Cite as Det. No. 13-0380, 33 WTD 380 (2014)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Refund of Assessment of . . .	)	D E T E R M I N A T I O N No. 13-0380 Registration No. . . .

[1] RULE 111; RCW 82.04.255; RCW 82.04.080; ETA 3145.2009: GROSS INCOME OF THE BUSINESS – REAL ESTATE BROKERAGE RECEIPTS FROM ASSOCIATES AND COMMISSIONS SHARED WITH CLIENTS. Amounts received from associates for expenses and commissions received at closing that are shared with clients are included in the real estate brokerage's gross income and subject to tax.

[2] RULE 254; RCW 82.32.070: RECORDS – RETAIL SALES TAX – RECORDKEEPING. A taxpayer must maintain and provide adequate records to demonstrate that it is entitled to an adjustment of a tax assessment.

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.

Margolis, A.L.J. – A Washington real estate broker and property manager (Taxpayer) that provides maintenance services for others' property appeals the assessment of service and other activities business and occupation (B&O) tax on grounds that the measure of tax includes commissions, reimbursements from its associates for business expenses, and income that it claims was duplicated in general ledgers. . . . Taxpayer's petition is denied.[1]

ISSUES

1. Whether, under RCW 82.04.255 and WAC 458-20-111, Taxpayer is entitled to exclude receipts from associates for expenses and commissions shared with clients from the measure of B&O tax.

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

2. Whether, under RCW 82.32.070, Taxpayer has provided adequate records to support a credit for tax paid at source on purchases resold when performing repair and maintenance service on others' property, and an adjustment to the measure of B&O tax on grounds that the assessment was based on income duplicated in general ledgers.

. . .

FINDINGS OF FACT

Taxpayer is a Washington corporation that holds a Real Estate Firm license and is engaged in the business of brokering real estate and managing and maintaining properties for others. The Department of Revenue's (Department's) Audit Division (Audit) examined Taxpayer's books and records for the period January 1, 2008 to March 31, 2012, and on October 9, 2012 assessed Taxpayer $. . . . The assessment is comprised of $. . . in service and other activities B&O tax, $. . . in retail sales tax, $. . . in retailing B&O tax, $. . . in negligent penalty, and $. . . in interest.

Audit based its assessment on a reconciliation of what Taxpayer reported on its combined excise tax returns and Taxpayer's books and records. Audit determined that Taxpayer's gross receipts subject to service and other activities B&O tax were the total of amounts recorded in general ledger accounts booked by Taxpayer that reflected its revenue, which exceeded the amounts that Taxpayer reported on its returns. Audit explained that this difference was the result of Taxpayer treating itemized expenses as "reimbursements" and not reporting the income from these amounts as part of its gross income. Taxpayer provided the following worksheet detailing amounts that it asserts should not have been included in the measure of B&O tax:

	2008	2009	2010	2011	2012
CIBA Dues/Reimb	$. . .	$. . .	$. . .	$. . . .	$. . .
Signage	. . .	. . .	. . .	. . .	. . .
L & I Reimb	. . .	. . .	. . .	. . .	. . .
Payroll Reimbursements	. . .	. . .	. . .	. . .	. . .
Client Rebates	. . .	. . .	. . .	. . .	. . .
Annual Total	. . .	. . .	. . .	. . .	. . .
Tax Rate	. . .	. . .	. . .	. . .	. . .
	. . .	. . .	. . .	. . .	. . .
				Total:	$. . .

Taxpayer explained what each of the above categories means as follows: "CBIA Dues/Reimb" are its associates' Commercial Brokers Association (CBA)[2] dues reimbursed by the associates; "signage" are for signs used to advertise properties for sale reimbursed by its associates; "L & I Reimb" are premiums that Taxpayer must pay to the Washington Department of Labor and Industries reimbursed by its associates; "payroll reimbursements" are medical insurance

[2] CBA is a multiple listing association. *See* http://www.commercialmls.com (last accessed December 3, 2013).

premiums for its associates reimbursed by a third party; and, "Client Rebates" are the share of the commissions that Taxpayer receives at closing and disburses to clients to earn business.[3]

Taxpayer provided a sample agreement to show its relationship with its associates, under which the associates are independent contractors responsible for their own insurance and other business expenses, and pay industrial insurance premiums (if requested by Taxpayer) and fees/costs for real estate associations. Taxpayer also provided an invoice from CBA, showing total charges of $. . . for 16 agents, and an invoice from . . . , a sign installation/removal company, issued to Taxpayer and showing a total due for signage ordered by various associates.

Taxpayer provided documents showing examples of sales involving these "Client Rebates." The documents include HUD-1 Settlement Statements showing that the full commission amounts were paid to Taxpayer, a cover letter from a title insurance company stating that Taxpayer's commission has been forwarded to Taxpayer's accounting office, Income by Customer Detail showing amounts of rebates credited to client accounts, Current Commission forms showing reduced commission amounts Taxpayer paid to agents, and transaction cover sheets and copies of checks indicating payment of rebate amounts. Taxpayer also provided a spreadsheet summarizing these amounts for the audit period.

ANALYSIS

Washington's B&O tax is imposed on every person "for the act or privilege of engaging in business activities" and applies to the gross income of the business. RCW 82.04.220. "Business" for B&O tax purposes includes "all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or to another person or class, directly or indirectly." RCW 82.04.140. "Gross income of the business" similarly is broadly defined as:

> [T]he 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,. . . 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 82.04.080(1) (emphasis added). Likewise, "value proceeding or accruing" is defined in pertinent part as "the consideration, whether *money*, credits, rights, or other property expressed in terms of money, *actually received or accrued*." RCW 82.04.090 (emphasis added).

The Legislature "intended to impose the business and occupation tax upon virtually all business activities carried on within the state." *Simpson Inv. Co. v. Dep't of Revenue*, 141 Wn.2d 139, 149, 3 P.3d 741 (2000) (quoting *Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971)).

[3] [An example of a "Client Rebate" is where a client agrees to use the services of a buyer's agent if that agent agrees to share his commission with the client, and after the sale closes, the agent pays part of his commission to the client.]

Unlike the federal income tax**,** the B&O tax is not a tax on profit net gain, capital gain, or sales "but a tax on the total money or money's worth received in the course of doing business." *Budget Rent-A-Car of Wash.-Oregon v. Dep't of Revenue*, 81 Wn.2d 171, 173, 500 P.2d 764 (1972). The B&O tax provisions "leave practically no business and commerce free of the business and occupation tax." *Id*. at 175. As a result, unless an exception or deduction applies, a taxpayer owes B&O tax on all income received.

RCW 82.04.255 applies the B&O tax to providers of real estate brokerage services as follows:

> (1) Upon every person engaging within the state in the business of providing real estate brokerage services; as to such persons, the amount of the tax with respect to such business is equal to the gross income of the business, multiplied by the rate of 1.5 percent.
>
> (2) The measure of the tax on real estate commissions earned by the real estate firm is the gross commission earned by the particular real estate firm including that portion of the commission paid to brokers, including designated and managing brokers, in the same firm on a particular transaction. However, when a real estate commission on a particular transaction is divided among real estate firms at the closing of the transaction, including a firm located out of state, each firm must pay the tax only upon its respective shares of said commission. Moreover, when the real estate firm has paid the tax as provided herein, brokers, including designated and managing brokers, within the same real estate firm may not be required to pay a similar tax upon the same transaction. . . .
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> (3) For the purposes of this section, "broker," "designated broker," "managing broker," and "real estate firm" have the same meaning as provided in RCW 18.85.011.

WAC 458-20-128 (Rule 128) is the administrative rule that implements RCW 82.04.255, and provides, in pertinent part:

> Thus, with the exception of cooperating brokerage offices, no deduction is allowed for commissions, fees, or salaries paid by a broker to another broker or salesman, nor for other expenses of doing business.
>
> *The term "gross income of the business" includes gross income from commissions, fees and other emoluments however designated which the agent receives or becomes entitled to receive*, but does not include amounts held in trust for others. (see also WAC 458-20-111, advances and reimbursements.) *No deductions are allowed for dues, charges, and fees paid to multiple listing associations.*

(Emphasis added.)

Taxpayer asserts that it pays part of the commissions that it receives to its clients as rebates, and argues that it does not earn this amount so it should not be included in the measure of tax. However, per Rule 128, Taxpayer's gross income includes commissions "however designated

which the agent receives." As demonstrated by the HUD-1 documents and other records showing that the commissions were paid to the Taxpayer upon closing, Taxpayer receives the commissions at issue. Thus, we conclude that Taxpayer cannot deduct these amounts from its measure of B&O tax.

Taxpayer also argues that receipts from its associates for business expenses are deductible as reimbursements. WAC 458-20-111 (Rule 111) is the administrative rule regarding advances and reimbursements. It provides as follows, in pertinent part (emphasis added):

> 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.*
>
> 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.
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> The foregoing is limited to cases wherein the taxpayer, as an incident to the business, undertakes, on behalf of the customer, guest or client, the payment of money, either upon an obligation owing by the customer, guest or client to a third person, or in procuring a service for the customer, guest or client which the taxpayer does not or cannot render and for which no liability attaches to the taxpayer. . . . .

ETA 3145.2009 explains how real estate commissions are taxable when shared between a broker and associate, and circumstances under which payments by associates for expenses are taxable. It provides options for use as a general guide, including the following:

> Option 2: The Broker and Associate agree that commissions will be split 50/50 for any real estate sold by the Associate. It is also agreed that the Associate will pay the Broker for one half of the Associate's expenses incurred during the month. During the current month the Associate made sales which resulted in the office receiving $6,000 of commissions. The Associate's actual expenses for the month were $3,000 which included advertising, multiple listing charges, telephone, etc. The Broker paid the Associate $3,000 in commissions. The Associate gave the Broker a check for $1,500 to cover half of the expenses.
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> The Broker is taxable on the gross commissions of $6,000 *plus the $1,500 payment from the Associate*. The $7,500 is taxable under the service B&O tax classification. The Associate is not subject to B&O tax.

ETA 3145.2009 (Emphasis added.) In this matter, the CBA invoices Taxpayer for its associates' dues, the sign installation company invoices Taxpayer for services ordered by agents, and Taxpayer has provided no evidence to indicate that it is authorized as an agent of its associates to contract with third parties for these purchases. All evidence indicates that Taxpayer is liable for

the charges, so because Taxpayer is primarily or secondarily liable to the third party providers, and not solely as its associates' agent, it cannot exclude these amounts received from its associates under Rule 111. Further, as we held in Det. No. 90-226, 10 WTD 19 (1990), where a real estate office made a similar claim, "[t]he mere fact that the taxpayer could contractually recover those expenses from its salespersons, simply does not relegate its own status to one of agency." Consistent with ETA 3145.2009, [Rule 111, and the definition of "gross income of the business" in RCW 82.04.080(1),] we conclude that Taxpayer cannot exclude these amounts from the measure of B&O tax.

RCW 82.32.070 requires taxpayers to maintain suitable records as may be necessary to determine the amount of any tax for which they may be liable. WAC 485-20-254 (Rule 254) is the administrative rule regarding recordkeeping. Rule 254(3) provides, in pertinent part:

> (b) It is the duty of each taxpayer to prepare and preserve all records in a systematic manner conforming to accepted accounting methods and procedures. Such records are to be kept, preserved, and presented upon request of the department or its authorized representatives which will demonstrate:
>
> > (i) The amounts of gross receipts and sales from all sources, however derived, including barter or exchange transactions, whether or not such receipts or sales are taxable. These amounts must be supported by original source documents or records including but not limited to all purchase invoices, sales invoices, contracts, and such other records as may be necessary to substantiate gross receipts and sales. . . .
> >
> > (iii) The payment of retail sales tax or use tax on capital assets, supplies, articles manufactured for your own use, and other items used by the taxpayer as a consumer.
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> (c) The records kept, preserved, and presented must include the normal records maintained by an ordinary prudent business person. Such records may include general ledgers, sales journals, cash receipts journals, bank statements, check registers, and purchase journals, together with all bills, invoices, cash register tapes, and other records or documents of original entry supporting the books of account entries. The records must include all federal and state tax returns and reports and all schedules, work papers, instructions, and other data used in the preparation of the tax reports or returns.

Taxpayer was assessed retail sales tax on its purchases of items for its property management business and Taxpayer claims that it already paid retail sales tax when it purchased these items. In support of this assertion, Taxpayer provided an email from [a bank] stating that its account is not flagged as tax exempt and three sample invoices from [vendor] credit services showing tax paid. However, the Department has already excluded purchases where Taxpayer provided invoices showing tax paid at source. Audit has agreed to make further adjustments upon the receipt of additional invoices, but Taxpayer has not provided such invoices.

Taxpayer also asserts that it was assessed twice on the same income because Audit used figures from Taxpayer's general ledgers that had already been included in the measure of tax or represented collected retail sales tax. Audit contacted Taxpayer to go over entries that show the duplication of income from general ledgers in the measure of tax, but Taxpayer has not provided this information. Absent evidence that Audit assessed tax twice on the same income or assessed tax on collected sales tax by including amounts from incorrect general ledgers, we have no grounds for adjustment.[4]

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DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 6th day of December 2013.

[4] On July 16, 2013, Taxpayer send an email indicating that it would provide a zip file containing a large volume of records, but it was never received.