Cite as Det. No. 93-180, 13 WTD 334 (1994).

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

In the Matter of the Petition For Refund of Taxes Paid	)	D E T E R M I N A T I O N
	)	No. 93-180
. . .	)	Registration No. . . .

[1] RULE 193: B&O TAX -- INTERSTATE SALES OF GOODS TO WASHINGTON CUSTOMERS -- NEXUS. The maintenance and servicing of equipment in Washington is a local activity. This local activity establishes nexus with the state and requires payment of B&O tax.

[2] RULE 193: B&O TAX -- INTERSTATE SALES OF GOODS TO WASHINGTON CUSTOMERS -- NEXUS -- DISASSOCIATION. An out-of-state business which has taxable nexus with Washington through a service representative who visits Washington customers may disassociate sales in this state where it has demonstrated that its instate activities are not significantly associated in any way with the sales.

[3] RULE 103, RULE 110; RCW 82.04.070, 82.08.020(1), 82.08.010(1): RETAIL SALES TAX -- FREIGHT CHARGES. Freight charges recovered by sellers are part of gross sales proceeds and may not be deducted from the measure of the seller's B&O tax and retail sales tax.

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.

. . .

NATURE OF ACTION:

The taxpayer protests the assessment of the retailing business and occupation (B&O) tax on its sales and repair income and the

assessment of B&O tax and retail sales tax on related freight charges billed to its customers.

FACTS:

Lewis, A.L.J. -- [The taxpayer's] tax returns were reviewed by the Department of Revenue (Department). Balance Due notices were issued [in July and September 1992] for tax deficiencies [found] in the January 1992 and May 1992 returns. The adjustments were made because the taxpayer had not reported retailing B&O tax on the value of its retail sales.

The taxpayer sells and services large equipment used by the forest industry. The taxpayer does not maintain a Washington office, outlet, agent or representative. The taxpayer does make sales in Washington. The taxpayer not only sells and ships repair parts into Washington but also, has an employee who makes on-site repairs of equipment in Washington.

The taxpayer has not paid B&O tax on its sales in Washington believing that insufficient nexus exists to allow the Department to impose and collect the retailing B&O tax. It contends that there is insufficient nexus because 1) they do not have a local facility, office, outlet, agent or representative, 2) they have no representation by a salesman in Washington, and 3) there is no in-state activity connected with the sale.

Additionally, the taxpayer has not collected and paid retail sales tax on the freight charges it bills to its customers. The taxpayer contends ". . . why would [the taxpayer] tax the customer for an overnight Federal Express bill when he could have the same freight charge billed directly to his Federal Express and not be taxed for it?"

ISSUES:

1. Whether sufficient nexus exists to allow the Department to assess the retailing B&O tax on sales made into Washington?

2. Whether freight charges billed by the taxpayer to its customers are subject to the B&O and/or retail sales tax?

DISCUSSION:

RCW 82.04.220 imposes the B&O tax:

> There is levied and shall be collected from every person a tax for the act or privilege of engaging in business

> activities. Such tax shall be measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be.

WAC 458-20-193 is the administrative rule that addresses the taxation of the inbound sale of tangible personal property.[1] It provides in pertinent part:

> Inbound sales. Washington does not assert B&O tax on sales of goods which originate outside this state unless the goods are received by the purchaser in this state and the seller has nexus. There must be both the receipt of the goods in Washington by the purchaser and the seller must have nexus for the B&O tax to apply to a particular sale. The B&O tax will not apply if one of these elements is missing.

[1] The Rule also cites various examples of activities that establish sufficient nexus for the Department to assess B&O tax. That part of the rule reads in pertinent part:

> The out-of-state seller, either directly or by an agent or other representative, performs significant services in relation to establishment or maintenance of sales into the state, even though the seller may not have formal sales offices in Washington or the agent or representative may not be formally characterized as a "salesperson."

The courts have addressed what types of business activity are sufficient to establish nexus. In Tyler Pipe Industries, Inc. v. Washington State Dept. of Revenue, 483 U.S. 232 (1987) the United States Supreme Court decided that sufficient nexus existed for the imposition of B&O tax where out-of-state sellers used independent contractors to solicit sales in Washington. In that case, the products were manufactured outside Washington. Tyler maintained no office, owned no property and had no employees residing in Washington. The state courts found the in-state representative engaged in substantial activities that helped establish and maintain Tyler's market in Washington by "calling on its customers and soliciting orders." 483 U.S. at 249.

The Supreme Court continued at 483 U.S. at 250-251 by agreeing with the Washington Supreme Court's holding that determined:

---

[1]WAC 458-20-193A and 458-20-193B were replaced with WAC 458-20-193. Rule 193 became effective January 1, 1992.

> . . . the crucial factor governing nexus is whether the activities performed in this state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales. 105 Wn.2d at 323, 715 P.2d at 126.

For example, the Department has held that infrequent visits to Washington customers by nonresident employees, who are not salespersons, constitute sufficient nexus to allow taxation of income from sales. Det. No. 88-368, 6 WTD 417. In that case, the employees provided advice to the customers regarding the safe handling of a product. Such activity was important in maintaining sales into the state. See also Standard Pressed Steel Co. v. Washington Revenue Dept., 419 U.S. 560 (1975) where nexus was established through the presence of a resident employee engineer who was not involved in sales, but instead consulted the customer regarding its product needs.
In this case, the taxpayer's service representative enters Washington to repair equipment. Furthermore, the servicing of an expensive, specialized piece of equipment is a necessary and important consideration in the purchaser's buying decision. The offering of on-site service allows the taxpayer to establish and maintain a market in the state. Furthermore, the servicing of equipment in Washington is a local activity. Accordingly, this activity establishes the requisite nexus needed for the Department to assert the B&O tax. Thus, because nexus exists and the repairs are local in nature, the B&O tax is due.

[2] The taxpayer argues that its income from the sale of parts should be exempt from B&O tax as there is no in-state activity connected with the sale. Rule 193 provides in pertinent part:

> If a seller carries on significant activity in this state and conducts no other business in the state except the business of making sales, this person has the distinct burden of establishing that the instate activities are not significantly associated in any way with the sales in to the state.

Thus, under Rule 193 when the taxpayer/seller has nexus with this state, the burden is on the seller to establish that its instate activities are not significantly associated in any way with sales into this state. Det. No. 87-69, 2 WTD 347 (1987); Det. No. 88-144, 5 WTD 137 (1988); Norton Company v. Dept. of Revenue, 340 U.S. 534, 537 (1951); Chicago Bridge v. Dept. of Revenue, 98 Wn.2d 814, at 822, 827 (1983). Accordingly, sales to customers that have occurred without any significant in-state contact may possibly be disassociated and not subject to B&O tax. However,

the burden is on the taxpayer to produce convincing evidence supporting disassociation. The taxpayer must show that the sale was not related in any significant way to its in-state activity. That is, the sale must result from a source completely independent of the taxpayer's in-state activity, e.g. an out-of-state trade show, or communication initiated by the customers when the taxpayer's service representative did not participate or have prior contacts in Washington with the customers.

However, even if the sale can be disassociated and no B&O tax or sales tax is due, the taxpayer is still obligated to collect use tax. Rule 193:

> . . . sets forth the conditions under which out-of-state sellers are required to collect and remit the use tax on goods received by customers in this state. A seller is required to pay or collect and remit the tax imposed by chapter 82.12 RCW if within this state it directly or by any agent or other representative:
>
> . . .
>
> (v) Regularly engages in any activity in connection with the leasing or servicing located within this state.

Thus, because the taxpayer regularly services equipment in Washington it must collect and pay use tax to the Department on disassociated sales income.

[3] The taxpayer ships parts to its customers and bills them for the freight charges. The taxpayer protests the assessment of B&O tax and retail sales tax on the income derived from billings for freight charges.

The B&O tax is imposed "for the act or privilege of engaging in business activities. Such tax shall be measured by the application of rates against value of products, gross proceeds of sale, or gross income of the business, as the case may be." RCW 82.04.220.

"Gross proceeds of sales" is statutorily defined in RCW 82.04.070:

> "Gross proceeds of sales." "Gross proceeds of sales" means the value proceeding or accruing from the sale of tangible personal and/or services rendered, without any deduction on account of the cost of property sold, the cost of materials used, labor costs, interest, discount paid, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses.

Similarly, the retail sales tax is imposed by RCW 82.08.020(1) as follows:

> There is levied and there shall be collected a tax on each retail sale in this state equal to [6.5] percent of the selling price. (Emphasis added.)

The term "selling price" is defined by RCW 82.08.010(1) in a manner nearly identical to the term "gross proceeds of sales," as follows:

> "Selling price" means the consideration, whether money, credits, rights, or other property except trade in property of like kind, expressed in the terms of money paid or delivered by a buyer to a seller without any deduction on account of the cost of tangible personal property sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes other than taxes imposed under this chapter if the seller advertises the price as including the tax or that the seller is paying the tax, or any other expenses whatsoever paid or accrued and without any deduction on account of losses; . . .

(Emphasis supplied.)

Thus, under the Washington Revenue Act, the statutory definitions of both "gross proceeds of sales" and "selling price," for purposes of calculating the B&O tax and retail sales tax, respectively, include "delivery costs" as part of the measure of the tax.

Additionally, WAC 458-20-110 (Rule 110) is the administrative rule that addresses the taxability of freight and delivery costs. It reads in part:

> Amounts received by a seller from a purchaser for freight and delivery costs incurred by the seller prior to completion of sale constitute recovery of costs of doing business and must be included in the selling price or gross proceeds of sales reported by the seller regardless of whether charges for such costs are billed separately and regardless of whether the seller is also the carrier.

According to WAC 458-20-103 (Rule 103), a sale is not completed until the delivery is accomplished. The rule states in pertinent part:

> For the purpose of determining tax liability of persons selling tangible personal property, a sale takes place in this state when the goods sold are delivered to the buyer in this state, irrespective of whether title to the goods passes to the buyer at a point within or without this state.

Thus, freight charges that are a recovery of delivery expenses are subject to both the payment of B&O tax and collection of the retail sales tax when the taxpayer has nexus and the sale has not been disassociated.

However, if the sale has been disassociated, the freight charges are not subject to the payment of B&O tax and the collection of the retail sales tax. Although use tax is still due on the value of the article sold, the freight charges are not subject to the collection and the payment of use tax.

WAC 458-20-178 provides:

> Value of article used. The tax is levied and collected on an amount equal to the value of the article used by the taxpayer. The term "value of the article used" is defined by the law as being the total of the consideration paid or given by the purchaser to the seller for the article used plus any additional amounts paid by the purchaser as tariff or duty with respect to the importation of the article used. In case the article used was extracted or produced or manufactured by the person using the same or was acquired by gift or was sold under conditions where the purchase price did not represent the true value thereof, the value of the article used must be determined as nearly as possible according to the retail selling price, at the place of use, of similar products of like quality, quantity, and character.

DECISION:

The taxpayer has not presented specific evidence supporting disassociation of any of its sales; accordingly, the taxpayer's petition for refund is denied.

Additionally, the taxpayer is instructed to report and pay B&O tax and retail sales tax or use tax on delivery charges recovered from its customers.

Dated this 25th day of June 1993.