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BEFORE THE INTERPRETATION AND APPEALS SECTION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Request for Ruling of Tax Liability of . . .	D E T E R M I N A T I O N No. 86-267 Registration No. . . .

[1] **Rule 146 - RCW 82.04.080 - RCW 82.04.290** - MEASURE OF TAX --EVIDENCES OF INDEBTEDNESS -- ASSIGNMENT -- LOAN. The assignment of the right to receive payments on a loan by the originating bank constitutes trading in evidences of indebtedness such that B&O tax applies only to gains realized in such a sale, as where the consideration for the assignment exceeds the face amount of the loan.

[2] **Rule 146 -- RCW 82.04.290 --** ASSIGNMENT -- LOAN. Where a bank pursuant to written contract assigns the right to receive payments on a loan and does not thereafter book any interest income but continues to collect loan payments and remit them to the assignee, the bank is not subject to B&O tax on interest on the loans following such assignment; however, Service and Other Activities B&O tax is due on fees charged for servicing loans.

[3] **Rule 194 - Rule 146 - RCW 82.04.290 - RCW 82.04.260.** NEXUS. Person with no place of business or employees and engaging in no business activities in this state is not taxable with respect to interest on loan payments the right to which was purchased from a Washington bank, despite the presence of the buyers and loan collateral in this state.

These 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: . . .

NATURE OF ACTION:

The taxpayer has requested a written opinion and ruling of tax liability in respect to a transaction in which a Washington branch of a foreign bank will sell its entire loan portfolio to an out-of-state affiliate with no business presence in Washington and continue to service the loans for a fee.

FACTS:

Ronald J. Rosenbloom, Administrative Law Judge -- The taxpayer's letter of August 13, 1986, explains the transaction as follows: The taxpayer, the Seattle branch of a . . . bank, will transfer its loan portfolio to a separate but related corporation (the "affiliate"). The taxpayer is a . . . corporation and the affiliate is a Delaware corporation. The affiliate has no offices or employees in Washington and engages in no business activities here.

The taxpayer has been engaged in the business of making loans to Washington borrowers and occasionally to out-of-state borrowers. These loans are commercial loans carrying either fixed or variable rates. The face amount (book carrying value) of the fixed-rate loans may vary from their fair market value because of fluctuations in market interest rates, while the face amount of the variable loans will normally equal their fair market value.

For business reasons, the parties plan to sell the entire loan portfolio, subject to the taxpayer's debt,[1] to the affiliate. The sales price will be the book carrying value of the portfolio, which is the face amount of the loans. The transfer will be accomplished by a written contract of sale between the taxpayer and the affiliate. The loan documents will not be physically endorsed to the affiliate since they

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[1] The taxpayer incurred this debt when it borrowed money, usually from its out-of-state branches, to fund the loans to its borrowers. The affiliate will assume the liability for this debt under the terms of the sale.

are not negotiable instruments. After the sale, the taxpayer will service the loans by making collections from the borrower and remitting payments to the affiliates. (The taxpayer will also initiate new loans, which it will sell to the affiliate and continue to service.) For these services, the taxpayer will be paid fees but will not earn or book any interest income.

ISSUES:

Based on the foregoing facts, the taxpayer requests a ruling on tax liability as to the following:

I. What is the measure of the business and occupation tax due on the sale of the loan portfolio by the taxpayer to its affiliate?

II. Will the taxpayer continue to be liable for business and occupation tax on interest received on the loans following the sale of the loan portfolio to its affiliate?

III. Will the affiliate be liable for business and occupation tax on interest received on the loans after purchasing the loan portfolio from the taxpayer?

TAXPAYER'S POSITION:

I. The taxpayer asserts that the business and occupation tax on the sale of a loan portfolio should be measured by the excess of the sales price over the book carrying value, and not the gross sales price. Since the loans at issue are being sold at their book value, the taxpayer would realize no gain on the transaction and therefore will not incur any business and occupation tax liability in respect to the sale.

II. The taxpayer asserts that it should not have any continuing business and occupation tax liability in respect to interest on the loans following the sale of the loan portfolio to the affiliate. The taxpayer will not own the loans after having transferred them to its affiliate and will not be legally entitled to keep the interest it collects from borrowers. Therefore, the taxpayer should be treated as a mere conduit in collecting interest for its affiliate. (The taxpayer concedes that the fees it charges for servicing the loans will be subject to tax.)

III. The taxpayer asserts that the affiliate should have no business and occupation tax liability in respect to interest on the loans, despite the presence of the borrowers and loan collateral in Washington, because the affiliate has no employees or places of business in this state, and engages in no business activities here.

DISCUSSION:

I. The assignment for a consideration of the right to receive payments on a loan is a sale of an intangible. The selling of intangible assets is a business activity which does not fall within any of the specific business and occupation tax classifications enumerated in Chapter 82.04 RCW. Accordingly, it is taxable under the Service and Other Activities classification measured by the gross income of the business. RCW 82.04.290.

RCW 82.04.080 defines the term "gross income of the business" as:

> the 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, gains realized from trading in stocks, bonds, or other evidences of indebtedness, 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.

[1] The assignment of the right to receive payments on a loan by the originating bank constitutes trading in evidences of indebtedness. Thus, if the taxpayer were to sell the loans for more than their face amount, then there would be "gains realized" from such trading in evidences of indebtedness. However, if the loans are sold for their face amount as the taxpayer proposes, we agree that no business and occupation tax liability will be incurred.

II. If the taxpayer services the loans following their assignment, it will technically receive "interest," which is specifically included within the definition of gross income of the business.

[2] However, there will be a written contract of sale wherein the right to receive payments on the loans will be assigned to the affiliate, and the taxpayer will no longer book any interest income. In short, the taxpayer will be a mere conduit in collecting loan payments and remitting them to the affiliate. Under these circumstances, we agree that the taxpayer will have no continuing business and occupation tax liability in respect to interest on the loans following the sale of the loan portfolio. Of course, amounts received as fees for servicing the loans, as well as amounts received as fees for originating and servicing new loans, will be subject to business and occupation tax under the Service and Other Activities classification.

III. Finally, we agree that the taxpayer's affiliate will have no business and occupation tax liability in respect to interest on the loans.

[3] The affiliate has no place of business or employees in this state, nor does it engage in any business activities here. The affiliate does not come within the taxing jurisdiction of the state merely by purchasing the right to receive loan payments, despite the presence of the borrowers and loan collateral in Washington.

This legal opinion may be relied upon for reporting purposes and as support of the reporting method in the event of an audit. This ruling is issued pursuant to WAC 458-20-100(18) and is based upon only the facts that were disclosed by the taxpayer. In this regard, the Department has no obligation to ascertain whether the facts disclosed are actually true. This legal opinion shall bind this taxpayer and the Department upon these facts. However, it shall not be binding if there are relevant facts which are in existence but have not been disclosed at the time this opinion was issued; if, subsequently, the disclosed facts are ultimately determined to be false; or if the facts as disclosed subsequently changes and no new opinion has been issued which takes into consideration those changes. This opinion may be rescinded or revoked in the future, however, any such rescission or revocation shall not affect prior liability and shall have a prospective application only.

DATED this 10th day of October 1986.