



Special Notice

WASHINGTON STATE DEPARTMENT OF REVENUE

JUNE 22, 2010

Director Fees are Subject to the Business and Occupation (B&O) Tax

Summary

All compensation received, in any form, for services rendered as a corporate director, including the reimbursement of expenses, is subject to Washington State B&O tax under the service and other activities classification.

Background

Washington State's B&O tax is intended to tax virtually all business activities carried on within the state, unless a specific exemption applies. One such exemption is for income earned as an employee. See Revised Code of Washington (RCW) 82.04.360. Under the Washington Business Corporation Act, Title 23B RCW, an "employee" includes an officer, but not a director, of a corporation; however, a corporate director may accept duties that make the director also an employee of the corporation. See RCW 23B.01.400(11).

New law

Second Engrossed Substitute Senate Bill (2ESSB) 6143, Part VII, (chapter 23, Laws of 2010 1st Special Session) ("the legislation") clarifies that:

- Corporate directors, while acting in that capacity, are not considered employees of the corporation whose board they serve on; and
- Amounts received by an individual from a corporation for serving as a member of that corporation's board of directors (director fees) are subject to the B&O tax effective July 1, 2010.

The legislation provides limited relief from the retroactive assessment of B&O tax on director fees received prior to July 1, 2010. However, the legislation does not authorize refunds of B&O taxes paid on director fees that were validly collected before July 1, 2010. To read the legislation go to the Department's website at dor.wa.gov/newlegislation.

Directors fees subject to B&O tax

The following are director fees subject to B&O tax:

- All compensation received, in any form, for services rendered as a corporate director including, but not limited to, fees, the value of stock options or property received in exchange for services, awards, and bonuses; and
- All amounts recovered for expenses incurred in connection with such services including, but not limited to, telephone costs, preparation fees for meetings, and travel expenses.

See Washington Administrative Code (WAC) 458-20-138. In most cases, director fees must be included on an official IRS Form 1099-MISC. Therefore, the Department will generally accept amounts shown on the IRS form 1099 as the amount subject to tax.

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Where a corporate director is also an employee of a corporation, only the nonemployee director fees received for services rendered as a corporate director are subject to B&O tax: income earned as an employee is exempt from the B&O tax under RCW 82.04.360.

Stock options

Director fees include the value of stock options granted as compensation (compensatory stock options) to the extent that amount should be reported on the official IRS Form 1099-MISC. Corporate directors are not subject to the B&O tax on the value of compensatory stock options that were granted prior to the effective date of the legislation (July 1, 2010).

Please note that all taxpayers are required to keep suitable records, including copies of all federal income tax and state tax returns, as may be necessary to determine the amount of any tax. See RCW 82.32.070. For information on accounting methods refer to WAC 458-20-199. For information on the timing of tax liability refer to WAC 458-20-197.

Determining nexus

Effective July 1, 2010, you may owe B&O tax on your director fees if you have a substantial nexus with this state.

Substantial Nexus

A corporate director is deemed to have substantial nexus with this state if the director is:

- A resident or domiciliary of this state; or
- A nonresident of this state, and in any tax year has:
 - More than \$50,000 of property in this state;
 - More than \$50,000 of payroll in this state;
 - More than \$250,000 of receipts from this state; or
 - At least 25 percent of his or her total property, total payroll, or total receipts in this state.

Note: The Department of Revenue (Department) has adopted a new emergency rule (WAC 458-20-19401) to provide guidance on the nexus standards established in section 104 of the legislation.

Apportioning directors fees

Corporate directors who are taxable on their director fees in Washington State and another state may be entitled to report their taxable income for B&O tax purposes on an apportioned basis.

A corporate director is taxable in another state if:

- He or she is subject to tax in another state on his or her director fee income; or
- Another state has jurisdiction to tax that corporate director's income under the same substantial nexus standards described above, whether or not that state actually imposes a tax.

In general, corporate directors entitled to apportion their director fee income will be taxable on that portion of their director fee income received from corporations headquartered in this state. However, corporate directors could be liable for B&O tax on director fees received from corporations headquartered out-of-state if the director performs at least some of the activity of a corporate director for the out-of-state corporation within this state and is not taxable on the director fees in the other state. Readers should refer to WAC 458-20-19402 for details on apportionment.

Registering

Corporate directors are not required to register with the Department if all of the following apply:

- Your gross income from all activities subject to B&O tax is less than \$12,000 per year,
- You are not required to collect or pay to the Department any other tax or fee administered by the Department, and
- You are not otherwise required to obtain a license under the Department of Licensing's (DOL) Master License Service.

To register, complete a Master Business Application (MBA) with the Department of Licensing. Go to DOL's web site at www.dol.wa.gov and click on *File a Master Business Application*.

Once the application is processed, you will receive a Master Business License. The license will note your nine-digit Tax Registration Number, also known as your Unified Business Identifier (UBI) number.

Reporting your tax

You must report amounts received as director fees to the Department on excise tax returns under the service and other activities classification. You may be eligible to claim a small business B&O tax credit of up to \$70 per month against the amount of B&O tax otherwise due. For additional information on the small business tax credit, refer to the Special Notice published on April 28, 2010. The Department is in the process of amending WAC 458-20-104 to incorporate changes to the small business credit.

Reporting of tax by the corporation

The Department may allow corporations to agree to report and pay taxes on behalf of their registered directors. However, participation by a corporation is voluntary and corporate directors remain responsible for ensuring the timely and accurate filing of tax returns and payment of all applicable taxes even when the corporation on whose board the director serves has been authorized by the Department to file returns and pay taxes on behalf of their directors. For more information on corporate reporting of director fees, interested corporations may contact the Department's Taxpayer Account Administration Division (TAA) at (360) 902-7151.

Filing your tax return

Once you have registered with the Department, you will receive a packet of information from the Department that includes a letter with your:

- UBI/tax registration number, and
- Filing frequency (monthly, quarterly, or annual).

Depending on your gross income, you may be required to report your excise taxes on a monthly, quarterly, or annual basis.

Electronic filing (e-file) is the preferred method for filing your tax return. E-file calculates the tax, checks for accuracy, and flags potential errors before you file. The small business B&O tax credit is automatically calculated for e-filers. Taxes can be filed electronically by setting up a secure account at dor.wa.gov.

For more information

Visit our website at dor.wa.gov, send an email to dorcommunications@dor.wa.gov, or call the Department's Telephone Information Center at 1-800-647-7706.