

Cite as Det. No. 92-006, 11 WTD 565 (1992).

BEFORE THE INTERPRETATION AND APPEALS DIVISION  
DEPARTMENT OF REVENUE  
STATE OF WASHINGTON

In the Matter of the Petition	)	<u>D E T E R M I N A T I O N</u>
For Correction of Assessment of	)	
	)	No. 92-006
. . .	)	
	)	Registration No. . . .
	)	Documents No. . . .
	)	. . .

[1] RULE 105 -- EMPLOYEE V. INDEPENDENT CONTRACTOR -- CRITERIA -- WEIGHING OF. Although control is the most important consideration in determining whether a person is an employee, other factors enumerated in the rule must also be weighed. When an optometrist receives a portion of the gross proceeds of an optical clinic's income, pays a portion of the clinic's telephone, advertising, and rent expenses, files a Schedule C with his federal income tax return, and employment taxes are not withheld from his remuneration, he will not be considered an employee even though the clinic may exercise some control over his activities.

[2] RULE 228 -- PENALTIES -- LATE PAYMENT -- LACK OF KNOWLEDGE. The failure of a taxpayer to determine that he is taxable for business and occupation taxes is not a circumstance beyond his control. Accord: Det. No. 86-299, 2 WTD 035 (1986).

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.

TAXPAYER REPRESENTED BY: . . .

NATURE OF ACTION:

Petition concerning whether an individual was an employee or an independent contractor.

FACTS:

Bauer, A.L.J. -- The taxpayer's business records were examined for the period January 1, 1983 through December 31, 1989. The above-referenced assessment was issued [in May 1990] in the amount of \$ . . . , which amount included interest and penalties. The taxpayer requested that his appeal be heard under the small claims procedure. Because this appeal concerns a recurring issue, the small claims procedure is not appropriate.

The taxpayer is a licensed optometrist. As such, he rendered eye examinations and sold prescription contact lenses at two optical clinics owned by others (who are not licensed opticians or physicians) during the audit period. The Department auditor concluded that the taxpayer had been operating as an unregistered independent contractor for many years, and assessed service and retailing business and occupation tax, retail sales tax, and penalties and interest for the audit year and the preceding seven year period.

The two clinics at which the taxpayer worked during the audit period are in the business of providing eye exams and new contacts or glasses for its customers. Both clinics use eye exams as a loss leader to get optical patients into their stores. The clinics control the fee structure, which is lower than the taxpayer prefers.

The clinic employees make up his appointment schedule for the week, and in some cases they will assign his appointments to another clinic doctor if he is not going to be in the office. They prepare the invoices and collect all fees. The taxpayer is then paid \$32 per eye exam once or twice a month. He performs 10 exams per day on average. He also receives a percentage of the contact lens sales he generates.

The clinics deal with the paperwork and fee collection problems. These clinics provide the work space, supplies, telephone and support employees. They control their store hours, the telephone number, examination fees, and do all the hiring and firing and have 100% of the employer responsibilities with the other clinic staff.

Both optical clinics require the taxpayer to turn the prescription that he writes over to the retail employees of the clinic so that they can sell his patients the supplies they need.

The clinics don't provide vacation, sick leave, or retirement plan fringe benefits to the taxpayer. The taxpayer's representative believes he has a strong foundation of facts to claim his rights to any Qualified Retirement Plan under the ERISA federal rules if he chooses to press the point. One of the clinics carries the taxpayer on its employee group medical

insurance plan; he pays that plan approximately \$270 per month. The plan requires its membership to be employees.

One of the clinics provided the taxpayer with a bookkeeper who prepared his Form 1099 and Schedule C for federal income tax purposes and wrote checks to cover his expenses. Expenses included telephone, advertising, office supplies, taxes, rent and the bookkeeping charge. FICA was calculated in his return. He was never advised by the bookkeeper that he was liable to the state for business and occupation taxes. Prior to this appeal, the taxpayer has never received any independent financial or accounting advice other than that supplied by the clinic bookkeeper.

The taxpayer's compensation is based on a 60/40 split on gross revenue in order to cover the overhead expenses of the clinics. He has not held himself out to the public as an independent optometrist since 1980 when he had his own shop, and has no separate by-name telephone listing as such.

The taxpayer has been working on a verbal contract basis for these two clinics for the past ten years. He is now 67 and needs to continue working. Therefore, he is very reluctant to get involved with negotiations for a more traditional employee status. The taxpayer's representative suspects that both clinics are using and abusing his predicament to their advantage to avoid paying payroll taxes, claiming he is a subcontractor by filing a 1099 plus keeping him from participating in any qualified retirement plan they might have in place.

#### TAXPAYER'S EXCEPTIONS:

The taxpayer objects to the assessment, arguing that he was essentially an employee and thus exempt from the business and occupation tax. His argument is based on the provisions of current WAC 458-20-105 (Rule 105), which provides in part: "the most important consideration is the employer's right to control the employee."

The taxpayer additionally requests a waiver of late payment penalties, since he had no intent to evade taxes.

#### DISCUSSION:

RCW 82.04.360 provides an exemption for employees:

This chapter shall not apply to any person in respect to his employment in the capacity of an employee or servant as distinguished from that of an independent contractor.

Generally, businesses can choose whether to utilize employees or independent contractors in carrying on their business. When a company chooses to create the relationship of principal and independent contractor, the independent contractor is liable for business and occupation tax.

WAC 458-20-105 (Rule 105), effective September 1, 1989, explains when a person will be considered an employee. It reads, in part:

(1) The Revenue Act imposes taxes upon persons engaged in business but not upon persons acting solely in the capacity of employees.

(2) While no one factor definitely determines employee status, the most important consideration is the employer's right to control the employee. The right to control is not limited to controlling the result of the work to be accomplished, but includes controlling the details and means by which the work is accomplished. In cases of doubt about employee status all the pertinent facts should be submitted to the department of revenue for a specific ruling.

(3) PERSONS ENGAGING IN BUSINESS. The term "engaging in business" means the act of transferring, selling or otherwise dealing in real or personal property, or the rendition of services, for consideration except as an employee. The following conditions will serve to indicate that a person is engaging in business.

If a person is:

(a) Holding oneself out to the public as engaging in business with respect to dealings in real or personal property, or in respect to the rendition of services;

(b) Entitled to receive the gross income of the business or any part thereof;

(c) Liable for business losses or the expense of conducting a business, even though such expenses may ultimately be reimbursed by a principal;

(d) Controlling and supervising others, and being personally liable for their payroll, as a part of engaging in business;

(e) Employing others to carry out duties and responsibilities related to the engaging in business and being personally liable for their pay;

(f) Filing a Statement of Business Income and Expenses (Schedule C) for federal income tax purposes;

(g) A party to a written contract, the intent of which establishes the person to be an independent contractor;

(h) Paid a gross amount for the work without deductions for employment taxes (such as Federal Insurance Contributions Act, Federal Unemployment Tax Act, and similar state taxes).

(4) EMPLOYEES. The following conditions indicate that a person is an employee.

If the person:

(a) Receives compensation, which is fixed at a certain rate per day, week, month or year, or at a certain percentage of business obtained, payable in all events;

(b) Is employed to perform services in the affairs of another, subject to the other's control or right to control;

(c) Has no liability for the expenses of maintaining an office or other place of business, or any other overhead expenses or for compensation of employees;

(d) Has no liability for losses or indebtedness incurred in the conduct of the business;

(e) Is generally entitled to fringe benefits normally associated with an employer-employee relationship, e.g., paid vacation, sick leave, insurance, and pension benefits;

(f) Is treated as an employee for federal tax purposes;

(g) Is paid a net amount after deductions for employment taxes, such as those identified in subsection (3)(h) of this section.

[Emphasis added]

[1] Thus, although control is the most important consideration in determining whether a person is an employee, other factors enumerated in the Rule 105 must also be weighed.<sup>1</sup>

While we concede that certain control factors in this case suggest that there might be an employer/employee relationship,<sup>2</sup>

---

<sup>1</sup>The prior version of Rule 105, effective May 29, 1970, provided:

. . . where a person is not construed to be an employee under the State Employment Security Act or the Federal Social Security Act, such person will not be considered to be an employee under the Revenue Act.

other criteria in Rule 105 suggest otherwise: The taxpayer's remuneration was based on a portion of the clinics' gross proceeds (subparagraph (3)(b)); the taxpayer was liable for a portion of the clinics' telephone, advertising and rent expenses (subparagraph (3)(c)); the taxpayer filed a Statement of Business Income and Expenses (Schedule C) for federal income tax purposes as though he were engaging in business as an independent contractor (subparagraph (3)(f)), and employment taxes were not deducted from amounts he received in payment for his services (subparagraph (3)(h)).<sup>3</sup>

Weighing all of the criteria of Rule 105, then, we must conclude that the taxpayer was and is an independent contractor not entitled to the employee exemption from business and occupation taxes.

As to the question of late payment penalties, WAC 458-20-228 (Rule 228) applies:

The department will waive or cancel the penalties imposed under RCW 82.32.090 and interest imposed under RCW 82.32.050 upon finding that the failure of a taxpayer to pay any tax by the due date was due to circumstances beyond the control of the taxpayer. The department has no authority to cancel penalties or interest for any other reason.

The following situations will constitute the only circumstances under which a cancellation of penalties will be considered by the department:

1. The return was filed on time but inadvertently mailed to another agency.
2. The delinquency was due to erroneous information given the taxpayer by a department officer or employee.
3. The delinquency was caused by death or serious illness of the taxpayer or his immediate family, or illness or death of his accountant or in the accountant's immediate family, prior to the filing date.

---

<sup>2</sup> Such criteria include the clinics' ability to set examination fees, hours, and their ownership of customers' records.

<sup>3</sup>For personal reasons independent of this appeal, the taxpayer has indicated that he will probably not challenge his federal tax status for the audit period and claim he is an employee.

4. The delinquency was caused by unavoidable absence of the taxpayer, prior to the filing date.
5. The delinquency was caused by the destruction by fire or other casualty of the taxpayer's place of business or business records.
6. The taxpayer, prior to the time for filing the return, made timely application to the Olympia or district office, in writing, for proper forms and these were not furnished in sufficient time to permit the completed return to be paid before its delinquent date.
7. The delinquent tax return was received under the following circumstances:
  - a. The return was received by the department with full payment of tax due within 30 days after the due date; i.e., within the five percent penalty period prescribed by RCW 82.32.090, and
  - b. The taxpayer has never been delinquent filing a tax return prior to this occurrence, unless the penalty was excused under one of the preceding six circumstances, and
  - c. The delinquency was the result of an unforeseen and unintentional circumstance, not immediately known to the taxpayer, which circumstances will include the error or misconduct of the taxpayer's employee or accountant, confusion caused by communications with the department, failure to receive return forms timely, and delays or losses related to the postal service.
  - d. The delinquency will be waived under this circumstance on a one-time basis only.

[2] None of the above circumstances apply in this case, and we must conclude that the failure of a taxpayer to determine that he is taxable as an independent contractor, when he files his federal tax returns as an independent contractor, is not a circumstance beyond his control.

The taxpayer's argument that the late payment penalties should be excused because he had no intent to evade must fail. Had he intended to evade tax, the 50% fraud penalty in RCW 82.32.050 would have been assessed:

If the department finds that all or any part of the deficiency resulted from an intent to evade the tax

payable hereunder, a further penalty of fifty percent of the additional tax found to be due shall be added.

In addition, we are constrained to note that, in the case of nonregistered taxpayers, the Department's policy (set forth in RPM 89-4) is to assess only the current year and seven previous years of activity, even though no such limitation exists under RCW 82.32.050 of the Washington Revenue Act:

. . . No assessment or correction of an assessment for additional taxes due may be made by the department more than four years after the close of the tax year, except (1) against a taxpayer who has not registered as required by this chapter, . . .

Thus, the taxpayer has enjoyed tax-free years which the Department could have lawfully taxed.

DECISION AND DISPOSITION:

The taxpayer's petition is denied.

DATED this 15th day of January, 1992.