

Cite as Det. No. 94-004, 14 WTD 167 (1995).

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. 94-004
)	
. . .)	Registration No. . . .
)	REFUND REQUEST
)	

RULE 111: ADVANCES AND REIMBURSEMENTS -- SCHOOL DISTRICTS -- COMPETITIVE BIDDING. A taxpayer who agrees to pay a third party vendor, to whom a public school district is indebted for goods or for services rendered, and who is neither primarily nor secondarily liable for the goods or services rendered, may exclude from its gross receipts those amounts received by the taxpayer as "reimbursement" from the public school district.

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:

A corporation seeks a refund of business and occupation (B&O) tax on amounts it received from Washington school districts as reimbursement for payments made by the taxpayer to food purveyors.¹

FACTS:

Gray, A.L.J. -- The Department of Revenue (Department) audited the taxpayer for the period January 1, 1988 through December 31, 1989. The Department issued an assessment against the taxpayer which it appealed to the Interpretation & Appeals Division (I&A). The Department denied relief to the taxpayer in a letter dated

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

July 30, 1991, in which the Administrative Law Judge (ALJ) wrote that the taxpayer's issues had previously been addressed in published determinations. The taxpayer timely requested reconsideration.

In a letter dated December 10, 1991, the ALJ denied reconsideration on the basis that the taxpayer had conceded liability for all items addressed in the July 30, 1991 letter, that the taxpayer raised a new issue not raised in its earlier appeal, and that the taxpayer could petition for a refund within four years after the year in which the assessment was paid.

The taxpayer paid the disputed tax and petitioned for a refund representing business and occupation (B&O) tax imposed on gross receipts in 1988 and 1989. In its petition, the taxpayer specifically wrote:

This Petition for Refund does not request refund for sums received by Taxpayer as reimbursement for its own payroll expenses. This refund is addressed to sums received by Taxpayer as reimbursement by the school districts for sums which had been advanced by Taxpayer to pay food purveyors which had also been awarded contracts to sell food to the school districts.

The taxpayer states that the ALJ had not been presented with the documents needed to determine the reimbursement issue. The taxpayer had not submitted the school district's invitation to bid directed to food purveyors interested in selling food to the school districts during the pertinent years.

The taxpayer is a corporation located outside of Washington. It is in the business of managing and operating cafeterias owned by school districts located in the state of Washington. The taxpayer operates under food management contracts entered into with school districts on a year-to-year basis. The taxpayer submitted a sample food management contract between it² and a public school district in southwest Washington. The contract authorized the taxpayer's predecessor (hereinafter, "predecessor") "to manage and operate on behalf of the school district, the school cafeteria, kitchens, snack bars and related food facilities located within the premises [of the schools]."

The contract required the predecessor to send invoices to the school district for actual "food service operating costs." The contract defined "food service operating costs" to include:

²Actually, its predecessor.

10.04(a) The actual cost of all food, beverages and supplies purchased under [the school district's] competitive bids by [the predecessor] for the food service operation on the premises (excluding donated commodities and sub-standard meals as defined in Section 2.12 of this Agreement), but including applicable taxes and delivery charges, less all applicable discounts and rebates.

Paragraph 10.05 required the school district to reimburse the predecessor "for all purchases incurred as defined in paragraph 10.04 of this Agreement." Finally, paragraph 14.01 declared that:

[The predecessor] is an independent contractor acting as an agent for [the school district] and shall not be, or be deemed for any purpose to be, an employee of the [school district.]³

The taxpayer also submitted a copy of an invitation to bid from a consortium of seven southwest Washington school districts that was issued to food vendors in 1988. The bid notified all potential vendors that each school district would act in its own behalf for "purchase order and payment of all vendor invoices," and that the school districts would determine whether food products were of acceptable quality and so whether to accept or reject the food products. The bid also warned potential vendors not to order any food products until they had received "a valid purchase order from the district's agents."

The taxpayer submitted an earlier copy of an invitation to bid from one of the school districts that was issued to potential food vendors (1983). This invitation to bid said:

5. The District currently contracts with [predecessor] for preparation of all meals in the District. [Predecessor] will act as the District's agent for payment of all vendor invoices, quality testing on food products, etc. Successful vendors shall be prepared to submit duplicate invoicing and pricing information to Interstate United as required.

The 1983 bid also informed potential vendors of their obligations

³We are aware that "[d]etermination of an agency relationship is not controlled by the manner in which the parties contractually describe their relationship." Rho Company, Inc. v. Department of Rev., 113 Wn.2d 561, 570, 782 P.2d 986 (1989). However, paragraph 14.01 is an expression of the parties' intention with regard to the nature of their relationship.

to meet with predecessor to determine schedules and to inform the vendors not to place their orders for food products until they received "a valid purchase order from the District or the District's agent."

The taxpayer also submitted the affidavit of the General Manager of the taxpayer, which declares, among other things:

The actual award of the bids [on the food supply contracts] is done exclusively by the school district purchasing agency.

We play no part in the award of the supply contracts and in fact our corporate office is not given any notice of the identity of the successful bidders.

. . .
We do not execute any written or oral agreements with any successful bidders for food supplies. All food suppliers are aware that their supply contract has been awarded to them by the school district purchasing agency. . . . All food suppliers are aware from the terms of the invitation to bid that Taxpayer has no part in the making of supply contracts and that Taxpayer serves solely as an agent of the school district in advancing payments on invoices.

ISSUE:

Whether the amounts the taxpayer received as reimbursement from the school districts for funds advanced by the taxpayer to pay food purveyors, who had been awarded contracts to sell food to the school districts, are excluded from the taxpayer's gross receipts under WAC 458-20-111 (Rule 111).

DISCUSSION:

[1] RCW 82.04.070 defines "gross proceeds of sales":

"Gross proceeds of sales" means the value proceeding or accruing from the sale of tangible personal property and/or for 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.

RCW 82.04.080 defines "gross income of the business":

"Gross income of the business" means the value proceeding or accruing by reason of the transaction of the business engaged in and includes gross proceeds of sales, compensation for the rendition of services, gains realized from trading in stocks,

bonds, or other evidences of indebtedness, interest, discount, rents, royalties, fees, commissions, dividends, and other emoluments however designated, all without any deduction on account of the cost of tangible property sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses.

RCW 82.04.090 defines "value proceeding or accruing":

"Value proceeding or accruing" means the consideration, whether money, credits, rights, or other property expressed in terms of money, actually received or accrued. The term shall be applied, in each case, on a cash receipts or accrual basis according to which method of accounting is regularly employed in keeping the books of the taxpayer. The department of revenue may provide by regulation that the value proceeding or accruing from sales on the installment plan under conditional contracts of sale may be reported as of the dates when the payments become due.

These definitions are intended to define the "gross receipts" of a business, upon which the B&O tax is imposed. The definitions expressly state that no deductions whatsoever are allowed from "gross proceeds of sales" or from "gross income of the business." The B&O tax is intended to apply to gross receipts, not to receipts after adjustments.

Nonetheless, the Department recognizes that some gross receipts ("advances" and "reimbursements") properly are not included as part of a taxpayer's gross proceeds of sales or gross income of the business. WAC 458-20-111 (Rule 111) embodies the Department's recognition of those instances and provides guidelines as to when advances and reimbursements may be excluded. Rule 111 defines "advances" and "reimbursements":

The word "advance" as used herein, means money or credits received by a taxpayer from a customer or client with which the taxpayer is to pay costs or fees for the customer or client.

The word "reimbursement" as used herein, means money or credits received from a customer or client to repay the taxpayer for money or credits expended by the taxpayer in payment of costs or fees for the client.

Rule 111 also makes clear that the taxpayer must have no liability other than liability as an agent for the fees or costs:

The words "advance" and "reimbursement" apply only when the customer or client alone is liable for the payment of the

fees or costs and when the taxpayer making the payment has no personal liability therefor, either primarily or secondarily, other than as agent for the customer or client.

Specifically, Rule 111 allows a taxpayer to deduct "advances" and "reimbursements" from its gross receipts:

There may be excluded from the measure of tax amounts representing money or credit received by a taxpayer as reimbursement of an advance in accordance with the regular and usual custom of his business or profession.

In construing Rule 111, the Supreme Court said, in Rho Company, Inc. v. Department of Rev., 113 Wn.2d 561, 782 P.2d 986 (1989), said, at 568:

This court has summarized the operation of Rule 111 by stating that the rule allows an exclusion from income for a "pass through" payment when the following three conditions are met: (1) the payments are "customary reimbursements for advances made to procure a service for the client"; (2) the payments "involve services that the taxpayer did not or could not render"; and (3) the taxpayer "is not liable for paying the associate firms except as the agent of the client." Christensen, O'Connor, Garrison & Havelka v. Department of Rev., 97 Wn.2d 764, 769, 649 P.2d 839 (1982); see Walthew, Warner, Keefe, Arron, Costello & Thompson v. Department of Rev., 103 Wn.2d 183, 186, 691 P.2d 559 (1984).

To resolve this issue, we must inquire whether:

- (1) the payments are "customary reimbursements for advances made to procure a service for the client"; and
- (2) the payments "involve services that the taxpayer did not or could not render"; and
- (3) the taxpayer "is not liable for paying the associate firms except as the agent of the client."

We conclude that the payments were "customary reimbursements for advances made to procure a service for the client." The contract expressly required the school district to reimburse the taxpayer for the actual cost of food, beverages, and supplies purchased under the school districts' competitive bids. We also conclude that the payments "involved services that the taxpayer did not render." The taxpayer was in the business of managing and operating cafeterias, not of supplying food.

The final question is whether the taxpayer had only an agent's liability for the goods or services. In this situation, the school districts contracted directly with the food vendors for the

purchase of the food. The taxpayer agreed that it should pay the food vendors because it could do so more quickly than could the school districts. The school districts agreed to reimburse the taxpayer for such payments.

We conclude that the taxpayer was identified as the school districts's agent, and that the food vendors were aware that the taxpayer was functioning only as the agent of the school districts. Therefore, the amounts received as reimbursements from the school districts are properly excluded from the taxpayer's gross receipts under Rule 111.

DECISION AND DISPOSITION:

The taxpayer's petition is granted.

DATED this 13th day of January, 1994.