SUSAN JESMER, d/b/a NATIVE TRADING ASSOCIATES 442 FROGTOWN ROAD HOGANSBURG, NY 13655,	§	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
Petitioner,	§	DOCKET NO. MISC. 08-858
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

FINAL ORDER

Susan Jesmer, d/b/a Native Trading Associates ("Petitioner"), appealed to the Administrative Law Division pursuant to Code of Ala. 1975,§40-2A-8(a) concerning her obligation to make escrow payments to the Department for cigarettes manufactured by the Petitioner and sold to Alabama customers by an unrelated third party internet seller. A hearing was conducted on January 12, 2010. Bryan Haynes represented the Taxpayer. Assistant Counsel Wade Hope represented the Department.

Alabama and 45 other States entered into a Master Settlement Agreement ("Agreement") with various major tobacco product manufacturers in 1998. The Agreement settled the States' claims that the manufacturers had misled the public concerning the dangers of cigarettes and had targeted their advertising to minors. The Agreement required each of the participating States to enact an escrow statute, which Alabama did in 1999. See, Code of Ala. 1975, §6-12-1 et seq.

The Alabama escrow statute requires that tobacco product manufacturers selling their products in Alabama must either join the Agreement and perform their financial obligations thereunder, or, in lieu of participating in the Agreement, make annual escrow payments based on the number of "units sold" in the State. "Units sold" is defined by

Alabama law as the "number of individual cigarettes sold in the state by the applicable tobacco product manufacturer . . . during the year in question, as measured by excise taxes collected by the state on packs, or roll-your-own tobacco containers, bearing the excise tax stamp of the state." Code of Ala. 1975, §6-12-2(10).

In 2003, Alabama enacted the Tobacco Master Settlement Complementary Legislation Act (the "Complementary Act"), Code of Ala. 1975, §6-12A-1 et seq. That Act required the Revenue Department to create and maintain a directory of approved tobacco product manufacturers that have satisfied their obligations under the escrow statute. Code of Ala. 1975, §6-12A-3. The Act also prohibits a nonparticipating manufacturer from selling its products in Alabama unless the manufacturer and its cigarette brand styles are listed in the directory.

The Petitioner in this case is a nonparticipating tobacco product manufacturer located in New York State. She manufacturers the "Native" cigarette brand, which she sells in approximately 30 states. As a nonparticipating manufacturer, the Petitioner is required to make escrow payments based on units sold in the participating states in which the Native brand is sold.

Before 2008, the Petitioner was not listed in Alabama's directory of approved tobacco manufacturers, nor did she sell the Native brand directly to customers in Alabama. Native brand cigarettes were, however, sold by an unrelated internet seller to customers in Alabama in 2006 and 2007. The internet seller sold the cigarettes in Alabama in those years without the Petitioner's knowledge or permission. The Petitioner contends, and the Department does not dispute, that the internet seller had purchased the Native brand cigarettes from one of the Petitioner's distributors on an Indian reservation in New York.

Cigarettes sold for consumption on Indian reservations are not considered "units sold," and thus are not subject to escrow payments under the Agreement. Consequently, the Petitioner did not factor in or add an escrow payment when she priced the Native brand cigarettes she sold on the New York reservation.

The internet seller was required by the federal Jenkins Act, 15 U.S.C. §376, to report his sales of Native brand cigarettes in Alabama to the Revenue Department. The Department subsequently collected the applicable Alabama excise tax due on the cigarettes from some, but not all, of the Alabama purchasers/consumers. It also notified the Petitioner that she was liable to make escrow payments on the cigarettes. Specifically, the Department demanded an escrow payment from the Petitioner of $638.98 for 29,800 Native brand cigarettes sold by the internet seller to Alabama customers in 2006, and $2,334.94 for 93,000 Native brand cigarettes sold by the internet seller in Alabama in 2007.

The Petitioner filed a petition for review and objected to the escrow payments, arguing that the Native brand cigarettes sold by the internet seller in Alabama were not "units sold," as defined by §6-12-2(10), because the cigarettes were not stamped with the Alabama excise tax stamp, and also because the Alabama excise tax was not collected on some of the cigarettes. While the petition was pending, the Petitioner remitted the requested escrow payments to the Department and applied to be listed in the Department's directory of approved manufacturers. She did so because she intended to directly sell the Native brand to Alabama customers in the future.

The Department added the Petitioner to the directory. It also subsequently denied the Petitioner's petition for review, holding that the Native brand cigarettes sold by the internet seller in Alabama in 2006 and 2007 were "units sold," and thus subject to the

escrow statute. This appeal followed.

This case turns on whether the Native brand cigarettes illegally sold by the internet seller in Alabama in 2006 and 2007 constituted units sold within the purview of the escrow statute. As indicated, "units sold" is defined at §6-12-2(10) as "[t]he number of individual cigarettes sold in the state by the applicable tobacco product manufacturer, . . . during the year in question, as measured by the excise taxes collected by the state on packs, or roll-your-own tobacco containers, bearing the excise tax stamp of the state."

The Department interprets the term "units sold" to include all cigarettes that are subject to Alabama's excise tax. It argues that requiring all taxable tobacco products sold in Alabama to be subject to escrow payments, whether stamped or not, is necessary to keep both participating and nonparticipating tobacco product manufacturers on an even footing.

> But basically the policy the Department of Revenue has got is that if it is subject to the state excise tax, in order to keep the escrow statutes and the MSA working together, to treat everybody equally, we require a deposit to be made into an escrow account.

T. at 17.

> Like I said, anything that's subject to the excise tax, we treat it as being subject to the escrow. We feel like that's the only way you could be fair about it.

T. at 40.

The Petitioner argues that the intent of the Legislature can only be gleaned from the language of the applicable statute. She claims that the plain, unambiguous language of §6-12-2(10) requires that for cigarettes sold in Alabama to be considered "units sold" for purposes of the escrow statute, they must "bear(ing) the excise tax stamp of the state."

The Petitioner's position is articulately stated in her post-hearing brief, as follows:

> I. Under the Escrow Statute's Clear and Unambiguous Terms, the Sales at Issue Were Not "Units Sold" and Therefore Were Not Subject to Escrow Payments.
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> As discussed above, the Escrow Statute requires non-participating manufacturers to make escrow payments only for "units sold" in the State. Ala. Code § 6-12-3(2)(a). "Units sold" are defined as cigarettes meeting the following requirements: (1) they were sold in the State; (2) applicable State excise taxes were paid on the cigarettes, and (3) the cigarettes were stamped with the State excise tax stamp. Id. § 6-12-2(10).
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> It is undisputed that the cigarettes at issue did not meet the third requirement - they were not stamped with the State excise tax stamp. Because Mr. Maybee sold "Native" cigarettes direct to consumers (in violation of State law), and not through authorized distribution channels, the cigarettes never bore the State excise tax stamp. Accordingly, the cigarettes were not "units sold" and therefore were not subject to escrow payments.
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> The cigarettes also were not "units sold" because applicable excise taxes were not paid on all of the cigarettes. Of the 29,800 "Native" cigarettes sold in 2006, the Department concedes that taxes were paid on only 24,723 cigarettes. Of the 93,000 "Native" cigarettes sold in 2007, the Department concedes that taxes were paid on only 79,000 cigarettes. Cigarettes sold in the State are not "units sold" unless applicable excise taxes are paid. Ala. Code § 6-12-2(10). Because applicable excise taxes admittedly were not paid on the cigarettes at issue, they are not subject to escrow payments under the Escrow Statute.
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> II. The Department's Position is Contrary to the Escrow Statute's Clear and Unambiguous Terms.
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> Even though the cigarettes at issue were never stamped, and even though taxes were not paid on all of the cigarettes, the Department asserts that the cigarettes were "units sold" and subject to escrow payments. In making this argument, the Department necessarily misreads the Escrow Statute. The Department claims that "units sold" includes all "taxable" cigarettes, and that the definition is designed to exclude only tax-exempt cigarettes. However, "units sold" is not defined to encompass all "taxable" cigarettes, but rather is limited to cigarettes bearing the State excise tax stamp and for which excise taxes have been paid. If the Legislature intended for "units sold" to include all "taxable" cigarettes, and to exclude only tax-exempt cigarettes, it readily could have done so by defining "units sold" to cover all cigarettes sold in the State except for tax-exempt cigarettes.

The Department also argues that cigarettes need not be stamped to constitute "units sold." The Department claims that all of Alabama's excise taxes are "stamp" taxes, and that the reference to excise tax stamps in Ala. Code § 6-12-2(10) necessarily includes all tobacco taxes. This argument is misplaced for several reasons. First, the premise for the Department's argument - that all of Alabama's excise taxes are "stamp" taxes - is incorrect. For example, Alabama's tobacco product use tax, Ala. Code § 40-25-41, which applies to unstamped cigarettes purchased outside normal distribution channels, is not a "stamp" tax. Indeed, the Alabama use tax applies to the sales at issue here because they were not sold through an authorized distributor and were never stamped. Because the Alabama use tax is not a "stamp" tax, the reference to excise tax stamps in Ala. Code § 6-12-2(10) necessarily does not include all tobacco taxes, including the use tax.

The gist of the Department's argument is that the reference to excise tax stamps in the definition of "units sold" includes all cigarette sales that are "stampable." However, the definition does not refer to cigarettes that are "stampable," but rather refers specifically to cigarettes "bearing the excise tax stamp of the State." Even if the definition of "units sold" could be read to include all cigarettes that are "stampable," the "Native" cigarettes sold by Mr. Maybee were not "stampable." As discussed above, NTA was not listed in the Alabama Directory when Mr. Maybee sold the cigarettes in 2006 and 2007. Because NTA and "Native" cigarettes were not listed in the Alabama Directory, the cigarettes sold by Mr. Maybee could not legally be stamped. See Ala. Code § 6-12A-3(c). The cigarettes also could not legally be stamped because they were not sold by an authorized distributor. See Ala. Code § 40-25-16.

In sum, the Department's attempt to compel NTA to make escrow payments for Mr. Maybee's sales is contrary to the Escrow Statute's clear terms. The Escrow Statute does not impose escrow liability for all "taxable" cigarettes, but only for cigarettes where applicable taxes have been paid. The Escrow Statute does not impose escrow liability for all "stampable" cigarettes, but only for cigarettes actually bearing the State excise tax stamp.

The Department has alternatively argued that the definition of "units sold" creates an inadvertent loophole defeating the purpose of the Escrow Statute, which is purportedly to impose escrow liability for all cigarettes sold by non-participating manufacturers in the State. However, the Escrow Statute's purported intent cannot trump its clear terms. See Deal v. Deal, 587 So. 2d 413, 415 (Ala. Civ. App. 1991) ("We are bound to follow the clear language of the Code. Unless a statute is ambiguous or unclear, we are not authorized to indulge in conjecture regarding the legislative intent or to look as to the consequences of the interpretation of the law as written.") Legislative intent is expressed in a statute's clear language, and if the legislature's intent differs from the statute's clear language, "it is the province of the legislature to clarify the matter in the language of the statute." State v. Brooks, 701 So. 2d 56, 58 (Ala. Crim. App. 1996). The statute must be enforced as

> written. Id.
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> Indeed, numerous other States that are signatories to the MSA have removed the stamping requirement by amending their versions of the Escrow Statute. See Alaska Stat. § 45.53.100; Ky. Rev. Stat. Ann. § 131.600; Mont. Code Ann. § 16-11-401; Neb. Rev. Stat. § 69-2701; N.D. Cent. Code § 51-25-01; Utah Code Ann. § 59-22-201; Wyo. Stat. Ann. § 9-4-1201. Each of these States altered the definition of "units sold" by passing an amendment to their versions of the Escrow Statute, not by unilaterally changing the definition through enforcement action. Alabama is free to do the same, of course, but the Department may not act for the legislature by amending the statute through its enforcement.
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> Even if the purported intent of the Escrow Statute could trump its unambiguous terms, it is just as likely that the Alabama Legislature intentionally crafted the Escrow Statute to remove escrow liability for rogue, illegal sales like those at issue here. By limiting "units sold" to stamped cigarettes, it appears that the Legislature sought to eliminate escrow liability for cigarettes that are sold illegally or outside normal distribution channels. Presumably the Legislature deemed it improvident to impose escrow liability for cigarettes sold illegally, without the non-participating manufacturer's knowledge and against their express wishes. Rather then prosecute the individuals who flagrantly violated State law - Mr. Maybee and his Alabama customers - the Department instead seeks to impose escrow liability on an innocent manufacturer whose products were unwittingly sold in the State. Such a result would be contrary to both the Escrow Statute's clear terms, as well as the Legislature's intent as evidenced by those clear terms.

Petitioner’s Post-Hearing Brief at 6 – 10.

The above argument is convincing. Alabama’s appellate courts have repeatedly held that the plain, unambiguous language of a statute must control. *Pilgrim v. Gregory*, 594 So.2d 119 (Ala. Civ. App. 1991); *Ex parte Kimberly-Clark Corp.*, 503 So.2d 304 (Ala. 1987). The clear language of §6-12-2(10) requires that to be considered units sold for purposes of the escrow statute, the tobacco product must bear the excise tax stamp of Alabama. The Legislature could have defined the term to include those products subject to the Alabama excise tax or those products that are required to be stamped, but it did not.

And as argued by the Petitioner, the Legislature may have intended to limit the term “units sold” to only stamped products because it did not intend to impose an escrow liability

on a manufacturer for cigarettes sold illegally in Alabama by a third party without the permission or knowledge of the manufacturer, as the internet seller did in this case.

The Department's attempt to fairly administer the escrow statute is commendable. But under the facts of this case, it would be unfair to require the Petitioner to make escrow payments on cigarettes illegally sold by an unrelated party in Alabama without her knowledge or permission. In any case, as discussed, the plain language of the applicable statute must control.

The Department is directed to return to the Petitioner the escrow payments made by the Petitioner on the Native brand cigarettes illegally sold by the internet seller to Alabama customers in 2006 and 2007. Judgment is entered accordingly.

This Final Order may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered April 13, 2010.

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BILL THOMPSON
Chief Administrative Law Judge

bt:dr
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