

Cite as 4 WTD 1 (1987)

BEFORE THE INTERPRETATION AND APPEALS SECTION
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 Correction of Assessment)	
)	No. 87-265
)	
. . .)	Registration No. . . .
)	
)	

[1] **RULE 164 AND RCW 82.04.280:** RCW 48.05.310--BUSINESS AND OCCUPATION (B&O) TAX--INDEPENDENT RESIDENT MANAGING GENERAL AGENT--MANAGERIAL FUNCTIONS. A person claiming to fall within the classification for a resident managing general agent must demonstrate that he or she is licensed as such by the insurance commissioner and perform the independent managerial functions listed in WAC 458-20-164 (Rule 164). Subsection 2(c), which requires that such a person "directly contracts for or hires all selling agents", is satisfied where the general agent hires selling agents for the insurance company.

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: May 7, 1987

NATURE OF ACTION:

The taxpayer protests the reclassification of income reported under the rate for a resident managing general insurance agent to the service rate.

FACTS AND ISSUES:

Frankel, A.L.J.--The taxpayer's records were examined for the period January 1, 1982 through March 31, 1986. The audit disclosed taxes and interest owing in the amount of \$ Assessment No. . . . in that amount was issued on October 23, 1986.

At issue in this appeal is the auditor's reclassification of the taxpayer's income for 1982 and 1983.¹ During that period, the taxpayer had reported its income as a resident managing general insurance agent (MGA rate). The auditor reclassified this income to the service rate, resulting in additional taxes of \$

The taxpayer objects to the reclassification on grounds it was reporting as it had been advised to report by the Department when it began business in 1963. At that time, the taxpayer submitted a completed application form and copies of its general agency agreements. The Department advised the taxpayer as follows:

Reference is made to your letter of December 13, 1963; wherein you advise you have enclosed our Questionnaire (TF-68) for determination of your qualification for the tax rate reduction on the portion of your income from your business as an independent resident managing general agent for Fire and Casualty Insurance Companies. This rate reduction from .01 to .0044 was enacted by the 1963 Washington State Legislature by amendment to RCW 82.04.280, effective June 13, 1963.

Please be advised, on the basis of the completed questionnaires and subject to future field audit, we have determined your business qualifies for the tax rate reduction as provided by the 1963 State Legislature. Therefore, you should have entered all income received as an independent resident managing

¹The additional amounts of the assessment are for use tax assessed on assets acquired by the taxpayer when it took over an office in Washington from an insurance company and for some additional commission income. The taxpayer does not protest this part of the assessment.

general agent under the classification of Wholesaling - Other, line 11 of the monthly Excise Return (Form 2406) after June 13, 1963. Review of your filed returns indicates you are paying gross income on all business under Service and Other Activities at .01. In order to adjust the account, please submit a schedule of all income from your business as an independent resident managing general agent from June 13, 1963 to date.

As you have stated in previous correspondence, your regular insurance business must be reported as "Service and Other Activities" line 14, on the monthly Excise Tax Return (Form 2406). (Letter of December 27, 1963 excise tax division.)

The taxpayer stated it was subsequently advised that it was correctly reporting at the MGA rate. The taxpayer's petition stated:

In February 1977 we applied for authorization to pay tax at the MGA rate on business produced for . . . Insurance Company and . . . Insurance Company. According to a note in our file we received verbal approval on our request from a In early 1979 Mr. . . . , auditor for the Washington Department of Revenue, audited our tax filings for 1975-1978 and used the MGA rate as the correct one.

The auditor's detail of differences and instructions verifies that the taxpayer was told to report under the MGA rate rather than the service B&O rate.

The taxpayer stated that it continued to pay as managing general agents until 1983 when the Washington Legislature created a special classification for Insurance Agents and Brokers. It stated it began paying at that rate, not because it no longer thought it should be paying at the MGA rate, but because the company's employees had changed and were not aware of the MGA classification and the previous advice from the Department.

In 1984, the taxpayer wrote the Department again requesting the Managing General Agent classification. The taxpayer's letter was addressed to the Office Audit supervisor at that time and stated:

We thank you for your letter of September 27, 1984 enclosing copies of the recent law passed in your state dealing with the taxation of certain managing general agents.

We have reviewed this material, and we feel that both [taxpayer] and . . . meet the criteria to be classed as managing general agents.

If you will refer to the items listed in the right hand column of the attached sheet captioned "WAC 458 - 20 - 164", we wish to confirm, firstly, under Item a. that we pay the salaries of special field representatives, underwriters, and inspectors as well as office expenses of rent, supplies and secretarial help. We pay selling agents a commission.

Secondly, under Item c., we directly contract for all selling agents by appointing them agents of the insurance companies which we represent.

Inasmuch as we pay and directly contract for selling agents, we meet all the qualifications for being classified as a managing general agent in your state for purposes of taxation. The confusion in this matter arose from the use of the word "employ" in Question 3 of the questionnaire which we submitted to your office. The actual wording of Rule 164 does not require that the selling agents be employees of the managing general agent.²

The Department denied the request on the basis that the taxpayer had not supplied documentation to support its assertion that it directly contracts for all selling agents by appointing them agents of the insurance companies it represents.

DISCUSSION:

²Question 3. asked: "Do you directly employ all selling agents under an agreement between you and the agent?" The taxpayer responded that it did not, that business is retailed by licensed independent insurance agents and brokers.

The Legislature provided the special B&O tax rate for independent residing managing general agents in 1963. The rate is set out in RCW 82.04.280 upon persons engaging within this state in the business of:

(5) representing and performing services for fire or casualty insurance companies as an independent resident managing general agent licensed under the provisions of RCW 48.05.310;

RCW 48.04.310 provides:

(1) An insurer appointing any person as its general agent or manager to represent it as such in this state shall file notice of the appointment with the commissioner on forms prescribed and furnished by the commissioner.

(2) Any such general agent or manager shall have such authority, consistent with this code, as may be conferred by the insurer. A general agent resident in this state and licensed, as in this section provided, may exercise the powers conferred by this code upon agents licensed for the kinds of insurance which the general agent is authorized to transact for the insurer so appointing him.

(3) Any such general agent may accept applications for insurance from licensed agents who are not appointed by the insurer of such general agent where the risk involved is placed in a nonstandard or specialty market of an authorized insurer as defined by regulation of the commissioner. Such nonstandard or specialty business shall not be bound by any agent not appointed by the insurer. A general agent may supply such licensed, nonappointed agent with material to write nonstandard or specialty insurance business including, but not limited to, applications for insurance, underwriting criteria, and rates. A general agent shall not provide any licensed, nonappointed agent with indicia of authority to bind an insurance risk and the general agent and nonappointed agent shall provide written disclaimers of binding authority to an applicant or prospective insured in such form as prescribed by the commissioner.

(4) The appointment of a resident general agent shall not be effective unless the person so appointed is licensed as the general agent of such insurer by the commissioner upon application and payment of the fee therefor as provided in RCW 48.14.010.

(5) Every such license shall expire as at close of business on the thirty-first day of March next following the date of issue, and may be renewed for an additional year upon application and payment of the fee therefor.

(6) The commissioner may deny, suspend, or revoke any such license for any cause specified in RCW 48.17.530 and in the manner provided in RCW 48.17.540.

The bare fact of licensing under RCW 48.04.310 is not enough to allow a business to fall under MGA B&O tax classification. Only those general agents in the fire and casualty field which perform general "managerial" functions for their insurers fall within this tax classification. WAC 458-20-164 (Rule 164).

Rule 164 states that a person claiming status as a managing general agent under RCW 82.04.280(5) must demonstrate:

1. That he is licensed as a resident general agent by the insurance commissioner; and
2. That he performs the following independent manager functions:
 - a. Pays all sales and/or production expense; including salaries of special field representatives, underwriters, and inspectors as well as all office expenses of rent, supplies, secretarial help, etc.
 - b. Bills all premiums for the company so represented.
 - c. Directly contracts for or hires all selling agents.
 - d. Exercises final responsibility with respect to selecting risks and underwriting matters.
 - e. Makes all arrangements for reinsurance.

f. Handles all claims adjustments directly with the insured (by his own staff or through hiring an independent adjuster).

The taxpayer documented that it was licensed in this state by the insurance commissioner.

At issue is subsection 2 c. which provides a general agent must directly contract for or hire all selling agents. The taxpayer stated it did hire selling agents for the insurance company. It interviewed prospective applicants, gave them a questionnaire regarding past employment, credit history, etc. The insurance company, not the taxpayer, appointed the agent as required by Washington law. RCW 48.17.150(h). We agree with the taxpayer that the fact the taxpayer did not directly employ all selling agents under an agreement running between itself and the agent is not dispositive.

The taxpayer hired the agents for the insurance company and met all of the other requirements of Rule 164. Furthermore, the taxpayer stated its relationship with agents was the same in 1984 as it was in 1977 when its application for classification as a resident general managing agent was granted. And during 1982 and 1983, the period at issue, the taxpayer stated Business Insurance³ rated it as the number one general managing agent in the country.

We find the taxpayer properly reported its income at issue during 1982 and 1983 under the rate of independent resident managing general agents.⁴

DECISION AND DISPOSITION:

The taxpayer's petition is granted. An amended assessment shall be issued which shall delete the taxes and interest assessed on the reclassification of the taxpayer's income.

³Business Insurance is a publication on the insurance industry which rates categories of insurers and agents.

⁴Because there are few managing general agents in the state, the Department advises general agents to report their tax under the Extracting for Hire tax classification, which is the same rate.

DATED this 7th day of August 1987.