

Cite as Det. No. 92-267, 12 WTD 447 (1992).

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

In the Matter of the Petition	)	<u>D</u> <u>E</u> <u>T</u> <u>E</u> <u>R</u> <u>M</u> <u>I</u> <u>N</u> <u>A</u> <u>T</u> <u>I</u> <u>O</u> <u>N</u>
For Refund	)	
	)	No. 92-267
	)	
. . .	)	Registration No. . . .
	)	. . ./Audit No. . . .
	)	

[1] RCW 82.04.315 - EXEMPTION - INTERNATIONAL BANKING FACILITY - SEGREGATION OF ACCOUNTS - RETROACTIVE CORRECTIONS. Because the Federal Reserve permits IBF accounts to be amended to reflect initial errors in classification of income, retroactive corrections to IBF accounts will be considered as "segregated" for purposes of the B&O exemption even though these amounts were segregated after-the-fact. There is no policy or legal reason to deny the RCW 82.04.315 exemption once accounts are amended in accordance with Federal Reserve directives.

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 the exemption applicable to international banking facilities.

FACTS:

Bauer, A.L.J. -- The taxpayer's business records were audited for the period April 1, 1983 to March 31, 1987. As a result, an assessment was issued in the amount of \$ . . . , which amount included interest. The taxpayer seeks a refund.

The taxpayer is the [Washington] branch of a major foreign bank. Taxpayer operates a domestic and an international banking

facility (IBF). The taxpayer is a wholesale banker and provider of large volume loans, letters of credit, banker acceptances, and the like.

The assessment at issue taxed certain gains from foreign exchange transactions and imposed use tax on consumable supplies on which sales tax had not been paid. The latter issue has not been appealed.

Tax was imposed on certain transactions which were Canadian and which should have been initially recorded in the IBF (International Banking Facility) accounts rather than the domestic accounts. Had that been done, the gains would have been entirely exempt from B&O tax.

According to the audit file, the auditor contacted an unnamed employee of the Federal Reserve Board and was advised that transactions could not be retroactively transferred from domestic to IBF accounts and qualify as IBF transactions. It was thus concluded that, once a transaction occurs and is recorded, no retroactive reclassification could be allowed on the transaction that gave rise to the gain, even though it was clear that some of the income could have been properly recorded in the IBF accounts in the first place.

#### TAXPAYER'S EXCEPTIONS:

The taxpayer objects to the taxation of gains from its Canadian transactions which should have been initially recorded in the IBF.

The taxpayer argues that the incorrect booking of amounts as domestic income rather than IBF income should not be dispositive of their ultimate tax treatment. An IBF is defined at RCW 82.04.315 as a set of asset and liability accounts segregated on the books and records of a bank, but says nothing regarding the time at which such segregation must occur.

The taxpayer argues that the state legislature has stipulated that income from IBF transactions is exempt from the B&O tax. A refusal to allow the taxpayer to correct an accounting error with respect to these transactions would frustrate the clear legislative intent of RCW 82.04.315 that such amounts not be subject to the B&O tax.

#### DISCUSSION:

RCW 82.04.315 provides:

This chapter shall not apply to the gross receipts of an international banking facility.

As used in this section, an "international banking facility" means a facility represented by a set of asset and liability accounts segregated on the books and records of a commercial bank, the principal office of which is located in this state, and which is incorporated and doing business under the laws of the United States or of this state, a United States branch or agency of a foreign bank . . . that includes only international banking facility time deposits (as defined in subsection (a)(2) of Section 204.8 of Regulation D (12 CFR Part 204), as promulgated by the Board of Governors of the Federal Reserve System), and international banking facility extensions of credit (as defined in subsection (a)(3) of Section 204.8 of Regulation D).

(Emphasis added.)

Federal regulations in 12 CFR Section 204.8 further define and expand on the definition and requirements of IBF accounts and transactions. None of these regulations, however, address whether incorrectly booked transactions can be corrected at a later date and still be considered to have been "segregated on the books and records" of the commercial bank.

Both the taxpayer's representative and the Department have contacted the Federal Reserve Bank, San Francisco, to determine whether the booking of International Banking Facility (IBF) assets can be amended and corrected after the fact on records submitted to the Federal Reserve. The Federal Reserve Bank's representative explained that IBF loan assets are designated pursuant to the Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks, more commonly known as the "Call Report," pursuant to 12 U.S.C. Section 3105(b)(2); 12 U.S.C. Section 1817(a)(1); 12 U.S.C. Section 3102(b). He further stated that U.S. branches of foreign banks are required to submit accurate Call Reports, and thus any error on a Call Report not only can but must be corrected and amended as soon as such error is discovered to comply with applicable federal regulations.

In summary, discussions with the Federal Reserve Bank now leave no doubt that a foreign bank is not only permitted, but is in fact required, to amend its Call Report to reflect the proper classification of IBF loan assets.

Based on our verification of this new information from the Federal Reserve, it appears that IBF accounts can be amended to

reflect initial errors in classification of income. Income can thus be segregated after-the-fact.

[1] Retroactive corrections to IBF accounts will be considered to have been "segregated" for purposes of the RCW 82.04.315 B&O exemption even though these amounts were segregated after-the-fact. This is because the Federal Reserve permits IBF accounts to be amended to reflect initial errors in classification of income. There is no policy or legal reason to deny the RCW 82.04.315 exemption once accounts are amended in accordance with Federal Reserve directives.

The taxpayer's petition as to this issue is therefore granted.

DECISION AND DISPOSITION:

The taxpayer's petition is granted. A refund or credit , plus statutory interest, will be issued.

DATED this 29th day of September 1992.