Cite as 1 WTD 103 (1986)

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

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. 86-234
. . .	)	Registration No. . . .
	)	Tax Assessment Nos. . .

[1] **RULE 111** -- ADVANCES/REIMBURSEMENTS -- PAYMASTER -- EMPLOYER/EMPLOYEE -- DETERMINATION. Where a taxpayer's affiliate is the actual employer and the taxpayer's sole function is to act as a paymaster for the affiliate's employees, the taxpayer is a mere conduit for payment of the affiliate's payroll expense and amounts received for that purpose constitute nontaxable reimbursements.

This headnote is provided as a convenience for the reader and is 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: . . . , President
. . . , Bookkeeper

DATE OF HEARING: January 15, 1986.

NATURE OF ACTION:

An examination of the taxpayer's account for the period February 27, 1980 through June 30, 1985 resulted in the assessment of Service and Other Activities business and occupation tax on amounts derived from the taxpayer's affiliates. The auditor characterized these amounts as charges for management and personnel services rendered to the affiliates by employees of the taxpayer. The taxpayer maintains that the employees in question are in fact employed

by the affiliates and that the taxpayer merely serves as a common paymaster for its affiliates.

FACTS:

Ronald J. Rosenbloom, Administrative Law Judge --The taxpayer provides a payrolling function for three corporate affiliates. The taxpayer is the employer of record for federal income tax and social security purposes as well as for state employment security and labor and industries purposes. The employees in question perform all activities of the affiliated corporations, none of which have any employees of their own. The taxpayer's sole business activity is paying these employees, for which it receives dollar-for-dollar reimbursement from its affiliates. Though there are three corporate affiliates, only one is engaged in any substantial business activity. The auditor's report confirms that this affiliate has been billed for 99% of all wages paid to the employees.

The one affiliate actively engaged in business (hereinafter referred to as the affiliate) is a securities broker/dealer registered with the National Association of Securities Dealers (NASD). The NASD requires its members to maintain a certain minimum net worth. This affiliate determined that it could more easily meet this net worth requirement by creating a separate corporation (the taxpayer) to handle its payrolling functions. The affiliate believed in so doing that it could relieve itself of any personal liability for paying its payroll expense, thereby increasing its net worth.

The affiliate's plan did not work. The outside auditor who provides the affiliate with audited financial statements for filing with the NASD took the position that the affiliate was obligated for the payroll expense and that the taxpayer was merely an escrow agent for satisfying this obligation. The outside auditor concluded that the payroll expense must be shown as a liability of the affiliate on its audited financial statements.

TAXPAYER'S EXCEPTIONS:

The taxpayer asserts that no tax is due on the amounts received from its affiliate as reimbursement for payroll expenses.

DISCUSSION:

To determine whether the tax is due, it is necessary to decide who in fact is the employer of the employees in question. If the taxpayer is the employer, then the taxpayer is rendering services to the affiliate by providing loaned servants for the conduct of the affiliate's business. Amounts received from the affiliate in return would be subject to Service and Other Activities B&O tax. Valley Cement Construction, Inc. v. Department of Revenue, Docket No. 71-70 (1973).

[1] On the other hand, if the affiliate is the employer and the taxpayer's sole function is to act as a paymaster, then the taxpayer is merely a conduit for payment of the affiliate's own payroll expenses and amounts received for that purpose are nontaxable reimbursements (see WAC 458-20-111).

The taxpayer represents itself as the employer to certain state and federal agencies. This raises a presumption that the taxpayer is the employer (see Valley Cement Construction, Inc. v. Department of Revenue, supra). This presumption is not conclusive, however. If the affiliate is the actual employer, then the taxpayer will not be treated as the employer merely because it reports itself to state and federal agencies as such.

A key consideration in determining who was the actual employer rests with an analysis of who controlled or had the right to control the activities of the employees. The element of control includes the right to hire, fire, and supervise the physical performance of the individual employees. This analysis is not very helpful in the present case since the same individual who owns all of the shares of stock of the affiliate also owns two-thirds of the shares of stock of the taxpayer.

Despite this we are satisfied that the taxpayer was organized solely to provide a payrolling function for its affiliate's employees. The taxpayer has no other business activity. Furthermore, an outside audit of the affiliate found that the payroll expense for the employees in question was a liability of the affiliate. While these audit findings are not binding on the Department, they certainly lend credence to the taxpayer's assertion that the employees are in fact employees of the affiliate. Finally, the taxpayer's bookkeeper testified it is her understanding that she actually works for the affiliate and is only nominally an employee of the taxpayer. Under these circumstances we conclude that the employees in question are actually employed by the affiliate.

We conclude that the affiliate is the actual employer and the taxpayer's sole function is to act as a paymaster. The taxpayer is merely a conduit for payment of the affiliate's own payroll expenses and amounts received for this purpose constitute nontaxable reimbursements. There is no business activity or gross income of the business upon which the business and occupation tax can be imposed.

DECISION AND DISPOSITION:

The taxpayer's petition for correction is granted. The Audit Section will issue amended assessments.

DATED this 29th day of August 1986.