Cite as Det. No. 01-023, 20 WTD 415 (2001)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

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| 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. 01-023 |
| . . . | ) | Registration No. . . . |
| | ) | Docket No. . . . |
| | ) | FY. . ./Audit No. . . . |

MISC: EQUITABLE ESTOPPEL – REASONABLE RELIANCE. In order for a taxpayer to succeed in a claim of equitable estoppel it must prove, among other things, that it reasonably relied on a statement made by the Department. Reliance on letters written by the Taxpayer Information and Education Section for persons other than the addressee is not reasonable. Likewise, reliance on telephone conversations with unnamed Department personnel and refunds paid but specifically made subject to future audit verification are insufficient to establish equitable estoppel.

NATURE OF ACTION:

A mortgage broker protests the assessment of business and occupation taxes on its receipt of fees relating to home mortgage loans the mortgage broker facilitated.[1]

FACTS:

Coffman, A.L.J. -- The taxpayer is a mortgage broker. Its books and records were reviewed by the Audit Division of the Department of Revenue (Department) for the period January 1, 1996 through September 30, 1999 (Audit Period). As a result of that review, the Department issued the above-referenced tax assessment, which the taxpayer appealed.

The Department published Det. No. 98-218, 18 WTD 46 (1999), which clarified the deductibility of loan fees charged by mortgage brokers. Det. No. 98-218 classified mortgage broker activities in three categories -- Pure Mortgage Brokers, Correspondent Brokers, and Lending Brokers. Det. No. 98-218 found that Pure Mortgage Brokers and Correspondent Brokers are not entitled

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

to the RCW 82.04.4292 deduction for their B&O taxes. The taxpayer provides Pure Mortgage Broker and Correspondent Broker services.

After the publication of Det. No. 98-218, 18 WTD 46 (1999), the taxpayer has not taken the RCW 82.04.4292 deduction on its excise tax returns. The taxpayer claims that Det. No. 98-218 should be applied prospectively only.

Further, the taxpayer is not appealing the correctness of the tax assessment, but rather claims that the Department is barred from issuing the tax assessment because it misled the taxpayer into believing it was entitled to the business and occupation (B&O) tax deduction authorized by RCW 82.04.4292. Specifically, the taxpayer relies on two letters written by the Department's Taxpayer Information and Education Section (TI&E) to third parties; telephone conversations with three unnamed Department personnel allegedly confirming the taxpayer was entitled to the RCW 82.04.4292 deduction; and the fact that the Department gave the taxpayer a refund for the period January 1, 1992 through September 30, 1996. Additionally, shortly after the Department issued the tax refund, the Audit Division scheduled the taxpayer for an audit, but the audit was placed on hold pending a court decision. The taxpayer understood this action to mean it was correctly taking the RCW 82.04.4292 deduction.

ISSUES:

1. Whether the taxpayer has established that it is entitled to equitable estoppel and, therefore, cannot be required to pay the taxes assessed due to denied deductions.

2. Whether Det. No. 98-218 has prospective application only.

DISCUSSION:

1. **Equitable Estoppel**.

The defense of equitable estoppel requires a taxpayer to prove:

> (1) an admission, statement or act inconsistent with a claim later asserted; (2) reasonable reliance on that admission, statement, or act by the other party; and (3) injury to the relying party if the court permits the first party to contradict or repudiate the admission, statement or act. Berschauer/Phillips Constr. Co. v. Seattle Sch. Dist. No. 1, 124 Wash. 2d 816, 831, 881 P.2d 986 (1994). Equitable estoppel against the government is not favored. Kramarevcky v. Department of Social & Health Serv., 122 Wash. 2d 738, 743, 863 P.2d 535 (1993). Therefore, when the doctrine is asserted against the government, equitable estoppel must be necessary to prevent a manifest injustice, and the exercise of government functions must not be impaired as a result of estoppel. Id. Each element must be proved by clear, cogent, and convincing evidence. Id. at 744.

Det. No. 99-011R, 19 WTD 423, 436 (2000), quoting Department of Ecology v. Theodoratus, 135 Wn. 2d 582, 599, 957 P.2d 1241 (1998).

The statements from the Department relied upon by the taxpayer fail to satisfy the second element of equitable estoppel -- reasonable reliance. Specifically, the TI&E letters were not addressed to the taxpayer. Rather, they were issued to others and, additionally, they clearly provided that fees for some services are not deductible under RCW 82.04.4292. The letters do not provide a recitation of the facts provided by the third party requesting the letter. Finally, the taxpayer did not receive the letters from the Department. As such, the letters do not constitute statements from the Department to the taxpayer and, therefore, the taxpayer was not entitled to rely on them.

As to the telephone conversations, the Department has stated it will not be bound by oral instructions given to taxpayers. Specifically, the Department stated:

> The department of Revenue gives consideration, to the extent of discretion vested in it by law, where it can be shown that failure of a taxpayer to report correctly was due to written instructions from the department or any of its authorized agents. The department cannot give consideration to claimed misinformation resulting from telephone conversations or personal consultations with a department employee.
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> There are three reasons for this ruling:
>
> > (1) There is no record of the facts which might have been presented to the agent for his consideration.
> >
> > (2) There is no record of instructions or information imparted by the agent, which may have been erroneous or incomplete.
> >
> > (3) There is no evidence that such instructions were completely understood or followed by the taxpayer.

Excise Tax Advisory 419.32.99 (emphasis in original).

Therefore, the Department will not allow equitable estoppel on the basis of telephone conversations.

The refund the taxpayer received as a result of its refund claim for the period January 1, 1992 through September 30, 1996 was issued "subject to future verification in the event of an audit."[2] Because the refund was issued specifically subject to verification and the Department had scheduled the verification process, the taxpayer's reliance on the refund as a basis to continue to take the deduction was not reasonable. In fact, the scheduling of the audit should have put the

[2] Letter accompanying the refund check, dated January 8, 1997.

taxpayer on notice that taking the deduction was a calculated risk and that it could be denied in a subsequent audit.

Finally, the taxpayer claims that it was led to believe it was entitled to the RCW 82.04.4292 deduction, because audits of mortgage brokers were put on hold pending litigation concerning the applicability of the deduction to mortgage brokers. The taxpayer's understanding was not reasonable. In fact, a reasonable conclusion from the Department's decision to place audits on hold pending the litigation, is that the Department was arguing in court that the deduction did not apply. If the Department had been arguing the deduction applied to mortgage brokers, the case would not have been in court. Rather, the Department would have issued the refund to the litigants.

. . .

DECISION AND DISPOSITION:

The taxpayer's petition is denied.

Dated this 14th day of February, 2001