Cite as Det. No. 05-0145, 25 WTD 120 (2006)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of Assessment and Refund of	)	D E T E R M I N A T I O N
	)	No. 05-0145
. . .	)	Registration No. . . .
	)	Document No. . . .
	)	Docket No. . . .

[1] RULE 246; RCW 82.04.423: B&O TAX -- EXEMPTION -- DIRECT SELLERS -- REPRESENTATIVES -- METHOD OF PAYMENT. For direct sellers to qualify for exemption, RCW 82.04.423 requires their representatives to work on a "buy-sell" or "deposit-commission" basis. Transactions are on a "deposit-commission basis" if the sales representatives are entitled to retain part or all of the purchase deposits paid in connection with sales transactions. Direct sellers do not qualify for exemption when they accept orders and payments directly from buyers and then mail commissions to their representatives.

[2] RULE 246; RCW 82.04.423: B&O TAX -- EXEMPTION -- DIRECT SELLERS -- PLACE OF SALE. When a direct seller sells through a direct representative who is selling at wholesale, the seller can qualify for the direct seller's exemption only if its products are never sold in a permanent retail establishment. The direct seller exemption is based on the notion of an itinerant sales force, and not the use of established retail places of business where consumers might go to purchase or order the direct seller's goods. When ultimate purchasers may go to and deal with a permanent retail establishment to choose and purchase a product, the fact that ultimate delivery and installation take place in the home does not qualify the sale for the exemption.

[3] RULE 246; RCW 82.04.423: B&O TAX -- EXEMPTION -- DIRECT SELLERS -- "CONSUMER PRODUCT." Custom made-to-order cabinets to be installed in a house are not "consumer products." They are major construction components destined to become a permanent part of real estate before being used.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

Bauer, A.L.J. – An out-of-state cabinet manufacturer requests a determination that it is exempt from Washington State business and occupation (B&O) tax under the RCW 82.04.423 direct sellers exemption. We hold that this exemption is not available to a seller of kitchen cabinets.[1]

ISSUE

Is an out-of-state kitchen cabinet manufacturer eligible for the RCW 82.04.423 direct sellers exemption?

FINDINGS OF FACT

The business records of [Taxpayer] were audited. . . . Taxpayer has appealed the entire assessment, arguing that it is eligible for the RCW 82.04.423 direct sellers exemption. Taxpayer has paid this assessment in full. Taxpayer requests a refund . . . .

Taxpayer is an out-of-state corporation that manufactures custom, made-to-order kitchen cabinetry. All of Taxpayer's employees, buildings, equipment and other corporate assets are located outside of Washington State. Taxpayer sells cabinets directly to independent dealers, using an independent contractor as its manufacturer's representative for Washington.

A. Taxpayer's Sales of Consumer Products to Independent Dealers. The ultimate retail buyers of Taxpayer's custom cabinetry are individuals who incorporate the cabinetry into their home kitchens. However, while the retail consumer is a homeowner, Taxpayer itself sells its cabinetry on a wholesale basis to a nation-wide network of independent dealers (Dealers).

The Dealers then resell Taxpayer's cabinetry, along with a variety of other kitchen building products manufactured by third party companies, to their own customers. In most cases, customers of the Dealers are contractors, architects, and designers, who resell the cabinetry to homeowners. However, a homeowner will sometimes buy cabinetry directly from a Dealer.

In connection with the sale of kitchen building materials, Dealers often provide services such as assisting customers in the selection of product choices, and design and layout of cabinetry. An essential component of the retail sale is a series of measurements taken of the home where the cabinets will be installed. After completing this selection process, Dealers will place an order for a particular cabinet with Taxpayer. Taxpayer will then manufacture the cabinet and ship it directly to the Dealer, F.O.B. Taxpayer's out-of-state place of business. Taxpayer's web site offers a list of 20 Washington dealers, many of whom maintain retail establishments and showrooms.

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

When a Dealer resells cabinetry manufactured by Taxpayer, the Dealer establishes its own markup and end selling price. The price typically includes both the cabinetry and Dealer services as described above.

Dealers are responsible for delivering the cabinetry to the retail consumer's home. In many cases, Dealers are also paid to install the cabinetry, although sometimes the wholesale customer of a Dealer (such as a contractor) will install the cabinetry. In no event does Taxpayer install the cabinetry.

B. Taxpayer's Direct Seller's Representative in Washington. To sell products in Washington, Taxpayer engages [Sales Representative], an independent contractor, as Taxpayer's manufacturer's representative for Washington. Sales Representative represents Taxpayer's exclusive sales force in Washington. Taxpayer does not maintain any employees, branches, or any other sales representatives in Washington.

A copy of the Manufacturer's Representative Agreement has been provided. Pursuant to this agreement, Sales Representative represents Taxpayer in selling Taxpayer's cabinetry to the Dealers. Sales Representative is paid a commission based on the net invoice price of goods sold by it. The Representative Agreement expressly provides that Sales Representative "shall be acting as an independent contractor and not as an employee of [Taxpayer]. . . . Sales Representative is an independent sales representative which also represents other cabinet manufacturers.

ANALYSIS

RCW 82.04.423 provides a "direct seller's" exemption from B&O tax as follows:

> (1) This chapter shall not apply to any person in respect to gross income derived from the business of making sales at wholesale or retail if such person:
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> (a) Does not own or lease real property within this state; and
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> (b) Does not regularly maintain a stock of tangible personal property in this state for sale in the ordinary course of business; and
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> (c) Is not a corporation incorporated under the laws of this state; and
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> (d) Makes sales in this state exclusively to or through a direct seller's representative.
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> (2) For purposes of this section, the term "direct seller's representative" means a person who buys consumer products on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment, or who sells, or solicits the sale of, consumer products in the home or otherwise than in a permanent retail establishment; and
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> (a) Substantially all of the remuneration paid to such person, whether or not paid in cash, for the performance of services described in this subsection is directly related to sales or other output, including the performance of services, rather than the number of hours worked; and

> (b) The services performed by the person are performed pursuant to a written contract between such person and the person for whom the services are performed and such contract provides that the person will not be treated as an employee with respect to such purposes for federal tax purposes. . . .[2]

WAC 458-20-246 (Rule 246) further implements the direct seller's exemption. Referring to this rule, we will herein address three factors[3] that disqualify Taxpayer from the direct seller exemption:

[1] **Taxpayer's Sales Representative does not work on a "deposit-commission" basis.** RCW 82.04.423 requires that the direct seller representative work on a "buy-sell" or "deposit-commission" basis. Rule 246(4)(b)(i)(A) provides definitions of these terms:

> A transaction is on a "buy-sell basis" if the direct seller's representative performing the selling or soliciting services is entitled to retain part or all of the difference between the price at which the direct seller's representative purchases the product and the price at which the direct seller's representative sells the product. The part retained is remuneration from the direct seller for the selling or soliciting services performed by the representative. A transaction is on a "deposit-commission basis" if the direct seller's representative performing the selling or soliciting services is entitled to retain part or all of a purchase deposit paid in connection with the transaction. The part retained is remuneration from the direct seller for the selling or soliciting services performed by the representative.

(Emphasis added.) Although noting that Sales Representative works on a commission basis, Taxpayer's petition does not state that it works on a "deposit-commission" basis. To work on a "deposit-commission" basis, a sales representative must collect the purchase deposit from the buyer, and the commission must be payable from that deposit. Sales Representative's contract with Taxpayer, however, provides that purchase orders will be forwarded to Taxpayer for acceptance and "direct billing" . . . and commissions will be "mailed" to Sales Representative "on the last day of the following month." . . . Therefore, Sales Representative does not meet the statutory requirement that it sell either on a "buy-sell" or "deposit-commission" basis.

[2] **Taxpayer's Sales Representative Sells to Dealers Who Sell in Permanent Retail Establishments.** Rule 246(4)(b)(i)) discusses how the sale must be made:

> How the sale is made. A direct seller's representative is "a person who buys consumer products on a buy-sell basis or a deposit-commission basis for resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment, or who sells, or solicits the sale of, consumer products in the home or otherwise than in a permanent retail establishment." The direct seller sells the product using the services of a representative in one of two ways, which are described by two clauses in the statute. The

[2] Section (3) of RCW 82.04.423 applies only to times prior to the enactment of this section in 1983, and is not here pertinent.
[3] The Department, however, does not concede any elements not addressed herein.

> first clause ("a person who buys . . . for resale" from the direct seller) describes a wholesale sale by the direct seller. The second clause (a person who "sells or solicits the sale" for the direct seller) describes a retail sale by the direct seller.

(Emphasis added.) Rule 246(4)(b)(i)(B) further discusses the location where the retail sale of the product may and may not be made:

> The location where the retail sale of the consumer product may take place is specifically delineated by the terms of the statute. The direct seller may take the exemption only if the retail sale of the consumer product takes place either in the home or otherwise than in a permanent retail establishment. The resale of the products sold by the direct seller at wholesale is restricted by the statute through the following language: "For resale, by the buyer or any other person, in the home or otherwise than in a permanent retail establishment." This restrictive phrase requires the product be sold at retail either in the home or in a nonpermanent retail establishment. Regardless of to whom the representative sells, the retail sale of the product must take place either in the buyer's home or in a location that is not a permanent retail establishment. Examples of permanent retail establishments are grocery stores, hardware stores, newsstands, restaurants, department stores, and drug stores. Also considered as permanent retail establishments are amusement parks and sports arenas, as well as vendor areas and vendor carts in these facilities if the vendors are operating under an agreement to do business on a regular basis. Persons selling at temporary venues, such as a county fair or a trade show, are not considered to be selling at a permanent retail establishment.

(Emphasis added.) In order to comply with Rule 246(4)(b)(i) and Rule 246(4)(b)(i)(B), when a direct seller sells through a wholesaler, the seller can qualify for the B&O tax exemption in RCW 82.04.423 only if its products are never sold in a permanent retail establishment. *See Stroh Brewery Co. v. Department of Rev.*, 104 Wn. App. 235, 15 P.3d 692 (2001).

Taxpayer, relying on RCW 82.14.020(4)[4] and WAC 458-20-103 (Rule 103),[5] asserts that the sales of its cabinets do not take place in permanent retail establishments, but in the homes of the ultimate consumers where the cabinets are delivered and/or installed.

We disagree with Taxpayer's analysis. RCW 82.14.020(4) and Rule 103 identify the location of sale for purposes of establishing which tax rate will apply, and not whether an out-of-state seller is eligible for the direct seller's exemption. The direct seller exemption is based on the notion of an itinerant sales force, and not the use of established retail places of business where consumers might go to purchase or order the direct seller's goods. In Taxpayer's case, ultimate purchasers may go to and deal with the permanent retail establishments of many of its Washington dealers

[4] RCW 82.14.020(4) provides: "A retail sale within the scope of RCW82.04.050(2), and a retail sale of taxable personal property to be installed by the seller shall be deemed to have occurred at the place where the labor and services involved were primarily performed."

[5] This portion of Rule 103 provides: "For the purpose of determining tax liability of persons selling tangible personal property, a sale takes place in this state when the goods sold are delivered to the buyer in this state, irrespective of whether title to the goods passes to the buyer at a point within or without this state."

to choose and purchase cabinets. This is the type of sales activity proscribed by the direct seller's exemption.

[3] **Taxpayer's custom, made-to-order, kitchen cabinets are not a "consumer product."** RCW 82.04.423(2) requires that direct sellers, to qualify for exemption, must be selling "consumer products." Rule 246(4)(b)(ii) discusses "consumer products":

> What product the direct seller must be selling. The direct seller must be selling a consumer product, the sale of which meets the definition of "sale at retail," used for personal, family, household, or other nonbusiness purposes. "Consumer product" includes, but is not limited to, cosmetics, cleaners and soaps, nutritional supplements and vitamins, food products, clothing, and household goods,. The term does not include commercial equipment, industrial use products, and the like, including component parts. However, if a consumer product also has a business use, it remains a "consumer product," notwithstanding that the same type of product might be distributed by other unrelated persons to be used for commercial, industrial, or manufacturing purposes. For example, desktop computers are used extensively in the home as well as in businesses, yet they are a consumer product when sold for nonbusiness purposes.

(Emphasis added.) Custom made-to-order cabinets to be installed in a house are not "consumer products." . . .

In Det. No. 88-20, 5 WTD 73 (1988), we held that a "consumer product" is a product that is sold for personal use or enjoyment, and is not limited to those products used in the home or to be worn by the user. We reasoned that the term includes only those kinds of items of tangible personal property which are customarily sold at stores, shops, and retail outlets open to the public in general. Thus, Det. No. 88-20 concluded that automotive products (aluminum wheels, sport grips, running boards, and seat belts) were within Rule 246's definition of "consumer products" because they were sold for personal use or enjoyment.

In Det. No. 99-348, 19 WTD 916 (2000), we examined whether a mobile home could be considered as a member of the "household goods" classification for use tax exemption[6] purposes:

> No case has been cited nor have we found any which would define "household goods" broadly enough to include a mobile home. The general definition of the phrase is that which is of a permanent nature, *i.e.*, not consumed in use, which is used by a person *for* his house. *Smith v. Findley*, 34 Kan. 316, 8 P. 871 (1885); *Marquam v. Sengfelder*, 24 Ore. 2, 32 P. 676 (1893). Alternatively, household goods are those articles with which a residence is equipped, other than fixtures. *Kramer v. Beebe*, 186 Ind. 349, 115 N.E. 83 (1917). "The term 'household goods' . . . includes everything *about* the house that is usually held and enjoyed *therewith* . . ." (Italics ours.) *Lawwill v. Lawwill*, 21 Ariz. App. 75, 77-78, 515 P.2d 900 (1973).

[6] RCW 82.12.0251.

Det. No. 88-42, 7 WTD 39 (1988) also explored the concept of "household goods":

> WAC 458-12-270[7] defined household goods and personal effects as follows:
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> > . . . Household goods and furnishings shall include movable items of necessity, convenience, or decoration, such as bedding, tables, chairs, refrigerators, stoves, freezers, food, clocks, radios, televisions, pictures, tools and equipment used to maintain the residence. It shall include all personal property normally located in or about a residence and used or held to enhance the value of enjoyment of the residence (including its premises). Those items of personal property constructed primarily for use independent of and separate from a residence do not qualify for the exemption (i.e., boats, pickup campers, (pickup campers attached to the vehicle by the methods authorized in department of licenses bulletin, dated January 26, 1965 shall be considered a part of the vehicle and are not taxable as personal property) etc.).

Custom made-to-order kitchen cabinets are major construction components destined to become a permanent part of real estate. As such, they are not intended to be used until they have become a part of real property. None of the above-cited authorities or the doctrine of *ejusdem generis* suggest that major components of a home can be considered to be either "consumer products," or "household goods." We therefore hold that major construction components destined to become a part of real property (and not just by annexation as fixtures) are not consumer products as described by Rule 246(4)(b)(ii). Custom made-to-order kitchen cabinets are major components that will be permanently installed in homes, and, as such, will become part of real property before being used.

For the above reasons, we conclude that Taxpayer is not eligible for the direct seller's exemption.

DECISION AND DISPOSITION

Taxpayer's petition for correction of assessment and refund is denied.

Dated this 29th day of June 2005.

STATE OF WASHINGTON DEPARTMENT OF REVENUE

[7] WAC 458-12-270, concerning the listing of Household Goods and personal property for purposes of the property tax exemption, was repealed October 5, 2002. We find the logic as to "household goods" to be persuasive.