

Cite as Det. No. 00-025, 19 WTD 937 (2000)

BEFORE THE APPEALS 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. 00-025
...	)	
	)	Registration No. . . .
	)	FY. . . /Audit No. . . .

- [1] RULE 179; RCW 82.04.080: B&O TAX – GROSS INCOME – SEWERAGE SERVICES – PROPORTIONATE SHARE OF MAINTENANCE AND OPERATING EXPENSES. Where a city's sewerage disposal service contract with another municipality required the other municipality to pay a percentage of operating and maintenance costs in addition to sewerage disposal fees, the additional proportionate share of costs was part of the city's gross income.
- [2] RCW 82.04.4291: B&O TAX – DEDUCTIONS – SERVICE RENDERED – AMOUNTS RECEIVED FROM ANOTHER POLITICAL SUBDIVISION. A Washington municipality was not allowed a deduction under RCW 82.04.4291 for amounts received for sewerage services rendered to a political subdivision of the State of Idaho.

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:

A municipal water department protests the assessment of service business and occupation (B&O) taxes on amounts received from an Idaho political subdivision for its pro-rata share of operating and maintenance costs.<sup>1</sup>

FACTS:

Okimoto, A.L.J. The City of . . . , Water Department (Taxpayer) operates a sewer treatment plant in . . . , Washington. Taxpayer's books and records were examined by the Audit Division (Audit) of the Department of Revenue (Department) for the period January 1, 1994 through December

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

31, 1997. The audit examination resulted in additional taxes and interest owing in the amount of \$. . . and Document No. FY. . . was issued on January 20, 1999.

Taxpayer paid the unprotested portion, and the balance remains due.

#### Schedule 4 – To Assess Tax on [Idaho City] Sewer Processing

In this schedule, Audit assessed additional service and other B&O taxes on amounts Taxpayer received from the [Idaho City], located in the State of Idaho, for its pro-rata share of operating and maintenance expenses of the expanded treatment plant. Taxpayer received this payment in accordance with a 1983 agreement with [Idaho City]. Taxpayer explains in its petition:

The City of . . . , Washington and [Idaho City], Idaho both sit on Washington/Idaho border; . . .

The City of . . . , Washington and the [Idaho City], Idaho had entered into an agreement in 1983 to enlarge and upgrade the existing Wastewater Treatment Plant which would service the [Idaho City] area for wastewater disposal. The contract was entered into with the understanding that the [Idaho City] would pay a percentage of Operation and Maintenance costs on a yearly calculation based on a “flow meter” installed to calculate [Idaho City]’s sewer flow.

#### TAXPAYER’S CONTENTIONS AND ARGUMENTS:

Taxpayer contends that this pro-rata payment is not income for services rendered, but only a reimbursement of costs incurred pursuant to the 1983-expansion agreement. Taxpayer points out that the computational formula for computing the reimbursement is a direct pro-ratio of actual expenses incurred.

Next, Taxpayer contends that it is entitled to deduct this income under RCW 82.04.4291.

Taxpayer points out that the State of Washington, Department of Ecology recognizes the [Idaho City] as a viable and legitimate "other municipality" for the purpose of calculating Wastewater Discharge Permit fees.

#### ISSUES:

- 1) Should amounts Taxpayer received from an Idaho municipality for that city’s share of sewer treatment plant operating and maintenance costs be included in its gross income?
- 2) Is Taxpayer entitled to a deduction under RCW 82.04.4291 for amounts received from a political subdivision of the State of Idaho?

#### DISCUSSION:

RCW 82.04.030 includes within the definition of "person" or "company" any individual, municipal corporation, political subdivision of the State of Washington or numerous other types of entities listed in the statute.

RCW 82.04.140 defines "business" as:

. . . all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or to another person or class, directly or indirectly.

RCW 82.04.150 states: "engaging in business means commencing, conducting, or continuing in business . . . ."

Thus, any person, including municipal corporations or political subdivisions of the State of Washington that engage in any activity with the object to benefit or gain for itself or another person, either directly or indirectly, is engaged in business. In this case, Taxpayer does not dispute that it is engaged in the water and sewerage treatment business.

RCW 82.04.290(2) imposes a B&O tax:

Upon every person engaging within this state in any business activity other than or in addition to those enumerated in RCW 82.04.230, 82.04.240, 82.04.250, 82.04.255, 82.04.260, 82.04.270, and 82.04.280, and subsection (1) of this section: as to such persons the amount of tax on account of such activities shall be equal to the gross income of the business multiplied by the rate of 1.5 percent.

RCW 82.04.080 further states:

"Gross income of the business" means 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, . . . 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. (Emphasis added.)

In this case, we find that Taxpayer is engaged in the wastewater and sewerage treatment business and the compensation received from [Idaho City] is simply computed pursuant to an agreed upon formula that is partly based on maintenance and operating costs.

Furthermore, although Taxpayer argues that it is not receiving compensation for sewerage and wastewater treatment services, but only being reimbursed for costs incurred, we disagree. The 1983 agreement between Taxpayer and [Idaho City] clearly provides that [Idaho City] is paying Taxpayer for sewerage disposal services. It states in pertinent part:

ITEM I

The purpose of this agreement is to provide continued sewerage disposal service to the District [Idaho City] and establish a method for the District to pay for said sewerage disposal service and provide for a method of calculation of the District's share of costs for the Phase II Sewage Treatment Plant expansion and improvements based on a percentage of flow ratio and growth factor, such share of costs hereinafter referred to as the "connection fee". (Emphasis added.)

We further find Taxpayer's reliance on the language contained in Item IX of the contract, misplaced. It states:

The percentage of flow ratio will determine the District's [Idaho City] share of actual operating and maintenance expenses of the City's Sewage Treatment Plant for a budget year. (Bracketed material added.)

This clause in the contract merely provides that in addition to any amounts paid for sewerage treatment services as determined by the flow meter, [Idaho City] is also required to pay for indirect and overhead costs related to the performance of those sewerage services. These amounts are compensation for sewerage services rendered by Taxpayer, regardless of how they are computed or characterized in the contract. RCW 82.04.080.

Next, we must determine whether Taxpayer is entitled to deduct these amounts from its gross income under RCW 82.04.4291. That deduction states:

In computing tax there may be deducted from the measure of tax amounts derived by a political subdivision of the state of Washington from another political subdivision of the state of Washington as compensation for services which are within the purview of RCW 82.04.290. (Emphasis added.)

RCW 82.04.4291 clearly limits this deduction to amounts received from "another political subdivision of the state of Washington." Since [Idaho City] is a political subdivision of the state of Idaho, the deduction does not apply. Accordingly, Taxpayer's petition is denied on this issue.

#### DECISION AND DISPOSITION:

Taxpayer's petition is denied.

Dated this 28<sup>th</sup> day of February, 2000.