Cite as 4 WTD 51 (1987)

BEFORE THE INTERPRETATION AND APPEALS SECTION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of Assessment and Refund of	DETERMINATION
	No. 87-286
. . .	Registration No. . . .
	Tax Assessments No. . . . and . . .

[1] **RULE 193B:** BUSINESS AND OCCUPATION TAX -- INTERSTATE COMMERCE -- NEXUS. Those examples of activities giving rise to local nexus which are listed in Rule 193B are not exclusive. The rule provides that any in-state activity (unless otherwise specifically exempt) that serves to "enable" the Washington sales of an out-of-state taxpayer is sufficient to render those sales taxable under the Washington business and occupation tax.

[2] **RULE 193B:** BUSINESS AND OCCUPATION TAX -- INTERSTATE COMMERCE -- NEXUS -- 15 U.S.C. 381. The federal act by its terms applies only to taxes on or measured by net income. The minimums prescribed for the exercise of nexus are therefore inapplicable to Washington's business and occupation tax, since it is measured by gross receipts.

[3] **RULE 193B:** BUSINESS AND OCCUPATION TAX -- INTERSTATE COMMERCE -- COMPLETE AUTO TRANSIT - FOURFOLD TEST. To be valid under Complete Auto Transit, the state tax on interstate commerce must meet four requirements: (1) there must be a sufficient nexus between the interstate activities and the taxing state; (2) the tax must be fairly apportioned; (3) the tax must not discriminate

against interstate commerce; and (4) the tax must be fairly related to the services provided by the state.

[4] **RULE 193B:** BUSINESS AND OCCUPATION TAX -- INTERSTATE COMMERCE -- COMPLETE AUTO TRANSIT -- NEXUS -- NONRESIDENT SALES PERSON. 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. Generally, if an in-state activity is economically meritorious for a taxpayer (if it is worth spending budget dollars to do it), then the activity is market driven and it establishes threshold nexus to tax. Tyler Pipe cited.

[5] **RULE 193B:** BUSINESS AND OCCUPATION TAX -- INTERSTATE COMMERCE -- NEXUS -- DISSOCIATION -- NORTON -- BURDEN OF PROOF. Once nexus has been determined, the burden shifts to the seller to show that any of its sales result from market stimulation other than that which forms the nexus.

[6] **RULE 193B:** BUSINESS AND OCCUPATION TAX -- INTERSTATE COMMERCE -- COMPLETE AUTO TRANSIT -- APPORTIONMENT -- 15 U.S.C. 381 -- DOUBLE TAXATION. Oregon taxpayer's argument rejected that the tax imposed by Washington is unconstitutional for the reason of "double taxation" since it is also taxed by Oregon under a three factor formula. Washington tax, by its very nature, is perfectly apportioned and does not offend any of the other constitutional prohibitions against taxing interstate sales. Standard Pressed Steel and Chicago Bridge cited. The fact that a business may be subjected to double taxation because of different state tax policies does not render the tax invalid. Moorman Mfg Co. v. Blair cited.

[7] **RULE 193B:** BUSINESS AND OCCUPATION TAX -- INTERSTATE COMMERCE -- COMPLETE AUTO TRANSIT -- DISCRIMINATION -- DOUBLE TAXATION. The U.S. Supreme Court has clearly rejected the notion that a multiple tax burden resulting from the varying tax schemes of more than one jurisdiction is an

unpermissible discrimination against interstate commerce. Tyler Pipe cited.

[8] **RULE 193B:** BUSINESS AND OCCUPATION TAX -- INTERSTATE COMMERCE -- COMPLETE AUTO TRANSIT -- DUE PROCESS -- RELATIONSHIP TO SERVICES PROVIDED -- NONRESIDENT SALES PERSONS. A state tax is constitutionally required to be fairly related to the services provided by the taxing state. This test requires a twofold determination: First, is a business active in the taxing state so that it creates a market for its goods or services in that state's marketplace? Second, is the measure of the tax reasonably related to the extent of the taxpayer's contact with the state? Wisconsin v. J.C. Penney Co. and Commonwealth Edison v. Montana cited.

[9] **RULE 228:** PENALTIES -- INTEREST -- LATE PAYMENT -- RETURNS -- REGISTRATION -- LEGAL ADVICE -- RELIANCE. Taxpayer's mistaken belief, based upon the advice of its legal department, that it was not subject to Washington tax liability is not a circumstance beyond the control of the taxpayer for purposes of waiving late payment penalties and interest associated with tax deficiencies assessed for periods in which the taxpayer was not registered with the Department and failed to file returns and pay taxes.

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.

TAXPAYER REPRESENTED BY: . . .
. . .
. . .
. . .

DATE OF HEARING: January 8, 1986

NATURE OF ACTION:

An Oregon taxpayer claims there was insufficient nexus in the state of Washington for the imposition of the wholesaling business and occupation tax.

FACTS:

Burroughs, A.L.J. -- The Department of Revenue examined the taxpayer's business records for the period January 1, 1978 to February 2, 1985. As a result of this audit, the Department issued the above-referenced tax assessments on October 1, 1985 assessing excise tax liability in the respective total amounts of $ . . . and $ . . . . A correction of assessment is sought for these amounts, which have not been paid. A refund is requested for amounts paid under protest since April 15, 1985.

The taxpayer has represented the facts in its brief as follows:

> [The taxpayer], an electrical products wholesaler organized under the laws of the State of Oregon, ... maintains its headquarters and warehouse in Portland, Oregon, but has no branch office, warehouse, resident personnel or service center in the State of Washington. Its sole contact with the State are periodic visits by approximately six (6) sales representatives, who very occasionally will take orders, but are more concerned with customer relations, including personal contact with customers.
>
> [The taxpayer] is not engaged in making local sales from a facility within the State of Washington, and conducts no training, pickup or delivery, engineering or technical services within the State. Sales made to Washington customers represent a relatively small portion of the Company's business, and are typically entered by telephone orders from the State of Washington to the Company's headquarters in Portland, with shipment either from the Portland warehouse to Washington points, or from remote points outside the State of Washington to Washington customers.
>
> Based upon legal advice given by the Company's prior legal counsel, to the effect that maintenance of offices, warehousing, advertising or other activities would result in imposition of the Washington Business and Occupation Tax, but that strictly solicitation of orders, followed by shipment from Oregon or remote points to Washington customers would not result in imposition of the Tax,

> the Company did not pay the Business and Occupation Tax until audited by the Washington Department of Revenue. Nonetheless, [the taxpayer] cooperated fully with the Department's auditors, and since receipt of the Assessment, [the taxpayer] has apportioned its Washington's receipts and paid the accruing Tax under protest and subject to refund.

The taxpayer's president explained that in 1975 one of his executives noticed an article in the paper regarding the Washington business and occupation tax. The corporate attorney was consulted, who advised that the taxpayer had no liability. A copy of his letter, dated March 31, 1975, was presented in evidence.

A year later the corporation received correspondence from the Department, a copy of which was not kept. The taxpayer filled out and returned a form, as had been requested, but had no idea that they were to pay tax.

Additionally, the taxpayer's CPA (who has worked with the taxpayer from 1976 to July 1978, and then from 1980 to the present) testified that although he had been familiar with the Washington business and occupation tax, he had not thought that there was nexus with this state, and was surprised when he was advised there was to be an audit. He did not have a great deal of contact with the auditor except at the supervisor's conference. He does concede that the numbers arrived at as a result of the audit are mathematically correct. The taxpayer normally kept records for four years, and then boxed them. The method of the audit was concurred with, but the taxpayer did note that the consumer market did not exist in 1980 and prior years, so taxes should not be imputed to this market prior to that time.

Oregon, which has a net income tax based on federal returns, allows apportionment. In April 1985 the taxpayer amended its Oregon returns to exclude about four percent of the taxes which had been paid there. The statute of limitations was about to close on the tax year 1981, and prior years were closed, so nothing could be retrieved from Oregon for those years. The Oregon tax department may still contest those years which were filed.

The taxpayer cooperated fully during the audit.

At the hearing, it was explained that the taxpayer has four markets:

1. Contractor Market - sales mainly to contractors who do installation. Three salesmen.

2. Manufactured Homes - products sold are identical to those of contractors. One full-time and one part-time salesmen.

3. Consumer Market - products sold to do-it-yourselfers through retail outlets. Mainly sold through Fred Meyer stores. These are not packaged in bulk. Two salesmen.

4. Original Equipment Manufacturer (OEM) - equipment is sold to manufacturers of other equipment, e.g., electrical motors, controls, fixtures, etc.

The taxpayer owns two buildings and a parking lot in Portland, and leases another building there. There are no branch warehouses. The taxpayer has approximately ninety to a hundred employees who are assigned to the various departments and divisions.

During the 1978 - 1985 audit period, the general level of company sales ranged from sixteen to twenty-one million dollars. At the time of the hearing, sales were estimated to be about twenty million dollars. The taxpayer noted that there had been a general decline in recent years in the economy and five of its major manufactured home customers had gone bankrupt.

As far as its business activities in Washington, the taxpayer pointed out that it has no branch offices or warehouses in this state, either owned or leased, and no corporate officers, directors or shareholders were residents of Washington. One salesman who is a resident of Vancouver, Washington works mainly in Portland. Starting in 1985, he started making some sales in Vancouver. This salesman is the only Washington resident who had made calls in Washington. With the exception of this man, no other Washington residents were involved in Washington during the audit period.

Additionally, no training or sales programs, service/maintenance activities, maintenance/technical assistance, or servicing is done in Washington. All warranties are covered by the factories from which the taxpayer obtains its inventory.

The majority of pickup and delivery to consumer markets is done by Fred Meyer trucks, or shipped to those stores by common carrier. Returns are by Fred Meyer truck. Another customer was Penguin Stores, of which there were several in Washington. Common carriers delivered goods to Penguin, except for the Vancouver store (since closed), to which the taxpayer would occasionally deliver in its own truck.

Goods sold to the mobile home market are delivered by common carrier. If an item is defective, the salesman will carry it back to the taxpayer if appropriate paperwork is first obtained by the customer.

Deliveries to contractors are made by the taxpayer's van if the delivery point is not far away (as far away as Pendleton). Other than that, a common carrier is used. If goods are returned, they can be given to salesman if accompanied by a returned goods authorization issued by the taxpayer, shipped back to the taxpayer by common carrier, or returned to the original manufacturer.

The taxpayer has no marketing program or phone listing in Washington. Despite this fact, Washington sales generally constitute ten to eleven percent of sales in the consumer, mobile home, and contractor sales areas. This figure has decreased, however, because of the mobile home decline.

In the consumer and manufactured housing sales areas, salesmen don't take orders, as they are too long and complicated. Forms are kept at the taxpayer's Portland office where there is a WATS line. Salesmen in the field stop in to see customers to ascertain if there are any problems, answer questions on special items, check on credit, and maintain good relationships. They might assist customers in inventorying merchandise. Orders are written in Portland, where the credit manager has the authority to approve or reject them, since accounts are constantly reviewed there. Orders are shipped by common carrier from the warehouse.

As far as the mobile home and recreational vehicle (RV) market, there were approximately nine such customers in the state of Washington. All sales prices for these customers were negotiated at the taxpayer's corporate level, and thus salesmen were not involved. Goods were shipped by common carrier twice a month, mostly from the warehouse in Portland.

Goods to the electrical construction and OEM market were handled by salesmen who would call on contractors to see when and if they needed anything. The salesmen would check on the availability of items, and the order would be handled in one of four possible ways: First, the salesman could place an order if one was given to him. Second, the customer could call in the an order. Third, the customer could come into Portland and order over the counter. Fourth, the customer could order by mail on a purchase order. Overall, there was no typical way for such customers to order. Manufacturers' representatives might negotiate prices from takeoffs. Goods would be shipped into the state of Washington by van, if the location was nearby, by common carrier, or shipped by manufacturers if items were large or destinations remote. There was no other technical or other expertise provided in Washington.

The manufactured housing market constitutes about six percent of the taxpayer's total sales. This division was selling to about six customers in the Washington market in 1978, when the market was in its heyday. By 1979 the market was going downhill, and by 1980 there were only three such customers in Washington.

One salesman assigned to the modular home market would routinely make calls twice a month on Glen River Homes and Moduline in Chehalis; calls were made less often to Fleetwood in Woodland. This salesman would merely continue his relationship with the account, check credit, pick up checks, and answer any questions which might arise. He would not call on the accounts in order to promote sales or take orders, although he might take complaints or return merchandise if a returned goods authorization had already been obtained. These latter services would be for customer accommodation only, and the salesman could not approve orders. It was emphasized that the salesman did not make the calls for the purpose of making sales, but because if no one travelled this area, the "locals would move in" on them. Therefore, the taxpayer "maintained" these accounts. Otherwise, there was no other training or promotional activity involved. The salesman's other accounts were in Oregon, and the other salesman assigned to modular home sales never went into Washington at all.

The consumer sales market, which consists of three percent of the taxpayer's sales, has been a growing market in the last ten years. Fred Meyers got them into this, and eighty-five to ninety percent of Washington consumer sales are through Fred Meyer outlets. Two salesmen work this market - in Yakima, Spokane, Lynnwood, etc. They have large areas to cover, and it takes a month or a month and a half cycle to cover all the stores in the area. Each store does its own ordering, as there is no central distribution. Pricing is done at the taxpayer's corporate headquarters. Most orders are placed by telephone.

Salesmen calling on Fred Meyers and other stores check on orders, look for problems, and generally maintain a relationship with the management. Both of the two salesmen assigned to the consumer market travel in Oregon and Washington. One travels in Washington approximately six days a month, and the other two days a month.

The electrical construction market, which consists of one to one and a half percent of the taxpayer's sales, has developed since the taxpayer started business. The activity for this market centers in the Longview, Long Beach and Vancouver area. There are now only two salesmen (there were three) for this market. One came into Washington about ten days every year, the second for four hours once or twice a month, and the third once every three weeks.
They normally passed on pricing information, checked stock by phone to the head office, and on occasion took an order. Most orders are made by telephone.

TAXPAYER'S EXCEPTIONS:

The taxpayer has offered an extensive brief outlining its arguments as to why the business and occupation tax should not apply to its activities. These arguments are summarized as follows:

1. That the taxpayer, with the exception of occasional order taking, engages in none of those activities which are included as "examples of sufficient local nexus" in WAC 458-20-193B (Rule 193B).

2. That 15 U.S.C. 381, which came into being in 1959, although technically a limitation only on the imposition of a net income tax, represents a fundamental federal minimum for the exercise of nexus beyond which the states may not proceed. The taxpayer has cited a number of cases to demonstrate the juridical background against which this statute was enacted (i.e., the underlying conflict between the States' need and power to tax in order to provide fundamental services to citizens of their States, balanced against the prospective burdens on interstate commerce).

3. That the state of Washington cannot subject the taxpayer to taxation since the four requirements set forth by Complete Auto Transit v. Brady, 430 U.S. 274 (1977) have not been met:

a. Nexus. The taxpayer argues that there is insufficient nexus with the State of Washington, since the activities in which it engages are not substantial enough to allow the imposition of the tax. For instance, the taxpayer does not maintain a branch office, distribution center, resident district managers, sales, training and service personnel, or conduct promotional advertising and sales campaigns (General Motors v. Washington, 60 W.2d 862 (1962)).

In addition, it claims that it does not maintain a full-time, resident, salaried employee whose activities are necessary to the taxpayer's sales activity. The taxpayer contends that, although periodic customer relations visits by non-resident sales personnel may facilitate its sales, it is doubtful that they make "possible the realization and continuance of valuable contractual relations." Standard Pressed Steel, 419 U.S. 560 (1975).

The taxpayer contends that no case, many of which it cited, has held there to be sufficient nexus where there is neither residence nor a virtually full-time effort to sell to Washington customers by sales personnel dispatched from out of state for that purpose. As a result, either a local outlet, resident employees, or varied substantial services in addition to sales activities must, under the applicable constitutional standard, be committed by an out-of-state vendor in order to be subjected to the Washington Business and Occupation Tax.

b. Apportionment. The taxpayer argues that the tax is not fairly apportioned. The taxpayer argues that it may be exposed to potential for double taxation, which would unfairly discriminate against interstate commerce.

The taxpayer contends that, based on the holdings of the Oregon cases Cal-Roof Wholesale, Inc. v. State Tax Commission, supra, and Miles Laboratories, Inc. v. Department of Revenue, supra, the mere solicitation of orders in a state is exempt from net income taxation under 15 U.S.C. 381. The taxpayer reasons, therefore, that additional activities within the state of Washington would be required before the state of Oregon would allow apportionment to this state. The disallowance of apportionment by the state of Oregon for income already taxed in Washington would then result in double taxation.

c. Non-discrimination. The taxpayer asserts that assessment of the tax, penalties and interest, back to 1978, in the face of a four-year statute of limitations under Oregon law on the right to apply for refund on the Oregon corporate income tax results in an unfair discrimination, and, at the least, the tax should be cancelled except for those years in which the taxpayer may obtain a refund from the state of Oregon.

d. Relationship to Services Provided. The taxpayer argues that imposition of the tax is not fairly related to the benefits provided it receives from the state of Washington. The taxpayer points out that it has no resident employees or property within the State of Washington, and in the absence of a license to do business in this state, it is highly questionable whether the taxpayer derives any benefit beyond the taxes it already pays to the state (e.g., gasoline taxes, telephone excise tax, and retail sales taxes paid by the travelling representatives).

The taxpayer asserts that there is no rational relationship between the taxes, penalties and interest which have been assessed in this case and the benefits which the taxpayer has received from the state of Washington. It contends that none of its sales in the state of Washington have been assisted by the regulation of any public activity such as the required upgrading and replacement of electrical distributions and supplies, and that the tax, if upheld, is a pure windfall to the state.

4. That, in light of good faith reliance on the opinion of its legal counsel, both penalties and interest for the entire period should be abated if the tax is upheld.

ISSUES:

There are four major issues to be resolved:

1. Whether the taxpayer's activities are sufficient to establish local nexus under the provisions of Rule 193B,

2. Whether 15 U.S.C. 381, although technically a limitation only on the imposition of a net income tax, represents a fundamental federal minimum for the exercise of nexus beyond which the state of Washington may not proceed.

3. Whether the taxpayer can be subjected to tax by the State of Washington under the fourfold Complete Auto Transit test, and

4. Whether penalties and interest should be abated because of the taxpayer's good faith reliance on the opinion of its legal counsel.

DISCUSSION:

ISSUE NO. 1: <u>Local nexus under Rule 193B.</u> Rule 193B reads in pertinent part as follows:

> RETAILING, WHOLESALING. Sales to persons in this state are taxable when the property is shipped from points outside this state to the buyer in this state and the <u>seller carries on or has carried on in this state any local activity which is significantly associated with the seller's ability to establish or maintain a market in this state for the sales.</u> If a person 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. <u>The characterization or nature of the activity performed in this state is immaterial so long as it is significantly associated in any way with the seller's ability to establish or maintain a market for its products in this state. The essential question is whether the instate services enable the seller to make the sales.</u>
>
> Applying the foregoing principles to sales of property shipped from a point outside this state to the purchaser in this state, the following activities are examples of sufficient nexus for application of the business and occupation tax:
>
> (1) The seller's branch office, local outlet or other place of business in this state is utilized in any way, such as in receiving the order, franchise or credit investigation, or distribution of the goods.
>
> (2) The order for the goods is given in this state to an agent or other representative connected with the seller's branch office, local outlet, or other place of business.

(3) The order for the goods is solicited in this state by an agent or other representative of the seller.

(4) The delivery of the goods is made by a local outlet or from a local stock of goods of the seller in this state.

(5) Where an out-of-state seller, either directly or by an agent or other representative, performs significant services in relation to establishment or[1] maintenance of sales into the state, the business tax is applicable, even though (a) the seller may not have formal sales offices in Washington or (b) the agent or representative may not be formally characterized as a "salesman."

(6) Where an out-of-state seller either directly or by an agent or other representative in this state installs its products in this state as a condition of the sale, the installation services shall be deemed significant services for establishing or[2] maintaining a market in this state for such installed products and the gross proceeds from the sale and installation are subject to business tax.

Under the foregoing principles, sales transactions in which the property is shipped directly from a point outside the state to the purchaser in this state are exempt only if there is and there has been no participation whatsoever in this state by the seller's branch office, local outlet, or other local place of business, or by an agent or other representative of the seller. A franchise or credit investigation of a prospective purchaser and/or recommendation or approval by a local office upon which subsequent transactions are based is such a utilization of the local office as to render such subsequent transactions taxable. (Emphasis provided.)

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[1] and 2: The word "or" replaced the word "and" in the 1983 revision of the rule.

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[1] Although the taxpayer claims that because its activities are not included in the examples given in Rule 193B they can not be held to establish local nexus, we are constrained to point out that its activities are included in example (5). Even were they not spelled out in one of the examples, it must be noted that the examples given are not an exclusive listing of activities which might give rise to taxability. The operative phrases in the rule (highlighted above) make it clear that any in-state activity (unless otherwise specifically exempt) that serves to "enable" the Washington sales of an out-of-state taxpayer are sufficient to render those sales taxable under the Washington business and occupation tax.

In this case, in the consumer and manufactured housing sales areas, the taxpayer's field salesmen, in stopping in to see Washington customers to ascertain if there are any problems, answer questions on special items, check on credit, and maintain good relationships, were engaged in activities which were "significantly associated with the taxpayer's ability to establish or maintain a market for its products in this state." By the taxpayer's own admission, if its sales persons had not travelled the area, the "locals would [have] move[d] in" on these sales opportunities.

Likewise, salesmen in the electrical construction and OEM market, by calling on contractors and assisting them in a variety of ways to order their goods, increased the taxpayer's ability to maintain a Washington market for its products.

Therefore, we hold that the taxpayer has established local nexus under the very terms of Rule 193B.

ISSUE NO. 2. Applicability of 15 U.S.C. 381. The taxpayer has argued that 15 U.S.C. 381 represents a fundamental federal minimum for the exercise of nexus beyond which the states may not proceed. That federal statute reads in pertinent part as follows:

Minimum Standards

> (a) No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after September 14, 1959, a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such

> person during such taxable year are either, or both, of the following:
>
>> (1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and
>>
>> (2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1).

This code section provides a tax exemption. The Washington Supreme Court has held on numerous occasions that tax exemption statutes must be strictly construed in favor of taxation. Budget Rent-A-Car v. State, 81 W.2d 171 (1972). Since the terms of 15 U.S.C. 381 are limited to a net income tax (the taxable incident), it simply does not apply to gross receipt taxes imposed on privileges. We note that 15 U.S.C 383 defines "net income tax" to mean "... any tax imposed on, or measured by net income."

We find additional support in the Department's position in Clairol, Incorporated v. Kingsley, 109 N.J. Super 22 (1970), sustained by the Supreme Court of New Jersey, 57 N.J. 199, 270 A.2d 702. The New Jersey Superior Court stated in pertinent part:

> The federal act by its terms applies only to taxes on or measured by net income. Whatever may be the effect of the act on the portion of Clairol's tax measured by allocated net income, it has no effect on the portion thereof measured by allocated net worth.

[2] Accordingly, we find the minimums prescribed by 15 U.S.C. 381 for the exercise of nexus to be inapplicable to the gross receipts tax imposed by the State of Washington.

ISSUE NO. 3. Fourfold Test of Complete Auto Transit. Washington's business and occupation tax is levied on every person for the act or privilege of engaging in business activities. RCW 82.04.220. A deduction is permitted for amounts derived from business which the Constitution or laws of the United States prohibit a state from taxing. RCW 82.04.4286.

As the taxpayer has correctly noted, in Complete Auto Transit, supra, the Court overruled certain prior decisions which held that a tax on the privilege of engaging in an activity in the state may not be applied to an activity that is part of interstate commerce. The court noted that such a rule has no relationship to economic realities. 430 U.S. at 279. "It was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing the business." Id., quoting Western Live Stock v. Bureau of Revenue, 303 U.S. 250, 254 (1938). It was thus recognized that the states could exact a reasonable charge in return for providing the commercial and economic benefits of their marketplaces.

[3] To be valid under Complete Auto Transit, the state tax on interstate commerce must meet four requirements: (1) there must be a sufficient nexus between the interstate activities and the taxing state; (2) the tax must be fairly apportioned; (3) the tax must not discriminate against interstate commerce; and (4) the tax must be fairly related to the services provided by the state. Complete Auto Transit at 279. Accordingly, if the tax at issue meets those requirements, it is not invalid even if the shipments are considered a part of interstate commerce.

a. Nexus. Our first inquiry under Complete Auto Transit must be whether the enterprise sought to be taxed has a substantial nexus with the taxing state. This aspect of the test was most forcefully addressed by the Supreme Court in Standard Pressed Steel Co. v. Department of Revenue, supra. The idea of "nexus," essentially a Due Process or jurisdictional concept, was framed by the Court in the broadest possible Commerce Clause context. The Court said that the significance of the instate activity was that it "made possible the realization and continuance of valuable contractual relations" between Standard Pressed Steel and its in-state customer, Boeing. The court concluded that the activity of Standard's lone employee here, though not a salesman and not even providing price lists for Standard's products, were so related to Standard's market in this state that it would "verge upon the frivolous" to argue lack of significant nexus.

The most recent restatement on this issue by our State Supreme Court is Tyler Pipe Industries, Inc. v. Department of Revenue, 105 W.2d 318 (1986). This case was argued on appeal to the U.S. Supreme Court, which affirmed, stating:

> As the Washington Supreme Court determined, "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." 105 Wash. 2d, at 823, 715 P.2d, at 126. The Court found this standard was satisfied because Tyler's "sales representatives perform any local activities necessary for maintenance of Tyler Pipe's market and protection of its interests ...." Id., at 321, 715 P.2d, at 125. We agree that the activities of Tyler's sales representatives adequately support the State's jurisdiction to impose its wholesale tax on Tyler.

Tyler Pipe Industries, Inc. v. Washington State Department of Revenue, ____ U.S. ____, at _____ (1987).

[4] Thus, in Washington State, the taxing agency has consistently taken the position that if the in-state activity is economically meritorious for a taxpayer (if it is worth spending budget dollars to do it), then the activity is market driven and it generally establishes threshold nexus to tax.

It is clear in this case that the taxpayer has, for valid market reasons, engaged certain of its employees in Washington activity. Such activities are clearly "significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales." Thus, we hold that the taxpayer has clearly established nexus with the state of Washington.

The states continue to respect the proposition established in Norton Company v. Illinois Department of Revenue, 340 U.S. 534 (1951), though its impact has been significantly eroded by General Motors v. Washington, 377 U.S. 436 (1964) and by Standard Pressed Steel, supra. Under the rule in Norton, even where nexus is present, the seller may dissociate certain sales or revenue producing transactions from the activities which constitute the nexus. This state takes the position that nexus to tax any sales is nexus to tax all sales delivered into the destination state unless the seller can dissociate.

[5] It is not fundamentally clear whether the concept of dissociation is a "nexus" consideration under the first prong or an "apportionment" consideration under the second prong of the Complete Auto test. It is clear, however, that once nexus has been determined, the burden under Norton shifts to the seller to show that any of its sales result from market stimulation other than that which forms the nexus.

In this case, the taxpayer has not carried its burden to demonstrate that its Washington sales have not been stimulated from its instate activities. Therefore, dissociation is not appropriate.

b. Apportionment. The second prong of Complete Auto asks, is the state tax fairly apportioned? Does the taxing scheme attribute to the taxing state only its fair fractional share of the revenues produced from multi-jurisdictional transactions? If so, the tax survives. If not, the Commerce Clause still prohibits its imposition. This is a more difficult test to apply in states which impose an income tax than in states with business privileges or franchise taxes like Washington.

[6] While income tax states use a 3-factor formula under UDITPA based upon (a) sales, (b) property, and (c) payroll, Washington State subjects all gross receipts to its business privileges tax (Business and Occupation Tax) if the goods are delivered to the buyer in this state. Also, all states which impose sales tax surrender sales taxing jurisdiction to the "destination" or "market" state. Thus, these taxes have been characterized as "self-apportioning" in nature, through allocation. See Standard Pressed Steel, supra, and Chicago Bridge & Iron Co. v. Department of Revenue, 98 Wn.2d 814 (1983), appeal dismissed, 464 U.S. 1014 (1983).

In evaluating the economic realities of state taxing schemes under the apportionment concept, the Court has ruled that any apportionment approach or formula is acceptable so long as it is reasonably related to the in-state activity sought to be taxed. Formulary consistency between the states is not required. Moorman Mfg. Co. v. Bair, 437 U.S. 267 (1978). Moreover, if apportionment is provided for, then the burden of proof shifts to the taxpayer to show, by clear and cogent evidence, that the result of the apportionment method is unfair or unreasonable. Exxon Company v. Wisconsin Dept. of Revenue, 447 U.S. 207 (1980).

As a practical matter, similar to the "nexus" prong, apportionment is also achieved by dissociation, whereby the out-of-state based business can show that certain transactions sought to be taxed have no relationship whatever with the in-state activity which provided threshold taxing jurisdiction. Again, the economic realities of the business-to-state relationship prevail.

The taxpayer has claimed that the tax is not fairly apportioned because it is exposed to the potential for double taxation, since "the mere solicitation of orders in a state is exempt from net income taxation under 15 U.S.C. 381" and Oregon would not allow apportionment to this state without additional activities herein.

We reject the taxpayers' argument that the tax imposed by Washington is not fairly apportioned since it might also be taxed by Oregon under a three factor formula. Here, different types of taxes are involved. The Washington tax, by its very nature, is perfectly apportioned and does not offend any of the other constitutional prohibitions against taxing interstate sales. Thus, the taxpayer's petition as to this issue is denied.

c. Non-Discrimination. The third prong of Complete Auto Transit asks, does the tax sought to be imposed discriminate against interstate commerce in favor of intrastate commerce? Again, the test seeks to determine the economic burden of a state tax. It begs the question, all things being equal, does the tax place a greater economic burden upon interstate business transactions than it places on intrastate transactions for persons similarly situated? If so, the tax is prohibited. The protection against state taxation under this aspect of the test is still alive and well.

The fact that a business may be subjected to double taxation because of different state tax policies, however, does not render the tax invalid. In Tyler Pipe, supra, the Court implies that there may be permissible interference with free trade. Rather than simply saying that the tax cannot interfere with free trade or that it violates the commerce clause, the Court has interjected the word "impermissible." This begs the question, what discrimination is permitted to interfere with free trade without violating the Commerce

Clause? Noteworthy, the Court made this same kind of conclusory remark in Armco, supra. When it encountered the objection that the actual results of varying tax schemes may result in a multiple tax burden for some and not for others, even though the taxing schemes of each are internally consistent, the Court replied: "such a result would not arise from impermissible discrimination against interstate commerces." Armco, 467 U.S. at 645. See also Chicago Bridge and Iron Company v. Department of Revenue, supra.

[7] The Court, then, has clearly rejected the notion that a multiple tax burden resulting from the varying tax schemes of more than one jurisdiction is an impermissible discrimination against interstate commerce.

In this case the taxpayer's perceived inability to apportion Washington sales under the Oregon taxing scheme, or to obtain refunds from that state for past periods, does not render the Washington wholesaling tax invalid.

d. Relationship of Services Provided. The fourth prong of the test asks, is the state tax fairly related to the services provided by the taxing state? This aspect of the Commerce Clause test, like the "nexus" aspect, is tantamount to the Due Process test requiring at least minimal connection between the person and the governing body seeking to regulate that person. The state must give something for which it can fairly exact a return, though it need not be an even exchange. The Court examined the economic relationships between the services provided by the taxing state and the intrastate enterprise of the business being taxed in Wisconsin v. J.C. Penney, 311 U.S. 435, 444-446 (1940), stating:

> A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society. ... The simple but controlling question is whether the state has given anything for which it can ask return. ... Here ... the incidence of the tax as well as its measure is tied to the earning which the State ... has made possible, insofar as government is the prerequisite for the fruits of civilization for which, as Mr. justice Holmes was fond of saying, we pay taxes. ...

In Commonwealth Edison Co. v. Montana, 453 U.S. 609, 620-623 (1980), the Court similarly stated:

> Appellants argue that they are entitled to an opportunity to prove that the amount collected under the Montana tax is not fairly related to the additional costs the State incurs because of coal mining. ... In objecting to the tax on this ground, appellants may be assuming that the Montana tax is, in fact, intended to reimburse the State for the cost of specific services furnished to the coal mining industry. Alternatively, appellants could be arguing that a State's power to tax an activity connected to interstate commerce cannot exceed the value of the services specifically provided to the activity. Either way, the premise of appellants' argument is invalid. ...
>
> ...
>
> This Court has indicated that States have considerable latitude in imposing general revenue taxes. ... [T]here is no requirement under the Due Process Clause that the amount of general revenue taxes collected from a particular activity must be reasonably related to the value of the services provided to the activity. Instead, our consistent rule has been:
>
>> "Nothing is more familiar in taxation than the imposition of a tax upon a class or upon individuals who enjoy no direct benefit from its expenditure, and who are not responsible for the condition to be remedied.
>>
>> "A tax is not an assessment of benefits. It is, as we have said, a means of distributing the burden of the cost of government. The only benefit to which the taxpayer is constitutionally entitled is that derived from his enjoyment of the privileges of living in an organized society, established and safeguarded by the devotion of taxes to public purposes. Any other view would preclude the levying of taxes except as they are used to compensate for the burden on those who pay them, and

> would involve abandonment of the most fundamental principle of government -- that it exists primarily to provide for the common good." Carmichael v. Southern Coal & Coke Co., 301 U.W. 495, 521-523 (1937) (citations and footnote omitted).

> ... The relevant inquiry under the fourth prong of the Complete Auto Transit test is not, as appellants suggest, the amount of the tax or the value of the benefits allegedly bestowed as measured by the costs the State incurs on account of the taxpayer's activities. Rather, the test is closely connected to the first prong of the Complete Auto Transit test. Under this threshold test, the interstate business must have a substantial nexus with the State before any tax may be levied on it. ... Beyond that threshold requirement, the fourth prong of the Complete Auto Transit test imposes the additional limitation that the measure of the tax must be reasonably related to the extent of the contact, since it is the activities or presence of the taxpayer in the State that may properly be made to bear a "just share of state tax burden," ...

(Citations and footnotes omitted.)

See also Japan Line Ltd. v. County of L.A., 441 U.S. 434 (1979), listing the many services to be considered.

As a practical matter, in view of the range of state provided services focused upon by the Court, it is difficult to perceive any intrastate business presence or the undertaking of any intrastate business function which is not enhanced by the privileges, opportunities and benefits conferred by the market state. No state taxes have been invalidated for failure to survive constitutional scrutiny exclusively under the fourth prong of the test.

[8] Thus, a state tax is constitutionally required to be fairly related to the services provided by the taxing state. This test requires a twofold determination: First, is a business active in the taxing state so that it creates a market for its goods or services in that state's marketplace? Second, is the measure of the tax reasonably related to the extent of the taxpayer's contact with the state?

In this case, it is clear that the taxpayer, by sending employees into this state, is actively engaged in cultivating a market for sales. To accomplish this end, it depends upon the opportunities and protections which this state government provides to all who enter its borders. Because the tax is measured by the amount of sales made to Washington customers, the measure of the tax is reasonably related to the taxpayer's activities within the State, and the taxpayer is shouldering its fair share of "the fruits of civilization for which we pay taxes." The taxpayer's petition as to this issue is therefore denied.

ISSUE NO. 4. Penalties. The taxpayer has argued that, in light of good faith reliance on the opinion of its legal counsel, penalties for the entire period should be abated if the tax is upheld. We must disagree.

We are unable to grant the taxpayer's request because the penalty for late payment of taxes is mandatory under Washington law. RCW 82.32.100 provides in part:

> If any person fails or refuses to make a return . . . the department shall proceed, in such manner as it may deem best, to obtain facts and information on which to base its estimate of the tax; . . .
>
> As soon as the department procures such facts and information as it is able to obtain upon which to base the assessment of any tax payable by any person who has failed or refused to make a return, it shall proceed to determine and assess against such person the tax and penalties due, . . . To the assessment the department shall add, the penalties provided in RCW 82.32.090 . . . . (Emphasis added.)

RCW 82.32.090 specifically provides for the imposition of penalties:

> If payment of any tax due is not received by the Department of Revenue by the due date, there shall be assessed a penalty of five percent of the amount of the tax; and if the tax is not received within thirty days after the due date, there shall be assessed a total penalty of ten percent of the amount of the tax; and if the tax is not received within sixty days after the due date, there shall be assessed a total of twenty percent of the amount of the tax. (Emphasis supplied.)

RCW 82.32.050 likewise provides for the imposition of interest:

> If upon examination of any returns or from other information obtained by the department it appears that a tax or penalty has been paid less than that properly due, the department shall assess against the taxpayer such additional amount found to be due and as to assessments made on and after May 1, 1965, including assessments for additional tax or penalties due prior to that date shall add thereto interest at the rate of nine percent per annum from the last day of the year in which the deficiency is incurred until date of payment. (Emphasis added.)

The use of the word "shall" is a clear indication of the legislature's intent that the penalty and interest provisions be mandatory.

RCW 82.32.105 declares that the Department will waive or cancel the penalties or interest when

> . . . the failure of a taxpayer to pay any tax by the due date was the result of circumstances beyond the control of the taxpayer ...

WAC 458-20-228, the administrative regulation that implements the above legislation, provides in part:

> The Department will waive or cancel the penalties imposed under RCW 82.32.090 and interest imposed under RCW 82.32.050 upon finding that the failure of a taxpayer to pay any tax by the due date was due to circumstances beyond the control of the taxpayer. The Department has no authority to cancel penalties or interest for any other reason.
> (Emphasis supplied.)

[9] The precise issue, then, is whether the taxpayer's mistaken belief, based upon the advice of its legal department, that it was not subject to Washington tax liability constitutes a circumstance beyond the control of the taxpayer. We hold that it does not.

It is the obligation of persons engaged in business within this state to correctly inform themselves of the tax consequences of their activities. This Department maintains a staff of qualified personnel to whom inquiries regarding such matters may be addressed, and information is freely available without charge. Had the taxpayer inquired, it would certainly have been advised that it was required to register with the Department and to report and pay taxes.

Consequently, the taxpayer's mistaken belief, based upon the advice of its legal department, that it was not subject to Washington tax liability cannot be construed as a circumstance beyond the control of the taxpayer.

Incidentally, the Department has not inferred any intent to evade payment of the tax from the taxpayer's failure to register and report taxable income. If such had been the case, then a much more severe penalty would have been imposed under RCW 82.32.050, which provides in part:

> If the department finds that all or any part of the deficiency resulted from an intent to evade the tax payable hereunder, a further penalty of fifty percent of the additional tax found to be due <u>shall</u> be added. (Emphasis supplied.)

DECISION AND DISPOSITION:

The taxpayer's petition for correction of tax assessments and refund is denied in part and sustained in part. Because the due date of the assessments has been extended for the sole convenience of the Department, interest on the assessments will be waived for the period from July 8, 1986 through the new due date.

DATED this 24th day of August 1987.