board's Br. at 35. But that is exactly what the rule requires, and there is no explanation how that somehow

undermines the three-tier system. The Legislature and the People, in repeatedly expanding exceptions to the three-tier system, have made clear that the relevance of the three-tier system is waning in the modern liquor marketplace. *See* I-1183, § 204 (striking the policy statement that the three-tier system is "valuable" to the state). Without any record of reports of undue influence being exerted by manufacturers, such lawyer argument is merely speculation. I-1183 specifically authorized the practice of central warehousing for retailers, a break from the traditional model where distributors had to deliver all product to the final destination. *See* I-1183, § 123 (establishing right to centrally warehouse product).

The Association's lawyers conjure an even more unlikely scenario: the threat of an "unscrupulous supplier" lying about the amount of product sold and giving it away for free. *Ass'n Br.* at 10. Nothing supports the assumption that distributors are less unscrupulous than manufacturers. The Board already requires rigorous reporting from all suppliers about all product sold or delivered in the state. *E.g.*, RCW 66.24.206 (out-of-state wine importers must file monthly reports, under oath, about the quantity of wine sold or delivered); RCW 66.24.203 (same report required for wine importers); RCW 66.24.230 (monthly reports required for "every domestic winery, wine certificate of approval holder, wine importer and wine distributor"). The Board also requires reports from licensed retailers about

the volume purchased. *E.g.*, RCW 66.24.210(c) (requiring monthly reports on volume of wine and cider purchased); RCW 66.24.630(2)(b) (requiring spirits retail licensees to maintain records of purchases and file reports with the Board).

In sum, even were there room for debate about whether a problem in fact exists and whether the "solution" imposed by the agency is a reasonable one, it was the agency's duty to engage in this process with the stakeholders. Speculation from lawyers about the good the rule might do cannot replace the exercise of the agency's reasoning.

D. The Superior Court Correctly Determined that the Board's 24-Liter Per Day Rule Was Invalid

Another of I-1183's innovations concerned the right of an off-premises retailer (*e.g.*, a grocery store) to sell spirits or wine to an on-premises retailer (*e.g.*, a restaurant). The Initiative imposed a limit on such new, retail-to-retail transactions: "no single sale shall exceed twenty four liters." RCW 66.24.630(1); RCW 66.24.360(2). The Board changed the Initiative's single-sale limitation to a per-day limitation, adding: "Single sales to an on-premises licensee are limited to one per day." WAC 314-02-103(2); WAC 314-02-106(1)(c) (together, the "Per Day Rule").

The Superior Court invalidated the Per Day Rule, holding that the Board lacked the authority to amend the plain language of the initiative. CP 778 (Op. at 7). After discussing the applicable statutory canons and

the parties' positions, the court concluded "it is not the Board's place, nor this Court's, to infuse a policy into statutory language that is not there, even if that policy improves the statute." *Id.* Nearly three years after the Superior Court invalidated the Rule, the Board chose not to appeal.

Whatever policy concerns drove the Board's adoption of the rule in the first place were apparently not significant enough to justify the investment in an appeal.

The Association had intervened at the start of the case to defend all of the rules being challenged by Petitioners. It now appeals the Superior Court's decision to invalidate the Per Day Rule. CP 877. But with the agency having abandoned this rule after years without incident or complaint, the Association is not an "aggrieved party" under RAP 3.1. Its appeal should be dismissed.

In addition, two independent reasons support affirmance. First, the court below was correct that the Board's restriction on the retail-to-retail right was contrary to the Initiative's plain language. Traditional principles of statutory construction confirm that the only limit intended by I-1183 was the per-sale one it expressly imposed. Second, the Board lacked the express or implied authority to add an additional limitation, one designed for "market ordering" purposes, to benefit certain financial interests at the

expense of others. Because the Per Day Rule was beyond the agency's authority, the Superior Court appropriately invalidated it.

1. The Association is not an "aggrieved party."

Appellate review is only available to an "aggrieved party." RAP 3.1. "An aggrieved party is one whose proprietary, pecuniary, or personal rights are substantially affected." *Cooper v. City of Tacoma*, 47 Wn. App. 315, 316 (1987); *Mestrovac v. Dep't of Labor & Indus.*, 142 Wn. App. 693, 704 (2008) (defining "aggrieved" as "a denial of some personal or property right, legal or equitable, or the imposition upon a party of a burden or obligation"). But when the trial court's order "does not order [the party seeking appeal] to do anything," "pay anything," or "refrain from doing or paying anything," a so-called aggrieved party's "interests [are] in no way affected." *Polygon Nw. Co. v. Am. Nat. Fire Ins. Co.*, 143 Wn. App. 752, 768 (2008) (holding a party dismissed prior to final order was not an aggrieved party allowed to appeal trial court judgment).

Washington courts have not considered whether an intervenor may appeal the invalidation of an agency rule when the agency itself fails to pursue such an appeal. But in an analogous situation, the Washington Supreme Court dismissed an appeal by an intervenor for failure to show she was an "aggrieved party" when a city chose not to appeal a lower court ruling enjoining municipal action. *Terrill v. City of Tacoma*, 195 Wash.

275 (1938). In that case, a citizen sued to enjoin the City of Tacoma from pursuing a referendum petition that threatened to overturn a city council ordinance. *Id.* at 276. Another citizen moved to intervene, and none of the parties objected. *Id.* The trial court sustained the petition and enjoined the city from proceeding with the referendum. *Id.* When the city did not appeal, the intervenor did. *Id.* The Supreme Court dismissed the appeal because "it is essential, in order that a person may appeal . . . that he shall be aggrieved or prejudiced by the judgment or decree." *Id.* at 280.

Similarly, the United States Supreme Court has repeatedly held that a party whose interests are aligned with a state's does not have an injury of its own sufficient to maintain standing on appeal after the state declines to defend the validity of its law. Most recently, the court addressed this issue in *Hollingsworth v. Perry*, 133 S.Ct. 2652 (2013). Proponents of California's Proposition 8, which sought to amend the state constitution to define marriage as between one man and one woman, appealed the district court's invalidation of the Proposition, despite the State's refusal to do so. *Id.* at 2660. But "the District Court had not ordered them to do or refrain from doing anything." *Id.* at 2662. In dismissing the case for lack of standing, the court explained that "[w]e have never before upheld the standing of a private party to defend the constitutionality of a state statute when state officials have chosen not to."

Id. at 2668. *See also Diamond v. Charles*, 476 U.S. 54 (1986) (refusing to entertain appeal by pediatrician who intervened to defend abortion law after the state chose not to appeal a permanent injunction against the law's enforcement).

Both Supreme Courts' analyses are persuasive here, where an intervenor seeks to defend the validity of an agency rule the agency itself has chosen not to pursue. And the agency here had more than ample time to assess the impact of not having the Per Day Rule. Under the unique circumstances of this case, the agency had nearly three years to assess things and still chose not to pursue an appeal.

Despite the years since the Per Day Rule was invalidated, the Association does not discuss a single concrete harm they are suffering from the lack of a Per Day Rule. That is not surprising. The Association represents distributors. *See* Mot. for Substitution of Party as Intervenor at 2-3 (Apr. 27, 2016). The Board's Per Day Rule applied only to retail-to-retail sales. (In contrast, Appellants are retailers who faced enforcement action by the Board. *See Diamond*, 476 U.S. at 64.)

The Superior Court's orders do not impose any obligation on the Association (or its members) and do not deny it any right. CP 857 (2016 Order); CP 790 (2013 Order). As relevant to the Per Day Rule, the court ordered the following:

The sentence in WAC 314-02-103(2) and WAC 314-02-106(1)(c) that creates a "per day" limitation on sales between retailers substantively changes the language of the statute these WACs implement and therefore exceeds the Board's authority. Those portions of WAC 314-02-103(2) and WAC 314-02-106(1)(c) are invalid and unenforceable. RCW 34.05.570(2)(c).

CP 790 (2013 Order at ¶ 1). The Association incurred no legal obligation to do, or refrain from, doing anything. And while some loss of revenue due to increased competition in the marketplace might be conceivable, the nature of the loss must be immediate, rather than future, contingent, and speculative. *Terrill*, 195 Wash. at 280 (finding a "future, contingent, or speculative interest is not sufficient").

2. The Board's per-day restriction was inconsistent with the Initiative's plain language.

An agency rule must be reasonably consistent with the statute. *H & HP'ship*, 115 Wn. App. at 168. The Per Day Rule was inconsistent with I-1183, violating three fundamental principles of statutory construction: (1) the unambiguous, plain language of I-1183 imposed only a per-sale limit; (2) the additional limitation rendered words in the statute superfluous; and (3) a per-day limitation was inconsistent with the statutory context.

First, unambiguous laws are not subject to judicial or administrative construction; only if a reasonable ambiguity exists may an

agency seek to resolve it through rulemaking. *Edelman v. State ex rel. Pub. Disclosure Comm'n*, 152 Wn.2d 584, 590 (2004). But "[w]here the statutory language is plain and unambiguous, courts will not construe the statute ... regardless of contrary interpretation" by an agency. *Agrilink Foods, Inc. v. Dep't of Rev.*, 153 Wn.2d 392, 396 (2005). And "if a statute is silent on an issue, [courts] generally decline to read into the statute what is not there." *Birgen v. Dep't of Labor & Indus.*, 186 Wn. App. 851, 859 (2015), *review denied*, 184 Wn.2d 1012 (2015).

The Initiative's language regarding retail-to-retail sales is plain and unambiguous: "no *single sale* may exceed twenty-four liters." RCW 66.24.630(1); RCW 66.24.360(2) (emphasis added). The People knew that more than one sale could occur in a day, and yet the Initiative's restriction applies only to each "single sale" regardless of the time between sales. The ordinary use of the words leaves no room for interpretation. "Single" has a plain meaning: "one in number." Merriam-Webster's Collegiate Dictionary (2016). The statute itself defines "sale" as an "exchange, barter, and traffic" of spirits or wine. RCW 66.04.010(39). Thus, no one individual retail-to-retail liquor transaction may exceed 24 liters. No ordinary voter would read the phrase "no single sale may exceed twenty-four liters" as imposing a temporal restriction—much less a daily one. *See Wash. Ass'n for Substance Abuse & Violence Prevention v.*

State, 174 Wn.2d 642, 662 (2012) (initiative must be interpreted according to voter's understanding).

The Association argues the failure to define "sale" in the statute renders it ambiguous. Ass'n Br. at 19-20. For a statute to be ambiguous, its text must be susceptible to more than one reasonable interpretation. *Spain v. Emp't. Sec. Dep't*, 164 Wn.2d 252, 257 (2008). Although the Association makes much of the alleged substantive deficiencies of the phrase and its practical effects on liquor transactions, it does not identify any plausible alternative reading of the words the statute uses: "no single sale shall exceed twenty-four liters." On the contrary, the Association concedes that the provision imposes only a per-sale limit. Ass'n Br. at 14 ("I-1183 fails to specify how much time must pass between one 24-liter sale and the next, so the Board stepped in to 'fill the gap.'").

Instead, the Association suggests the ambiguity arises because the word "sale" could describe separate payments or an entire series of payments. Ass'n Br. at 19-20. But this argument ignores the word "single," which precedes "sale." The phrase "single sale" permits only one interpretation: the purchase volume in any individual retail-to-retail liquor transaction may not exceed 24 liters, but the frequency of single sales is unlimited.

Second, the Board's addition of a per-day limit failed to give effect to each word in the provision. "[S]tatutes should be construed so that all of the language used is given effect, and no part is rendered meaningless or superfluous." *City of Bellevue v. Lorang*, 140 Wn.2d 19, 25 (2000). The Board's Per Day Rule converted the retail-to-retail provision into a daily aggregate restriction, rendering the word "single" superfluous. Under the Board's editing, the Initiative could (and if intended, naturally would) simply read "no licensee may purchase more than 24 liters per day." But it does not.

Third, the Board's Per Day Rule was inconsistent with the statutory context. In construing a statute, a court must consider the statutory context and related provisions in the same statute. *Ass'n of Wash. Spirits & Wine Distribs.*, 182 Wn.2d at 350. "[W]here the Legislature uses certain statutory language in one instance, and different language in another, there is a difference in legislative intent." *Agrilink Foods*, 153 Wn.2d at 396. Temporal restrictions are specified in some sections of the Initiative, but omitted in the 24L provision. That omission must be deemed intentional—and respected. *Birgen*, 186 Wn. App. at 860-61.

For instance, I-1183 amended RCW 66.24.145, allowing any craft distillery to sell its own spirits for consumption off-site "up to two liters per person per day," 1183, § 204, and limiting tasting samples to a

"maximum total per person per day" to two ounces, *id.* Such temporal limits are common and explicit; the Legislature and the People know how and when to add them to laws both in the context of regulating liquor and otherwise. *See, e.g.,* RCW 66.24.170 (imposing a per-day limit on amount of wine served at sampling sessions); RCW 66.08.170 (imposing a per-day requirement for liquor fund deposits); RCW 90.44.050 (permission to withdraw groundwater up to 5,000 gallons per day). The choice to use a per-day restriction in one instance, and only a per-sale restriction in another, "means [the voters] intended the words to have different meanings." *State v. Keller*, 143 Wn.2d 267, 278 (2001).

The Association also argues the Initiative's 24L provision is "utterly pointless." Ass'n Br. at 15 (invoking statutory canon rejecting interpretations leading to absurd results). But as noted by the trial court, "the parties agree, however, that the rule without the 'per day' restriction would not be meaningless." CP 778 (Op. at 6). "The Board concede[d] that even without the 'per day' restriction, multiple transactions of 24 liters would still require multiple invoices and other record-keeping obligations."⁹ *Id.* What the Association is really pressing then is not an

⁹ The testimony from Appellants during the rulemaking, as well as comments submitted to the Board, made clear the 24L provision burdened the retail-to-retail commerce by imposing additional record-keeping requirements and increasing the inconvenience of the transaction. *E.g.,* Appendix D (LCB00000653) (describing 24L as adding a "degree of friction" that interferes

argument of absurdity, but one of degree—arguing that the statute, as written, does not go far enough to impose a "real" limit on retail-to-retail sales.

The Association cannot impose its vision of what a "real" limit entails under the guise of interpreting an ambiguity or to correct an "absurdity" that does not exist. Courts will not alter a statute's plain meaning: "[W]e should not . . . make an absurd interpretation to reach a desired result. To engraft such an interpretation upon the statute would be to supply a perceived deficiency under the guise of interpretation. That is beyond our power." *Cooper's Mobile Homes, Inc. v. Simmons*, 94 Wn.2d 321, 326 (1980). Absurdity is often in the eye of the beholder, informed by a policy perspective and desired outcome. But Washington courts require greater deference to legislation; additional deference is due to the Board's policy choice now to abandon the Per Day limitation. Neither I-1183 nor the agency record support a conclusion that the 24L provision was intended to be any more restrictive than written.

Ultimately, agencies may not legislate to correct perceived deficiencies in how a law's means serve its ends. The Washington

with their preferred business practice); *id.* (LCB00000675) (describing hassles imposed on purchases under the 24L provision); *id.* (LCBS00011) (discussing burden on restaurants). That "friction" in the business transaction can be avoided by purchasing the same product at a former contract liquor store or from a distributor, which are not subject to the 24L limit.

Supreme Court has repeatedly upheld this principle and limited agency action.

In the case of *United Parcel Services, Inc. v. Department of Revenue*, 102 Wn.2d 355 (1984), UPS argued the plain language of the statute led to an "irrational" result. The Court agreed, but the Court still refused to ignore the fact that the Legislature had used "certain statutory language in one instance, and different language in another." *Id.* at 362.

Similarly, in *Dot Foods, Inc. v. Department of Revenue*, a business challenged a B&O tax rule. 166 Wn.2d 912 (2009). While acknowledging the agency's interpretation "results in the statute being clearer," the Court observed that to affirm the agency's interpretation it "would have to import additional language into the statute that the legislature did not use. [The court] cannot add words or clauses to a statute when the legislature has chosen not to include such language." *Id.* at 920 (citing *State v. J.P.*, 149 Wn.2d 444, 450 (2003)); *see also* Appellants' Opening Br. at 29-30 (discussing *Edelman* case).

The same reasoning applies here, where the Initiative's plain language imposes only one limit on retail-to-retail sales: "no single sale may exceed twenty-four liters." The Board grafted on a second, new limitation: "Single sales may not exceed one per day." To amend the Initiative exceeded the Board's authority.

Finally, the Association makes much of a sentence of testimony given by a representative of one of the Appellants. The Association claims the Per Day Rule was justified to prevent some kind of "gotcha" orchestrated on the public. Ass'n Br. at 20. The facts are otherwise. The unambiguous language of the Initiative explained to every voter just what the limit entailed: "no single sale shall exceed twenty-four liters." The public was not fooled.

Neither was the agency. As early as May 2011, months before the election, the Washington Restaurant Association (one of the Appellants) prepared and distributed a summary of the Initiative, and the Board received a copy of it. CP 746-48 (LCBS000093-95). The first page of that summary says: "*On premise licensee can purchase up to 24-liters per transaction from another retail licensee with no limit on number or frequency of transactions.*" CP 746. Then and now, that formulation of the provision is perfectly consistent with the language of the statute.

3. The Board had no authority to regulate economic behavior.

The Association further argues that, regardless of what the Initiative meant, the Board had authority to promulgate a rule governing the "sale of liquor" and limit retail-to-retail sales to one 24 liter transaction per day. Ass'n Br. at 26. While acknowledging the repeal of the Board's

authority to "supply[] any deficiency" in Title 66, the Association still claims the Board retained authority to further limit retail-to-retail sales because the Per Day Rule "implements a specific statutory provision." *Id.*

As discussed above in Part II.A.2, it would defeat the People's choice to remove the Board's authority to "supply[] any deficiency" in Title 66 to construe the Board's authority to extend to "filling in the gaps in I-1183," as the Association urges. *Id.* Similarly, to construe the Per Day Rule as "implementing" the statute ignores the fact that I-1183 addressed the scope of the Board's authority to implement the retail-to-retail right. I-1183 only authorized *ministerial* record-keeping rules for the 24L provision. RCW 66.24.055(3)(d) (directing Board to make rules on the method of collecting fees owed on retail-to-retail sales).

But more importantly, the Board here was not "merely fill[ing] in the gaps in I-1183." Ass'n Br. at 26. The agency was making deliberate policy choices about which market participants should benefit how much under the new, private scheme. That was not authority granted to the Board, no matter how broadly its regulatory powers are construed.

During the rulemaking process, the Board made clear that the "one sale per day" rule was motivated by economic concerns, not public safety. The Board decided to impose the per-day limit to effectuate its own vision of "fair" economic competition instead of being grounded in the

Initiative—regardless of the burden on small businesses. *See* CP 790 (2013 Order at ¶ 6) (Superior Court's ruling the Board failed to conduct statutorily required analysis of proposed rule on small business). For example, then-Board Member Marr explained that his interest was to establish a "level playing field" and that the amount of competition the Initiative expressly allowed to off-premises retailers against distributors was "unfair." CP 215. In fact, he went so far as to claim that the Board had a *duty* to act to protect the financial interests of distributors: "[W]holesalers should rely on the expectation that the LCB will act to insure that those not licensed to act as distributors (except under those exceptions allowed under the initiative) are prevented from doing so." CP 214.

The Board's discussions during the rulemaking focused on which businesses can do what and how large their profit margins should be, and this focus illustrates how far the Board drifted from its statutory purpose. Appendix D (LCB00000648) (February 22, 2012, hearing transcript); *id.* (LCB00001743-76) (May 24, 2012, hearing transcript). I-1183 *authorized* retail-to-retail sales, but it did not authorize the Board to restrict such sales for purposes of economic ordering. The economic structure of the marketplace is no longer within the Board's purview after I-1183—if it ever was a legitimate concern.

Finally, the Association relies on the fact that the Board has authority to regulate the sale of liquor under RCW 66.08.030(6) or (12). Ass'n Br. at 24. But as discussed above, "[i]t is a cardinal rule of administrative law that an agency by its rulemaking authority may not amend or nullify a statute under the guise of interpretation." *State v. Dodd*, 56 Wn. App. 257, 260 (1989). Rules that impose a stricter requirement on licenses than that imposed by statute are a classic example of such overreaching. 1 Frank E. Cooper, *State Administrative Law* 256 (1965) (also collecting cases); see *H & H P'ship*, 115 Wn. App. at 170 (striking rule imposing additional filing requirement not included in statute). The "per day" language amends the per-sale volume limit imposed by the plain language of the statute, imposing an additional requirement on licensees' retail-to-retail rights.

The Attorney General's Office, analyzing House Bill 1161, concluded that adding a definition of "single sale" to the Initiative constituted an "amendment" requiring a supermajority. CP 753-57. It is difficult to fathom how an agency's addition of an entirely new limitation does not amend the Initiative if the Legislature's effort to return to what was originally intended does do so.

The Board lacked the authority to contradict the plain language of I-1183 and graft a temporal limit on what the People chose to make a

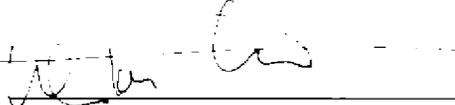
purely quantitative one. The Superior Court correctly invalidated the rule; the Board has now abandoned the rule; and this court should affirm.

III. CONCLUSION

The fair application of the APA requires the invalidation of all three rules.

RESPECTFULLY SUBMITTED this 28th day of September, 2016:

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CERTIFICATE OF SERVICE

On September 28, 2016, I caused to be served upon the below named counsel of record, at the address stated below, via the method of service indicated, a true and correct copy of the foregoing documents.'

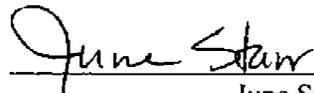
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I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

EXECUTED at Seattle, Washington, on September 28, 2016.



 June Starr

PERKINS COIE LLP

September 28, 2016 - 3:32 PM

Transmittal Letter

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