

Cite as Det No. 08-0134, 27 WTD 232 (2008)

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. 08-0134
)	
...)	Registration No. . . .
)	Document No. . . .
)	Audit No. . . .
)	Docket No. . . .
)	
)	

- [1] RULE 24003; RCW 82.04.4452: B&O TAX -- HI-TECH CREDIT – TEMPORARY STAFFING CO. – ELIGIBILITY. A temporary staffing company may be entitled to a high tech credit allowed by RCW 82.04.4452 and Rule 24003 provided that it meets all of the statutory requirements.

- [2] RULE 268; RCW 82.04.4452: B&O TAX -- HI-TECH CREDIT – AFFIDAVIT – LATE FILING -- PENALTY. For the periods prior to June 10, 2004, a taxpayer was required to file an affidavit with the excise tax return upon which it claimed the High-Tech credit. Because the prior statute did not provide a penalty for the delinquent filing of the affidavit, a taxpayer may still be eligible for the B&O tax credit under RCW 82.04.4452 provided that it meets the statutory requirements and completes the required affidavits.

- [3] RULE 268; RCW 82.04.4452: B&O TAX -- HI-TECH CREDIT – ANNUAL SURVEY – FILING DUE DATE. For surveys due after June 10, 2004, RCW 82.04.4452’s requirement that the annual survey be filed “by March 31st following any year in which a credit is claimed” was held to refer to the calendar year during which the research and development spending was made. Because Taxpayer had failed to file its annual survey by their respective due dates, taxpayer’s surveys were held untimely.

- [4] RULE 268; RCW 82.04.4452: B&O TAX -- HI-TECH CREDIT – SURVEY – UNTIMELY FILING -- CONSEQUENCES. Where a taxpayer failed to timely file a required annual survey for the year 2004 by its March 31, 2005 due date, it

was precluded from claiming the B&O tax credit for the year in which the taxpayer failed to timely file a completed survey (2005).

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.

Okimoto, A.L.J. – A temporary staffing company seeks to offset a previously unclaimed high tech business and occupation (B&O) tax credit authorized under RCW 82.04.4452 and WAC 458-20-268 (Rule 268) against additional taxes assessed in an audit assessment. We hold that a temporary staffing company may be entitled to a high tech credit and remand the issue back to Audit for evaluation and verification. We hold that because Taxpayer failed to timely file a required annual survey for the year 2004 by its March 31, 2005 due date, Taxpayer may not claim any credit for the year 2005.¹

ISSUES

- 1) May a temporary staffing company claim a high tech credit under RCW 82.04.4452 and WAC 458-20-24003 (Rule 24003)?
- 2) When must a taxpayer claiming a high tech credit for the years 2004 and 2005 file its annual survey under RCW 82.04.4452 and WAC 458-20-268 (Rule 268)?
- 3) What are the consequences when a taxpayer fails to timely file an annual survey under RCW 82.04.4452 and Rule 268?

FINDINGS OF FACT

[Taxpayer] provides information technology (IT) solutions and services such as consulting, integrating computer systems, developing software, and managing IT infrastructures to customers for a fee. The Audit Division (Audit) of the Department of Revenue (Department) examined Taxpayer's records for the period January 1, 2002, through December 31, 2005. The examination resulted in additional taxes, interest, and penalties due of \$. . . , and Document No. . . was issued in that amount Taxpayer appealed the assessment and it remains due.

During the audit period, Taxpayer reported all income under either the retailing B&O and retail sales tax classification or the wholesaling B&O tax classification. Through a sampling of Taxpayer's invoices, Audit determined that much of Taxpayer's income was derived from computer service contracts entered into with a few of Taxpayer's customer. The computer services being performed included consulting, programming, as well as a temporary staffing activity related to research and development. Based on the sampling, Audit reclassified this income from the wholesaling B&O tax classification to the service and other activities B&O tax

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

classification. The temporary workers primarily performed research and development services related to software and hardware.

In its petition of appeal, Taxpayer originally argued that the computer software and hardware related temporary staffing services should be taxed under the processing for hire tax classification. During a supplemental petition filed . . ., however, Taxpayer abandoned that argument and raised a totally new and different argument. Taxpayer now acknowledges that its temporary staffing activities should be taxed under the service and other activities tax classification, but that it should be entitled to a high tech B&O tax credit under RCW 82.04.4452 for research and development activities performed by its employees.

Because Taxpayer was unaware that it may be eligible for the high tech credit, it failed to file with the Department annual surveys required by RCW 82.04.4452 for the years 2004 and 2005.

ANALYSIS

1) May a temporary staffing company claim a high tech credit under RCW 82.04.4452 and WAC 458-20-24003 (Rule 24003)?

RCW 82.04.4452 provides a high technology credit from B&O taxes for “each person whose research and development spending during the year in which the credit is claimed exceeds 0.92 percent of the person’s taxable amount during the same calendar year.” RCW 82.04.4452(1).

WAC 458-20-24003 (Rule 24003) explains how the high tech credit applies to temporary staffing companies performing research and development activities. Rule 24003(23) deals specifically with temporary staffing companies and provides:

A staffing company may be eligible for the credit if its research and development spending in the calendar year for which credit is claimed exceeds 0.92 percent of the person's taxable amount for the same calendar year.

(a) Qualifications of the credit. In order to qualify for the credit, a staffing company must meet the following criteria:

(i) It must conduct qualified research and development through its employees;

(ii) Its employees must perform qualified research and development activities in a project or a phase of the project, without considering any activity performed:

(A) By the person contracting with the staffing company for such performance; or

(B) By any other person;

(iii) It must complete an annual survey by March 31st following any year in which the credit was taken; and

(iv) It must document any claim of the B&O tax credit.

(b) Examples.

(i) Company M, a staffing company, furnishes three employees to Company N for assisting a research project in electronic device technology. N has a manager and five employees working on the same project. The work of M's employees and N's employees

combined as a whole constitutes qualified research and development. M's employees do not perform sufficient activities themselves to be considered performing qualified research and development. M does not qualify for the credit.

(ii) Company V, a staffing company, furnishes three employees to Company W for performing a phase of a research project in advanced materials. W has a manager and five employees working on other phases of the same project. V's employees are in charge of a phase of the project that results in discovery of technological information. The work of V's employees alone constitutes qualified research and development. V qualifies for the credit if all other requirements of the credit are met.

(iii) Same as (b)(ii) of this subsection, except that the phase of the research project involves development of computer software for W's internal use. The work of V's employees alone constitutes qualified research and development. V qualifies for the credit if all other requirements of the credit are met.

[1] Because Taxpayer did not present any information or documentation on this issue to the Audit Division, subject to the following discussion on the annual survey requirements, this issue is remanded to the Audit Division for an evaluation of Taxpayer's high tech credit claim in accordance with Rule 24003. *See also* ETA 2021.04.24003.

2) When must a taxpayer claiming a high tech credit for the years 2004 and 2005 file its annual survey under RCW 82.04.4452 and WAC 458-20-268 (Rule 268)?

Annual Survey Requirement:

[2] For the periods prior to June 10, 2004, a taxpayer was not required to file a survey in order to claim a B&O tax credit for R&D spending pursuant to RCW 82.04.04452. Instead, taxpayers were required to file an affidavit with the excise tax return upon which the credit was claimed. The prior statute did not provide a penalty for the delinquent filing of the affidavit, however. Consequently, Taxpayer may still be eligible for the B&O tax credit under RCW 82.04.4452 provided that it now completes the required affidavits for years 2002 and 2003. *See* WAC 458-20-268(3)(e)(iii).

In 2004, however, the Washington Legislature passed Engrossed Substitute House Bill 2546 (ESHB 2546), which amended RCW 82.04.4452 to replace the affidavit with an annual report due on March 31st following any year in which a credit is taken. In addition, the Legislature specifically recognized that accountability and effectiveness were important aspects of setting tax policy, and that information on how tax incentives were used was necessary to make informed policy choices on the best use of limited state resources. Consequently, the Legislature added the requirement that all claimants agree to complete an annual informational survey due on March 31st following any year in which a credit was claimed. The new legislation also specified certain penalties in the event a required survey was not timely filed.

RCW 82.04.4452(6)(b) sets the due date for filing the required annual survey. It provides:

(b) A person claiming the credit shall file a complete annual survey with the department. The survey is due by March 31st following any year in which a credit is claimed. The department may extend the due date for timely filing of annual surveys under this section as provided in RCW [82.32.590](#). The survey shall include the amount of the tax credit claimed, the qualified research and development expenditures during the calendar year for which the credit is claimed, the taxable amount during the calendar year for which the credit is claimed, the number of new products or research projects by general classification, the number of trademarks, patents, and copyrights associated with the research and development activities for which a credit was claimed, and whether the credit has been assigned under subsection (3) of this section and who assigned the credit. The survey shall also include the following information for employment positions in Washington:

Underlining added.

[3] Even though Taxpayer has not filed the required completed annual survey for the years 2004 or 2005, it nevertheless contends that it may still claim the high tech credit for those years, because the due date for filing the annual survey is “March 31st following any year in which a credit is claimed.” Taxpayer reasons that since it first claimed the high tech credit for 2004 and 2005 during March of this year (2008), that the due date for filing the annual surveys is not until March 31st of the year following the date when the credit was first claimed, or March 31, 2009.

Over the years, Washington courts have developed several broad rules for interpreting statutes.

The goal when construing statutory language is to carry out the intent of the Legislature. [Seven Gables Corp. v. MGM/UA Entertainment Co., 106 Wash.2d 1, 6, 721 P.2d 1 \(1986\)](#). When determining intent, this court must interpret the language at issue in the context of the entire statute. [In re Sehome Park Care Ctr., Inc., 127 Wash.2d 774, 778, 903 P.2d 443 \(1995\)](#). Words that are not statutorily defined must, whenever possible, be given their ordinary and usual meaning. [Palmer v. Department of Revenue, 82 Wash.App. 367, 372, 917 P.2d 1120 \(1996\)](#). "Strained, unlikely or unrealistic" statutory interpretations are to be avoided. [Bour v. Johnson, 122 Wash.2d 829, 835, 864 P.2d 380 \(1993\)](#).

Sacred Heart Medical Center v. Dep't of Revenue., 88 Wn. App. 632, 946 P.2d 409 (1997).

In this case, Taxpayer's interpretation fails to comply with the spirit and overall intent of the statutory requirement for filing the annual survey. The legislature's intentions for enacting the survey requirement can be found in RCW 82.04.4452(6)(a). It provides:

(6)(a) The legislature finds that accountability and effectiveness are important aspects of setting tax policy. In order to make policy choices regarding the best use of limited state resources the legislature needs information on how a tax incentive is used.

The clear stated legislative intent for enacting the annual survey requirement was to timely supply the legislature with needed accurate information to make informed policy choices regarding the best use of limited state resources. To be useful to the legislature, that information must be both current and accurate. It would simply not be consistent with the legislature's stated intent to obtain timely and accurate information, to allow taxpayers to wait several years after the R&D spending was incurred, before filing the required annual surveys. The surveys contain essential information that needs to be transmitted to the legislature in a timely manner. Such a policy would undermine the accuracy of the information relied upon by the legislature and possibly frustrate its intent to make informed policy decisions.

Next, Taxpayer's interpretation for the words "year in which a credit is claimed" is inconsistent with how that phrase was used in other sections of the statute.

For example, RCW 82.04.4452(1) provides in pertinent part:

(1) In computing the tax imposed under this chapter, a credit is allowed for each person whose research and development spending during the **year in which the credit is claimed** exceeds 0.92 percent of the person's taxable amount during the same calendar year.

(Bolding added.)

RCW 82.04.4452(5) also states:

(5) For any person claiming the credit, including any credit assigned to a person under subsection (3) of this section, whose research and development spending during the calendar **year in which the credit is claimed** fails to exceed 0.92 percent of the person's taxable amount during the same calendar year or who is otherwise ineligible, the department shall declare the taxes against which the credit was claimed to be immediately due and payable. (Bolding added.)

In both RCW 82.04.4452(1) and RCW 82.04.4452(5) the phrase "year in which the credit is claimed" clearly refers to the calendar year during which the research and development spending was made. Consequently, we conclude that Taxpayer's annual survey for the years 2004 and 2005 were due on March 31, 2005 and March 31, 2006, respectively. Since Taxpayer did not file its annual survey by its due date for either year, the surveys are untimely.

3) What are the consequences when a taxpayer fails to timely file an annual survey under RCW 82.04.4452 and Rule 268?

[4] RCW 82.04.4452(6)(e) explains the consequences for when a persons fails to timely file a complete annual survey. It provides:

If a person fails to file a complete annual survey required under this subsection with the department by the due date or any extension under RCW [82.32.590](#), the person entitled to the credit provided in subsection (2) of this section is not eligible to claim or assign the credit provided in subsection (2) of this section in the year the person failed to timely file a complete survey.

WAC 458-20-268 (Rule 268) further explains that failure to timely file a required annual survey makes the person ineligible to claim the credit in the year it failed to file the survey. Rule 268(11) states:

(b) High technology business and occupation (B&O) tax credit. If a person claiming the B&O tax credit provided by RCW 82.04.4452 for persons engaged in qualified research and development fails to timely file a complete annual survey by the date due, the person is not eligible to take or assign the credit in the year the person failed to timely complete the annual survey. See RCW 82.04.4452. For example, if a person claims the credit in 2006 but fails to file a complete annual survey by March 31, 2007, then the person is not eligible to take or assign the credit in 2007. If a person claims the B&O tax credit during this period of ineligibility, the department will declare the amount of taxes for which the credit was claimed during the period of ineligibility to be immediately due and payable with interest and penalties, as provided in chapter 82.32 RCW.

Therefore, since Taxpayer claims a credit for the year 2004 and failed to file a completed annual survey by its March 31, 2005, due date, it is precluded from claiming the B&O tax credit for the year in which Taxpayer failed to timely file a complete survey (2005). Accordingly, Taxpayer may not take a high tech tax credit under RCW 82.04.4452 and Rule 268 for the year 2005. Taxpayer may claim a credit for the year 2004, however, provided that it meets all the other statutory requirements including filing its annual report.

DECISION AND DISPOSITION

Taxpayer's petition for high tech B&O tax credit is denied for the year 2005. Taxpayer's petition is remanded to Audit for review of documents to support possible credits for the years 2002, 2003 and 2004.

Dated this 21st day of May, 2008.