

Cite as 1 WTD 219 (1986)

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

In the Matter of the Petition for) D E T E R M I N A T I O
N
Refund of))
) No. 86-260
)
 . . .) Registration No. . . .
) Tax Assessment No. . .
 .)
)

[1] **RULE 164; RCW 82.04.280(5):** B & O TAX -- MANAGING
GENERAL AGENT. The income received by one who is
licensed as a resident general agent by the
insurance commissioner and who performs the
independent management functions set forth in WAC
458-20-164 is subject to business and occupation (B
& O) tax at the special rate provided by RCW
82.04.280(5) for managing general agents.

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: . . .

DATE OF HEARING: September 4, 1986

NATURE OF ACTION:

The taxpayer petitions for a refund of tax paid and assessed
under the service and insurance agents categories and a ruling
that its income should all be taxed under one rate, as a
Managing General Agent as provided by RCW 82.04.280(5).

FACTS AND ISSUES:

Anne Frankel, Administrative Law Judge -- The taxpayer registered its business in Washington in 1976 as a general insurance agent, both casualty and property. In 1978, the president of the company at that time wrote the Department requesting a refund of excise taxes paid under the wrong rate. He stated he had been advised the income should be reported under the rate specified for independent resident managing general agents. He enclosed copies of the company's General Agents licenses and signed forms from insurance companies indicating the company's appointment as a general agent.

The Department reviewed the company's records and granted the taxpayer's request for a refund. The Department concluded that the company should report its income on Line (1) of the excise tax return, indicating "Income for Insurance Managing General Agent" taxable under RCW 82.04.280(5). A copy of WAC 458-20-164 (Rule 164) was attached to the letter granting the refund. (Letter from Arnold T. Jarvinen 12/5/78.) The taxpayer's returns were adjusted at that time as the returns showed a deduction from gross income for payments made to other agents. The following language from Rule 164 was relied on:

The term "Gross Income of the Business" includes gross income from commissions, fees or other emoluments however designated which the agent, broker, or solicitor receives or becomes entitled to receive No deduction is allowed for commissions, fees, or salaries paid to other agents, brokers, or solicitors nor for other expenses of doing business.

The taxpayer reported its income under the general agent category as instructed.

The taxpayer's books and records were subsequently examined for the period January 1, 1982 through December 31, 1985. The auditor determined the tax on the income from the taxpayer's "fee account" should have been computed under the Service and Other Activities rate for periods prior to July 1, 1983, and at the special rate for insurance agents after that date.

The income from the fee account was reclassified and Assessment No. . . . was issued on March 27, 1986. The assessment also included use tax on consumable supplies which the taxpayer purchased without paying retail sales tax.

The taxpayer paid the assessment under protest. The taxpayer contends that RCW 82.04.280(5) provides that all income received by a Managing General Agent is taxed under one rate; thus the auditor should not have segregated the income from policy fees and taxed it under a separate rate. The taxpayer does not protest the assessment of use tax.

DISCUSSION:

In 1963, the Legislature provided a special B & O tax rate for independent residing managing general agents. The rate is set out in RCW 82.04.280 which states:

Upon every person engaging within this state in the business of:

. . . .

(5) representing and performing services for fire or casualty insurance companies as an independent resident managing general agent licensed under the provisions of RCW 48.05.310; . . .

RCW 48.04.310 provides:

(1) An insurer appointing any person as its general agent or manager to represent it as such in this state shall file notice of the appointment with the commissioner on forms prescribed and furnished by the commissioner.

(2) Any such general agent or manager shall have such authority, consistent with this code, as may be conferred by the insurer. A general agent resident in this state and licensed, as in this section provided, may exercise the powers conferred by this code upon agents licensed for the kinds of insurance which the general agent is authorized to transact for the insurer so appointing him.

(3) Any such general agent may accept applications for insurance from licensed agents who are not appointed by the insurer of such general agent where the risk involved is placed in a nonstandard or specialty market of an authorized insurer as defined by regulation of the commissioner. Such nonstandard or specialty business shall not be bound by any agent not appointed by the insurer. A general agent may supply such licensed, nonappointed agent with material to write nonstandard or specialty insurance

business including, but not limited to, applications for insurance, underwriting criteria, and rates. A general agent shall not provide any licensed, nonappointed agent with indicia of authority to bind an insurance risk and the general agent and nonappointed agent shall provide written disclaimers of binding authority to an applicant or prospective insured in such form as prescribed by the commissioner.

(4) The appointment of a resident general agent shall not be effective unless the person so appointed is licensed as the general agent of such insurer by the commissioner upon application and payment of the fee therefor as provided in RCW 48.14.010.

(5) Every such license shall expire as at close of business on the thirty-first day of March next following the date of issue, and may be renewed for an additional year upon application and payment of the fee therefor.

(6) The commissioner may deny, suspend, or revoke any such license for any cause specified in RCW 48.17.530 and in the manner provided in RCW 48.17.540.

After the special classification for general agents was added, the Department asked the Insurance Commissioner's office to help devise a rule which came within the language of the 1963 amendment. The Insurance Commissioner concluded that the bare fact of licensing under RCW 48.04.310 was not dispositive, as many licensed general agents performed no "managerial" functions for their insurers, but only sold or "produced" insurance. The Insurance Commissioner's office understood the rationale of the 1963 amendment was to reduce the tax disadvantages suffered by general agents who, as independent contractors, performed the same managerial functions for an insurer as an employee in a local branch office might perform.¹

¹In Armstrong v. State, 61 Wn.2d 116 (1962) the Washington Supreme Court upheld the imposition of the business and occupation tax on a general insurance agent. In that case, the taxpayer contended the B & O tax was unconstitutional because RCW 82.04.320 exempts branch offices of insurance companies from the tax. Arguably, the Legislature was responding to that decision when it added the special rate for general agents.

Based on the information it received from the Insurance Commissioner's office, the Department prepared a questionnaire to determine if an applicant qualified as a resident managing general agent of a fire or casualty insurance company and, therefore, was entitled to report the income earned as a resident managing general agent under the special rate. The instructions stated the applicants should fill out a separate questionnaire for each company for which the applicant claimed a general managing resident agency relationship, and send a copy of any written contract the general agent had with the insurance company. The questionnaire was to be signed by the applicant and an officer of the insurance company. The applicant was asked to state whether he or she performed the following functions:

1. Pay all sales and/or production expense, including salaries of special field representatives, underwriters and inspectors; office rent; supplies?
2. Bill all premiums?
3. Directly employ all selling agents under an agreement running between you and the agent?
4. Have final responsibility with respect to selecting risks and other underwriting matters?
5. Make all arrangements for reinsuring?
6. Handle claims adjustment directly with the insured either by your own staff or through an independent adjustment bureau?

The taxpayer's file indicates the questionnaire was filled out, indicating the taxpayer's status as a general agent when the refund request was granted in 1978. Rule 164 also states that a person claiming to fall within the special classification for a managing general agent must show he is licensed as a resident general agent and that he or she performs the independent manager functions listed in the questionnaire.

During the hearing, the taxpayer explained that its status as a general agent has not changed. It states it is a wholesaler only and does not sell to the public directly.

The problem in this case seems to be a misunderstanding of the facts.² The separate "fee account," which the auditor believed was income earned from underwriting policies, represents administrative fees earned from London carriers and other surplus lines. The fees are paid to the taxpayer for such functions as property inspections, printing forms, typing, obtaining motor vehicle records, telexing, etc.--typical "managerial" functions. We agree with the taxpayer, therefore, that the income from this account is properly subject to the rate specified in RCW 82.04.280(5). Only in those cases where a general agent, although licensed under RCW 48.05.310, does not meet the two-part test of Rule 164 is the income taxable under the special rate for insurance agent/broker commissions.

DECISION AND DISPOSITION:

The taxpayer's petition is granted. The tax . . . plus interest assessed based on a reclassification of its income reported under the Managing General Agent classification shall be refunded.

DATED this 26th day of September 1986.

²We believe the taxpayer's appeal could have been resolved at the audit level if the taxpayer had presented the facts relating to the "fee account" to the auditor. The administrative manager stated that she tried to call the auditor, but did not reach him and petitioned for a refund instead.