

Cite as Det. No. 99-243, 20 WTD 338 (2001)

BEFORE THE 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. 99-243
...)	
)	Registration No. . . .
)	FY. . . /Audit No. . . .

[1] Rules 193D; 194 – B&O TAX – IN-STATE ALARM MONITORING – OUT-OF-STATE CUSTOMERS. Taxpayer’s activity of providing monitoring services to its out-of-state customers does not fall within the description of “interstate commerce.” Although the services provided by Taxpayer to its out-of-state customers are performed both in and out-of-state, these services do not constitute commercial trading or the transportation of persons or property across state lines.

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:

Petition requesting exemption from tax as interstate commerce the in state monitoring of out-of-state customer alarm systems.¹

FACTS:

Bauer, A.L.J. – -- The Audit Division (Audit) of the Department of Revenue (Department) examined the business records of (Taxpayer) for the period January 1, 1994 through September 30, 1997 (audit period). As a result of this examination, the above-referenced assessment was issued on July 17, 1998 in the total amount of This total amount included interest accrued to that date, and a payment of . . . , for unprotested amounts due, which had been made by Taxpayer on April 30, 1998. Taxpayer timely petitioned for correction of assessment by letter dated July 28, 1998.

Schedule 4 assessed the selected business service B&O tax on income received for monitoring the alarms of several customers located out-of-state in . . . and Taxpayer monitored these accounts

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

from its Washington business location. Taxpayer's Washington-located monitoring center includes personnel, computers, phone, video screens, and other equipment used in the actual monitoring process. Taxpayer's personnel are physically located at the center watching for alarm messages. All of the alarm responses are made from this Washington center. When an alarm is sounded, authorities near the customer's location are notified from Taxpayer's Washington monitoring center.

Audit concluded that Taxpayer's Washington monitoring activity was inherently local in nature, and the income therefore subject to the selected business service B&O tax. Audit also believed there to be some degree of installation/maintenance service that had taken place at the out-of-state locations, and that this out-of-state activity might warrant apportionment.

The assessment was done on a projected basis because Taxpayer did not report amounts received for services to its out-of-state customers on its excise tax returns. Apportionment was not accomplished because Taxpayer did not provide its costs to Audit. Audit estimated the taxable amounts due based on the best data it had available, using the total monitoring income from out-of-state customers as a percentage of total monitoring sales. A test period, jointly selected by and agreed to by Audit and two of Taxpayer's CPAs, was used to project gross receipts for Taxpayer's activity of monitoring the alarms of its out-of-state customers for the entire audit period.

TAXPAYER'S EXCEPTIONS:

Taxpayer objects to the imposition of tax on its monitoring activity of out-of-state customers. In support of its position, Taxpayer cites provisions of WAC 458-20-193D (Rule 193D).

In computing tax there may be deducted from gross income the amount thereof derived as compensation for performance of services which in themselves constitute interstate or foreign commerce to the extent that that a tax measured thereby constitutes an impermissible burden upon such commerce.

...

EXAMPLES OF EXEMPT INCOME: . . . (3) Income from services rendered by an out-of-state branch or office of the taxpayer regularly maintained outside the state is exempt. (See WAC 458-20-194.)

...

In computing public utility tax, there may be deducted from gross income so much thereof as is derived from actually . . . transmitting communications or electrical energy, from this state to another state or territory or to a foreign country and vice versa.

Based on the above Rule 193D provisions, Taxpayer argues that it is engaged in interstate commerce, and therefore exempt from the assessment of tax. Taxpayer contends substantially all of

the services that Taxpayer's out-of-state customers receive are either "[s]ervices rendered by an "out-of-state branch or office regularly maintained outside the State of Washington," or services received via telephone lines to locations outside the State of Washington. Taxpayer emphasizes that, in each case, it owns the actual computer chip necessary to receive and send the telephone signals, and that this equipment is located on each out-of-state customer's premises.

Taxpayer also cites WAC 458-20-194 (Rule 194):

Whether or not such persons are subject to business tax under the law depends upon the kind of business and the manner in which it is transacted. ...When the business involves a transaction in or related to interstate or foreign commerce, see WAC 458-20-193.

Taxpayer disagrees with Audit's position that taxation with apportionment under Rule 194 applies, and, specifically, the provision that discusses tax treatment for taxpayers who maintain places of business both inside and outside the state which contribute to the performance of a service. Taxpayer notes that each of the Rule 194 examples refers to some kind of professional rendering a professional service for a fee by transaction (i.e., a doctor, accountant, engineer...) rather than to an ongoing monitoring account. Therefore, Taxpayer disagrees that Rule 194 applies, and believes it is more closely related to the activities discussed in Rule 193D. Taxpayer contends this is so, because the language of Rule 193D is similar to the actual activity being conducted by Taxpayer, even though the tax might not specifically be assessed under the public utility tax.

ISSUE:

Whether a taxpayer that provides burglar/fire alarm monitoring to out-of-state customers is engaged in the interstate rendering of services exempt as a public utility.

DISCUSSION:

WAC 458-20-100(8) provides:

(8) The department may grant a conference for review of such petitions, fixing the time and place therefor and notifying the petitioner by mail.

(Emphasis added.) Because Taxpayer's file and appeal letter provide adequate information for resolution of this case, we have exercised our discretion to not grant a hearing in this matter

"Interstate commerce" has been described as:

Traffic, intercourse, commercial trading, or the transportation of persons or property between or among the several states of the Union, or from or between points in one state and points in another state; commerce between two states, or between places lying in different states.

(Black's Law Dictionary, West Publishing Co., Revised Fourth Ed. (1968), citations omitted.)

Rule 193D explains the extent of the exemption from state tax for those engaged in interstate (and/or foreign) commerce. It explains the tax consequences of those providing services ancillary and in support of such commerce, although not directly engaged in interstate commerce. As noted above by Taxpayer, Rule 193D also directs taxpayers doing business in more than one state, although not engaged in interstate commerce, to Rule 194, which provides:

Persons domiciled in and having a place of business in this state, who (1) sell or lease personal property to buyers or lessees outside this state, or (2) perform construction or installation contracts outside this state, or (3) render services to others outside this state, are doing business both inside and outside this state. Whether or not such persons are subject to business tax under the law depends upon the kind of business and the manner in which it is transacted. The following general principles govern in determining tax liability or tax immunity.

. . . When the business involves a transaction taxable under the classification service and other business activities, the tax does not apply upon any part of the gross income received for services incidentally rendered to persons in this state by a person who does not maintain a place of business in this state and who is not domiciled herein. However, the tax applies upon the income received for services incidentally rendered to persons outside this state by a person domiciled herein who does not maintain a place of business within the jurisdiction of the place of domicile of the person to whom the service is rendered.

Rule 194 emphasizes the necessity of maintaining an out-of-state place of business (a nexus contact) when the services rendered out-of-state might otherwise be deemed "incidental," such that they would not provide taxing nexus to the out-of-state jurisdiction. If a taxpayer's activities performed out-of-state are more than "incidental," and if benefits derived by a customer are the direct result of these out-of-state activities, the taxpayer's gross receipts are properly subject to apportionment. See Det. No. 89-553, 9 WTD 039 (1989); Det. No. 93-132, 13 WTD 271 (1993).

[1] Taxpayer's activity of providing monitoring services to its out-of-state customers does not fall within the description of "interstate commerce." Although the services provided by Taxpayer to its out-of-state customers are performed both in and out-of-state, these services do not constitute commercial trading or the transportation of persons or property across state lines. Although alarm signals to Taxpayer's monitoring facility in Washington are carried by telephone lines across state lines, the telephone companies providing such services, and not Taxpayer, are the interstate carriers exempt from tax under Rule 193D. Taxpayer, therefore, is not entitled to an "interstate commerce" deduction from the B&O tax for its monitoring activities.

Taxpayer's monitoring activity takes place in Washington and is properly taxable by this state, even though the customers might be located outside the state. The B&O tax is a tax on business activities conducted within this state.

Taxpayer's arguments that it owns the computer chips necessary to receive and send alarm telephone signals, and that these chips are located on its out-of-state customers' premises, do not entitle Taxpayer to an interstate commerce exemption. These arguments, however, do imply that Taxpayer installs and/or maintains alarm equipment at these out-of-state customer locations. Such an out-of-state installation/maintenance activity, being more than "incidental," is not properly taxable by this state. As the Audit report indicates, apportionment would be appropriate.

Because Taxpayer has not provided Audit with data on gross income or costs relevant to gross receipts and costs related to its out-of-state customers and activities, gross receipts were merely projected without the benefit of apportionment. [In the disposition of this determination, Taxpayer is given the opportunity to provide this data.] Thus, taxes were assessed on estimated amounts in accordance with WAC 458-20-254, which allow estimates based on the best data available. Absent Taxpayer's provision of suitable records, the assessment may not be disputed under RCW 82.32.070(1)(a), which provides:

Any person who fails to comply with the requirements of this section shall be forever barred from questioning, in any court action or proceedings, the correctness of any assessment of taxes made by the department of revenue based upon any period for which such books, records, and invoices have not been so kept and preserved.

DECISION AND DISPOSITION:

Taxpayer's petition is denied. Taxpayer will have 30 days to provide Audit with records concerning its gross receipts and costs relative to the monitoring of its out-of-state customers' alarm systems. If such records are provided, Audit will issue an amended assessment, payment of which will be due on the date contained thereon. Absent the provision of such records, Document No. FY. . . in the amount of . . ., plus extension interest of . . ., for a total of . . . is due for payment by August 20, 1999.

DATED this 20th day of July 1999.