Cite as Det. No. 07-0363, 27 WTD 136 (2008)

BEFORE THE APPEALS DIVISION
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. 07-0363
. . .	)	Registration No. . . .
	)	Document No. . . .
	)	Audit No. . . .
	)	Docket No. . . .

RULE 24003; RCW 82.04.4452 – B&O TAX -- HIGH TECHNOLOGY CREDIT. Real estate rental expenses and patent attorney fees are not qualified research and development expenditures under RCW 82.04.4452 and Rule 24003.

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.

C. Pree, A.L.J. – A taxpayer that designs products that perform characterization and measurement of light emitting components and systems protests the disallowance of a portion of its claimed business and occupation ("B&O") high technology credit (RCW 82.04.4452). We conclude that the disallowed portions of the claimed credit, which were claimed for real estate rental expenses and patent attorney's fees, were not "qualified research and development expenditures" and sustain the assessment.[1]

ISSUE

Whether real estate rental expenses and patent attorney's fees constitute "qualified research and development expenditures" for purposes of the high technology credit (RCW 82.04.4452).

FINDINGS OF FACT

The taxpayer engages in business in Washington designing, manufacturing, and selling products or services that perform and enable characterization and measurement of a wide variety of light emitting components and systems. These include flat panel displays, light sources, projectors,

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

instrument panels, and luminaries. The taxpayer also provides testing, design, and consulting services.

The Audit Division of the Department of Revenue reviewed the taxpayer's records for the period of January 1, 2002, through March 31, 2006. As a result, the Audit Division issued an assessment, which included disallowance of a portion of the taxpayer's claimed high technology credit (RCW 82.04.4452). Specifically, the Audit Division disallowed the taxpayer's claimed credit for real estate rental charges and patent attorney's fees. The taxpayer determined the disallowed amount applicable to these items to be $. . . .

The taxpayer explained that a portion of the office space, which it rented and for which it claimed the high technology credit, is painted black and is used for testing equipment that is designed to measure light and color.

ANALYSIS

RCW 82.04.4452 allows a B&O tax credit "for each person whose research and development spending during the year in which the credit is claimed exceeds 0.92 percent of the person's taxable amount during the same calendar year." The credit is allowed for persons engaging in research and development in Washington in any of five areas of high technology. The Audit Division concluded the taxpayer engaged in "electronic device technology," one of the qualifying areas. The Audit Division further concluded that the taxpayer's spending exceeded the spending requirement.

However only "qualified research and development expenditures" are eligible for the credit, and the Audit Division concluded that the taxpayer's expenditures for rental of real estate and patent attorney's fees did not meet this requirement. RCW 82.04.4452(9)(b)[2] defines "qualified research and development expenditures" as:

> Operating expenses, including wages, compensation of a proprietor or a partner in a partnership as determined under rules adopted by the department, benefits, supplies, and computer expenses, directly incurred in qualified research and development by a person claiming the credit provided in this section. The term does not include . . . capital costs and overhead, such as expenses for land, structures, or depreciable property.

As a preliminary matter, we note that B&O tax exemptions and credits are construed strictly, though fairly, and in keeping with the ordinary meaning of their language, against the taxpayer. *See, e.g., Budget Rent-a-Car, Inc. v. Dep't of Revenue.*, 81 Wn.2d 171, 500 P.2d 764 (1972); *Group Heath Coop. v. Tax Comm'n*, 72 Wn.2d 422, 429, 433 P.2d 201 (1967); Det. No. 07-0034E, 26 WTD 212 (2007); Det. No. 04-0102, 23 WTD 340 (2004); Det. No. 03-0079, 23 WTD 83 (2004). Thus, "the burden of showing qualification for the tax benefit afforded likewise rests with the taxpayer." *Group Health*, 72 Wn.2d at 429.

[2] Although the statute was amended during the audit period, this definition remained unchanged.

We will first address the issue of the taxpayer's claimed credit for patent attorney's fees. WAC 458-20-24003 (Rule 24003), the administrative rule regarding the high technology credit, specifically states, "Qualified research and development expenditures do not include legal expenses, patent fees, or any other expense not incurred directly for qualified research and development."[3] The taxpayer argues that the patent attorney's fees are "an integral part of our product development and are absolutely necessary to protect our product." While we do not doubt the necessity of these fees, we must be guided by the statutes and rules as written. As noted above, Rule 24003 specifically excludes legal expenses and patent fees from the definition of "qualified research and development expenditures." This provision of Rule 24003 has been in effect, without change, since the Rule's adoption in 2003. Although the statute has been amended twice since 2003, the legislature has not disturbed the Department's conclusion that patent fees and legal expenses do not qualify as "qualified research and development expenditures." Accordingly, we must deny the taxpayer's petition on this issue.

We will next address the issue of whether the taxpayer's real estate rental expenses constitute "qualified research and development expenditures." The Audit Division disallowed these expenses because it concluded these expenses constitute "overhead," which is specifically excluded from the definition of "qualified research and development expenditures" in the statute. The statute, however, does not define the term "overhead."

It is well-settled that "Words in a statute are given their ordinary and common meaning absent a contrary statutory definition." *John H. Sellen Constr. Co. v. Dep't of Revenue,* 87 Wn.2d 878, 882, 558 P.2d 1342 (1976); *see also, e.g.*, Det. No. 05-0217E, 26 WTD 91 (2007). Further, "Washington courts use WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY in the absence of other authority." *State v. Glas*, 106 Wn. App. 895, 27 P.3d 216 (2001), *citing, In re Personal Restraint of Well*, 133 Wn.2d 433, 438, 946 P.2d 750 (1997); *see also, e.g.*, Det. No. 05-0217E.

In reaching the conclusion that real estate rental expenses constitute "overhead," the Audit Division relied on Webster's Third New International Dictionary ("Webster's"), p., 1608 (1993). This dictionary defines "overhead" as "those general charges or expenses in a business which cannot be charged up as belonging exclusively to any particular part of the work or product (as rent, taxes, insurance, lighting, heating, accounting, and other office expenses, and depreciation). Thus, the Audit Division properly relied on Webster's, and Webster's specifically includes rent in its definition of overhead.

In response, the taxpayer argues we should use a different dictionary, such as a legal and accounting dictionary. However, as noted above, the Audit Division's use of Webster's to determine the definition is well-supported. The taxpayer further argues that rent is also considered an "operating" expense in Webster's. However, we did not find "rent" specifically listed in the definition of "operating." Instead, the most closely applicable definition to

[3] Rule 24003 was amended after the audit period, but this provision remained unchanged.

"operating expense" we were able to find in Webster's defines "operating" as "Arising out of or concerned with the current operations of a concern engaged in transportation or manufacturing as distinct from its financial transactions and its permanent improvements." Webster's, p. 1581. Balancing this definition of "operating," which does not specifically include "rent," against the definition of "overhead," which does specifically include rent we conclude that the Audit Division properly determined that rent is an overhead expense.

Finally, the taxpayer notes that more expenses are allowed for purposes of the manufacturing machinery and equipment credit than are allowed for the credit at issue. The taxpayer further notes that the failure to allow these expenses "detracts from the business environment in the State of Washington." As to these further arguments, the Department, as an administrative agency, has no authority to grant an exemption where none exists in the law. Only the legislature, through enactment of appropriate legislation, may do so. *See, e.g., Budget Rent-a-Car, Inc. v. Dep't of Revenue*, 81 Wn.2d 171, 500 P.2d 764 (1972); Det. No. 05-0027, 26 WTD 87 (2007).

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 21st day of December 2007.