

Cite as Det. No. 14-0417, 34 WTD 392 (2015)

BEFORE THE APPEALS DIVISION  
DEPARTMENT OF REVENUE  
STATE OF WASHINGTON

|   |   |                                  |
|---|---|----------------------------------|
| In the Matter of the Petition for Correction of | ) | <u>D E T E R M I N A T I O N</u> |
| Assessment of                                   | ) |                                  |
|   | ) | No. 14-0417                      |
| . . .   | ) |                                  |
|   | ) | Registration No. . . .           |
|   | ) |                                  |

[1] RULE 193; RCW 82.04.067: NEXUS. Taxable nexus is created by a taxpayer’s representative who solicits sales and maintains customer relations with the taxpayer’s clients while in Washington. These activities are significantly associated with establishing or maintaining a market for the sales of taxpayer’s products in Washington.

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.

Sattelberg, A.L.J. – An out-of-state trailer manufacturer (“Taxpayer”) protests the Department of Revenue’s (“Department”) assessment of wholesaling business and occupation (“B&O”) tax and accompanying penalties and interest. We conclude that the Department properly assessed B&O tax because the taxpayer has substantial nexus with Washington. We also conclude that delivery of Taxpayer’s products occurs in Washington. Accordingly, we deny the taxpayer’s petition.<sup>1</sup>

### ISSUES

1. Did Taxpayer’s nonresident representative have sufficient contact with Washington to maintain or establish its market in Washington, creating substantial nexus with Washington under RCW 82.04.067(6) and WAC 458-20-193 (“Rule 193”)?
2. Were any of the taxpayer’s sales to its Washington customers delivered out of state and, therefore, not subject to wholesaling B&O tax under Rule 193?

### FINDINGS OF FACT

Taxpayer is an [out of state]-based trailer manufacturer and sells trailers to dealers who sell the trailers at retail. The taxpayer does not have any physical property, such as inventory or equipment, an office, a warehouse, or similar facilities in Washington. Taxpayer does not have any employees or representatives based in Washington. Taxpayer manufactures and sells trailers

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<sup>1</sup> Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

and conducts business operations from its [out of state] location. Taxpayer hired an independent sales representative, [the Representative], in 1998. The Representative's duties include fielding phone calls from potential and existing customers, promoting Taxpayer's products, and contacting potential customers by phone or written correspondence to establish clients. The Representative is compensated on a commission basis and is paid based on the amount of sales generated by his calls or correspondence.

In 2007, the Representative formed a delivery business, [Delivery], to supplement his income. In May of 2007, the Representative purchased a 1999 Ford F350 truck from . . . , Taxpayer's principal shareholder. The Representative purchased the vehicle to be used on behalf of Delivery as well as individually. The vehicle had Taxpayer's decal painted on the side, which was not removed after the sale.

Thereafter, the Representative contacted customers of Taxpayer on behalf of Delivery, independent of his capacity as a representative of Taxpayer, to solicit delivery business. Delivery started making deliveries of Taxpayer's orders into Washington in 2007. Taxpayer claims that Delivery may make deliveries for other businesses into Washington as well, but has not provided any evidence of this. Prior to the Representative forming Delivery, Taxpayer's customers arranged for delivery of Taxpayer's products via third parties. After the Representative formed Delivery, Taxpayer's customers could arrange for delivery either through third parties or Delivery.

In 2013, the Department's Audit Division ("Audit") initially investigated Taxpayer's activities in Washington after a Department employee observed a truck bearing Taxpayer's logo hauling trailers in Washington. On April 30, 2013, Audit met with Taxpayer as part of the investigation. Taxpayer's General Manager, . . . ("the General Manager"), explained to the auditor that an "independent customer service representative visits Washington dealers about one month per year to answer dealers' questions about [Taxpayer's] products, as he (the General Manager) is very busy with his managerial role in the company."<sup>2</sup> The "independent customer service representative" refers to the Representative. The General Manager also explained that:

Washington dealers normally arrange trucking companies to pick up the trailers. Once the dealers in Washington receive the trailers, they sign their names on the sales invoices and return the signed invoice to [Taxpayer]. Therefore, [Taxpayer] always keeps two copies of sales invoices: one copy with dealers' signatures and another copy generated from QuickBooks.<sup>3</sup>

At this meeting, the General Manager provided the auditor a sales invoice for an order of various trailers and trailer parts to a . . . retailer dated April 3, 2013. The "Rep" listed on the invoice is . . . , a reference to Delivery. On the second page of the invoice is a signature block with this paragraph in small print below: "By signing this document you are verifying receipt of the goods listed. [Taxpayer] will not be held responsible for damage caused in transit. It is your responsibility to examine goods upon receipt. Claims for apparent defects or shortages must be made in writing within five [illegible]."

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<sup>2</sup> Audit's response to Taxpayer's petition, dated January 22, 2014.

<sup>3</sup> *Id.*

. . . , Taxpayer's CPA ("the CPA"), later wrote on April 30, 2013, to clarify that the Representative infrequently visits Washington on behalf of Taxpayer.<sup>4</sup> Not long thereafter,<sup>5</sup> the General Manager submitted a letter stating that in fact the Representative never visits Washington on behalf of Taxpayer, but only visits Washington on behalf of Delivery. On June 18, 2013, the CPA wrote to clarify the relationship between Taxpayer and Delivery, reiterating the General Manager's claim that the Representative only visits Washington on behalf of Delivery. The CPA also stated that the General Manager was mistaken about customers accepting deliveries in Washington, but instead insisted that they were accepted [out of state].

In an effort to gather more information about the Representative's activities in Washington, Audit contacted three Washington trailer retailers on July 10, 2013, and asked them these questions:

1. How did you learn of [Taxpayer's] products?
2. When did you start to sell [Taxpayer's] trailers?
3. Has any [representative of Taxpayer] come to visit your business?
4. How often does he visit?
5. Any warranty work performed by [Taxpayer] in Washington?
6. How are [Taxpayer's] product shipped to your business?

The answers to question #1 varied from the long established to not knowing when. The answers to question #2 were all longer than ten years. The answers to question #3 all named the Representative, with one stating that he makes sales calls. The answers to question #4 were (1) once per year, (2) not often, and (3) several times per month in the high season. The answers to question #5 were two "yes" and one "no." The answers to question #6 were by (1) semi truck delivery, (2) the Representative, and (3) the Representative and a third party.

In response to these inquiries, Taxpayer subsequently contacted each of the retailers the Department had contacted in an effort to clarify the Representative's dual role as representative of Taxpayer and as independent delivery business owner. The retailers each sent letters to the Department in response to this contact.<sup>6</sup> Each letter explained that they hire the Representative

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<sup>4</sup> The pertinent part of the email states:

. . . Based on the conversation today between you (the auditor), me (the CPA), and [the General Manager], I heard that the independent sales representative INFREQUENTLY visits Washington on behalf of [Taxpayer]. Additionally, my understanding is that any visits by the independent sales representative to Washington are not to 'maintain [Taxpayer's] market'. My understanding is that [Taxpayer] would receive those sales regardless of whether the independent sales rep ever visited any Washington vendors. [The General Manager] told you and I today that he regularly receives unsolicited calls from potential customers asking to buy [Taxpayer's] product.

<sup>5</sup> The letter is undated; the auditor states the letter was provided on May 21, 2013. Audit's response to Taxpayer's petition, dated January 22, 2014.

<sup>6</sup> [A Retailer] of . . . , Washington sent a letter dated August 19, 2013, stating:

It is my understanding that [Audit] recently contacted an employee of my Company with respect to [Taxpayer] and [the Representative]. I spoke to my employee about the phone call, and my employee said he was nervous, uncomfortable and even felt intimidated by [Audit]. In fact, my employee thought he was talking with the IRS, and not the Washington Department of Revenue.

for delivery purposes, and one of the letters stated that the Representative does not make sales calls on behalf of Taxpayer.

In an effort to gather even more information, the auditor and a colleague visited two other Washington trailer dealers on November 20, 2013. According to the auditors, one trailer dealer, . . . said it does not sell Taxpayer's products, but was familiar with the Representative from his sales calls. The auditors also met with the President of [a Retailer in] Washington. They claim he said he initially arranged with the Representative to begin selling Taxpayer's products while at a meeting with the Representative in Washington. According to the auditors, [the Retailer] does not pay any commission to the Representative, nor does the Representative have the [Retailers] purchase order when he picks up trailers [out of state] for delivery to [the Retailer] in . . . Washington.

Based on its investigation, Audit determined that Taxpayer had created nexus with Washington, and on December 2, 2013, assessed Taxpayer for the period January 1, 2009, through June 30, 2013. The assessment consisted of \$. . . in wholesaling B&O tax, \$. . . in delinquent penalties, a \$. . . assessment penalty, and \$. . . in interest.

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I have seen a copy of the questions asked and the answers [Audit] says were given. Some of the answers are inaccurate. I'm not certain whether the answers are inaccurate because my employee was nervous or uncomfortable and therefore gave inaccurate information, or if [Audit] simply misunderstood the answers given. Either way, this letter is to clarify any confusion.

[The Representative] is a service rep and delivery driver. I pay him to pick up trailers from various manufacturers and deliver those trailers to my Company. He has the right of inspection and the right to accept or reject goods at every manufacturer where he picks up the trailers. My employees do not know of this arrangement; therefore, they are not in a position to accurately answer the questions you asked.

[The Representative] does not make sales calls on behalf of [Taxpayer]. [Taxpayer] has never solicited orders from me; I order from them by email, phone or faxing in order forms to [Taxpayer's] office [out of state]. In fact, we were a dealer for [a Manufacturer] which was the company that existed before [Taxpayer]. [Taxpayer] did not contact us for sales order since we were already a customer when they purchased the company. There are no product demonstrations at my location.

[A Retailer] of . . . , WA, sent a letter dated September 24, 2013, stating:

My company, . . . , formally [sic] . . . (The previous Trailer Dealership I worked for, now out of business) and had been purchasing trailers from [Taxpayer] since the mid 1990's, has been purchasing trailers from [Taxpayer] since we re-opened under the new name in 2010.

I order my trailers primarily by fax, occasionally by e-mail to [Taxpayer's] home office [out of state].

I hire [the Representative] directly, to delivery [sic] my trailers. He is authorized to up the trailers from [Taxpayer], on my behalf.

[Taxpayer] builds one of the highest quality and respected trailers for the northwest and we are proud to do business with them. I have customers that will not buy any other trailer.

[A Retailer] of . . . , WA, sent a letter dated September 26, 2013, stating:

[Retailer] buys trailers from [Taxpayer]. Orders are placed by phone or fax direct to the factory [out of state]. It is our responsible [sic] to arrange transportation of the trailers from the factory. [The Representative] is one of the contractors we use to transport trailers. Drivers have the right to inspect trailers at the time of delivery and have the right to accept or reject the trailer at that time.

Taxpayer timely appealed the assessment, arguing that it does not have nexus with Washington. Taxpayer later provided a response from [a Retailer] to the information the Department's auditors had gathered from it in November of 2013. The letter from Retailer's President, . . . , dated June 3, 2014, states that his initial meeting with the Representative was [out of state] and that the meeting to initially begin doing business together was also in [out of state]. The letter states that orders are made via fax, phone, or email, and that they make as many of their own deliveries as possible. [Retailer] says that it picks up some of the trailers it buys from Taxpayer [out of state], though the Representative has been hired on occasion to deliver Taxpayer's products into Washington.

On appeal, Taxpayer provided invoices from Delivery to one of its and Taxpayer's common Washington customers. The invoices cover the first six months of 2012, with 21 total deliveries. The invoices are handwritten on various pre-printed invoice forms with the most common billing amount being \$. . . for a single delivery. No additional information regarding Delivery's operations was provided.

Taxpayer argues that the Representative, through Delivery, began acting as an agent of Taxpayer's customers, even if he'd initially accepted the order in his capacity as representative for Taxpayer. Taxpayer argues that the Representative, through Delivery, accepts delivery of Taxpayer's customer's orders [out of state], before delivering them into Washington. Taxpayer claims that the Representative had authority to accept or reject trailers on behalf of Taxpayer's/Delivery's customers, though no written authority has been provided. Taxpayer claims that the Representative does not visit Washington on behalf of Taxpayer. Taxpayer claims that the majority of its customers were established before the Representative joined Taxpayer.

### ANALYSIS

Washington imposes its B&O tax "for the act or privilege of engaging in business" in this state. RCW 82.04.220. The B&O tax rate varies based on the type of business activity the taxpayer engages in and the statute provides numerous classifications of activities. Chapter 82.04 RCW. The measure of the B&O tax is the application of rates against "value of products, gross proceeds of sales, or gross income of the business, as the case may be." RCW 82.04.250, RCW 82.04.270, and RCW 82.04.220. B&O tax is imposed on wholesale sales under RCW 82.04.270

Rule 193(7) explains when Washington's B&O tax applies to inbound sales of tangible personal property:

**Inbound sales.** Washington does not assert B&O tax on sales of goods which originate outside this 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. The B&O tax will not apply if one of these elements is missing.

## 1. Nexus

The Commerce Clause grants Congress the power “to regulate commerce among the several states.” U.S. Const. Art. 1, § 8, cl. 3. The United States Supreme Court in numerous decisions has interpreted the Commerce Clause to prohibit, by negative implication, state taxes that unduly burden or discriminate against interstate commerce. *See, e.g., Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 289 (1977).

The Constitutional nexus limitation requires that the transaction being taxed have “substantial nexus” with the taxing state. *Complete Auto Transit*, 430 U.S. at 279. In *Complete Auto Transit*, the U.S. Supreme Court articulated a four-pronged test that a state tax must satisfy to withstand a Commerce Clause challenge to its jurisdiction to tax. The Court held that the Commerce Clause requires that the tax: (1) be applied to an activity with “substantial nexus” with the taxing state, (2) be fairly apportioned, (3) not discriminate against interstate commerce, and (4) be fairly related to the services provided by the state. 430 U.S. at 279.

A substantial nexus exists when a company’s activities in Washington are . . . significantly associated with its ability to establish and maintain a market in Washington for its sales. *Space Age Fuels Inc. v. State of Washington*, 178 Wash. App. 756, 762, 315 P.3d 604; *Tyler Pipe Indus., Inc. v. Wash. 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 Wash.2d 838, 842, 246 p.3d 788, *cert. denied*, 132 S. Ct. 95 (2011). A company’s physical presence in Washington can establish a substantial nexus. *Space Age*, 178 Wash. App. at 762 (citing *Lamtec*, 170 Wash.2d at 845). Periodic visits can create a physical presence. *Id.* at 762.

For substantial nexus to exist, a person need not send employees into Washington. Det. No. 05-0376, 26 WTD 40 (2007). Rather, nexus may be created through independent contractors. *Id.* (citing *Tyler Pipe*, 483 U.S. 232 (1987) (holding that a showing of sufficient nexus cannot be defeated by the argument that the seller’s representative was properly characterized as an independent contractor instead of as an agent)); *Scripto, Inc. v. Carson*, 362 U.S. 207 (1960) (holding that nexus was established by a seller’s in-state solicitation performed through independent contractors); and Det. No. 01-074, 20 WTD 531 (2001).

The employees or independent contractors do not need to be continually present in Washington to create nexus, but can create nexus through periodic visits. *Lamtec*, 170 Wash.2d at 846; *Space Age*, 178 Wash. App. at 762. In *Lamtec*, the taxpayer, based out of state, made sales into Washington. 170 Wash.2d at 841. *Lamtec* did not have any employees, property, or office space located in Washington. *Id.* *Lamtec* sent employee sales representatives into Washington about two or three times each year to visit major customers. *Id.* During those visits, the employees did not solicit sales directly, but they answered questions and provided information about *Lamtec* products. *Id.*

The Washington Supreme Court held the following:

The contacts made by *Lamtec*’s sales representative were designed to maintain relationships with its customers and to maintain its market within Washington State. Nor

were the activities slight or incidental to some other purpose or activity. We hold that Lamtec's practice of sending sales representatives to meet with its customers within Washington was significantly associated with its ability to establish and maintain its market.

170 Wash.2d at 851. *See also* RCW 82.04.067(6), which applies for the portion of the audit period beginning June 1, 2010.<sup>7</sup>

Consistent with the above authority, the Department has found on numerous occasions that visits to Washington that don't involve soliciting sales can constitute significant services in relation to the establishment or maintenance of its Washington market. *See* Det. No. 05-0174, 25 WTD 48 (2006) (twice-yearly visits to present new or existing products and demonstrate use of products), Det. No. 04-0208, 24 WTD 217 (2005) (participation in trade shows), Det. No. 00-003, 19 WTD 685 (2000) (regular and recurring in-state training and introducing and promoting new products), Det. No. 97-061, 18 WTD 211 (1999) (one or two visits per year to cultivate goodwill, obtain input on taxpayer products, address user concerns, resolve problems with accounts, and dispense information about taxpayer products), Det. No. 98-146, 18 WTD 175 (1998) (two or three visits per year to deliver catalog updates, provide technical advice, and explain new products), Det. No. 91-213, 11 WTD 239 (1991) (occasional visits to show product samples and to explain the company's policies).

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Just [as] in *Lamtec*, we find, based on the evidence presented, that Taxpayer sends the Representative into this state to visit its customers and at least maintain its customer relations and answer questions. These activities are specifically designed to ensure that Taxpayer keep these customers. These visits need not be to solicit sales. Courts recognize that an out-of-state company need not engage in direct selling activities in the taxing jurisdiction for substantial nexus to exist. *E.g.*, *Standard Pressed Steel Co. v. Dep't of Revenue*, 419 U.S. 560 (1975); *General Motors Corp. v. Washington*, 377 U.S. 436 (1964); *Space Age Fuels*, 178 Wash. App. at 166; *General Motors Corp. v. City of Seattle*, 107 Wash. App. 42, 52, 25 P.3d 1022 (2001), *review denied*, 145 Wash.2d 1014, *cert. denied*, 535 U.S. 1056 (2002).

One Washington trailer dealership said that it knew the Representative from his sales calls. Two Washington trailer dealerships initially said they knew the Representative from his sales calls, but then later said they only knew him from his association with Delivery. Two other

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<sup>7</sup> RCW 82.04.067(6) provides:

For purposes of the taxes imposed under this chapter on any activity not included in the definition of apportionable activities in RCW 82.04.460, a person is deemed to have a substantial nexus with this state if the person has a physical presence in this state, which need only be demonstrably more than a slightest presence. For purposes of this subsection, a person is physically present in this state if the person has property or employees in this state. A person is also physically present in this state if the person, either directly or through an agent or other representative, engages in activities in this state that are significantly associated with the person's ability to establish or maintain a market for its products in this state.

Washington trailer dealerships initially said they knew the Representative through visits to their business. They both later wrote to clarify their relationship with the Representative, but neither of these businesses state that the Representative does not solicit sales, answer questions, or otherwise maintain customer relations. Both letters state that orders are placed by phone, fax, or e-mail, but that only means that orders were transmitted in that method, it doesn't contradict what they said to Audit initially.

In addition to visiting customers in Washington, the Representative drives into Washington for Delivery hauling trailers manufactured by Taxpayer in a truck bearing Taxpayer's logo. While this is not the exact circumstance in *Space Age*, it is another way in which Taxpayer's Washington market is being maintained or established through the Representative's activities in Washington. We find that the Representative has created nexus for Taxpayer through his in-state activities.

## 2. Delivery

The taxpayer next argues its sales to its Washington clients are not subject to B&O tax because the goods were not received by its clients in this state. Washington does not impose B&O tax on "sales of goods which originate outside this state unless the goods are received by the purchaser in this state and the seller has nexus." Rule 193(7). Because we have already determined that the taxpayer has nexus with this state, we must analyze where the taxpayer's sales occurred for Washington tax purposes.

RCW 82.04.040(1) explains that a "sale" occurs when there is "any transfer of the ownership of, title to, or possession of property for a valuable consideration . . . ." WAC 458-20-103 ("Rule 103") defines when and where a sale occurs for Washington tax purposes. That rule provides, in relevant part:

For the purpose of determining tax liability of persons selling tangible personal property, a sale takes place in this state when the goods 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 the state.

*Id.* Pursuant to RCW 82.04.040 and Rules 103 and 193, a Washington sale for B&O tax purposes takes place if the goods are delivered by the purchaser or its agent in this state. Rule 193(7)(a) explains as follows:

Delivery of the goods to a . . . for-hire carrier located outside this state merely utilized to arrange for and/or transport the goods into this state is not receipt for the goods [outside this state] by the purchaser or its agent unless the . . . for-hire carrier has express written authority to accept or reject the goods for the purchaser with the right of inspection.

Excise Tax Advisory 3091.2009 ("ETA 3091") clarifies Rule 193 with respect to what constitutes receipt at an out-of-state location where the for-hire carrier is given express written authority to accept the goods for the purchaser. ETA 3091 provides, in pertinent part:



For receipt to occur at the out-of-state location, the for-hire carrier must take those actions that would generally be taken by a prudent buyer to assure that the goods conform to the purchase order or contract. *This generally requires at a minimum that the goods be physically examined by the receiving agent.* The agent must also have access to the purchase order or contract in order to determine if the goods conform. The mere giving to the for-hire carrier of a written authority to accept the goods at an out-of-state location, without some further act of acceptance, will not be considered as receipt by the purchaser or the purchaser's agent at that location. *In short, the carrier must not only have written authority to accept or reject goods for the buyer, it must actually do so and provide documentation of that fact to the seller.*

ETA 3091 (Emphasis added).

The evidence does not show that delivery of its goods occurred [out of state] in compliance with ETA 3091. There is no proof that Delivery or any third party delivery businesses accepted goods [out of state] on behalf of the Washington dealers. There is no proof that Delivery or any third party delivery businesses had written authority to do so. Moreover, there is no evidence that Delivery or any third party delivery businesses physically inspected the goods [out of state]. The little documentation Taxpayer has provided, such as the invoices provided by General Manager, actually show that Taxpayer's customers had the obligation to inspect the goods upon receiving them in Washington and could file claims with Taxpayer for repairs of the goods. Finally, the Representative's dual role as sales representative for Taxpayer and delivery agent for the customer casts doubt on whether the Representative could actually accept or reject the goods [out of state]. We find that Taxpayer delivered its trailers into Washington where its customers received the products.

#### DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 31st day of December, 2014.