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NO. 92080-0

SUPREME COURT OF THE STATE OF WASHINGTON

STATE OF WASHINGTON, DEPARTMENT OF REVENUE,

Respondent,

v.

AVNET, INC.,

Petitioner.

DEPARTMENT OF REVENUE'S ANSWER TO BRIEF OF AMICUS CURIAE COUNCIL ON STATE TAXATION

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I. INTRODUCTION

The Department of Revenue properly assessed business and occupation (B&O) taxes on Avnet's wholesale sales of goods delivered to buyers in this state, as the Court of Appeals correctly held. Counsel on State Taxation (COST) disagrees, arguing that the Department is "ignoring its own rules" and disregarding United States Supreme Court precedent by assessing B&O taxes on the wholesale sales at issue. COST Br. at 1. Neither charge is true.

At its core, the dispute in this appeal is not about "ignoring" administrative rules or Supreme Court cases. Rather, the Department is simply asking this Court to correctly apply the relevant rules pertaining to inbound and out-bound sales of goods, and to correctly apply Supreme Court cases permitting the state to tax interstate sales when the seller has nexus with the state and the sale is consummated in the state by delivery to the purchaser or its designee. Avnet has nexus with Washington, and the sales at issue were consummated by physical delivery in Washington. The Court of Appeals agreed with the Department, properly rejecting each of Avnet's arguments for excluding dropped-shipped and "national" sales from the measure of the B&O tax. COST offers no valid reason for this Court to reverse or to accept Avnet's preferred interpretation of the law.

II. ARGUMENT

A. COST Misreads Former Rule 193.

COST misreads the language of WAC 458-20-193 (1991) (hereinafter "former Rule 193"), the Department's administrative rule on interstate sales. The rule did not, as COST contends, authorize a company to "dissociate" transactions when the seller's instate office played no role in particular Washington-destination sales. COST Br. at 5. Like Avnet, COST relies on decontextualized rule language that favors its argument while ignoring key operative provisions. When former Rule 193 is properly read as a whole and in the context of the governing statutory and constitutional law, it is clear the wholesaling B&O tax applies to *all* the inbound sales of goods made by a business that engages in activities designed to *establish a market* in the state for its goods.

1. Former Rule 193(7)(c) applies narrowly and requires proof that no nexus-creating activity occurred.

According to COST, former Rule 193 allows the "dissociation" of "particular sales" in which Avnet's Redmond office "played no role." COST Br. at 4-5. The rule language COST relies on states: "If a seller carries on significant activity in this state and conducts no other business in the state except the business of making sales, this person has the distinct burden of establishing that the instate activities are not significantly associated *in any way* with the sales into this state . . . ." Former Rule

193(7)(c) (emphasis added).

The Department has interpreted and applied this provision narrowly, consistently ruling that a seller seeking to "dissociate" some of its inbound sales must establish that the sales were unrelated to its "in-state promotion and marketing activities." *See* CP 377-78 (DOR Det. No. 04-0208, 24 WTD 217, 218 (2005) (addressing the issue of whether "the Taxpayer established that sales of its products . . . may be dissociated from its in-state promotion and marketing activities under Rule 193?") (copy attached as Appendix A). As the Department explained in a 2005 published determination, "establishing that a particular transaction may be dissociated requires proving a lack of association to all of the taxpayer's in-state activities that create substantial nexus." CP 385 (24 WTD at 225). In applying this analysis, the Department looks to "the entire bundle of a taxpayer's in-state activities. Accordingly, establishing that a particular transaction may be dissociated requires proving a lack of association to **all** of the taxpayer's" nexus creating activities. *Id.* (emphasis in original). Consequently, a taxpayer who engages in activities within the State designed to establish or maintain the market for its products cannot "dissociate" any of its inbound sales of goods merely by asserting that no "sales related" activity occurred in the state. CP 386 (24 WTD at 226) . The taxpayer must, instead, prove that no nexus-creating activities occurred in the state, a burden Avnet is unable to meet.

COST offers nothing but its mistaken interpretation of the rule's language to support its erroneous contention that the Department's "longstanding position" permitted a taxpayer to avoid the B&O tax when its local sales office or in-state personnel were not directly involved in the sale. *See* COST Br. at 5. In reality, the Department's "longstanding position" has been to recognize and apply evolving dormant Commerce Clause case law. *See* CP 385 (24 WTD at 225) and cases cited therein. The current test for evaluating a taxpayer's claim of dissociation is whether "the bundle of corporate activity" carried on within the state generally supports the taxpayer's ability to establish and hold a market for its inbound sales. *General Motors Corp. v. Washington*, 377 U.S. 436, 447-48, 84 S. Ct. 1564, 12 L. Ed. 2d 430 (1964). This analysis "does not require a direct connection between Avnet's activities in Washington and [the] specific sales" it claims are exempt from tax. *Avnet, Inc. v. Dep't of Revenue*, 187 Wn. App. 427, 447, 348 P.3d 1273 (2015); *accord, General Motors Corp. v. State*, 60 Wn.2d 862, 875-76, 376 P.2d 843 (1962), *aff'd* 377 U.S. 436 (1964) (holding that a taxpayer cannot meet its burden of proving disassociation by showing "the mechanical aspects of the wholesale sales" occurred outside the state).

Rule 193 has been revised several times over the years to reflect evolving dormant Commerce Clause case law, including a 1974 amendment explaining that inbound sales are taxable if "the seller carries on or has carried on . . . any local activity which is *significantly associated with the seller's ability to establish and maintain a market in this state for the sales*." CP 637 (emphasis added). Thus, since 1974, the Rule has recognized the "market sustenance" philosophy embodied in *General Motors*. The Rule did not rely on *Norton Co. v. Illinois Department of Revenue*, 340 U.S. 534, 71 S. Ct. 377, 95 L. Ed. 517 (1951), or the "free trade immunity" concept that guided the Supreme Court in 1951 when it decided *Norton*. *See Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 288-89, 97 S. Ct. 1076, 51 L. Ed. 2d 326 (1977) (overruling *Spector Motor Serv., Inc. v. O'Connor*, 340 U.S. 602, 71 S. Ct. 508, 95 L. Ed. 573 (1951), and rejecting the "free trade" rationale underlying the decision).

During the 2003 through 2005 periods at issue here, a taxpayer like Avnet seeking to dissociate some of its inbound sales from its Washington business activity must "establish[] that the instate activities are not significantly associated *in any way* with the sales into this state." Former Rule 193(7)(c) (emphasis added). The Court should interpret and apply the former version of Rule 193 consistent with its actual language and purpose. In light of Avnet's extensive nexus with the state and its varied market-creating activities, neither the Department's Rule nor the dormant Commerce Clause exempts Avnet's dropped-shipped or "national" sales from the state's wholesaling B&O tax.

2. Under former Rule 193, the sales were "received by the purchaser in this state" when they were delivered to the "ship to" address indicated on Avnet's sales documents.

Former Rule 193 comprehensively addresses how the B&O tax and retail sales tax apply to interstate sales of tangible personal property. The former Rule should be read in its entirety and its provisions construed together, not piecemeal. *ITT Rayonier, Inc. v. Dalman*, 122 Wn.2d 801, 807, 863 P.2d 64 (1993). Key terms used throughout the former Rule are defined in the Rule. *See* former Rule 193(2). These defined terms are crucial in correctly interpreting and applying the rule. *Cf., State v. Morris*, 77 Wn. App. 948, 950, 896 P.2d 81 (1995) (the statutory definition of a term controls its interpretation). Defined terms applicable to both inbound and out-bound sales include "delivery," "receipt," "agent," and "nexus." *See* former Rule 193(2)(c)-(f).

Former Rule 193 goes on to explain that Washington does not tax sales of goods originating in the state if receipt of the goods occurred outside the state. *See* former Rule 193(3). In turn, Washington does not assert B&O tax on sales of goods originating outside the state "unless the goods are received by the purchaser in this state and the seller has nexus.

There must be both the receipt of the goods in Washington by the purchaser and the seller must have nexus for the B&O tax to apply to a particular sale." Former Rule 193(7).

"Nexus" means "the activity carried on by the seller in Washington which is significantly associated with the seller's ability to establish or maintain a market for its products in Washington." Former Rule 193(2)(f). That definition mirrors the *Tyler Pipe* nexus standard. *See Tyler Pipe Indus., Inc. v. Dep't of Revenue*, 483 U.S. 232, 250, 107 S. Ct. 2810, 97 L. Ed. 2d 199 (1987); *Lamtec Corp. v. Dep't of Revenue*, 170 Wn.2d 838, 849-50, 246 P.3d 788 (2011). Avnet undeniably has nexus in Washington under this standard, a point the company concedes.

"Receipt" by the purchaser means that either the purchaser *or its agent* took physical possession of the goods or acquired dominion and control over them. Former Rule 193(2)(d). "Agent" is defined as "a person authorized to receive goods with the power to inspect and accept or reject them" upon delivery. Former Rule 193(2)(e). With respect to each sale at issue in this case, Avnet's customer undertook the contractual obligation to pay for the goods and provided Avnet with the name and address of the person who was authorized to receive the goods. *E.g.*, CP 82 (example invoice listing both the buyer and the person designated by the buyer to receive the goods). The person designated by Avnet's customer to receive the goods in Washington plainly was the customer's "agent" as defined in Rule 193.

This common sense conclusion is fully supported by other provisions in Rule 193. For example, former Rule 193(7)(b) explained that "[w]hen the sales documents indicate goods are to be shipped to a buyer in Washington," a seller seeking to prove that delivery actually occurred elsewhere had to provide documentation "to establish the fact of delivery outside Washington." Here, it is undisputed that the Department assessed wholesaling B&O taxes only on transactions in which Avnet's *own sales documents* indicated the goods were shipped to a buyer in Washington. CP 82; CP 90; CP 228-39; CP 247-59. Avnet does not contend that it can "establish the fact of delivery outside Washington," as permitted by former Rule 193(7)(b). Consequently, delivery of the goods at issue occurred in this state under the express terms of the Rule.

The Department and the Court of Appeals correctly interpreted and applied the "receipt" requirement in concluding that the wholesaling B&O tax applies to all of Avnet's inbound sales of goods. *Avnet, Inc.*, 187 Wn. App. at 440. Under former Rule 193, in order to establish that the B&O tax does not apply, Avnet was required to provide documentary evidence "to establish the fact of delivery outside Washington." That key evidence is nonexistent because all of the sales at issue were shipped to instate locations where the goods were physically received by the person authorized to receive them.

3. The Court of Appeals did not "ignore" former Rule 193; it correctly applied it.

COST claims the Court of Appeals erred by relying on *Ass'n of Washington Bus. v. Dep't of Revenue*, 155 Wn.2d 430, 120 P.3d 46 (2005) (*AWB*), "to support its determination that the DOR may ignore its own rule because it was merely interpretive." COST Br. at 6. COST urges this Court to clarify that *AWB* does not allow the Department to repudiate tax regulations that taxpayers have relied upon. However, COST's initial premise is unfounded—the Department is not "ignoring" former Rule 193. Moreover, COST misinterprets *AWB*.

The Court of Appeals' decision in this case no more sanctioned the Department's "disavowal" or "repudiation" of its own rules than did any of this Court's numerous decisions rejecting taxpayer arguments that the language of a tax regulation entitled them to avoid B&O tax even if the governing tax statutes did not. It is well established that the Department's interpretive rules cannot expand or contract tax liability. "Rules must be written within the framework and policy of the applicable statutes." *Kitsap-Mason Dairymen's Ass'n v. State Tax Comm'n,* 77 Wn.2d 812, 815, 467 P.2d 312 (1970). In view of the legislative intent to apply the

B&O tax as broadly as possible, Washington courts reject taxpayer efforts to seize upon ambiguous rule language to obtain tax benefits that are neither statutorily authorized nor constitutionally required.

This Court repeatedly has affirmed the principle that a taxpayer may not rely on ambiguous rule language to obtain a tax exemption that contravenes the governing tax statutes. *See, e.g.*, *Tesoro Ref. and Mktg., Inc. v. Dep't of Revenue,* 164 Wn.2d 310, 323-24, 190 P.3d 310 (2008) (rejecting taxpayer's "plausible interpretation" of language in a rule that reflected an "outdated" view of the applicable tax statute); *Coast Pac. Trading, Inc. v. Dep't of Revenue,* 105 Wn.2d 912, 916, 719 P.2d 541 (1986) (rejecting taxpayer's reliance on Department rule granting tax immunity broader than required by the Import-Export Clause); *Budget Rent-A-Car v. Dep't of Revenue*, 81 Wn.2d 171, 500 P.2d 764 (1972) (rejecting taxpayer's unduly broad reading of an interpretive rule on the casual sales exemption); *Wasem's, Inc. v. State*, 63 Wn.2d 67, 68-69, 385 P.2d 530 (1963) (rejecting taxpayer's "liberal interpretation" of language in Rule 193 relating to interstate sales).

In *AWB*, this Court held that the Department of Revenue had implied authority to issue interpretive rules through the process outlined in the Administrative Procedure Act. *AWB*, 155 Wn.2d at 445-46. The Court also explained that legislative rules "bind the court if they are within the agency's delegated authority, are reasonable, and were adopted using the proper procedure." *Id.* at 446-47. Interpretive rules, by contrast, are not binding on the courts. *Id.* at 447. An agency is expected to defend its interpretive rule—as the Department has done in this case—but the rule is "afforded no deference other than the power of persuasion." *Id.*

COST incorrectly asserts that *AWB* did not address a fact pattern "where a taxpayer filed [its excise tax returns] in accordance with the DOR's rule and the DOR disavowed a position in that rule." COST Br. at 7. To the contrary, in that opinion this Court observed that "in *Coast Pacific* we disallowed an export exemption from the state business and occupation tax because it was based on a regulation that attempted to expand tax immunity beyond what the underlying statute and constitution required." *AWB*, 155 Wn.2d at 441 (citing *Coast Pac.*, 105 Wn.2d 912). Consistent with *AWB* and *Coast Pacific*, and contrary to the arguments advanced by Avnet and COST, former Rule 193 cannot reasonably be interpreted as providing tax immunity that is neither statutorily authorized nor constitutionally required.

When addressing and rejecting Avnet's proposed interpretation of the former Rule 193, the Court of Appeals correctly relied on this Court's holdings in *AWB* and "[m]ore specifically" *Coast Pacific*. *Avnet*, 187 Wn. App. at 439. The Court of Appeals correctly recognized that Avnet's interpretation would create a de facto tax exemption that is not authorized by the Legislature or required by the dormant Commerce Clause.

When read as a whole and in proper context, former Rule 193 does not exempt Avnet's drop shipment sales or its "national" sales from the wholesaling B&O tax. First, it is undisputed that Avnet has nexus with Washington. Moreover, all of the drop shipped sales at issue were shipped to a buyer in Washington that was authorized to receive the goods, which establishes both "transactional nexus" with the state and "receipt" in the state. Finally, no intervening "receipt" occurred outside the State. Under these undisputed facts, the sales are properly subject to B&O tax under the Washington tax code *and* under former Rule 193.

4. The 2015 amendment to Rule 193 did not change the Department's interpretation of dissociation or drop shipments.

COST suggests that the Department has changed its interpretation of dissociation and drop shipments under former Rule 193 without going through the APA rule-making process until after the periods at issue here. COST Br. at 10. COST is incorrect in its implied assertion that the current rule is a significant departure from former Rule 193.

As discussed above, the language and purpose of former Rule 193 supports the Department, not Avnet, with respect to both the dissociation issue and the drop shipment issue. Moreover, the 2015 rule revision merely emphasized the Department's existing policy on both issues. *See generally* Wash. St. Reg. 15-15-025 (filed July 7, 2015) (amendment intended to provide "current and clearer guidance"). While COST argues as if the 2015 rule revision was a bolt out of the blue, the Department had already informed taxpayers of its position on dissociation through the numerous published determinations it has issued since 1991. *See, e.g.*, CP 377 (Det. No. 04-0208, 24 WTD 217 (2005)); CP 672 (Det. No. 99-216E, 18 WTD 264 (1999)). In addition, while the Department's former rule did not specifically address how the wholesaling B&O tax applies to drop shipments, the proper application of the rule's generally applicable provisions pertaining to inbound sales results in the taxation of such transactions, as the Department previously had ruled. *See* CP 412 (Det. No. 08-0111, 27 WTD 221 (2008)).[1] The 2015 amendment to Rule 193 underscored the Department's established policy. It did not change the Department's interpretation of the law.

B. The Department Is Not Ignoring Supreme Court Precedent; It Is Asking This Court To Correctly Apply That Precedent.

The Court of Appeals correctly analyzed and applied the "governing legal standard" set out by the United States Supreme Court for

[1] Former Rule 193(11)(h) did provide an example pertaining to the retail sale of drop-shipped goods. That example did not address the wholesale sale of goods by a business such as Avnet that has nexus with the state. *See Avnet*, 187 Wn. App. at 437-38 (rejecting Avnet's contention that the example in former Rule 193(11)(h) applies here).

establishing nexus with interstate sales delivered into Washington when it held that "Avnet's national sales and drop-shipped sales here at issue are subject to Washington's B&O tax." *Avnet*, 187 Wn. App. at 448-49.[2] This Court should affirm.

1. Following *Complete Auto Transit*, a gross receipts tax is not subject to a stricter nexus standard than a sales tax.

COST contends that a more onerous nexus standard applies to a tax "directly imposed" on taxpayer's business activities, including Washington's gross receipts tax, than the standard applicable to an "indirect" sales or use tax collection requirement. COST Br. at 14-15. This is flatly incorrect. The distinction between "direct" and "indirect" tax burdens no longer is part of the dormant Commerce Clause analysis. Following *Complete Auto Transit*, the constitutionality of a state tax depends on the practical effect of its operation, not on a formulaic distinction between "direct" and "indirect" burdens. *See Dep't of Revenue v. Ass'n of Washington Stevedoring Cos.*, 435 U.S. 734, 750, 98 S. Ct. 1388, 55 L. Ed. 2d 682 (1978) (the "distinction between direct and indirect taxation" is constitutionally irrelevant after *Complete Auto*).[3]

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[2] The opinion has been cited with approval in the leading treatise on state taxation, wherein the authors comment that our Court of Appeals "cogently distills the reasons . . . for questioning the continuing force of *Norton*." *See* 1 Jerome R. Hellerstein, Walter Hellerstein, and John A. Swain, *State Taxation* ¶ 19.02[3][b] (3d ed. 2015 rev.) (copy attached at Appendix B).

[3] If anything, a *stricter* nexus standard applies to a sales or use tax than to a gross receipts or income tax. *See Lamtec*, 170 Wn.2d at 848-49 (recognizing that the

COST is also incorrect when it contends that "transactional nexus" does not apply to all tax types. COST Br. at 15. The power to tax requires a connection with both the taxpayer and with the activity or transaction subject to tax. Under long-established dormant Commerce Clause case law, the physical delivery of goods in this State created the requisite "nexus" with all of Avnet's Washington destination sales. *Oklahoma Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 184, 115 S. Ct. 1331, 131 L. Ed. 2d 261 (1995). The fact that the orders were received, accepted, and shipped from outside the State does not negate the "transactional nexus" arising from the physical delivery of the goods in Washington.

COST contends that "*Jefferson Lines* is inapposite" with respect to its transactional nexus argument because that case involved the imposition of a state sales tax, not a gross receipts tax. COST Br. at 15. The argument lacks merit. The Supreme Court in *Jefferson Lines* made the point that nexus with the transaction the state seeks to tax, while required as part of the *Complete Auto Transit* four part test, is not a demanding standard and was easily met in that case. 514 U.S. at 184. "Oklahoma is where the ticket is purchased, and the service originates there. These facts are enough for concluding that '[t]here is nexus aplenty here.'" *Id.* (quoting *D.H. Holmes Co. Ltd. v. McNamara*, 486 U.S. 24, 33, 108 S. Ct.

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physical presence nexus standard that applies to sale and use taxes likely does not apply to Washington's wholesaling B&O tax).

1619, 100 L. Ed. 2d 21 (1988)) (some internal quotations omitted). The Court did not hold that transactional nexus is unimportant or, as COST suggests, constitutionally irrelevant.

The more "difficult question" faced by the Supreme Court in *Jefferson Lines* involved the manner in which the States may apportion a taxable service that occurs in more than one state. *Id.* at 184-85. With respect to the fair apportionment requirement, the imposition of a gross receipts tax on transportation services may present a risk of multiple taxation that is not present in the sales tax context, which the Court in *Jefferson Lines* discussed in great detail. *Id.* at 185-96. But there is no genuine risk of multiple state taxation with respect to Washington's wholesaling B&O tax, which is "fairly apportioned to the activities taxed." *Chicago Bridge & Iron Co. v. Dep't of Revenue*, 98 Wn.2d 814, 829, 659 P.2d 463 (1983); *see also W.R. Grace & Co. v. Dep't of Revenue*, 137 Wn.2d 580, 596-98, 973 P.2d 1011 (1999) (rejecting taxpayers' apportionment challenge as inconsistent with settled law). Moreover, there is no principled justification for distinguishing between sales taxes and gross receipts taxes with respect to nexus. And the Court in *Jefferson Lines* engaged in no analysis, and cited no cases, that would support a bifurcated "sales tax nexus versus gross receipts tax nexus" approach.

COST simply conflates the apportionment analysis in cases like *Jefferson Lines* and *Goldberg v. Sweet*, 488 U.S. 252, 109 S. Ct. 582, 102 L. Ed. 2d 607 (1989), with the nexus analysis applied by the Supreme Court in those cases. *See* COST Br. at 16. In *Goldberg*, nexus was not even an issue. "As all parties agree that Illinois has a substantial nexus with the interstate telecommunications reached by the [Illinois tax], we begin our inquiry with apportionment, the second prong of the *Complete Auto* test." *Goldberg*, 488 U.S. at 260. And, as discussed above, nexus with the transaction was easily established in *Jefferson Lines*. So too in this case, nexus with the interstate sales that Avnet seeks to exempt from the Washington B&O tax is easily established. Each sale was completed in Washington when the goods were delivered to the person designated to receive them. The dormant Commerce Clause does not require more.

2. The contested sales transactions are not part of a "discrete business enterprise."

COST is correct, however, when it explains that a state may not impose an income tax on amounts derived from a "discrete business enterprise" that is unrelated to the activities carried out within the State. COST Br. at 17 (citing *MeadWestvaco Corp. v. Ill. Dep't of Revenue*, 553 U.S 16, 128 S. Ct. 1498, 170 L. Ed. 2d 404 (2008)). *See* DOR Resp./Reply Br. at 26 (explaining when certain income may be excluded from the pre-apportionment tax base of a multistate business). But the inbound sales at issue in this appeal are not part of a "discrete business enterprise," separate and distinct from the inbound sales that Avnet admits are taxable by the state. To the contrary, all of Avnet's business activities are part of the same unitary business operation. *See e.g.*, CP 447-50 (describing the "virtual" integration of Avnet's business operations). As a result, Avnet could not rely on unitary business cases like *MeadWestvaco* to shield its sales from Washington tax.

3. Post-*Norton* cases such as *Tyler Pipe*, *Standard Pressed Steel*, and *General Motors* are applicable and support the Department in this appeal.

The final argument presented by COST asserts that *Tyler Pipe*, *Standard Pressed Steel Co. v. Dep't of Revenue*, 419 U.S. 560, 95 S. Ct. 706, 42 L. Ed. 2d 719 (1975), and *General Motors* are "inapplicable," and that reliance on those cases is "unfounded" or "misplaced." COST Br. at 17, 19. The argument is effectively refuted by this Court's decision in *Chicago Bridge*, 98 Wn.2d 814. In that case, this Court discussed and applied post-*Norton* cases in rejecting the taxpayer's dissociation claim with respect to in-state sales that did not involve the taxpayer's Seattle sales office. Citing *Standard Pressed Steel* and *General Motors*, this Court explained how these cases "reveal that the presence and participation of a sales office in [the] state is not decisive in determining the existence of nexus." *Id.* at 820. Instead, for a business to "exempt itself from the local tax by showing no in-state activities were associated with the interstate business," it must show that "its in-state services were not decisive in *establishing and holding the market*." *Id.* at 822 (emphasis added) (citing *General Motors* and *Norton*). The proper focus is on the bundle of corporate activities a company undertakes to establish and create a market in the state for its sales, not on whether particular sales are channeled though a local sales office.

COST attempts to distinguish the post-*Norton* Supreme Court cases by relying on insignificant differences in the facts of those cases. *See* COST Br. at 19 (arguing that in *Standard Pressed Steel* "there was no attempt by the taxpayer to dissociate its salesperson's activities from the actual sales being made to a customer in Washington"). But any minor difference in the facts presented or the arguments advanced by the taxpayers are not material. As this Court recognized in *Chicago Bridge*, the important point is that the Supreme Court has decisively rejected the premise that a taxpayer with nexus in Washington can dissociate subcategories of inbound sales from the measure of the wholesaling B&O tax merely by asserting that some portion of the sales activity occurred outside the state. 98 Wn.2d at 820-822. Consistent with *Chicago Bridge*, *General Motors*, *Standard Pressed Steel*, and *Tyler Pipe*, Washington may impose its fairly apportioned, nondiscriminatory wholesaling B&O tax on all of Avnet's Washington-destination sales of goods, including its dropped-shipped and "national" sales.

III. CONCLUSION

The Court of Appeals correctly rejected Avnet's interpretation of the law and correctly held that the company had not met its burden of dissociating any of its inbound Washington sales from its market-creating activities. The arguments advanced by COST criticizing the Court of Appeals and charging the Department of Revenue with "ignoring" the law do not withstand scrutiny. This Court should affirm the Court of Appeal.

RESPECTFULLY SUBMITTED this 27TH day of April, 2016.

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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.

DATED this 27th day of April, 2016, at Tumwater, WA.

Candy Zilinskas

Candy Zilinskas, Legal Assistant

APPENDIX A

Cite as Det. No. 04-0208, 24 WTD 217 (2005)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Refund of	)	DETERMINATION
	)	
	)	No. 04-0208
	)	
. . .	)	Registration No. . . .
	)	Petition for Review of Audit
	)	Refund Denial Letter
	)	Docket No. . . .
	)	

[1] RULE 193: B&O TAX — NEXUS — DISSOCIATION — INDEPENDENT SOURCE. For a taxpayer to dissociate sales from its nexus creating activities in Washington, it must document that those sales are derived from an exclusively independent source and are not significantly associated, in any way, with any of the taxpayer's in-state activities that establish or maintain a market for its products.

[2] RULE 193: B&O TAX — NEXUS — DISSOCIATION — BRAND NAME PRODUCTS. An out-of-state taxpayer with taxing nexus in Washington cannot dissociate select sales of brand name products where the select sales are made pursuant to sales contracts negotiated and executed outside of Washington because the taxpayer cannot prove that the select sales are not significantly associated in any way with its in-state promotion and support activities for these brand name products.

Kreger, A.L.J. – . . . (Taxpayer), a manufacturer of consumer products, contends that the Department of Revenue (Department) erred in denying a request for refund of business and occupation tax paid on sales of consumer products in Washington. Taxpayer contends that some sales should be dissociated from its Washington activities[1]. . . .

[1] Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

ISSUES

1. Has the Taxpayer established that sales of its products sold by its . . . [A] Group may be dissociated from its in-state promotion and marketing activities under Rule 193?

2. Has the Taxpayer established that sales of its products sold by its [B] Group may be dissociated from its in-state promotion and marketing activities under Rule 193?

3. Has the Taxpayer established that sales of its products sold by the [C] Group may be dissociated from its in-state promotion and marketing activities under Rule 193?

FINDINGS OF FACT

The Taxpayer, a [State X] Corporation, manufactures and sells consumer products. The taxpayer groups its products into four lines . . . . The taxpayer sells its products throughout the United States and around the world.

Sales Groups and Product Lines:
The Taxpayer has established four different sales groups to sell and market its products: [A] Group, [B] Group, [C Group], and [D Group]. Each sales group focuses on a particular market sector and is responsible for sales of specific products that are tailored to the needs of that market sector.

The [A] Group sells to large retail stores, club stores, drug stores and grocery stores . . . . The majority of these accounts are serviced on a national basis. These large retailers do not generally retain local purchasing and buying agents. Instead, the stores (Taxpayer's customers) gather sales data and purchase requests from their individual branches and then negotiate with suppliers on a consolidated order. A Taxpayer's sales representative negotiates sales with the customer's purchasing representative, generally at the company's national headquarters. The sales representatives then coordinate the delivery of the products to particular stores. It is common for the Taxpayer's sales representatives' interactions with these national account customers to occur predominantly or exclusively at the customers' headquarters. Indeed, it is common for national sales representatives to take orders for and arrange for shipping to stores in regions they have never visited.

The sales representatives in the [A] Group strive to increase the total number of the Taxpayer's products that the customers' stores carry (*i.e.*, stocking six different [types] of a particular [product] as opposed to three and carrying four different [product] brands as opposed to two) and to negotiate the most prominent placement possible (*e.g.*, center shelf center aisle as opposed to higher or lower placement, and a higher number of special displays or end of aisle placements) for those products. Product range and placement are governed by the master contracts the sales representatives negotiate with the customers. These master contracts are supplemented by addenda to cover special promotions[2] and additions or substitutions to the product mix. The national account sales representatives' primary responsibility is managing order and delivery transactions. They receive customer complaints and are responsible for managing and resolving order and delivery problems but do not have responsibility for actual in-store promotion or verification work.[3] Common carriers actually deliver all of the Washington sales made by this sales group, and third party service providers, who are not representatives of Taxpayer, provide and direct in-store promotion and marketing work. These national sales representatives provide an important conduit for customer information to the Taxpayer's advertising and marketing staff and have some input into product promotion decisions. However, the national sales representatives do not make decisions on which products to promote or how to market those products. Promotion and marketing decisions are primarily driven by sales data and are made at a higher corporate level and then conveyed to the sales representatives.

A significant portion of the taxpayer's refund claim involves [A] Group sales to national retail stores where the Taxpayer's account representatives take orders at the customers' headquarters and then arrange for delivery of products to the customers' Washington stores. For these national sales, the Taxpayer asserts that the particular sales representatives responsible for the accounts never visit Washington on company business. The Taxpayer provided information on where these national sales representatives are based and work and asserts that detailed travel records, in the form of expense reports, for these employees substantiate that they did not visit Washington on company business. The Taxpayer particularly emphasizes that all of the sales representatives' work in supporting, maintaining, and soliciting the sales included in the dissociation claim occurs outside of Washington.

The next sales group is the [B] Group. This group makes sales to three market areas: hospital and health care organizations, the hotel and hospitality industry, and commercial enterprises and institutions (such as restaurants, businesses, government agencies, schools, etc.). The Taxpayer has specialized product lines tailored to meet the needs of these market areas.

All of the Washington [Group B] sales are delivered from points outside Washington by common carrier.

The [Group B] is subdivided into two divisions, [Division 1] and [Division 2], both of which are serviced by third-party brokers. A third party broker, located in [State Y], takes orders for the [Division 1] sales included in the refund claim. This broker primarily conducts business by telephone and does not personally visit any Washington customers. The Taxpayer asserts that the Washington [Division 1] accounts included in the dissociation claim are exclusively negotiated and serviced outside of Washington.

[2] One example of a promotion addendum would be an agreement to assure additional stocks of a particular product that will be featured in a national or regional coupon distribution in newspapers.

[3] The Taxpayer clarified that some customers actually limit by contract the extent and nature of in-store activities the Taxpayer can have.

Third-party brokers also service the [Division 2] accounts. (See employee information below.) The Taxpayer asserts that the [Division 2] accounts included in the dissociation claim are also negotiated out of state and that these customers are not visited in Washington by any of the Taxpayer's employees or agents.

In addition to the direct sales activities of these third-party brokers, the [B Group] also participates in trade shows to further support the sale of its product lines. . . . During the refund period the [B] group participated in two trade shows in Washington. . . .

[Taxpayer] has several military accounts that are serviced by a third-party broker located in Washington. This broker only visits military account customers and does not have any responsibility for or contact with customers serviced by the other sales groups. None of the sales to the [D] Group are included in the claim for refund, and the Taxpayer does not seek to dissociate any of these sales.

The final sales group is [C Group], which is an independent sales company located in [State G] specializing in telephone sales. The Taxpayer hired [C Group] to handle its smaller accounts, which are defined as accounts that annually purchase $. . . or less of the Taxpayer's products. Typical examples of such accounts are small, independent grocery stores, mini-marts, and independent gas stations. [C Group] manages existing accounts and engages in telephone canvassing soliciting new customers. All [C Group] sales to Washington customers are delivered from outside the state by common carrier. [C Group] only provides telemarketing services to the Taxpayer and does not send its sales associates or agents into Washington to support sales. The Taxpayer does not send any of its employees or representatives to visit Washington [C Group] accounts.

<u>In-state Employees:</u>
During the refund period the Taxpayer employed sales representatives living in Washington and also employed some resident independent contractors. None of these sales representatives or contractors was responsible for or personally serviced any of the sales that the Taxpayer is seeking to dissociate. The Taxpayer explains that the location of these employee sales representatives is generally fungible. They work from home and conduct a significant portion of their work by telephone, internet, and e-mail so the location where they live is largely discretionary.

[Ms. H] is the national sales manager for [products], which are produced at the [State H] plant. [Ms. H] lived in Washington for part of the refund period and worked from her home. She no longer resides in Washington as her spouse was transferred to [State K] and she now works from her home there.

[Ms. J] is the [company J] Region Distribution Manager and lives in . . . , Washington. [Ms. J] manages brokers who call on the . . . divisions of [company J]. [Ms. J] performs a significant amount of her work from her home office supplemented by regular visits to the [company J] regional corporate office in [State J]. Her work responsibilities do not include visiting local stores in a professional capacity; those activities are the responsibility of the brokers she supervises and independent marketing contractors who are hired to handle promotions. The refund claim does not include any sales made by [Ms. J] or the brokers and contractors she supervises.

[Contractor] is an independent contractor employed by the Taxpayer. [Contractor] is headquartered in [State F] and maintains over . . . offices serving the United States . . . . [Contractor] provides a diverse range of sales and marketing tasks, including in-store marketing to the Taxpayer. Two regional [contractor] employees, [Mr. K] in [Washington City 1] and [Mr. L] in [Washington City 2], are responsible for sales and marketing calls to Washington [company J division] stores. [Mr. K] also serves additional regional retail customer accounts for the Taxpayer. The dissociation claim does not include any sales to customers served by the Washington [contractor] representatives.

[Ms. R] is the National Account Manager for [Store R] and lives in Washington. [Ms. R] sells to buyers at [Store R] and frequently visits the company headquarters in . . . , Washington. She also is not responsible for visiting local or regional [Store R] stores in a professional capacity as those activities are handled by other brokers. The Taxpayer works with an independent broker, . . . , which is a Washington corporation that . . . provides manufacturer's representatives to [Store R]. None of the Taxpayer's sales to Washington [Store R] stores are included in the refund claim.

In July of 2002, the Taxpayer hired [Mr. D] of . . . , Washington to assume sales promotions activities for the Taxpayer's [B Group] Wholesale Distributor. [Mr. D] is the [B Group] broker referenced above and is responsible for distributors in . . . , Washington, [and several other states]. [Mr. D] personally makes sales calls to both distributors and end users and also manages other sales agents. He also provides the sales agents with market information developed by the Taxpayer through surveys that are distributed to both consumers and distributors and feedback received from trial distribution of potential products. The [B Group] also has a local marketing group that it works with in Washington, [Marketing Group]. The Taxpayer has indicated that this marketing firm uses "direct sales marketing" to market products to wholesale distributors and consumers. The [B Group] sales included in the dissociation claim do not include any of [Mr. D's] accounts. However, the Taxpayer has not indicated what Washington [B Group] accounts the [Marketing Group] serves or verified that the [B Group] accounts that are part of the dissociation claim were not visited or contacted by these in-state marketing agents.

ANALYSIS

Elements of Dissociation:

Washington imposes the wholesaling B&O tax on interstate sales of goods into Washington pursuant to RCW 82.04.220, RCW 82.04.270, and WAC 458-20-193 (Rule 193). These taxes may not be constitutionally imposed on interstate commerce unless a taxpayer has substantial nexus with the taxing state. *Quill Corp. v. North Dakota,* 504 U.S. 298, 313 (1992). Taxpayer acknowledges substantial nexus with Washington and does not contest that it is responsible for reporting and remitting B&O tax to Washington. At issue here is whether some of Taxpayer's sales into Washington may be dissociated under Rule 193.

Limited Applicability of *Norton*:

The Taxpayer relies on *Norton Co. v. Department of Rev.*, 340 U.S. 534 (1951), and Rule 193 to argue that it should be allowed to dissociate select sales that are negotiated and supported by out-of-state sales representatives and marketing agents from its in-state activity. The sales included in the dissociation claim are select national sales made by three sales groups; the [A] Group, [B] group, and [C Group]. The sales identified by the Taxpayer as eligible for dissociation are sales where all contact between the sales agent responsible for the sale and the customer occurs outside of Washington.

The Department addressed its position regarding dissociation, *Norton,* and Rule 193 in recently-published Det. No. 00-098, 22 WTD 151 (2003). In that case, the taxpayer had also relied on *Norton* to support the dissociation of sales of electronics and computers sold to national accounts from its other Washington sales activities. In limiting that reliance, we stated:

> Taxpayer cites *Norton Co. v., Department of Revenue*, 340 U.S. 534 (1951) (*Norton*) for the principle that a seller may dissociate the sales of its national accounts from its activities of authorizing repair centers for its products in a state. Norton was a Massachusetts manufacturer of abrasive machines and supplies. It maintained a branch office and warehouse in Illinois from which it made local retail sales to over-the-counter customers. The branch office also serviced machines after they were purchased and gave engineering and technical advice. Other orders for sales were sent by Illinois residents directly to the home office of the Massachusetts company and were accepted and filled there. The Court allowed these latter sales to be dissociated from the taxpayer's other Illinois activities . . .
>
> We doubt the continued validity of *Norton*. . . . [T]he premise in *Norton* was that states could not tax interstate commerce. And see *Id* at 536-37. That premise was overruled in *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274, 289 (1977) (*Complete Auto*). No federal court has relied upon *Norton's* dissociation holding after *Complete Auto.* Second, *Norton* stated that merely sending solicitors (itinerant drummers) into the state would not provide nexus for any resulting sales. This holding has not been followed in numerous cases, *e.g. Scripto Inc. v. Carson,* 362 U.S. 207; 80 S.Ct. 619, 4 L.Ed. 2d 660 (1960). Today, sending sales personnel into a state and delivering the goods here is sufficient presence to create both Due Process and Commerce Clause nexus.
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> Nevertheless, Rule 193(7)(c) continues to allow dissociation where the taxpayer can meet its terms:
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>> If a seller carries on significant activity in this state and conducts no other business in this state except the business of making sales, this person has the distinct burden of establishing that the instate activities are not significantly associated in any way with the sales into this state."

> It is the Rule, not *Norton*, that controls our discussion of dissociation. (Footnotes omitted.)

Id.. As the foregoing discussion illustrates, the holding in *Norton* relies on a far more restrictive interpretation of the boundaries of state taxation of interstate commerce than is applicable today.[4] The restrictive presumption that interstate commerce was beyond the reach of state taxing authority has been altered by modern nexus analysis based on the four factor analysis established by *Complete Auto.*[5] Delineating revenue that a state may tax from that which is beyond its reach involves determining the boundaries of a state's taxing authority. The world of permissible state taxation has added new territories since *Norton* was issued, and this expansion limits the utility of *Norton. Norton* does not detail how to navigate the current boundaries of state taxation because that boundary line is simply beyond the area it mapped. It is for this reason that our dissociation analysis focuses on the specific requirements of Rule 193 and case law that addresses the current boundaries of Washington taxation.

The Taxpayer cites *National Geographic Soc'y v. California Bd. of Equalization*, 430 U.S. 551 (1977), for the premise that the Supreme Court "continues to follow the concept of dissociation." Taxpayer's Brief of April 19, 2004 at page 5. However, we read *National Geographic* differently. The lone reference to dissociation in that case is as follows:

> The Society argues in other words that there must exist a nexus or relationship not only between the seller and the taxing State, but also between the activity of the seller sought to be taxed and the seller's activity within the State. We disagree. However fatal to a direct tax a showing that particular transactions are dissociated from the local business . . ., *Norton Co. v. Illinois Rev. Dept.*, supra, at 537, 71 S.Ct. at 380; *American Oil Co. v. Neill*, supra; *Connecticut Gen. Life Ins. Co. v. Johnson*, 303 U.S. 77, 58 S.Ct. 436, 82 L.Ed. 673 (1938), such dissociation does not bar the imposition of the use-tax-collection duty.

430 U.S. at 560. This single reference, citing authority from 1951, 1965, and 1938, does not support the assertion that *National Geographic* follows the concept of dissociation. Rather the court expressly declines to agree with the premise that taxing nexus is a transaction by transaction

[4] *See, e.g.*, Arthur R. Rosen, Melissa A. Connell, *State Tax Nexus Issues--The Decades-Old Debate Continues in the Shadow of the Internet*, 95 J. Tax'n 303, 306 (2001) (The introduction examines the states' attempts during the last several decades to extend their tax jurisdiction to out-of-state businesses and addresses litigation arising our of those efforts and specifically refers to Washington as follows: "The argument that nexus is created where a business' activities are specifically directed towards creating or maintaining a market within the state has recently had a high degree of success in Washington State."); Jerome R. Hellerstein & Walter Hellerstein, *State Taxation* §6 - § 13 (3d ed. 1998 & Supp. 2002).(Covering recent changes in commerce clause analysis with regard to taxation of interstate commerce.); William R. Jones, *Increasing State Taxing Power over Interstate Commerce*, 32 Tulsa Law Journal 75 (Fall 1996).

[5] The *Complete Auto* test requires that the tax must (1) be applied to an activity with a substantial nexus with the taxing state; (2) be fairly apportioned; (3) be nondiscriminatory towards interstate commerce; and (4) be fairly related to the services provided by the state. *Complete Auto*, 430 U.S. at 279. *Complete Auto* is extensively cited, and the four factor test it established still forms the foundation for current analysis of whether interstate commerce is subject to state taxation. *See e.g., Oklahoma Tax Com'n v. Jefferson Lines, Inc.*, 514 U.S. 175 (1995); *General Motors Corp. v. City of Seattle*, 107 Wash. App. 42, 25 P.3d 1022, 1029 (2001).

analysis. Far more pertinent than this limited reference to dissociation is the court's central holding in *National Geographic* that:

> [T]he relevant constitutional test to establish the requisite nexus for requiring an out-of-state seller to collect and pay the use tax is not whether the duty to collect the use tax relates to the seller's activities carried on within the State, but simply whether the facts demonstrate "some definite link, some minimum connection, between the State and the person . . . it seeks to tax."

Id. at 561. *National Geographic* held that the presence of two California offices that solicited advertising sales for the company's magazine established the requisite taxing nexus to require the company to collect use tax on mail-order sales to California made by a different division of the company, despite the fact that the company's activities in California were not connected to and did not support those mail-order sales. The fact that in *National Geographic* taxing nexus was based on the totality of a company's in-state activities as opposed to only those activities directly connected to a particular sale, or particular line of business, is of greater relevance to our discussion than the tangential reference to dissociation.

The Taxpayer also asserts that Washington courts have "embraced dissociation," citing *B.F. Goodrich Co. v. State*, 38 Wn.2d 663, 231 P.2d 325 (1951) (Holding that sales made by an out-of-state manufacturer in Washington without aid or intervention of a Washington office were not subject to the tax, but that sales in any way channeled through local outlets were not entitled to immunities of interstate business.) It is significant that the single state case cited by the Taxpayer is more than 50 years old. As detailed above, the significant changes to nexus case law and analysis since then dramatically limit the utility and applicability of this analysis.

Similarly, the most recent departmental determination cited by the taxpayer is [nine] years old. Det. No. 94-209R, 15 WTD 100 (1996)(citing *Norton* and Rule 193 for the proposition that Alaska sales delivered to a Washington freight forwarder may be eligible for dissociation provided proof is provided that the customer relationship was derived from an exclusively independent source and that the Washington independent sales representatives were not involved "in any way" with the disputed sales). The provisions of Rule 193 still guide our analysis, and are addressed in detail below, but the reliance on *Norton*, is no longer persuasive.

<u>Dissociation Requirements under Rule 193:</u>

Rather than delving further into the evolution of dissociation, we will instead focus on the particular requirements for dissociation established by Rule 193 and the application of current case law addressing taxing nexus. For, as we stated in Det. No. 00-098, it is Rule 193 that controls dissociation analysis. Rule 193 provides that if a seller carries on significant activity sufficient to create nexus with this state, then the seller has the **distinct burden** of establishing that its in-state activities are not significantly associated ***in any way*** with the sales made into this state. Nexus for one sale is nexus for all sales unless some sales are specifically divorced from the activity which created the nexus. Det. No. 94-209, 15 WTD 96 (1994)(*citing* Det. No. 87-69, 2 WTD 347 (1987)).

The Taxpayer's dissociation analysis focuses on the physical location where sales are negotiated and places particular emphasis on the fact that interaction between the sales representative and customer occurs outside Washington. However, this emphasis on where particular sales are negotiated essentially inverts the dissociation analysis set forth by Rule 193. The question is not whether there is a direct link between the consummation of a particular sale and the Taxpayer's Washington activity but rather whether any of the Taxpayer's Washington activities are **in any way** associated with the sale. Dissociation requires proving that none of the Taxpayer's in-state activities are associated with, or contributed to, that sale.

The determination of whether in-state activities create nexus looks to the entire collection of a taxpayer's different activities, the totality of which creates substantial nexus. *GMC v. City of Seattle*, 107 Wn. App. 42, 25 P.3d 1022 (2001);[6] *see also General Motors Corp. v Washington,* 377 U.S. 436 (1964), *overruled on other grounds, Tyler Pipe Indus., Inc. v. Department of Rev.*, 483 U.S. 232, 250(1987) (Holding that it is the bundle of corporate activity that determines whether a taxpayer has nexus with a state); Rule 193 Thus, establishing taxing nexus requires consideration of the entire bundle of a taxpayer's in-state activities. Accordingly, establishing that a particular transaction may be dissociated requires proving a lack of association to **all** of the taxpayer's in-state activities that create substantial nexus.

Rule 193(7)(c) provides for dissociation where in-state activities "are not significantly associated in any way with the sales into this state." The rule does not define significantly associated activities, but nexus cases provide some guidance on what constitutes a significant activity. A significant activity is one performed by an agent or other representative. . . that establishes or maintains a market within this state. *See e.g.,* Det. No. 00-098 (*citing Chicago Bridge & Iron Co. v. Department of Rev., 98* Wn.2d 814, 822, 659 P.2d 463 (1983) ("[I]t is the corporation's burden to exempt itself from the local tax by showing no in-state activities were associated with the interstate business. . . . To meet this burden, a corporation must show that its in-state services were not

[6] In *GMC,* the Washington Court of Appeals recognized that it is the collective activities of a taxpayer within the state that may be used to support a finding of substantial nexus for B&O tax purposes. The court in *GMC* stated:

> In this case, both GM and Chrysler direct national advertising to the City of Seattle. They send sales, service, and parts managers to their dealers in Seattle on a monthly basis to discuss market conditions, new products, retail customer satisfaction levels, and the like. These representatives speak with dissatisfied customers and discuss problems that may be occurring with certain makes of automobiles. The representatives also train the dealers in sales and management techniques. Finally, the Seattle dealers actively market the automakers' warranties that accompany the sale of an automobile and make service repairs at the dealerships in Seattle on behalf of the automakers. These warranties serve an important marketing function because customers are unlikely to purchase a new vehicle without a warranty.
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> . . .
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> We are satisfied that in this case, **the collective activities** of each automaker are strategically designed to maximize their sales within the City and that the absence of these activities would significantly affect their ability to maintain a share of the Seattle market. Without these activities, their name recognition, goodwill, ability to obtain market data, customer feedback, and trends unique to Seattle, and their ability to compete with other automakers would be adversely impacted. We hold that substantial nexus exists to justify the City's imposition of its business and occupation tax upon the automakers. (Bolding added.)

GMC v. City of Seattle, 107 Wn. App. at *13 -17.*

decisive in establishing and holding the market ") In addition, the representative's activity does not have to be the most important factor. Instead, "the crucial factor governing nexus is whether the activities performed in this state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales." *Tyler Pipe Indus., Inc. v. Department of Rev.*, 483 U.S. 232, 250 (1987). So, significant activities are ones that establish or maintain a market for the taxpayer's products. Therefore, to be eligible for dissociation, a sale must not be in any way associated with any of the taxpayer's in-state activities that establish or maintain a market for its products.

The Taxpayer's dissociation argument, consistent with the older *Norton* based approach, focuses on procedural aspects of the sales process. This focus logically directs the Taxpayer to emphasize where its sales representatives and agents serve their customers. While this information remains pertinent to establishing dissociation, it is not the only factor at issue. Taxpayer's in-state activities that support and maintain a market for its products are not limited to the activities of sales representatives. Before addressing the particular sales at issue in the refund claim, we must first consider the full range of the Taxpayer's Washington activities that support and maintain a market for its products. For the Taxpayer to sustain its burden to dissociate, it must dissociate the sales at issue from the all of its in-state activities that support or maintain a market for its products.

The physical presence of the Taxpayer's employee sales representatives and third party sales and promotions agents in Washington unequivocally establishes taxing nexus. Rule 193(7)(iii)(iv). The activity of these employees and agents supports and maintains a market for the Taxpayer's products in Washington. The work of these employees is supported and enhanced by the Taxpayer's broader advertising and promotion activities discussed below. Dissociation is not restricted to consideration of the physical location and conduct of a specific sales representative who consummates a particular sale, but must also encompass consideration of all of the activities undertaken by the Taxpayer within Washington to establish and maintain a market for its products in Washington. For, in addition to the activities of its sales representatives and agents, the Taxpayer also engages in significant consumer marketing efforts.

The products at issue in this [determination] are [predominantly] brand name commercial goods. The Taxpayer expends considerable resources and effort to develop, maintain, protect, and promote its brand names and to establish a good reputation for its products. The activities of the sales representative and those directed towards consumers are interrelated and focus in large part on supporting and enhancing the brand name. The Taxpayer's promotional and advertising activities in or reaching into this state in support of its products are extensive in scope and reach. It uses traditional means of advertising such as television commercials, print advertisements in magazines and newspapers, coupon offers, and promotional distributions. The Taxpayer enhances this traditional advertising with an internet site . . . . The site contains information about the different product lines and brands, as well as the company. There is also an online store where customers can purchase products. Alternatively, customers can search on-line for local retail stores that carry particular products. In addition to broad based brand name advertising and promotion, the Taxpayer has also participated in trade shows in Washington, discussed in greater detail below, that target sales of specific commercial product lines. All of these activities reach Washington consumers and are undertaken for the purpose of encouraging current consumers to continue their purchasing habits and to solicit new consumers. Consumer focused promotion activities are supplemented by marketing and sales activities directed at the Taxpayer's customers.[7] These activities are clearly undertaken to establish, maintain and enhance the market for the Taxpayer's products, and we find that they are all significant in supporting sales.

Having addressed the general principles and necessary elements to support dissociation of sales, we now turn to consideration of the particular sales the Taxpayer is seeking to dissociate. We will address each of the product lines/sales groups in turn.

National Sales by the [A] Group:
The majority of these sales are sales of brand name products, and they are the same products that are sold by the Taxpayer's in-state employees to local and regional stores (such as [Store R] and [Company J Division]). While the customers are served by different sales representatives and different promotional agents, the Taxpayer's efforts to serve its wholesale customers are not the only activities at issue. To maintain its Washington market, the Taxpayer does not only focus on serving and supporting the retailer but also directs resources to develop and maintain a consumer base. In order to dissociate for B&O tax purposes, a taxpayer must dissociate the particular sale from the total collection of its Washington activities, and for its brand name products these activities include its advertising and promotional activities in addition to the work of its in-state sales representatives and agents. For example, Taxpayer must dissociate its national advertising campaigns from sales of its products promoted by those campaigns within the state of Washington.[8]

For, as noted above, under Rule 193 dissociation is not just a question of segregating the activities of specific sales representatives but rather of establishing that a sale negotiated out-of-state is not **in any way** associated with the Taxpayer's collective in-state activities that maintain a market for that product.

It is not possible to delineate the influence of brand name advertising and promotional efforts. In Det. No. 00-098, we disallowed dissociation of computer sales because the nexus-creating activity of having local warranty repair agents prevented the company from dissociating sales of the same brand of products.[9] Similarly, here the Taxpayer's in-state activity supports the sale of

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[7] Such as the efforts and work of the sales representatives, third-party brokers, and promotions agents detailed in the fact section.

[8] *But see,* Det. No. 96-144, 16 WTD 201 (1996); Det. No. 93-155, 13 WTD 297 (1994); Det. No. 91-279, 11 WTD 273 (1991); Det. No. 91-213, 11 WTD 239 (1991) (suggesting that dissociation might be allowed if the in-state activity related to the sale was limited **solely** to national advertising). We note that in the present case the Taxpayer's in-state activities are not limited solely to national advertising and so these cases are distinguishable. Furthermore, as discussed in detail above, these determinations rely primarily on *Norton,* which is not binding authority. Det. No. 00-098, 22 WTD 153 (2003).

[9] In that case we stated:

> The simple fact that some customers chose to use the service centers rather than mail in their products for repair supports our conclusion upholding the Audit division's assessment. The services performed by the independently operated service centers cannot be separated from the taxpayer's ability to establish and

all of its brand name products sold in Washington. For example, the Taxpayer engages in activities in Washington to create, maintain, and expand the market for [product]. These include the targeted efforts of its in-state sales representatives and marketing agents, national and regional advertising through a variety of media, on-line marketing, and local promotional activities. The fact that a sales contract between the Taxpayer with a particular retailer, store X, to sell [product] at its Washington branches was negotiated outside of Washington is insufficient to establish dissociation of those sales.[10] It is not possible to say that the Taxpayer's in-state activities did not in any way contribute to the sale of [product] at store X's Washington branches. We therefore find that dissociation will not be allowed for any brand name products and product lines that are supported by any of the Taxpayer's marketing and promotion activities in Washington. . . .

[B Group] Sales

To the extent that these sales involve the sales of brand name products the foregoing rationale applies and dissociation of those sales is disallowed. The Taxpayer's in-state activities to support and maintain sales of [B Group] brand name products, whether directed towards consumers or customers, help establish and maintain a market for all Washington [B Group] brand name sales. The Taxpayer's [B Group] web site includes repeated references to their brand recognition and consumer confidence in their products. . . .

As with the national retail sales, the Taxpayer employed a [B Group] broker who resided in Washington and also engaged in general marketing and promotion activities in Washington.

We find that these in-state activities in conjunction with marketing and advertising its brand names served to establish and maintain a market for all [B Group] brand name sales into Washington precluding dissociation. For, just as the collective brand name marketing and sales efforts of the taxpayer support sales to both retailers who are served by in-state sales representatives and those served by out-of-state sales representatives, the in-state support of these brand names also maintains a market for brand name sales made by the [B Group]. Again, for dissociation the Taxpayer must isolate a particular sales transaction from any association of in-state activities. For brand name products that includes not only specific [B Group] customer

maintain a market in Washington. The sales of all of taxpayer's electronic equipment through both its regional accounts and national accounts were subject to wholesaling B&O tax. . . .

It is not necessary for the warranty service centers to service any or all of the computer hardware sold by the taxpayer for a significant association to exist between the presence of the service centers and the sales of computer hardware. Computer hardware is not so dissimilar from electronic goods to erase any linkage consumers might make with the taxpayer's name and products. Servicing of other electronic goods helps establish and maintain a market and good reputation for computer hardware sold by the Computer Division. Therefore, we conclude that taxpayer's sales of computers and computer monitors into the state may not be dissociated either prior to September, 1995 or thereafter.

[10] While the accounts may be served by different sales representatives, the Taxpayer's efforts in Washington to promote the sale of a particular brand of [product] at a [store] through the actions of its in-state employees and advertising and promotion will also promote sales of that same brand of [product] at other retail outlets such as . . . even though the sales representative for those accounts works exclusively outside Washington.

and consumer activities but any in-state activities that maintain a market for that brand name product.

Additionally, we find that Taxpayer promotion of [B Group] sales at local trade shows also served to help establish and maintain a market for these products and constitutes significant in-state activities preventing dissociation. The Taxpayer emphasizes that the Washington trade shows are national or regional meetings and events, which are regularly scheduled at various locations throughout the country. The Taxpayer asserts that its participation at such shows is not directed at supporting or maintaining Washington sales in particular. This argument again focuses on the consummation of the sale as the pivotal activity at issue. However, the fact that a particular [B Group] order may have ultimately been concluded by phone or mail from [another state] is insufficient to establish dissociation of that sale. As discussed in detail above, the pertinent inquiry is not limited to where negotiation for a sale is ultimately concluded but whether any of the Taxpayer's in-state activities (such as trade show participation, efforts of its in-state [B Group] [broker], and other advertising or marketing efforts) were undertaken to establish or maintain a market for [B Group] products. We therefore conclude that the trade show promotional efforts were significant and prevent dissociation of any [B Group] products marketed or sold at those trade shows. . . .

<u>[C Group] sales</u>:

As described by the Taxpayer, the products sold by the [C Group] agents exclusively involve brand name products. The Taxpayer's claim for dissociation on these brand name products is denied.

DECISION AND DISPOSITION

The Taxpayer's petition is denied for dissociation of any brand name products.

Dated this 31st day of August 2004.

APPENDIX B

State Taxation ¶ 19.02
*1 State Taxation: Third Edition
Current Through 2015
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Part V. Sales and Use Taxes
Chapter 19. Collection of Sales or Use Taxes by the Seller

¶ 19.02 CONSTITUTIONAL RESTRICTIONS ON STATES' POWER TO IMPOSE, AND REQUIRE VENDOR COLLECTION OF, SALES AND USE TAXES ON GOODS SOLD IN INTERSTATE COMMERCE

The U.S Supreme Court established the basic analytical framework governing the states' power to impose and collect sales and use taxes on goods sold in interstate commerce in two cases— *McLeod v. JE Dilworth Co.*[8] and *General Trading Co. v. State Tax Commission*[9] —decided on same day in 1944. *McLeod* involved a challenge to an Arkansas *sales* tax on goods shipped from Tennessee; *General Trading* involved an Iowa *use* tax on goods shipped from Minnesota. The facts of the two cases were substantially the same.

In *McLeod*, the sellers were Tennessee corporations engaged in selling machinery and mill supplies from their places of business in Memphis to purchasers in Arkansas. The sellers had no offices or places of business in Arkansas. The sellers solicited orders from Arkansas by traveling sales representatives who resided in Tennessee or by mail and telephone. The sellers accepted the orders in Tennessee, from which they shipped the goods to Arkansas. Title to the machinery and supplies passed to the purchaser on delivery of the goods to the carrier in Memphis. The sellers collected payment for the orders outside of Arkansas. As the Court summarized the facts, "we are here concerned with sales made by Tennessee vendors that are consummated in Tennessee for the delivery of goods in Arkansas."[10]

In a five-to-four decision, the U.S. Supreme Court held that the Commerce Clause prevented Arkansas from imposing a sales tax on the transaction.[11] Justice Frankfurter, who wrote the majority opinion, stated that "[f]or Arkansas to impose a tax on such transaction would be to project its powers beyond its boundaries and to tax an interstate transaction."[12] The Court distinguished *Berwind-White*[13] on the grounds that the seller in that case "maintained its sales office in New York City, took its contracts in New York City and made actual delivery in New York City."[14]

In *General Trading*, a Minnesota-based vendor sold its products in Iowa through traveling solicitors. Like the Tennessee corporations in the *McLeod* case, the Minnesota company had no place of business, employees, or property in the purchasers' state. Its activities in Iowa were in all relevant respects identical to those of the Tennessee companies in Arkansas. As indicated above, the only material difference between the two cases was that Iowa imposed a *use* tax, which it sought to require the Minnesota vendors to collect, whereas Arkansas imposed a *sales* tax, which it sought to have the Tennessee vendors collect. The Court found that difference to be crucial, and it unanimously sustained the Iowa assessment.[15]

*2 The Court justified its holding on the following grounds:

> The tax is what it professes to be—a non-discriminatory excise laid on all personal property consumed in Iowa. The property is enjoyed by an Iowa resident partly because the opportunity is given by Iowa to enjoy property no matter whence acquired. The exaction is made against the ultimate consumer—the Iowa resident who is paying taxes to sustain his own state government. To make the distributor the tax collector for the State is a familiar and sanctioned device.[16]

Justice Rutledge, who concurred in the Iowa decision but dissented from the Arkansas holding, put the issue before the Court as follows:

Vendor to Collect Use Tax: *National Geographic*

The National Geographic Society, a District of Columbia corporation, made substantial mail-order sales of maps, atlases, globes, and books to California residents who responded to its magazine and direct mail solicitations.[151] National Geographic also maintained two offices in California that solicited advertising for its magazine, but it conducted no activities relating to its mail-order business at those offices. California assessed a use tax against National Geographic on its mail-order sales to California customers.[152] The California Supreme Court sustained the state's position, reasoning that the "slightest presence" of the seller within the state established a sufficient nexus to require the seller to collect use tax. Although the U.S. Supreme Court affirmed, it disavowed the state court's "slightest presence" test, stating:

> Our affirmance of the California Supreme Court is not to be understood as implying agreement with that court's "slightest presence" standard of constitutional nexus. Appellant's maintenance of two offices in the State and solicitation by employees assigned to those offices of advertising copy in the range of one million dollars annually, establish a much more substantial presence than the expression "slightest presence" connotes. Our affirmance thus rests upon our conclusion that appellant's maintenance of the two offices in California and activities there adequately establish a relationship or "nexus" between the Society and the State that renders constitutional the obligations imposed upon appellant.[153]

*22 In response to National Geographic's contention that the case was controlled by *Bellas Hess*, the Court said that its opinion in that case had

> carefully underscored... the "sharp distinction... between mail order sellers with retail outlets, solicitors, or property within [the taxing] State, and those [like Bellas Hess] who do no more than communicate with customers in the State by mail or common carrier as part of a general interstate business." Appellant Society clearly falls into the former category.[154]

The Court also rejected National Geographic's argument that the two California offices should be disregarded for purposes of determining whether the requisite nexus existed, because such offices played no role with respect to the mail-order sales at issue:

> The Society argues in other words that there must exist a nexus or relationship not only between the seller and the taxing State, but also between the activity of the seller sought to be taxed and the seller's activity within the State. We disagree. However fatal to a direct tax a "showing that particular transactions are dissociated from the local business...," *Norton Co. v. Department of Revenue, supra,* 340 U.S. 534, 537 (1951),... such dissociation does not bar the imposition of the use tax collection duty.... [T]he relevant constitutional test to establish the requisite nexus for requiring an out-of-state seller to collect and pay the use tax is not whether the duty to collect the use tax relates to the seller's activities carried on within the State, but simply whether the facts demonstrate "some definite link, some minimum connection, between [the State and] the *person*... it seeks to tax." *Miller Bros. v. Maryland*, 347 U.S., 340, at 344-345 (1954) (emphasis supplied).[155]

¶ 19.02[3][b][i] The questionable continuing force of *Norton v. Department of Revenue* [new].

Although the Court in *National Geographic* reached the correct result as a matter of contemporary Due Process and Commerce Clause jurisprudence, the Court's opinion in the case introduced needless uncertainty into the law of state tax jurisdiction by adverting to the formal distinction between a "direct tax" and "the imposition of a use tax collection duty." The *Norton* decision cited by the Court addressed the imposition of an Illinois occupation tax "upon persons engaged in the business of selling tangible personal property at retail in this State."[155.1] The tax was measured by gross receipts. The taxpayer's receipts included those from sales orders placed by buyers directly with the taxpayer's out-of-state headquarters and filled by shipment directly to the buyers. The taxpayer also maintained a Chicago place of business that made retail sales and in some instances facilitated the placement and delivery of home office orders. The Court held that sales either made or facilitated by the Chicago place of business were sufficiently local to be subject to the Illinois tax, but that the direct sales from the home office to Illinois customers were "so clearly interstate in character"[155.2] and "dissociated from the local business"[155.3] that they enjoyed the then-prevailing immunity from direct taxation of interstate commerce.[155.4] The Court distinguished cases involving "sales and use tax[es]" because "the impact of those taxes is on the local buyer or user," whereas "this tax falls on the vendor."[155.5] In so doing, the Court echoed the view, also prevailing at the time, that imposing a use tax collection obligation on an interstate seller was permissible, although imposing a sales tax directly on the seller violated the prohibition against state taxation of interstate commerce.[155.6]

*23 *Norton*, however, was rendered obsolete by *Complete Auto Transit, Inc. v. Brady*,[155.7] which the Court decided just three weeks prior to *National Geographic*. In *Complete Auto*, the Court "rejected the line of cases holding that the direct taxation of interstate commerce was impermissible,"[155.8] as well as the "formal distinction between 'direct' and 'indirect' taxes on interstate commerce, because that formalism allowed the validity of statutes to hinge on 'legal terminology,' 'draftsmanship' and 'phraseology.'"[155.9] The Court "adopted instead a 'consistent and rational' method of inquiry [that focused on] the *practical effect* of [the] challenged tax."[155.10]

Indeed, if there were any doubt about this point, the Court reaffirmed it more recently in *Comptroller of the Treasury v. Wynne*.[155.11] In *Wynne*, the Court relied heavily on three gross receipts tax cases[155.12] in concluding that portions of Maryland's personal net income tax regime violated the Commerce Clause.[155.13] In response to Justice Ginsburg's claim in dissent that the Court had traditionally distinguished between gross receipts and net income taxes, the Court rejected the claim as inconsistent with its contemporary approach to state taxation under the Commerce Clause: "We see no reason why the distinction between gross receipts and net income should matter, particularly in light of the admonition that we must consider 'not the formal language of the tax statute but rather its practical effect.'"[155.14] In the Court's view, "the discarded distinction between taxes on gross receipts and net income was based on the notion, endorsed in some early cases, that a tax on gross receipts is an impermissible 'direct and immediate burden' on interstate commerce, whereas a tax on net income is merely an 'indirect and incidental' burden."[155.15]

In fairness to the Court in *National Geographic*, its decision did not actually apply the Court's observation about "direct taxes," because it was sufficient for the Court to reject the taxpayer's argument regarding "disassociated" activity by its conclusion that a use tax collection obligation was distinguishable from a "direct tax." In any event, any lingering notion that a "direct" tax obligation enjoys greater dormant Commerce Clause protection than an "indirect" use tax collection obligation was turned on its head by the Court's decision in *Quill Corp. v. North Dakota*.[155.16] Relying in part on the doctrine of *stare decisis*, but also on an examination of the "practical effect of [the] challenged tax,"[155.17] which included the burden of complying with "'many variations in rates, in allowable exemptions, and in administrative and record-keeping requirements,'"[155.18] the Court preserved a physical-presence nexus standard for use tax collection obligations, while at the same time implying that physical presence may not be required for "other types of taxes," many of which are direct taxes.[155.19] Indeed, judicial and administrative decisions across the country have overwhelmingly supported the view that *Quill*'s physical-presence test does not extend to direct taxes such as income and gross receipts taxes.[155.20] These authorities have held that physical presence—whether "dissociated" or not from the subject matter of these taxes—is not required to establish nexus under the Commerce Clause.

*24 A Washington appellate court considered the precedential value of the *Norton* decision in a case involving Washington's Business and Occupation (B&O) tax.[155.21] The taxpayer (Avnet) was an Arizona-based distributor of electronic components that maintained an office in Washington with over forty employees serving customers in Washington and eastern Idaho, where they conducted various marketing and product development activities. Some of Avnet's sales, denominated "national sales" and "drop-shipped" sales, resulted from orders placed with Avnet sales offices outside of Washington. These orders were filled from out-of-state inventory which was shipped directly to the customer (or, in the case of drop-shipped sales, to the Washington customers of Avnet's customers). The Washington office had no direct involvement with those sales.[155.22] Avnet took the position that these sales were not subject to B&O tax, because, among other reasons, "the dormant Commerce Clause allows Avnet to 'dissociate' its Washington-bound national and drop-shipped sales by showing that its instate personnel played no significant roles in these transactions," contending that *Norton* "control[s] and... impose[s] such a requirement."[155.23]

The court disagreed, and we reproduce an extended excerpt of the court's analysis, because it cogently distills the reasons (reflected in the foregoing discussion) for questioning the continuing force of *Norton*:

> As an initial matter, we note that *Norton*'s foundations have been eroded by subsequent precedent. For example, the *Norton* Court based its conclusion in part on a then-prevailing view that
>
> [w]here a corporation chooses to stay at home in all respects except to send abroad advertising or drummers to solicit orders which are sent directly to the home office for acceptance, filling, and delivery back to the buyer, it is obvious that the State of the buyer has no local grip on the seller.

The Court has long since rejected that view. The *Norton* Court's reasoning also relied on the "immunity" from state taxation that interstate commerce then enjoyed. The Court soundly rejected this immunity in *Complete Auto Transit*, expressly overruling precedents to the contrary. Thus, the United States Supreme Court has explicitly removed at least two of *Norton*'s chief doctrinal underpinnings.

More to the point, the Department is correct that subsequent precedents have expanded the range of activities relevant to the substantial nexus analysis. In *General Motors*, the company challenged imposition of the B&O tax on various transactions, including sales of parts to independent dealers in Washington, which orders were placed with and filled from its Portland, Oregon office. The *General Motors* Court declined to look at particular transactions in isolation, instead considering whether General Motors could show that "the bundle of corporate activity" in Washington was not a "decisive factor[ ] in establishing and holding" the market for its goods here, and concluding that it could not.

***25** In *Tyler Pipe Industries*, the Court found sufficient nexus for imposition of B&O tax on all of Tyler Pipe's sales into Washington

> even though it maintains no office, owns no property, and has no employees residing in the State... [and i]ts solicitation of business in Washington is directed by executives who maintain their offices out-of-state and by an independent contractor located in Seattle.

The Court agreed with our Supreme Court that "'the crucial factor governing nexus is whether the activities performed in this state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales."' *Tyler Pipe*, 483 U.S. at 250, 107 S.Ct. 2810 (quoting *Tyler Pipe Indus., Inc. v. Dep't of Revenue*, 105 Wash.2d 318, 323, 715 P.2d 123 (1986)). Significantly, in the portion of its opinion affirmed by the United States Supreme Court, our Supreme Court rejected an argument very similar to Avnet's, that the portion of Tyler Pipe's sales attributable to orders placed directly with its main office were exempt from tax.

These precedents show a progressive broadening of the types of activities that may establish substantial nexus for purposes of state taxation of interstate commerce. They show that a state need not demonstrate a direct connection between a taxpayer's nexus-creating activities and particular sales into the state in order to tax those sales.[155.24]

¶ 19.02[3][c] Reaffirmation of *Bellas Hess*'s Bright-Line Physical-Presence Rule of Nexus for Use Tax Collection Duty: *Quill*

In *Quill Corp. v. North Dakota*,[156] the U.S. Supreme Court reaffirmed the rule of *Bellas Hess* and held that the Commerce Clause bars a state from imposing a use tax collection duty on an out-of-state seller with no physical presence in the state. The facts in *Quill* were in all essential respects identical to those in *Bellas Hess*. Quill Corporation was an Illinois-based vendor of office equipment and supplies. It had neither outlets nor sales representatives in North Dakota, and all of its contacts with the state were via mail, telephone, or common carrier. Quill solicited orders in North Dakota through catalogs and flyers, advertisements in national periodicals, and telephone calls. All of the orders were accepted outside North Dakota and were filled by shipment, via mail or common carrier, from out-of-state locations. Quill's sales to North Dakota customers were substantial, amounting to nearly $1 million per year, making Quill the sixth largest vendor of office supplies in the state. Despite its lack of physical presence in the state, Quill was required to collect North Dakota's use tax on goods purchased for use in North Dakota, because the requirement was imposed on any retailer engaging in "regular or systematic solicitation of a consumer market in th[e] state,"[157] which included three or more advertisements within a twelve-month period.

¶ 19.02[3][c][i] The North Dakota Supreme Court's opinion.

***26** Notwithstanding *Bellas Hess*, the North Dakota Supreme Court sustained the levy, justifying its disregard of *Bellas Hess* on two grounds. First, it reasoned that the "economic, social, and commercial landscape upon which *Bellas Hess* was premised no longer exists."[158] The court pointed to the growth of the mail-order business "from a relatively inconsequential market niche" in 1967 to a "goliath" with annual sales of close to $200 billion in 1989.[159] The court also observed that

for a state's compliance with the requirements of due process in this area are similar. *See Central R. Co. v. Pennsylvania*, 370 U.S. 607, 621–622 (concurring opinion of Mr. Justice Black). As to the former, the Court has held that "State taxation falling on interstate commerce... can only be justified as designed to make such commerce bear a fair share of the cost of the local government whose protection it enjoys." *Freeman v. Hewit*, 329 U.S. 249, 253. *See also Greyhound Lines v. Mealey*, 334 U.S. 653, 663; *Northwestern Cement Co. v. Minnesota*, 358 U.S. 450, 462. And in determining whether a state tax falls within the confines of the Due Process Clause, the Court has said that the "simple but controlling question is whether the state has given anything for which it can ask return." *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444. *See also Standard Oil Co. v. Peck*, 342 U.S. 382; *Ott v. Mississippi Barge Line*, 336 U.S. 169, 174. The same principles have been held applicable in determining the power of a state to impose the burdens of collecting use taxes upon interstate sales. Here, too, the Constitution requires "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 344–345; *Scripto, Inc. v. Carson*, 362 U.S. 207, 210–211. *See also American Oil Co. v. Neill*, 380 U.S. 451, 458.
Bellas Hess, 386 US 756–757, 87 S. Ct. 1389 (1967). These comments must now be read in light of the Court's opinion in Quill Corp. v. North Dakota, 504 US 298, 112 S. Ct. 1904 (1992), discussed infra ¶ 19.02[3][c], which distinguished between Due Process Clause nexus and Commerce Clause nexus.

146 *Miller Bros.*, 347 US 340, 344–345, 74 S. Ct. 535 (1954).

147 *Bellas Hess*, 386 US 753, 758, 87 S. Ct. 1389 (1967).

148 *Bellas Hess*, 386 US 753, 759–760, 87 S. Ct. 1389 (1967) (footnotes omitted).

149 *Bellas Hess*, 386 US 753, 760, 87 S. Ct. 1389 (1967).

150 *Bellas Hess*, 386 US 753, 761–763, 87 S. Ct. 1389 (1967) (Fortas, J., dissenting) (footnotes omitted). See generally S. McCray, "Overturning *Bellas Hess*: Due Process Considerations," 1985 BYUL Rev. 265; S. McCray, "Commerce Clause Sanctions Against Taxation on Mail Order Sales: A Re-evaluation," 17 Urb. Law 529 (1985); D. Simet, "The Concept of 'Nexus' and State Use and Unapportioned Gross Receipts Taxes," 73 NW UL Rev. 112 (1978).

151 National Geographic Soc'y v. State Bd. of Equalization, 430 US 551, 97 S. Ct. 1386 (1977).

152 California, like most states, makes a retailer liable to the state for any sales or use taxes it is required to collect, whether or not it collects the tax. Cal. Rev. & Tax. Code § 6204 (Westlaw 2012).

153 *National Geographic*, 430 US 551, 556, 97 S. Ct. 1386 (1977) (citation omitted).

154 *National Geographic*, 430 US 551, 559, 97 S. Ct. 1386 (1977).

155 *National Geographic*, 430 US 551, 560, 97 S. Ct. 1386 (1977). See Rev. Rul. 05-25, Tenn. Dep't of Revenue, Dec. 19, 2005, available at www.checkpoint.thomsonreuters.com (one in-state employee working from home using employee-owned equipment creates substantial nexus even if employee did not contribute to Tennessee sales, citing *National Geographic*); Ltr. 200611818L, Tex. Comp. of Pub. Acc'ts, Nov. 16, 2006, available at www.checkpoint.thomsonreuters.com (out-of-state web-page producer had substantial nexus with Texas by reason of the presence of two in-state employees who worked from their homes, notwithstanding that these employees performed no work for the company's Texas customers). In an administrative decision that completely disregards the *National Geographic* rule, the Indiana Department of Revenue held that an out-of-state taxpayer did not have taxable nexus with Indiana because the taxpayer's in-state employees (who worked out of their homes) were sales staff and technical advisors who served "regional, non-Indiana clients and do not engage in selling to Indiana customers." Letter of Finding 09-0939, Ind. Dep't. of State Revenue, Apr. 26, 2010, available at www.checkpoint.thomsonreuters.com.

155.1 Norton Co. v. Department of Revenue, 340 US 534, 535, 71 S. Ct. 377 (1951) (quoting the statute).

155.2 Norton Co. v. Department of Revenue, 340 US 534, 539, 71 S. Ct. 377 (1951).

155.3 Norton Co. v. Department of Revenue, 340 US 534, 537, 71 S. Ct. 377 (1951).

155.4 Norton Co. v. Department of Revenue, 340 US 534, 539, 71 S. Ct. 377 (1951).

155.5 Norton Co. v. Department of Revenue, 340 US 534, 537, 71 S. Ct. 377 (1951). The Court seems to have assumed that the legal incidence of a sales tax necessarily fell on the buyer, which is not always the case. Indeed, the Illinois tax at issue in *Norton* was, in substance, a retail sales tax, whose legal incidence fell on the seller. See ¶ 12.01. For the purposes of our analysis here, we assume that the Court was making a distinction between taxes whose legal incidence falls on the seller and taxes whose legal incidence falls on the buyer, regardless of nomenclature.

155.6 As we describe supra ¶¶ 19.01 and 19.02, at a time when the Commerce Clause was interpreted "to create an area of [tax] free trade among the several States," McLeod v. JE Dilworth Co., 322 US 327, 330, 64 S. Ct. 1023 (1944), the Court held that an Arkansas tax imposed on sales by a Tennessee seller to Arkansas buyers violated the Commerce Clause, while an Iowa tax on the use of goods sold by a Minnesota seller to Iowa buyers was constitutional, as was the associated vendor collection obligation. McLeod v. JE Dilworth Co., 322 US 327, 64 S. Ct. 1023 (1944) (holding sales tax on interstate sales unconstitutional); General Trading Co. v. State Tax Comm'n, 322 US 335, 64 S. Ct. 1028 (1944) (holding use tax and associated use-tax-collection obligation imposed on out-of-state seller constitutional). The Court reasoned that to tax a cross-border "sale" is to tax interstate commerce, which lay beyond the state's taxing power, whereas a use tax was imposed on a "local" event over which the state had well-recognized authority. As for imposing a use tax collection obligation on the out-of-state seller, the Court said in *General Trading* that "[t]o make the distributor the tax collector of the tax obligation for the State is a familiar and sanctioned device." General Trading Co. v. State Tax Comm'n, 322 US 335, 338, 64 S. Ct. 1028 (1944). If contemporary Commerce Clause analysis had been applicable at the time states were adopting sales and use taxes, this "triumph of formalism" would not have been necessary, and a properly drawn sales tax statute (which would require, among other things, a credit for any taxes paid to the state in which the sale originates) would have brought most interstate sales within the states' constitutional reach. Complete Auto Transit v. Brady, 430 US 274, 281, 97 S. Ct. 1076 (1977). See ¶¶ 4.07–4.12 for a discussion of the historical development of state tax dormant Commerce Clause doctrine. That said, most states continue to adhere to the dichotomy established in *McLeod* and *General Trading* and impose sales tax on intrastate sellers while imposing use tax (and an associated vendor collection obligation) on purchases from out-of-state sellers. See generally J. Swain, "The Sales and Use Tax Dichotomy and the Streamlining Movement," State Tax Notes, Jan. 15, 2007, p. 129.

155.7 Complete Auto Transit, Inc. v. Brady, 430 US 274, 97 S. Ct. 1076 (1977).

155.8 Quill Corp. v. North Dakota, 504 US 298, 303, 112 S. Ct. 1904 (1992).

155.9 Quill Corp. v. North Dakota, 504 US 298, 310, 112 S. Ct. 1904 (1992) (quoting Complete Auto Transit, Inc. v. Brady, 430 US 274, 281, 97 S. Ct. 1076 (1977).

155.10 Quill Corp. v. North Dakota, 504 US 298, 304, 112 S. Ct. 1904 (1992) (quoting Mobil Oil Corp. v. Commissioner of Taxes, 445 US 425, 443, 100 S. Ct. 1223 (1980) (emphasis supplied).

155.11 Comptroller of the Treasury v. Wynne, 575 US ___, 135 S. Ct. 1787 (2015).

155.12 JD Adams Mfg. Co. v. Storen, 304 US 307, 58 S. Ct. 546 (1938), Gwin, White & Prince, Inc. v. Henneford, 305 US 434, 59 S. Ct. 325 (1939), and Central Greyhound Lines, Inc. v. Mealey, 334 US 653, 68 S. Ct. 1260 (1948).

155.13 We provide a detailed analysis of various aspects of the Court's opinion in *Wynne* elsewhere in this treatise. See ¶¶ 4.16[1][a][vii] (*Wynne* and internal consistency, in general); 4.16[1][b] (tax credits as a remedy for an internally inconsistent statute); 4.16[1][d][v] (tax regimes containing insufficiently protective credits); 4.16[1][e] (evaluation of the internal consistency doctrine); 8.02[1] (the constitutional right to the division of the tax base); 8.02[1][a] (the implications of *Wynne v. Comptroller of the Treasury* on the Court's multiple taxation doctrine); 20.10 [2][b] (constitutional restraints on the denial by a taxpayer's state of residence of a credit for personal income taxes paid to other states). See also W. Hellerstein, "Deciphering the Supreme Court's Opinion in *Wynne*," 123 J. Tax'n 4 (2015).

155.14 Comptroller of the Treasury v. Wynne, 575 US ___, ___, 135 S. Ct. 1787 (2015) (citation omitted).

155.15 Comptroller of the Treasury v. Wynne, 575 US ___, ___, 135 S. Ct. 1787 (2015) (citation omitted).

155.16 Quill Corp. v. North Dakota, 504 US 298, 112 S. Ct. 1904 (1992).

155.17 Quill Corp. v. North Dakota, 504 US 298, 304, 112 S. Ct. 1904 (1992) (quoting Mobil Oil Corp. v. Commissioner of Taxes, 445 US 425, 443, 100 S. Ct. 1223 (1980)).

155.18 Quill Corp. v. North Dakota, 504 US 298, 313 n.6, 112 S. Ct. 1904 (1992) (quoting National Bellas Hess, Inc. v. Department of Revenue, 386 US 753, 759–760, 87 S. Ct. 1389 (1967)).

155.19 Quill Corp. v. North Dakota, 504 US 298, 314, 112 S. Ct. 1904 (1992).

155.20 See ¶¶ 6.03[2], 6.11.

155.21 Avnet v. State, Dep't of Revenue, 187 Wash. App. 427, 348 P3d 1273 (2015).

155.22 Avnet v. State, Dep't of Revenue, 187 Wash. App. 427, 348 P3d 1273, 1274–1275 (2015).

155.23 Avnet v. State, Dep't of Revenue, 187 Wash. App. 427, 348 P3d 1273, 1280–1281 (2015).

155.24 Avnet v. State, Dep't of Revenue, 187 Wash. App. 427, 348 P3d 1273, 1281–1282 (2015) (some citations omitted). See also Tax Comm'r v. MBNA Am. Bank, N.A., 220 W. Va. 163, 640 SE2d 226, 235 (2006), cert. denied, 551 US 1141, 127 S. Ct. 2997 (2007) (dismissing *National Geographic* allusion to *Norton* rule as dictum).

156 Quill Corp. v. North Dakota, 504 US 298, 112 S. Ct. 1904 (1992).

157 *Quill*, 504 US 298, 302–303, 112 S. Ct. 1904 (1992) (quoting the North Dakota statute).

158 State v. Quill Corp., 470 NW2d 203, 208 (ND 1991).

159 *Quill Corp.*, 470 NW2d 203, 208 (ND 1991).

160 *Quill Corp.*, 470 NW2d 203, 215 (ND 1991).

161 *Quill Corp.*, 470 NW2d 203, 209 (ND 1991).

162 Complete Auto Transit, Inc. v. Brady, 430 US 274, 97 S. Ct. 1076 (1977).

163 *Quill Corp.*, 470 NW2d 203, 216 (ND 1991).

164 *Quill Corp.*, 470 NW2d 203, 218 (ND 1991).

165 *Quill Corp.*, 470 NW2d 203, 219 (ND 1991).

166 See supra ¶ 19.02[3][a]; see also Trinova Corp. v. Michigan Dep't of Treasury, 498 US 358, 373, 111 S. Ct. 818 (1991) (Commerce Clause nexus requirement "encompasses as well the Due Process requirement that there be 'a "minimal connection between the interstate activities and the taxing State"'").

167 Quill Corp. v. North Dakota, 504 US 298, 305, 112 S. Ct. 1904 (1992).

168 *Quill*, 504 US 298, 312, 112 S. Ct. 1904 (1992).

169 *Quill*, 504 US 298, 312, 112 S. Ct. 1904 (1992).

170 *Quill*, 504 US 298, 312, 112 S. Ct. 1904 (1992).

171 *Quill*, 504 US 298, 312, 112 S. Ct. 1904 (1992).

172 *Quill*, 504 US 298, 307, 112 S. Ct. 1904 (1992) (quoting International Shoe Co. v. Washington, 326 US 310, 316, 66 S. Ct. 154 (1945)).

173 *Quill*, 504 US 298, 307, 112 S. Ct. 1904 (1992).

174 Burger King v. Rudzewicz, 471 US 462, 476, 105 S. Ct. 2174 (1985). Indeed, insofar as the U.S. Supreme Court's state tax jurisprudence regarding due process nexus is informed by its due process jurisprudence addressed to jurisdiction over a nonresident defendant, as *Quill* indicates it is, two 2011 Supreme Court cases holding that states lacked personal jurisdiction over nonresident

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