

Cite as Det. No. 16-0296, 36 WTD 255 (2017)

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. 16-0296
)	
...)	Registration No. . . .
)	

RULE 193; RCW 82.04.067: NEXUS. Taxable nexus is created by a taxpayer’s employees maintaining existing customer relationships with the taxpayer’s Washington 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, T.R.O. – A shooting sports products distributor (“Taxpayer”) protests the Department of Revenue’s (“Department”) assessment of wholesaling business and occupation (“B&O”) tax and argues that it did not have contacts with Washington sufficient to constitute nexus during the audit period. We deny the petition.¹

ISSUE

Does the taxpayer have substantial nexus with Washington . . . if nonresident representatives entered into Washington no more than three times per year visiting six to nine customers over the course of two to six days each to maintain existing customer relationships?

FINDINGS OF FACT

Taxpayer distributes shooting sports products from its main location in [out-of-state], and from its distribution center in [out-of-state]. Taxpayer reported wholesaling B&O tax to Washington from February of 1992 through May of 2009. On June 19, 2009, Taxpayer’s Controller at the time wrote the Department a letter explaining that it historically had nexus with Washington from a sales representative soliciting sales in-state, but that the representative’s last visit was in May of 2004. Taxpayer’s Controller requested that the Department close its account in the letter, and the Department closed it.

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

In 2014, the Department’s Compliance Division (“Compliance”) began investigating Taxpayer’s business activities in Washington. In September, Compliance sent Taxpayer a Washington Business Activity Questionnaire (“Questionnaire”), which Taxpayer completed and returned. The Questionnaire indicated that nonresident employees were making visits to Washington to maintain existing customer relationships. The Questionnaire also indicated that Taxpayer was still shipping goods into Washington via common carrier. Compliance called Taxpayer’s Controller, who confirmed a nonresident employee had been making trips into Washington for the last ten years to maintain existing customer relationships. Compliance called the employee who said she makes three or four trips a year to different retailers in Washington with one trip being to eastern Washington and the remainder to Seattle. Compliance stated that the employee said she informs the Washington retailers of new products and fosters corporate goodwill. Compliance also stated that the employee said she solicits sales on the in-state visits, although Taxpayer disputes this statement. We make no finding whether the employee does or doesn’t solicit sales in Washington.

Based on the information provided, Compliance concluded that Taxpayer had nexus with Washington. Compliance contacted Taxpayer to obtain actual sales figures for Washington for the period June 1, 2009, through July 31, 2015. Taxpayer did not provide them. On November 6, 2015, Compliance issued two assessments to Taxpayer based on estimated figures for a combined total of \$²

Taxpayer timely petitioned for review of the assessments and provided affidavits from three employees. The affidavits state that at least one of the employees visited Washington every year no more than three times per year visiting six to nine customers over the course of two to six days. Taxpayer argues that this level of in-state contact is insufficient to establish nexus. Taxpayer also provided actual sales figures for the audit period on review.

ANALYSIS

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

² The assessment covering January 1, 2009, through December 31, 2010, consists of \$. . . in wholesaling B&O tax, \$. . . in delinquent penalties, \$. . . in interest, a \$. . . substantial underpayment penalty, and a \$. . . unregistered business penalty. The assessment covering January 1, 2011, through July 31, 2015, consists of \$. . . in wholesaling B&O tax, \$. . . in delinquent penalties, \$. . . in interest, a \$. . . substantial underpayment penalty, and a \$. . . unregistered business penalty.

the services provided by the state. 430 U.S. at 279. [Taxpayer challenges only the first prong, substantial nexus.]

...

[Courts have not established a bright-line definition of the term ‘substantial nexus.’ However, the United States Supreme Court, and Washington courts, have held that substantial nexus is established by activities designed to establish or maintain a market within the state for the taxpayer’s goods or services. *Lamtec Corp. v. Dep’t of Revenue*, 170 Wash.2d 838, 842, 246 P.3d 788, *cert. denied*, 132 S. Ct. 95 (2011); *see also Tyler Pipe Industries, Inc. v. Dep’t. of Revenue*, 483 U.S. 232, 250, 107 S. Ct. 2810 (1987).] The Washington Supreme Court has held that a person does not have to solicit sales in order to engage in activities that are significantly associated with the person’s ability to establish or maintain a market for its products in Washington. *Lamtec Corp.*, 170 Wash.2d at 842, 246 P.3d 788. In *Lamtec*, the taxpayer, based out of state, made sales into Washington. *Id.* 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.

Id. at 851.

Just as in *Lamtec*, Taxpayer here sends non-resident employees into Washington to visit its customers and maintain existing relationships. These activities are specifically designed to ensure that the taxpayer keep these customers. [Even if the purpose of the visits was to maintain customer relationships and did not involve actual sales solicitation, we would conclude that physical presence is established.]. 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, Inc. v. Dep’t of Revenue*, 178 Wn. App. 756, 315 P.3d 604 (2013); *General Motors Corp. v. City of Seattle*, 107 Wn. App. 42, 52, 25 P.3d 1022 (2001), *review denied*, 145 Wn.2d 1014, *cert. denied*, 535 U.S. 1056 (2002).

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. 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).

In accordance with the above authority, we find that Taxpayer's employees entering Washington to maintain existing customer relationships constitutes significant services in relation to the establishment or maintenance of its sales into Washington. This gives Taxpayer a physical presence in Washington and, therefore, it is liable for B&O tax on its wholesale sales in to Washington.³ Therefore, we deny its petition.

We note that Taxpayer provided actual sales figures on review. We remand to Compliance to recalculate the amount of B&O tax Taxpayer owes based on these actual figures.

DECISION AND DISPOSITION

Taxpayer's petition is denied. We remand the assessments to Compliance to adjust them based on actual figures provided. Compliance will issue new assessments with a new due date.

Dated this 15th day of September 2016.

³ After September 1, 2015, nexus for wholesale sales for out-of-state entities is determined based on Washington's economic nexus thresholds. RCW 82.04.067(6)(a). These thresholds for 2015 are:

- (1) More than fifty three thousand dollars of property in this state;
- (2) More than fifty three thousand dollars of payroll in this state;
- (3) More than two hundred sixty seven thousand dollars of receipts from this state; or
- (4) At least twenty-five percent of the person's total property, total payroll, or total receipts in this state.