

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. 97-080
)	
. . .)	Registration No. . . .
)	FY. . ./Audit No. . . .
)	
)	

RCW 82.16.050(8); ETB 331: INTERSTATE COMMERCE INCOME DEDUCTION FOR FREIGHT FORWARDERS. Freight forwarders that have common carrier liability for their customers loss during shipping and that are contractually liable for the interstate transportation of goods qualify for the deduction of income derived from interstate commerce under RCW 82.16.050(8). ETB 331 is limited accordingly.

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:

The taxpayer appeals the Department of Revenue's determination that its activities are freight forwarding and not exclusively interstate transportation for the purposes of the income deduction allowed by RCW 82.16.050(8).¹

FACTS:

Munger, A.L.J. -- (The taxpayer) was audited by the Department of Revenue (the Department) for the period January, 1991 through December, 1994. An assessment for business and occupation (B&O) tax was issued. Prior to this audit, the taxpayer had not been

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

reporting taxable income in Washington based on its belief that its activities were not taxable as interstate transportation of goods under RCW 82.16.050(8).

The taxpayer has offices in Washington and Alaska. It provides a specialized delivery service for its customers. The taxpayer's employees pick up cargo from the customer's business, usually in a Washington County area. Then, under its own name, and at its own expense, it has the cargo flown to another location (usually Alaska). The taxpayer itself does not own or lease any airplanes, but rather it uses various airline shipping services to fly their customer's cargo from Washington to Alaska. Once the cargo arrives in Alaska, the taxpayer's employees pick it up and deliver it to the local destination requested by the customer. The reverse process occurs at the taxpayer's Alaska office.

The taxpayer issues its customers an airbill that shows the customer's local (Washington) address as well as the ultimate destination (usually Alaska) for the described goods. This document also shows the total charge to the customer. This is the only airbill or bill of lading that the customer ever receives. The customer never has any knowledge of, or contractual relationship with, the air carrier used by the taxpayer. The taxpayer is issued an airbill by the airline that shows the taxpayer's cost for that portion of the trip.

The taxpayer's profit comes from the mark-up of its local delivery costs and in keeping its rates higher than what the airlines charge the taxpayer. The advantage for the taxpayer's customers is in the convenience and efficiency of having the taxpayer provide a complete door-to-door delivery service. Contractually, the taxpayer is obligating itself for the complete shipping of its customers goods and not just the local pick-up. The taxpayer is also liable to its customer in the event of loss or damage to the customers goods while in transit.

The audit report took the position that the income was taxable because the taxpayer was not an interstate carrier. Citing ETB 331.04.193, 2 ETB 67 (1968), (ETB 331), the audit report noted that the taxpayer does not hold an Interstate Commerce Commission (ICC) permit or have common carrier responsibility. Both of these conditions must be met for the taxpayer to be exempt as an interstate carrier under ETB 331. It is undisputed that the taxpayer does not have an ICC permit. The taxpayer asserts that in light of federal deregulation, this requirement should no longer be controlling. Finally, the taxpayer disputes the

Department's characterization of its airbill/contract with its customers as not confirming its common carrier status.

ISSUE:

Are the taxpayer's business activities properly classified as freight forwarding and subject to state taxation under RCW 82.16.050(8)?

DISCUSSION:

Income earned by a Washington business from the interstate transportation of goods is deductible from the taxpayer's gross income for B&O tax purposes under RCW 82.16.050(8):

In computing tax there may be deducted from the gross income the following items:

(8) Amounts derived from the transportation of commodities from points of origin in this state to final destination outside this state, . . . under a through freight rate from point of origin to final destination;

The operation of the interstate commerce exemptions is illustrated in the examples shown in WAC 458-20-192D:

EXAMPLES OF EXEMPT INCOME:

(1) Income from those activities which consist of the actual transportation of persons or property across the state's boundaries is exempt.

. . .

EXAMPLES OF TAXABLE INCOME:

(1) Compensation received by persons engaged in business within this state for performance of business activities which are only ancillary to transportation across the state's boundaries is taxable.

The Department addressed the issue of taxing "freight forwarding" income in ETB 331:

The taxpayer, a freight forwarder, maintained that the doctrine expressed in the Department of Revenue's ETB

286.04.193 was not applicable to his business activity since any tax assessed upon him under those guidelines is barred by the commerce clause of the Federal Constitution.

The Department of Revenue ruled that published Rule 193 was controlling. The Rule states under Section III, Business and Occupation Tax, Service and Other Business Activities: Interstate and Foreign Commerce, that:

Engaging in interstate or foreign commerce is
exempt . . .

Types of Exempt Income:

(1) Those activities which involve the actual transportation of goods or commodities in interstate or foreign commerce . . .

Thus, where a freight forwarder has the contractual responsibility to move the freight to its destination in interstate commerce it is an interstate carrier. Any freight forwarder claiming the exemption must comply with the following qualifications:

(1) It must be regulated as a common carrier under Part IV of the Interstate Commerce Act (49 U.S.C., Sec. 1001) and hold a permit issued by the Interstate Commerce Commission.

(2) It must file all tariffs with the Interstate Commerce Commission and issue a uniform bill of lading as prescribed by the Commission.

(3) The bill of lading must indicate that the freight forwarder has common carrier responsibility to the consignor from point of origin to the out-of-state consignee at an out-of-state delivery point.

Income earned by a freight forwarder from intrastate shipments is not exempt. The fact that a freight forwarder owns no rolling stock and contracts with others for actual handling and transportation of the goods (including pickup and delivery) is immaterial to the exemption.

(Emphasis added.)

Subsequent federal deregulation of the trucking industry has changed the ICC regulations relied on by the Department in ETB 331. Accordingly, in order to qualify for treatment as interstate carriers, the Department may no longer require that freight forwarders be federally licensed by or subject to ICC tariffs. Such regulations may be relevant in demonstrating that a taxpayer is engaged in interstate commerce. However, the absence of ICC licensing requirements or tariffs does not conclusively prove that the taxpayer is not engaged in interstate transportation. The two remaining qualifications, however, continue in force.

These two requirements are: (1) that the taxpayer must be contractually liable for the interstate transportation of the goods itself; and (2) that the taxpayer must have common carrier liability to its customers in case of loss during shipping.

The sample airbill provided by the taxpayer demonstrates that it does meet these two tests. Nowhere on the airbill is there any indication that any party other than the taxpayer is responsible for the complete shipping of the goods. In fact, if the taxpayer's business name did not include the term "forwarding," it would look like any other interstate carrier's airbill or bill of lading. Item "8" under the "conditions of contract" section on the reverse side of the airbill specifically shows the taxpayer's liability for loss during shipment. Item "12." even refers to the Warsaw Convention regarding liability for international shipments. Finally, the taxpayer's airbill meets the statutory (RCW 82.16.050(8)) requirement of showing a "...through freight rate from point of origin to final destination."

DECISION AND DISPOSITION:

The taxpayer's petition is granted.

DATED this 23rd day of April, 1997.