

Cite as Det. No. 20-0128, 41 WTD 100 (2022)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of)	<u>D E T E R M I N A T I O N</u>
Assessment of)	
)	No. 20-0128
)	
...)	Registration No. . . .
)	

[1] WAC 458-20-193; RCW 82.04.067(1)(c)(iii): B&O TAX – WHOLESALING – SUBSTANTIAL NEXUS – SOURCING. For a seller of goods to be liable for B&O tax, (1) the seller must have nexus in Washington, and (2) the sale must occur in, or be “sourced” to, Washington. A sale is properly sourced to Washington where third-party carriers pick up the sold goods from the seller outside of Washington and deliver those goods to customers in Washington.

[2] WAC 458-20-228; RCW 82.32.105; RCW 82.32.090: WAIVER OR CANCELLATION OF PENALTIES – CIRCUMSTANCES BEYOND THE TAXPAYER’S CONTROL – LACK OF KNOWLEDGE. A taxpayer’s lack of knowledge of its tax liability is not a circumstance beyond its control, and does not allow for the waiver or cancellation of penalties.

[3] WAC 458-20-228; RCW 82.32.105: WAIVER OR CANCELLATION OF INTEREST. The Department may only waive or cancel interest in two limited circumstances: (1) The failure to timely pay the tax was the direct result of written instructions given to the taxpayer by the Department; or (2) the extension of a due date for payment of an assessment of deficiency was not at the request of the taxpayer and was for the sole convenience of the Department.

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.

Roberts, T.R.O. – An out-of-state wholesaler protests an assessment of business and occupation tax. The wholesaler argues that it did not have nexus sufficient for Washington to assert tax on its business. We deny the petition.¹

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

ISSUES

1. Whether, under RCW 82.04.067(1)(c)(iii) and WAC 458-20-193(104) (“Rule 193(104)”), Taxpayer met the economic threshold for substantial nexus with Washington where third-party carriers picked up the sold goods from Taxpayer outside of Washington and delivered those goods to customers in Washington.
2. Whether, under RCW 82.32.105 and WAC 458-20-228 (“Rule 228”), Taxpayer demonstrated any circumstance entitling it to a waiver or cancellation of penalties.
3. Whether, under RCW 82.32.105 and Rule 228, Taxpayer demonstrated any circumstance entitling it to a waiver or cancellation of interest.

FINDINGS OF FACT

... (“Taxpayer”), is a wholesaler of [tangible personal property] and is headquartered [out of state]. Taxpayer sells its goods to third-party wholesalers in Washington.

In 2018, the Department of Revenue’s Compliance Division (“Compliance”) conducted an investigation of Taxpayer’s business activities in Washington, and mailed a Washington State Business Activities Questionnaire to Taxpayer. Based upon Taxpayer’s completed Questionnaire . . . , Compliance determined that Taxpayer had exceeded the economic nexus thresholds for wholesaling in the year 2017.

In April 2019, Compliance notified Taxpayer that it was under audit for the period of January 1, 2017, through December 31, 2018 (“Tax Period”), and asked Taxpayer to complete a business license application and a sales data form, which requested revenue figures for the period of January 1, 2017, through December 31, 2018.

On May 15, 2019, Taxpayer submitted a completed business license application to Compliance and became registered to do business in Washington. Taxpayer also provided the completed sales data form, which indicated that Taxpayer made total gross wholesale income attributable to Washington in the amounts of \$. . . in 2017 and \$. . . in 2018.

Thus, Compliance determined that Taxpayer had met economic nexus thresholds for wholesaling business and occupation (“B&O”) tax during the Tax Period because (1) Taxpayer made sales and delivered goods via common carrier to retailers in Washington for resale; and (2) Taxpayer exceeded the gross receipts threshold for wholesaling.

On July 10, 2019, Compliance completed its audit and issued a tax assessment against Taxpayer in the amount of \$. . . for wholesaling B&O tax, penalties, and interest due.²

On August 6, 2019, Taxpayer submitted a Review Petition with the Department, contesting the entirety of the assessment. Taxpayer asserts that the sales data previously submitted to Compliance

² The \$. . . tax assessment is composed of \$. . . in wholesaling B&O tax, an \$. . . delinquency penalty, a \$. . . assessment penalty, a \$. . . unregistered business penalty, and \$. . . in interest.

included “gross amounts . . . purely based on goods shipped to WA State regardless of the sales arrangement with customers or shipping/freight terms.” *Petition*, p. 1. Taxpayer alleges that because of these different sales arrangements, certain sales should not be sourced to Washington and that Taxpayer’s gross revenue attributable to Washington should thereby be reduced to below the economic nexus thresholds for the Tax Period.

Specifically, Taxpayer identifies three different sales arrangements under which the ownership of the sold goods should be deemed transferred at an out-of-state warehouse and thus not be considered a Washington sale:

1. **“Pick Up” Sales Arrangements:** Taxpayer describes these arrangements as “[Free on Board (“FOB”) shipping] paid by customers and customers [who] pick up goods from each of Taxpayer’s [out-of-state] warehouses. Because customers use third party common carriers, [Taxpayer] indicates delivery location in WA State only for information purposes.” *Petition*, p. 2.
2. **“Third Party” Sales Arrangements:** Taxpayer describes these arrangements as “Goods shipped from [Taxpayer’s out-of-state] warehouses under which shipping & freight costs is directly charged to customers’ account with third-party carriers designated by customers, and goods are delivered to a WA State location under the customers’ delivery instructions.” *Id.*
3. **“Collect” Sales Arrangements:** Taxpayer describes these arrangements as “[C]ustomers paid all shipping & freight costs and goods are delivered to WA State locations specifically designated and instructed by the customers [A]ll sales negotiation, price decision, and sales terms were set by [the customer’s and Taxpayer’s out-of-state offices]. Only goods are delivered to a WA distribution center designated by [customer’s] delivery instruction.” *Id.*

ANALYSIS

1. Economic Threshold for Substantial Nexus

Washington imposes a B&O tax on “every person that has a substantial nexus” with Washington “for the act or privilege of engaging in business” in this state. RCW 82.04.220(1). “[T]he legislative purpose behind the B&O tax scheme is to tax virtually all business activity in the state.” *Impehoven v. Dep’t of Revenue*, 120 Wn.2d 357, 363, 841 P.2d 752 (1992); *see also Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971). Thus, in general, all business activity is subject to B&O tax unless some specific exemption applies. The applicable B&O tax rate is determined by a taxpayer’s specific business activity. *See generally* Chapter 82.04 RCW.

Here, Taxpayer does not dispute that, to the extent its sales of electronic home appliances are taxable in Washington, such sales are properly classified under the Wholesaling B&O Tax Classification pursuant to RCW 82.04.270. Rather, Taxpayer challenges whether it established the substantial nexus with Washington required in order to be subject to the wholesaling B&O tax.

Rule 193 provides, “In general, Washington imposes its B&O [tax] on the sales of tangible personal property if the seller has nexus in Washington and the sale occurs in Washington.” Specific to wholesale sales, Rule 193(103)(b) states that “[a] person that makes wholesale sales of tangible personal property and has nexus with Washington . . . is subject to B&O tax on that person’s wholesale sales **sourced** to Washington.” (Emphasis added.) Thus, Rule 193 makes clear that for a particular seller of goods to be liable for B&O tax, (1) the seller must have nexus in Washington, and (2) the sale must occur in, or be “sourced” to, Washington.

RCW 82.04.067 provides that an out-of-state wholesaler establishes substantial nexus with Washington based on its economic presence where the wholesaler’s receipts from sales in Washington exceed a specified threshold in the current or immediately preceding calendar year. [RCW 82.04.067(4)(c) (economic nexus thresholds apply to “persons taxable under RCW 82.04.0270” (wholesalers));] RCW 82.04.067(1)(c)(iii). Pursuant to RCW 82.04.067(5), the Department is required to annually review and adjust the economic threshold to reflect inflation. For the years at issue here, the economic thresholds for an out-of-state business are \$267,000 for the year 2017 and \$285,000 for the year 2018. ETA 3195.2018.

Washington defines “sale” as “any transfer of the ownership of, title to, or **possession of property** for a valuable consideration . . .” RCW 82.04.040(1) (emphasis added). WAC 458-20-103 (Rule 103) further defines the place of sale:

For the purpose of determining tax liability of persons selling tangible personal property, a sale takes place in this state when the goods sold are delivered to the buyer in this state, **irrespective of whether title to the goods passes to the buyer at a point within or without this state.**

Rule 103 (emphasis added).

A taxpayer with substantial nexus in Washington is subject to B&O tax on wholesale sales “sourced” to Washington. Rule 193(103)(b). [Gross proceeds from wholesale sales taxed under RCW 82.04.270 are sourced according to RCW 82.32.730. RCW 82.04.067(4)(c).] RCW 82.32.730(1) provides two general rules for “sourcing” sales. First, when tangible personal property “is **received** by the purchaser at a business location of the seller, the sale is sourced to that business location.” RCW 82.32.730(1)(a) (emphasis added). *See also* Rule 193(203)(a). Second, when tangible personal property “is not **received** by the purchaser at a business location of the seller, the sale is sourced to the location where receipt by the purchaser . . . occurs.” RCW 82.32.730(1)(b) (emphasis added). *See also* Rule 193(203)(b).

RCW 82.32.730(9)(f) defines “receive” or “receipt” as “taking possession of tangible personal property.” Rule 193(202)(a) defines those terms further as meaning “the purchaser first either taking physical possession of, or having dominion and control over, tangible personal property.” RCW 82.32.730(9)(f) specifically states that receipt **does not** include “possession by a shipping company on behalf of the purchaser.” *See also* Rule 193(202)(b)(i); Det. No. 15-0281, 36 WTD 28 (2017). According to Rule 193(202)(b)(ii), a shipping company is defined as a “separate legal entity that ships, transports, or delivers tangible personal property on behalf of another, such as a

common carrier, contract carrier, or private carrier either affiliated or unaffiliated with the seller or purchaser.”

Rule 193(203)(a) contains two relevant examples, as follows:

Example 3. An out-of-state purchaser sends its own trucks to Washington to receive goods at a Washington-based seller and to immediately transport the goods to the purchaser's out-of-state location. The sale occurs in Washington because the purchaser receives the goods in Washington. The sale is subject to B&O and retail sales tax.

Example 4. The same purchaser in Example 3 uses a wholly owned affiliated shipping company (a legal entity separate from the purchaser) to pick up the goods in Washington and deliver them to the purchaser's out-of-state location. Because “receive” and “receipt” do not include possession by the shipping company, the purchaser receives the goods when the goods arrive at the purchaser's out-of-state location and not when the shipping company takes possession of the goods in Washington. The sale is not subject to B&O tax or retail sales tax.

Here, Compliance found that Taxpayer had receipts attributed to Washington that were significantly higher than the economic thresholds, and, thus, Taxpayer established substantial nexus in Washington pursuant to the economic threshold under RCW 82.04.067(1)(c)(iii). However, Taxpayer argues its sales and delivery arrangements with Washington customers exclude the majority of sales from being sourced to Washington, and that the remaining sales correctly sourced to Washington are insufficient to trigger substantial economic nexus.

In each of Taxpayer’s three described sales arrangements (“Pick Up,” “Third Party,” and “Collect”), Taxpayer indicates that it was a third-party common carrier that picked up the customer’s purchased goods at Taxpayer’s out-of-state location and delivered it to the customer in Washington. As such, the customers could not have “received” the goods at Taxpayer’s out-of-state location. Instead, the goods were received at the customers’ locations in Washington. This is consistent with Example 4 in Rule 193(203)(a), in which an affiliated shipping company picked up goods at the seller’s location in Washington and delivered them out of state, and instead of “receipt” occurring in Washington where the shipping company picked up the goods, “receipt” occurred out-of-state, where delivery to the customer occurred.

While in both the “Pick Up” and “Third Party” sales arrangements, Taxpayer argues that ownership of the goods was transferred from Taxpayer to the customer at the time the “third-party common carrier” picked up the goods at Taxpayer’s out-of-state locations, this fact is irrelevant to where the goods are “received” for taxation purposes. *See* Rule 103; Det. No. 14-0383, 34 WTD 265 (2015) (“However, where legal title to goods passes is not determinative of whether delivery has occurred in Washington under Rule 193.”); *see also* Rule 193(203)(b)(iii) (“Commercial law delivery terms, and the Uniform Commercial Code’s provisions defining sale or where risk of loss passes, do not determine where the place of receipt occurs.”); *Lamtec Corp. v. Dept. of Revenue*, 151 Wn. App. 451, 460, 215 P.2d 968 (2009), *aff’d*, 170 Wn.2d 838, 346 P.3d 788 (2011) (holding that “the UCC provisions regarding ownership or the passage of title of goods do not determine

whether Washington's B&O tax applies”). Simply because the goods are shipped FOB outside of Washington does not mean the goods are not received in Washington.

Taxpayer’s customers took actual physical possession of the goods in Washington, regardless of whether [the goods were] delivered to them via a third-party common carrier.[³] On this basis, we conclude that the goods at issue, based on the record before us, and consistent with Rule 103 and Rule 193, were received at locations in Washington. Accordingly, the sales were properly sourced to Washington.

2. Waiver of Penalties

Legal Basis for Imposition of Penalties

RCW 82.32.090(1) requires the Department to impose the delinquent penalty for the late payment of taxes as follows:

If payment is not received by the . . .	Then the Department must assess a total delinquent penalty of . . .
Due date	9% penalty on the amount of the tax
Last day of the month following the due date	19% penalty on the amount of the tax
Last day of the second month following the due date	29% penalty on the amount of the tax

In addition, pursuant to RCW 82.32.090(2), if the Department concludes that any tax has been substantially underpaid, there is assessed an assessment penalty of 5% of the amount of the tax determined to be due. *Substantially underpaid* means that (1) the taxpayer has paid less than 80% of the amount of tax determined by the Department to be due for all taxes included in the Department’s examination, and (2) the amount of underpayment is at least one thousand dollars. *Id.*

Further, if the Department finds that a business has engaged in any taxable activity without first obtaining a registration certificate from the Department under RCW 82.32.030, the Department must impose an unregistered business penalty of 5% of the amount of tax due from that business for the period that the business was not properly registered. RCW 82.32.090(4).

Taxpayer did not pay the tax liabilities that arose from its Washington business activities, beginning January 1, 2017, through December 31, 2018, because it was unaware of its reporting responsibilities. Since Taxpayer did not pay its tax liabilities when they arose, the Department was obligated to assess delinquent⁴ and assessment⁵ penalties on this liability. Because Taxpayer had

³ [Taxpayer did not provide any evidence that showed its customers took dominion and control of the goods outside of Washington before taking physical possession.]

⁴ The Department assessed a 29% delinquent penalty on Taxpayer’s tax liability.

⁵ Since Taxpayer failed to pay any portion of the tax liability when it became due, and the amount of the underpayment was over \$1,000, Taxpayer substantially underpaid the tax liability.

not voluntarily registered the business prior to being contacted by the Department to do so in April 2019, the Department was obligated to assess the unregistered business penalty.

Legal Basis for Waiver of Penalties

The Department has limited authority to waive or cancel penalties. RCW 82.32.105. With regard to the penalties at issue here, the Department may cancel the penalties where the act leading to the imposition of the penalties, i.e., delinquent payment, failure to register business, etc., are “the result of circumstances beyond the control of the taxpayer.” RCW 82.32.105(1); RCW 82.32.090(2). Rule 228(9)(a)(ii) explains that “[c]ircumstances beyond the control of the taxpayer are generally those which are immediate, unexpected, or in the nature of an emergency. Such circumstances result in the taxpayer not having reasonable time or opportunity to obtain an extension of the due date or otherwise timely file and pay.” The circumstances must directly cause the act leading to the imposition of the penalties. *Id.*

Rule 228(9)(a)(ii) lists examples of circumstances that are generally considered to be sufficiently beyond a taxpayer’s control such as to cancel penalties. Such circumstances include erroneous written information from the Department; emergency circumstances around the time of the due date, such as the death or serious illness of the taxpayer; destruction of the business or records by fire or other casualty; or an act of fraud or conversion by the taxpayer’s employee, which the taxpayer could not immediately detect or prevent. *Id.*

Rule 228(9)(a)(iii) also lists examples of situations that are generally *not* considered beyond the control of a taxpayer. These include financial hardship; a misunderstanding or lack of knowledge of a tax liability; or mistakes or misconduct on the part of employees or other persons contracted with the taxpayer. *Id.*

The second basis for waiving penalties is only available in the case of a delinquent penalty under RCW 82.32.090(1). In such a case, RCW 82.32.105(2) requires the Department to waive or cancel the delinquent penalty upon request if the taxpayer has a 24-month record of timely filing and payment. Specifically, the Department must grant a taxpayer’s request for waiver of such a delinquent penalty if “[t]he taxpayer has timely filed and remitted payment on all tax returns due for that tax program for a period of twenty-four months immediately preceding the period covered by the return for which the waiver is being requested.” RCW 82.32.105(2)(b). *See also* WAC 458-20-228(9)(b).

However, the Department only applies the above waiver to the following situation:

If a taxpayer has obtained a tax registration endorsement with the department prior to engaging in business within the state and has engaged in business activities for a period less than twenty-four months, the taxpayer is eligible for the waiver if the taxpayer had no delinquent tax returns for periods prior to the period covered by the return for which the waiver is being requested. . . . This is the only situation under which the department will consider a waiver when the taxpayer has not timely filed and paid tax returns covering an immediately preceding twenty-four month period.

WAC 458-20-228(9)(b)(i)(B) (emphasis added).

Taxpayer has not shown a circumstance beyond its control to be entitled to a waiver of the penalties. The primary reason Taxpayer provided for its failure to timely pay the taxes was that it did not know about the tax liability because it was unaware that it had established nexus in the state of Washington. However, lack of knowledge of a tax liability is not a circumstance beyond a taxpayer's control. Rule 228(9)(a)(iii)(B). Because of the nature of Washington's tax system, the burden of becoming informed about tax liability falls upon the taxpayer, and it is the taxpayer who bears the consequences of a failure to be correctly informed. Det. No. 01-165R, 22 WTD 11 (2003). Taxpayers are responsible to know their tax reporting obligations, and when they are uncertain about their obligations, to seek instructions from the Department. RCW 82.32A.030(2); *see also* Det. No. 01-165R, 22 WTD 11 (2003).

Nor is Taxpayer entitled to a waiver of the delinquent payment penalty under the twenty-four month payment history provision. The Department cannot waive the delinquent penalty assessed under the 24-month provision because Taxpayer had not obtained a tax registration endorsement with the Department until May 2019, which was after Taxpayer started conducting business in this state.

We hold that Taxpayer does not qualify for a waiver of delinquent penalties, the substantial underpayment penalty, or the unregistered business penalty under either of the avenues available under RCW 82.32.105.

3. Waiver of Interest.

Regarding the interest assessed, the Department may only waive or cancel interest in two limited circumstances: (1) The failure to timely pay the tax was the direct result of written instructions given to the taxpayer by the Department; or (2) the extension of a due date for payment of an assessment of deficiency was not at the request of the taxpayer and was for the sole convenience of the Department. RCW 82.32.105(3); Rule 228(10).

These limited circumstances were not present in Taxpayer's case. As such, there is no basis to waive the assessed interest.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 5th day of May 2020.