STATE OF FLORIDA
DIVISION OF ADMINISTRATIVE HEARINGS

BRANDY'S PRODUCTS, INC.,

Petitioner,

vs. Case No. 14-3496

DEPARTMENT OF BUSINESS AND PROFESSIONAL REGULATION, DIVISION OF ALCOHOLIC BEVERAGES AND TOBACCO,

Respondent.
_____/

DEPARTMENT'S EXCEPTIONS TO THE RECOMMENDED ORDER

Respondent, Department of Business and Professional Regulation, Division of Alcoholic Beverages and Tobacco (DBPR or Department), pursuant to section 120.57(1)(k), Florida Statutes and rule 28-106.217 of the Florida Administrative Code, files the following exceptions to the Administrative Law Judge's Recommended Order, filed on February 24, 2015.

ABBREVIATIONS

Administrative Law Judge	ALJ
Recommended Order page/paragraph	RO p./para.
Final Hearing Transcript page	T 1 or 2, at p. number

INTRODUCTION

A reviewing agency may not reject or modify findings of fact unless the agency determines on the basis of a review of the complete record that there is no competent substantial evidence from which findings could be inferred. Groin v. Comm'n on Ethics, 658 So. 2d 1131 (Fla. 1st DCA 1995). Substantial evidence is evidence that provides a substantial basis from which the fact at issue can be reasonably inferred, and it is competent evidence if it is relevant

and material to the issue or issues presented for determination. Gainesville Bonded Warehouse, Inc. v. Carter, 123 So. 2d 336 (Fla. 1960).

Contemporaneous construction of a statute by the agency charged with its enforcement and interpretation is entitled to great weight, PW Ventures, Inc. v. Nichols, 533 So.2d 281 (Fla. 1988), and such interpretation should not be overturned unless unauthorized or "clearly erroneous." Dep't of Envtl. Regulation v. Goldring, 477 So. 2d 532 (Fla. 1985). If the agency's interpretation is within the range of possible and reasonable interpretations, it is not clearly erroneous and should be affirmed. Dep't of Educ. v. Cooper, 858 So. 2d 394, 396 (Fla. 1st DCA 2003).

Section 120.57(1)(e)1, Florida Statutes, places an independent duty on the ALJ not to base recommended agency action that determines the substantial interests of a party on an unadopted rule. An "unadopted rule" is defined as an agency statement that meets the definition of the term rule but that has not been formally adopted [1] § 120.52(20), Fla. Stat. However, this prohibition against reliance on an unadopted rule does not preclude the application of adopted rules and law to the facts. § 120.57(1)(e)1, Fla. Stat.; *see also* Amerisure Mut. Ins. Co. v. Dep't of Fin. Servs., 2015 WL 46515 (Fla. 1st DCA Jan. 2, 2015).

As set forth below, the RO erroneously applied law within the Department's substantive jurisdiction and made findings wholly lacking in record support.

[1] A rule is "an agency statement of general applicability that implements, interprets, or prescribes law or policy or describes the procedure or practice requirements of any agency and includes any form which imposes any requirements or solicits any information not specifically required by statute or by an existing rule." § 120.52 (16), Fla. Stat. A rule is invalid if it exceeds delegated legislative authority by enlarging, modifying, or contravening the specific provisions of law implemented. § 120.52(8)(c), Fla. Stat.

Exception No. 1

Paragraph 5[2] recites that the Department's position on the applicability of section 210.25(11), Florida Statutes, "hardened in the first half of 2009 after a period of internal discussion triggered by Congress's enactment of legislation which expanded the Internal Revenue Code's definition of "roll-your-own tobacco" to include tobacco-based wrappers for cigarettes or cigars . . . ."

The Department takes exception to the implicit finding that the Department's determination in 2009 that blunt wraps were taxable tobacco products was based on a change in federal law. Although it is not clear why this finding is relevant[3], the finding appears to be based on email correspondence included in petitioner's exhibit 6, which was admitted into evidence over the Department's hearsay objection. T 1 at 72 - 74. The exhibit contains some select email correspondence between individuals identified as employees of the Department (e.g., Benjamin Pridgeon (T 1 at 70), Cesar Torres (T 1 at 70), Hector Mendoza (T 1 at 70), Tim Wood (T 1 at 70), and Marie Fraher (T 1 at 76)). Other than the Department's main witness, Gerald Russo, none of the individuals included in the email addresses who were identified by Mr. Russo in his testimony as employees of the Department (T 1 at 70, 76) testified at hearing.

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[2] Throughout these exceptions, where the Department files an exception to the paragraph, included in such exception are any footnotes which appear in that paragraph.

[3] Estoppel does not apply to prevent an agency from correcting its position if the original position was a mistake of law, not fact. Dolphin Outdoor Advertising v. Dep't of Transp., 582 So. 2d 709 (Fla. 1st DCA 1991). To the extent employees of the Department asserted a federal statutory basis for the determination that blunt wraps are taxable, those assertions were a mistake of law, and the Department is not estopped to assert a legally correct position. Moreover, estoppel only applies against the state in extraordinary circumstances, after a showing of detrimental reliance. Dolphin Outdoor Advertising, at 711. No record evidence was adduced in this matter regarding estoppel.

Hearsay evidence may be used for the purpose of supplementing or explaining other evidence, but it is not sufficient in itself to support a finding unless otherwise admissible over objection. § 120.57(1)(c), Fla. Stat., *see also* Dieguez v. Dep't of Law Enforcement, Criminal Justice Standards & Training Comm'n, 947 So. 2d 591 (Fla. 3d DCA 2007).[4] Because there was no evidence to corroborate the hearsay statements contained within the emails, they cannot form the basis for a finding that the Department's determination regarding the taxable nature of blunt wraps as a tobacco product was "triggered" by a change in federal law. Therefore, this finding of fact should be rejected by the Director upon a review of the entire record, because it is not based upon competent substantial record evidence.

Moreover, record evidence in the form of testimony by Department representative Gerald Russo supports a finding that the Department determined that blunt wraps are taxable as loose tobacco suitable for smoking under section 210.25(11), Florida Statutes. T 1 at 49 – 51.

Exception No. 2

Paragraph 6 recites that the Department did not give any "official notice" to licensed distributors of the determination that the blunt wrap product was subject to taxation starting on July 1, 2009. The Department takes exception to any implied conclusion of law[5] that liability

[4] Although the ALJ admitted the composite exhibit into evidence over the department's hearsay objections, the basis for the ALJ's ruling on the objection does not appear in the transcript of hearing (T 1 at 72, 73) and there is no evidentiary ruling on this issue in the RO. Petitioner's counsel argued that the emails are statements against interest. Under section 90.804(2)(c), Florida Statutes, a statement against interest is only admissible as a hearsay exception if the declarant is unavailable. Petitioner's counsel made no attempt to depose any of the employee-authors of the emails, and as stated above, none of these individuals testified at hearing. Accordingly, petitioner's burden to overcome a hearsay objection was not met.

[5] Upon administrative or judicial review, the agency is not bound by the labels affixed by an administrative law judge designating various portions of a recommended order as "findings of

for payment of taxes under chapter 210 is contingent on notice from the Department. Taxes and surcharges under sections 210.276 and 210.30, Florida Statutes, are payable at the time a "tobacco product" is brought into the state by a distributor for resale, and the obligation is on the distributor to calculate and remit such taxes each month. § 210.55, Fla. Stat. The interpretation that such liability is imposed by statute, and is independent of action by the agency charged with administering the statutes, is as reasonable or more reasonable than the ALJ's statement with respect to this point.

Exception No. 3

Paragraph 7 of the RO finds that the Department's 2009 interpretation of the definition of tobacco products to include blunt wraps as a taxable tobacco product under section 210.25(11), Florida Statutes, was an "expansive reinterpretation." The Department takes exception to the ALJ's implicit finding that the Department had at any time affirmatively interpreted section 210.25(11) *not* to support the taxation of blunt wraps. Further, the Department takes exception to the finding that petitioner's failure to remit taxes on the purchases of blunt wraps during the audit period was attributable to reliance on such an interpretation. These findings are simply not supported by any record evidence.

To the contrary, the evidence supports a finding that once the Department became aware of the existence of the product in the Florida market and finalized its internal discussions for the first time in 2009, the Department concluded that the products were taxable tobacco products under existing statutory authority. T 1 at 45, 46. This record facts established support a finding that this was an initial interpretation, not a reinterpretation.

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fact" or "conclusions of law". See Battaglia Properties v. Fla. Land & Water Adjudicatory Comm'n, 629 So. 2d 161, 168 (Fla. 5th DCA 1993).

Moreover, the Department takes exception to the contradictory findings that: 1) no Department interpretation regarding the taxability of blunt wraps existed before 2009; and yet 2) petitioner relied on this nonexistent interpretation as justification for not remitting taxes. There is simply no record evidence to support such findings. In fact, the only record evidence supports a finding that petitioner did not rely on assurances from the Department that the product was not taxable – petitioner simply made that determination itself. T 2 at 206. Therefore, these findings of fact should be rejected by the Director upon a review of the entire record, because they are not based on competent substantial record evidence.

Exception No. 4

Paragraph 8 contains a finding that during its routine audits of petitioner's business, the Department's auditors "never asked to see records relating to blunt wraps . . . ." The Department takes exception to this finding as it is not supported by competent, substantial evidence. The auditor's notes from a field audit in March 2010 clearly indicate that the auditor looked for the product in petitioner's warehouse and looked specifically for invoices of purchases of the product, and found neither. T 1 at 59, 60 – 62; Petitioner's Exh 7 at 137. Therefore, this finding of fact should be rejected by the Director upon a review of the entire record, because it is not based upon competent substantial record evidence.

Exception No. 5

Paragraph 18 recites the conclusions that: "The legislature did not tax all products containing tobacco. Rather, it "'taxed only those specifically enumerated in the statute.' *See*, Fla. S & L Servs., Inc. v. Department of Revenue, 443 So.2d 120 (Fla. 1st DCA 1983)." The

Department takes exception to this conclusion. It bootstraps an analysis of a sales tax statute, which clearly articulates specific taxable services, onto the interpretation of section 210.25(11). Section 210.25(11) provides that taxable tobacco products include: "loose tobacco suitable for smoking; snuff; snuff flour; cavendish; plug and twist tobacco; fine cuts and other chewing tobaccos; shorts; refuse scraps; clippings, cuttings and sweepings of tobacco, and other kinds and forms of tobacco prepared in such a manner as to be suitable for chewing . . . ." "Other kinds and forms of tobacco," "clippings, cuttings and sweepings of tobacco," and most relevant to this case, "loose tobacco suitable for smoking," are not specifically enumerated items, as were the specific telecommunications services set forth in Florida S & L Services. Instead, in addition to a few enumerated items, section 210.25(11) also lists categories of other tobacco products, all of which are subject to taxation. The conclusion of law that the statute comprises categories of tobacco as well as specifically enumerated items is as reasonable or more reasonable than the ALJ's statement with respect to this point.

Exception No. 6

Paragraphs 20, 33, 34 and 35 all conclude that the Department's interpretation of "loose tobacco suitable for smoking" to include blunt wraps as a taxable tobacco product is an erroneous interpretation of the law. The Department takes issue with this conclusion. The Department's interpretation, in addition to being supported by clear, unrebutted testimony of the Department's witness as to how the Department interprets the phrase "loose tobacco," is a plausible and reasonable interpretation of the meaning of "loose tobacco suitable for smoking."

According to the Department's witness, "loose tobacco" is an industry term, connoting all parts of the tobacco leaf, after it is harvested, dried, fermented or flavored, and after the unusable

stem of the leaf has been removed. T 1 at 49. As it relates specifically to a blunt wrap, the Department representative testified that the wrap is suitable for smoking (as opposed to chewing), so it falls within the category of "loose tobacco suitable for smoking."

The Department is charged with administrative construction of the provisions of part II, chapter 210, Florida Statutes, including the definitional provisions in section 210.25(11). Deference should be given to the department's interpretation. *See* Fla. Hosp. v. Agency for Health Care Admin., 823 So.2d 844, 847 (Fla. 1st DCA 2002). Because the Department's interpretation gives effect to the meaning of "loose tobacco suitable for smoking" in section 210.25(11), and gives a more reasonable interpretation of the statute in the context of the manner in which tobacco products are manufactured and categorized in the industry, it is eminently reasonable and not clearly erroneous. *See* Kessler v. Dep't of Mgmt. Servs., Div. of State Group Ins., 17 So.3d 759, 762 (Fla. 1st DCA 2009) (an interpretation doesn't have to be the only possible interpretation, it just has to be reasonable); *see also*, PW Ventures, Inc. v. Nichols, 533 So. 2d 281 (Fla. 1988) (interpreting the meaning of the statutory phrase "to the public" as that phrase was used in section 366.02(1), Florida Statutes, regarding the sale of electricity by a utility, to include sale of electricity to a single industrial customer). In PW Ventures, the Florida Supreme Court, relying on the principle that the contemporaneous construction of a statute by the agency charged with its enforcement and interpretation is entitled to great weight, held that the agency's interpretation of the phrase was "consistent with the legislative scheme" it was charged with enforcing, and was therefore not unauthorized. The interpretation that "loose tobacco suitable for smoking" has a meaning recognized within the industry which, as applied to these record facts, includes the product taxed in this instance is a statutory interpretation which is as reasonable or more reasonable than the ALJ's construction.

Exception No. 7

Paragraphs 21, 22, 23, 24, 25, 26, 27, 28, 29, 30, 31, and 32 conclude that the Department's interpretation of "loose tobacco suitable for smoking," as support for the determination that blunt wraps are a taxable tobacco product, is an unadopted rule. The Department takes exceptions to these conclusions.

As noted above, although the ALJ cannot base a determination of substantial interests on an unadopted rule (§ 120.57(1)(e)1), the Department's conclusion that blunt wraps are taxable as loose tobacco suitable for smoking is not an unadopted rule, but simply an application of the law to the record facts relating to the blunt wrap products at issue. Not every agency statement explaining how an existing rule of general applicability will be applied in a particular set of facts is itself a rule. The First District affirmed this concept in a recent case: Amerisure Mutual Ins. Co. v. Department of Financial Services, 2015 WL 46515 (Fla. 1st DCA Jan. 2, 2015).

In Amerisure, the First District overturned an ALJ's determination that the Department of Financial Services' interpretation and application of section 624.5094, Florida Statutes, was an unadopted rule. Section 624.5094, Florida Statutes, excuses a workers' compensation insurer from the payment of certain statutory assessments in any year in which that carrier has no net premium on which to base the assessments. Equating this to a tax "credit," the insurer argued that if it had excess "credits" in any year, it should be allowed to apply those against future assessments. The insurer filed a petition for administrative hearing and alleged that the department's denial of the insurer's accrual of excess tax credits amounted to an unadopted rule. Id. at 3.

The ALJ concluded that the department's denial of the accrual of credits was attributable to unadopted rules in that the department's position "was 'not a simple application of the law to the information provided, because no statute referenced by the department makes any mention of excess credits and how they are to be treated.'" Id. at 4. She further concluded that the department's interpretation of section 624.5094 was erroneous because the statute did not mandate specifically that the department could eliminate excess credits. Id. As a separate matter, the ALJ found that department staff had used forms, not adopted as rules, which clearly reflected that an insurer could accrue excess credits--a finding seemingly consistent with the insurer's arguments regarding an unadopted rule--and that the department staff had held its position for many years by the time of the recommended order. Id. at 9, fn.12.

In its final order, the department adopted the ALJ's finding as to the use of the forms by department staff, but concluded that the ALJ's determination that this fact carried legal significance was an erroneous conclusion of law. Id. at 6. On appeal, the First District affirmed the department's decision to reject the ALJ's conclusion, finding that the department had "simply applied the governing statute," id. at 8, and that because the forms could not create an entitlement to something that was not statutorily authorized, there was no need for the agency to create a rule directing how the unauthorized credits would be applied by the department. Id. at 9, fn. 12. The court concluded:

> The Department's construction and application of section 624.5094 in the present case is consistent with and required by the statute. No unadopted rule need be conjured up to explain the Department's denial of refunds to Amerisure, and the final order did not err in concluding as much.

Amerisure, at 9.

In a similar manner, the Department in the case at bar concluded that blunt wraps are within one of the categories of taxable products listed in section 210.25(11); i.e., "loose tobacco

suitable for smoking." This construction and interpretation is consistent with and required by the Department, which is charged with administering chapter 210, Florida Statutes. The application of this statute to tax the products at issue in this case does not amount to the Department's application of an unadopted rule, or reliance on an unadopted rule to determine petitioner's substantial interests.

Exception No. 8

Paragraph 36, 37, and 38 conclude that part of the assessment at issue is time-barred under section 95.091(3)(a)1.b. The Department takes exception to this conclusion. As noted in footnote 11 of the RO, this is purely a matter of law, and requires interpretation of the time limits set forth in section 95.091. Section 95.091(3)(a)5, Florida Statutes, provides that where a taxpayer has failed to make required payments of a tax and has not disclosed the liability in writing to the Department before the Department contacts the taxpayer, the Department is authorized, as it did in this case, to assess taxes for the entire audit period at issue.

CONCLUSION

The Recommended Order makes findings of fact that are not based on competent, substantial evidence, characterizes some conclusions as findings, and incorrectly applies the law governing taxation of the blunt wrap products at issue. The Director should reject unsupported findings of fact, reject erroneous and incorrect interpretations of law (including, without limitation, the conclusion that the Department determined petitioner's substantial interests on the basis of an unadopted rule), and uphold the assessment of taxes, surcharges, penalties and interest in its entirety.

_____/s/Elizabeth Teegen_____

Respectfully submitted,

PAMELA JO BONDI
ATTORNEY GENERAL
Lisa M. Raleigh
Florida Bar No. 0858498
Special Counsel
Elizabeth Teegen
Fla. Bar No. 833274
Assistant Attorney General
Counsel for Respondent
Complex Litigation Unit
Office of the Attorney General
PL-01, The Capitol
Tallahassee, FL 32399-1050
Ph. (850) 414-3300
Fax (850) 414-9650
Email:
lisa.raleigh@myfloridalegal.com
Elizabeth.teegen@myfloridalegal.com

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing was served by electronic mail to the following on this 11th[h] day of March, 2015.

Gerald J. Doninni II
JerryDonnini@FloridaSalesTax.com
Moffa, Gainor, & Sutton, P.A.
One Financial Plaza, Suite 2202
100 SE Third Avenue
Fort Lauderdale, FL 33394
Phone: (954) 761-3700
Fax: (954) 761-1004
Counsel for the Petitioner

Jason Douglas Borntreger
jason.borntreger@myfloridalicense.com
Department of Business and
Professional Regulation
1940 North Monroe Street, Suite 40
Tallahassee, Florida 32399-2202
Co-Counsel for the Respondent