Cite as 2 WTD 391 (1987)

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

In the Matter of the Petition For Correction of Assessment of)	D E T E R M I N A T I O N
)	No. 87-76
. . .)	Registration No. . . .
)	Tax Assessment No. . . .
)	
)	

[1] **RULE 159, RCW 82.04.480:** BROKERS AND AGENTS -- SEAFOOD INDUSTRY. A taxpayer claiming that it is an agent must show that a contract or agreement exists which "clearly establishes" a principal and agent relationship. How a taxpayer reports income on its federal tax returns does not, by itself, establish such a relationship. All requirements of Rule 159 must be met.

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: . . .
. . .
. . .

DATE OF HEARING: January 29, 1986

NATURE OF ACTION:

The taxpayer was audited for the period from January 1, 1981 to Februaryá28, 1983. The auditor reclassified certain income from commission (service) business and occupation to wholesaling. The taxpayer appeals that reclassification.

FACTS AND ISSUES:

Normoyle, A.L.J. (successor to M. Clark Chandler, A.L.J.) -- The taxpayer, during the period of the audit, engaged in buying and selling seafood, sometimes as a wholesaler, sometimes as a broker or agent. The sales in dispute took place during the first quarter of 1981. The auditor contends that the taxpayer was taxable under the Wholesaling business and occupation classification. The taxpayer contends it was an agent and taxable under the business and occupation Service tax classification.

The following sets forth the history of the transactions at issue:

1. A company which bought crab and then sold it to retailers, such as restaurants, depleted its crab inventory. The company, which throughout this Determination will be called the "Buyer," wanted to buy more crab but the only sources were its competitors. They couldn't buy directly from them because the competitors wouldn't sell to them. Even disclosure of the fact that the Buyer was out of crab would be damaging, as the competitors could then control the market price, at least temporarily.

2. The taxpayer found out about the Buyer's need and the competitors' ability to provide crab. The taxpayer claims that an oral agreement was struck between it and the Buyer whereby the Buyer agreed to pay $3.07 per pound and that, if the taxpayer could obtain the crab at a lower price, the difference was its to keep.

3. On January 30, 1981, one of the competitors invoiced the taxpayer for 543,930 pounds of crab, at $3.00 per pound. The invoice states that the crab was "Sold To: (taxpayer)." Payment was due in ten days. The Buyer's name is not mentioned on the invoice. The taxpayer states that it is the custom of the industry for agents to make undisclosed purchases for their principals.

4. On February 4, 1981, the Buyer sent the taxpayer a "Purchase Order." The order was for up to 544,000 pounds, at $3.07 per pound. It specifically mentioned the competitor's name as the source of the crab. Payment was to be made by the Buyer when the product was received.

5. Two days later, on February 6, the taxpayer sent a bill to the Buyer for the crab purchased from the competitor. The bill states that the crab was "sold to" the Buyer for $3.07 per pound.

6. From that point on, the trail becomes a little harder to follow, but apparently the crab was sent by the competitor to a cold storage facility in Seattle and then shipped by the cold storage company to the Buyer in Bellingham. This process took from Februaryá9 to Februaryá13. The cold storage company's bill of lading showed that the competitor was "the shipper" and the product was shipped to the Buyer.

7. The other transactions in dispute were handled the same way. The total paid by the Buyer was approximately $3,360,000. Each "sale" by the competitors to the taxpayer was for $3.00 per pound. Each "sale" from the taxpayer to the Buyer was for $3.07 per pound.

There are four additional facts to be considered. First, the taxpayer, at least for these sales, did not or could not provide the auditor with accounting records, such as a sales journal, check register or cash receipts book, indicating that these were agency transactions rather than sales to and then by the taxpayer in its own name.

Second, the taxpayer reported the income from these sales as commissions on its federal income tax returns.

Third, as support for its position that it was acting as agent for the Buyer, the taxpayer submitted a copy of a letter from the successor corporation of the Buyer, dated July 30, 1985. That letter was addressed to the taxpayer and states that the successor, with regard to the February 1981 sales, ". . . inquired of its former employees regarding the transactions and they do recall generally that (the taxpayer) did act as broker on the transactions which were represented by the purchase orders, on behalf of (Buyer)." (Emphasis added.)

Fourth, again in support of its agency claim, the taxpayer supplied a copy of letters from the Buyer to the taxpayer, and from the taxpayer to one of the competitors. The substance of the letter from the Buyer was that, in October 1980 (before the audit), they bought crab "through" the taxpayer's firm, that there was a product defect, that the Buyer shipped the defective crab directly back to the competitor, and the taxpayer should arrange with the competitor for repayment to the Buyer. The other letter, from the taxpayer to the competitor, did request such repayment.

Issue:

Was the taxpayer acting as agent for the Buyer, under RCW 82.04.480 and Washington Administrative Code 458-20-159?

DISCUSSION:

RCW 82.04.270 imposes a business and occupation tax on persons making sales at wholesale. The tax is based on the gross proceeds of sale. The auditor believed that the taxpayer's activities brought it within this statute. Tax was assessed based on the total sales price of the "sale" by the taxpayer to the Buyer, i.e., the $3.07 per pound price.

The taxpayer believes that the proper tax classification is Service, under RCW 82.04.290, and that the tax should be based only on those portions of the sales which were its "commission," i.e., the $.07 per pound differential.

In short, if the taxpayer bought and sold the crab, it was a wholesaler. If the taxpayer acted merely as agent for the Buyer, it was not a wholesaler and the Service B&O tax applies.

RCW 82.04.480 and WAC 458-20-159 (Rule 159) both deal with agency. The statute reads as follows:

> Every consignee, bailee, factor, or auctioneer having either actual or constructive possession of tangible personal property, or having possession of the documents of title thereto, with power to sell such tangible personal property in his or its own name and actually so selling, shall be deemed the seller of such tangible personal property within the meaning of this chapter; and further, the consignor, bailor, principal, or owner shall be deemed a seller of such property to the consignee, bailee, factor, or auctioneer.
>
> The burden shall be upon the taxpayer in every case to establish the fact that he is not engaged in the business of selling tangible personal property but is acting merely as broker or agent in promoting sales for a principal. Such claim will be allowed only when the taxpayer's accounting records are kept in such manner as the department of revenue shall by general regulation provide.

Rule 159, as it read during the period of the audit, provided as follows, in pertinent part:

> AGENTS AND BROKERS. Any person who claims to be acting merely as agent or broker in promoting sales for a principal or in making purchases for a buyer, will have such claim recognized only when the contract or agreement between such persons clearly establishes the relationship of principal and agent and when the following conditions are complied with:
>
> 1. The books and records of the broker or agent show the name of the actual owner of the property for whom the sale was made, or the actual buyer for whom the purchase was made.
>
> 2. The books and records show the amount of gross sales, the amount of commissions and any other incidental income derived by the broker or agent from such sales.
>
> SERVICE AND OTHER BUSINESS ACTIVITIES. Every consignee, bailee, factor or auctioneer who makes a sale in the name of the actual owner, or as agent of the actual owner, or who purchases as agent of the actual buyer, is taxable under the Service and Other Business Activities classification upon the gross income derived from such business.

Focusing on that part of the rule titled "AGENTS AND BROKERS," for the taxpayer to be considered an agent, it must show all of the following:

1. A contract or agreement existed between it and the buyer which "clearly establishes" the relationship of principal and agent; and

2. The taxpayer's records show the name of the actual buyer for whom the purchase was made; and

3. The records show the amount of the gross sale; and

4. The records show the amount of the commission.

We don't believe that the taxpayer has shown compliance with even one of these requirements, let alone all of them. While the rule does not require that the contract or agreement be in writing, the burden is on the taxpayer to show that the terms of the agreement clearly establish a principal and agent

relationship. We find that the taxpayer has not met its burden of proof.

While the substance of the transactions, under common law, may have been principal-agent, the clear language of RCW 82.04.480 and Rule 159 is controlling, not common law principles. All that the taxpayer could show to establish the existence of a "contract or agreement" was a letter from the successor corporation of the Buyer, written some four years after the sales, stating only that the Buyer's former employees "do recall generally" that the taxpayer acted as broker on the sales at issue. We do not believe that this letter, even when combined with other documents supplied by the taxpayer, show an agreement which clearly establishes the principal and agent relationship.

As further support that an agency relationship existed, the taxpayer relies on the fact that its federal income tax returns reported the income as commissions, not sales. We are aware of the contents of a letter dated Decemberá6, 1984 from the then Director of the Department of Revenue to an attorney representing the seafood industry, which states that federal income tax returns could be of assistance in determining whether a taxpayer was an agent or a wholesaler. However, the general guidelines of that letter cannot prevail over the specific language of Rule 159. We fail to see how the reporting of income in a certain way on federal tax returns can, in itself, satisfy the requirement that the taxpayer show the existence of a contract or agreement which clearly establishes the principal and agent relationship. Further, the letter was written almost four years after the sales, and no estoppel argument could be made.

Because we conclude that the taxpayer has failed to prove an agency relationship under requirement number 1, we need not engage in a detailed analysis of the facts as they relate to the other requirements of the rule. We do note, though, that the taxpayer also did not comply with the record-keeping requirements of the rule and would not prevail in this appeal even if the agency relationship were clearly established by a contract or agreement. The lack of accounting records indicating that these were agency transactions is also fatal to this appeal.

DECISION AND DISPOSITION:

The petition for correction of assessment is denied. Because the delay in the issuance of this Determination was for the

sole convenience of the Department, interest will be waived from February 8, 1986 to April 7, 1987. Tax Assessment No. . . . in the amount of $ . . . , plus unwaived extension interest of $..., for a total of $ . . . is due by April 7, 1987.

DATED this 18th day of March 1987.