Cite as Det. No. 15-0026, 34 WTD 373 (2015)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Refund of	)	D E T E R M I N A T I O N
	)	
	)	No. 15-0026
. . .	)	
	)	Registration No. . . .
	)	

[1] RCW 82.04.394: SERVICE AND OTHER ACTIVITIES B&O TAX – PROPERTY MANAGEMENT COMPANY – REQUIREMENTS OF WRITTEN PROPERTY MANAGEMENT AGREEMENT. The agreements provided by Taxpayer did not satisfy all of the requirements under RCW 82.04.394(2)(c) because (1) employee compensation was not the ultimate obligation of the property owners, (2) the property manager was not liable for payment only as an agent, and (3) the property manager was not a mere agent of the property owner with respect to other actions such as hiring, firing, and other conditions of employment of onsite personnel.

[2] RULE 254; RCW 82.32.100: RETAIL SALES TAX – RETAILING B&O TAX – RECORDKEEPING – REASONABLE ESTIMATES. The Department may base estimated income and estimated uncollected retail sales tax on records of wages paid to maintenance staff that performed retail maintenance work in the absence of actual records of income from such retail maintenance work.

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.

Yonker, A.L.J. – An out-of-state property management company (Taxpayer) protests the Department's denial of a refund request in which Taxpayer claimed (1) it should have been allowed to exclude from its measure of business and occupation (B&O) tax amounts that it received from its customers to cover Taxpayer's own payroll expenses, and (2) protests the classification of a portion of [its] income to retail sales. We deny Taxpayer's petition.[1]

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

ISSUES

1. Are amounts Taxpayer received from its customers as payment for Taxpayer's payroll expenses properly excluded from Taxpayer's measure for B&O tax liability under former RCW 82.04.394?

2. Did the Department properly assess estimated retailing B&O tax and retail sales tax against Taxpayer on certain retail service sales under RCW 82.32.100 where the Department based its estimate on figures provided by Taxpayer?

FINDINGS OF FACT

[Taxpayer] is a for-profit [out of state] corporation that serves as the property management company for two mobile home parks located in Washington. The two mobile home parks are separate Washington limited liability companies. The governing persons of Taxpayer and the members of both mobile home parks are the same individuals. A number of agreements describe the nature of the relationship between Taxpayer and the two mobile home parks:

- According to two "Payroll Service Agreements" entered into by Taxpayer and each of the two mobile home parks in 2007, the mobile home parks "designated" Taxpayer "to administer payroll records, bookkeeping, payroll taxes, workers compensation, hiring, firing, and employee garnishments." Taxpayer also agreed to "pay employees." In exchange, Taxpayer received compensation from the mobile home parks in two forms: (1) a $75 fee per employee per pay period, and (2) "reimbursement" of "the gross employee wages, taxes, workers compensation and other charges" for each employee. The Payroll Service Agreements do not specifically identify the employer of the employees, nor do they specifically identify what, if any, duties the two mobile home parks have in relation to the employees.

- According to two "Property Management Agreements" entered into by Taxpayer and each of the two mobile home parks in 1993, the two mobile home parks "designated" Taxpayer "as the exclusive managing and leasing agent for" the two mobile home parks. As the manager for both parks, Taxpayer was given the "authority to hire, supervise and terminate, on behalf of [the mobile home parks], any independent contractors and Property employees reasonably required in the operation of Property." The agreement goes on to state, "[i]t is agreed that all Property employees are employees of [Taxpayer] and are not employees of [the mobile home parks]." In exchange, the mobile home parks agreed to pay Taxpayer "as the fee for its management services the sum cost of managers payroll plus 10%" each month.[2]

- According to a "Resident Property Manager Agreement" entered into by Taxpayer and two individuals in 2009, Taxpayer is identified as the "employer" of the two individuals, who agreed to work jointly as on-site managers for one of the mobile home parks. Taxpayer agreed to pay the individuals' salaries and other reimbursements. In exchange, the individuals agreed to perform a variety of duties, categorized generally in the

[2] The initial term of these agreements was from April 1, 1993, through April 1, 1994, and then monthly thereafter so long as neither party terminates the agreements. We have no evidence that these agreements have ever been terminated by the parties.

> agreement as (1) marketing, (2) rent collection, (3) rule enforcement, (4) park maintenance, and (5) administrative duties. In addition to these regular duties, Taxpayer paid the individuals "over and above normal pay" for such duties as painting, cleaning, and repairing manufactured homes in the customer's park. This agreement does not identify the mobile home parks as having any duty to pay the individuals, and does not identify the mobile home parks as employers of the individuals.

Taxpayer provided no other agreements related to (1) the relationship between Taxpayer and the mobile home parks, or (2) the relationship between Taxpayer and the on-site employees working at the mobile home parks. In addition, Taxpayer specifically represented that no written agreements exist related to the nature of the relationship between the two mobile home parks and the on-site employees working at the parks.

In 2011, the Department's Taxpayer Account Administration (TAA) conducted a limited review of Taxpayer's books and records for the period of January 1, 2007, through December 31, 2010 (review period). During that review, TAA made two findings that are relevant to this appeal. First, TAA found that Taxpayer had incorrectly excluded amounts Taxpayer was paid by the mobile home parks to cover the payroll expenses for on-site employees at the mobile home parks. This was based on TAA's finding that Taxpayer was the employer of those employees, and, therefore, primarily responsible for paying the salaries of such employees. Second, TAA found that Taxpayer had reported all of its gross income under the service and other activities B&O tax classification, but that a portion of its previously unreported income was received for performance of retail services, and, therefore, was subject to retailing B&O tax and retail sales tax, which Taxpayer failed to collect from the mobile home parks at the time such retail services were performed.

On May 10, 2011, TAA specifically requested further information for the review period regarding Taxpayer's gross income "received for improvements, installations and maintenance." On May 12, 2011, in response to that request, Taxpayer submitted two . . . lists of "maintenance wages," which included monthly totals of wages Taxpayer paid to employees for maintenance work they performed at each of the two mobile home parks for the entire review period. Taxpayer provided no other documentation in response to TAA's request. Based on this information, TAA classified a portion of Taxpayer's previously unreported gross income for the review period under the retailing B&O tax classification, using the amount of the "maintenance wages" Taxpayer reported in the . . . lists as the estimated amount of retail service income. TAA also assessed retail sales tax against Taxpayer based on that same estimated amount of retail service income.

On June 14, 2011, as a result of TAA's findings, the Department issued a tax assessment for $. . . , which included $. . . in additional tax liability, a $. . . five-percent assessment penalty, and $. . . in interest. On June 23, 2011, Taxpayer paid the full amount of the tax assessment. Taxpayer subsequently requested a refund in the form of amended returns in which it claimed an exemption from its taxable income certain payroll expenses. On December 12, 2013, TAA denied Taxpayer's refund request. Taxpayer subsequently appealed that decision, and amended its refund request to include TAA's assessment of retailing B&O tax and retail sales tax on its estimated retail service income during the review period.

ANALYSIS

In Washington, "there is levied and collected from every person that has a substantial nexus with this state a tax for the act or privilege of engaging in business activities." RCW 84.04.220. The B&O tax measure is "the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be." *Id.* The rate used is determined by the type of activity in which a taxpayer engages. *See generally* Chapter 82.04 RCW.

The B&O tax is a gross receipts tax, meaning that it applies to all value proceeding or accruing to the company, and not only to its profit margins. *Lamtec Corp. v. Dep't of Revenue*, 170 Wn.2d 838, 843, 246 P.3d 788, 791 (2011). By enacting Washington's B&O tax system, the legislature intended to impose the B&O tax on virtually all business activities carried on within the state. *Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971). Further, the B&O tax system was meant to "leave practically no business and commerce free of . . . tax." *Budget Rent-A-Car of Washington-Oregon Inc. v. Dep't of Revenue*, 81 Wn.2d 171, 175, 500 P.2d 764 (1972).

RCW 82.04.140 defines "business" broadly and includes "all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or another person or class, directly or indirectly." Generally, all gross income of the business is subject to B&O tax, without any deductions for costs such as labor, materials, taxes, or any other expense. *See* RCW 82.04.080. This holds true unless the legislature has carved out a specific exception. We note that when interpreting exemption or deduction provisions, "the burden of showing qualification for the tax benefit . . . rests with the taxpayer . . . [and] in the case of doubt or ambiguity, [the provisions are] to be construed strictly, though fairly and in keeping with the ordinary meaning of their language, against the taxpayer." *Group Health Coop. of Puget Sound, Inc. v. Washington State Tax Comm'n*, 72 Wn.2d 422, 429, 433 P.2d 201 (1967).

1. Exemption for Property Managers

Taxpayer does not dispute that it is subject to B&O tax generally. Instead, Taxpayer argues that a portion of its gross income during the audit period should be excluded from the measure of its B&O tax liability due to the exemption for property managers under RCW 82.04.394.

Before June 1, 2010, RCW 82.04.394 provided for a B&O tax exemption for amounts received by a property management company for wages of certain personnel as follows:

> (1) [The B&O tax] does not apply to amounts received by a property management company from the owner of a property for gross wages and benefits paid directly to or on behalf of on-site personnel from property management trust accounts that are required to be maintained under RCW 18.85.310.
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> (2) As used in this section, "on-site personnel" means a person who meets **all** of the following conditions: (a) The person works primarily at the owner's property; (b) the person's duties include leasing property units, maintaining the property, collecting rents, or similar activities; and (c) under a **written** property management agreement: (i) **The person's compensation is the ultimate obligation of the property owner and not the property manager**; (ii) **the property manager is liable for payment only as agent of the owner**; and (iii) **the property manager is the agent of the owner with respect to the on-site**

> **personnel and that all actions, including, but not limited to, hiring, firing, compensation, and conditions of employment, taken by the property manager with respect to the on-site personnel are subject to the approval of the property owner**.

RCW 82.04.394 (1998) (emphasis added). Then, effective June 1, 2010, that statute was amended to limit the exemption described above to only (1) nonprofit property management companies and (2) property management companies from a housing authority. RCW 82.04.394 (2010); *see also* Excise Tax Advisory 3111.2010 (June 24, 2010). All other requirements of the exemption remained substantively the same.[3]

Preliminarily, we conclude that Taxpayer could not have qualified for the exclusion under RCW 82.04.394 beginning on June 1, 2010 due to the change in the statute that occurred on that date. This is because (1) Taxpayer is not a "nonprofit" property management company and (2) there has been no evidence presented that Taxpayer is affiliated with "a housing authority." Thus, if Taxpayer qualifies at all for the exclusion under RCW 82.04.394, we conclude that it can only be from the beginning of the review period, January 1, 2007, through May 31, 2010.

Nevertheless, even for the time period prior to June 1, 2010, we conclude that Taxpayer has failed to prove that it is entitled to the exemption available under RCW 82.04.394 because there is no written property management agreement in the record that meets all of the requirements under RCW 82.04.394(2)(c). First, the Residential Property Manager Agreement between Taxpayer and the on-site managers at one of the mobile home parks specifically identifies Taxpayer – not the mobile home park – as the employer of the on-site managers. Indeed, this agreement is silent as to the nature of the relationship between the mobile home parks, or owners, and the on-site managers. Further, the two Property Management Agreements between Taxpayer and the two mobile home parks indicate the precise opposite of what RCW 82.04.394(2)(c)(i) requires, stating that Taxpayer is the employer of the on-site employees, and that the mobile home parks are specifically not to be considered employers of such employees.

Second, neither the Residential Property Manager Agreement nor the Property Management Agreement state that Taxpayer's liability to pay the employees is as the mobile home parks' agent only, as required under RCW 82.04.394(2)(c)(ii). While the Property Management Agreement identifies Taxpayer as the mobile home parks' "agent," such title is in relation to Taxpayer's duty to provide management services, and clearly does not use the term "agent" to describe Taxpayer's obligation to hire and pay on-site employees since those agreements specifically identify Taxpayer as the employer of such employees.

Third, nowhere in any of the agreements is it evident that the mobile home parks have reserved for themselves any final authority in the hiring, firing, compensation, or other conditions of employment, of on-site employees at the parks as required under RCW 82.04.394(2)(c)(iii). Instead, the Resident Property Manager Agreement speaks only in terms of Taxpayer having the authority to make decisions on all of those matters. Likewise, the Property Management Agreements state that Taxpayer "shall have authority to hire, supervise and terminate" on-site employees.[4]

[3] RCW 82.04.394 was subsequently repealed on August 24, 2011 and replaced by RCW 82.04.4274.

[4] . . .

Despite Taxpayer's argument that the substance of the agreements was such that the mobile home parks were the employers of their on-site employees, and Taxpayer a mere agent for the mobile home parks, the clear language to the contrary contained in the agreements we have received cannot be disregarded. The agreements indicate that while Taxpayer may have served as an agent for management services generally, it was Taxpayer – as opposed to the mobile home parks – that was the employer of the on-site employees, and that had ultimate authority, as opposed to mere agency authority, over all aspects of the employment of the on-site employees. Therefore, Taxpayer has failed to satisfy all of the requirements of 82.04.394, and cannot exclude the payments it received from the mobile home parks from its measure of B&O tax liability.

2. Retailing B&O Tax and Retail Sales Tax

RCW 82.04.250 imposes retailing B&O tax "[u]pon every person engaging within this state in the business of making sales at retail," as measured by the person's gross proceeds of sales of the business. Gross proceeds of sales of the business, in turn, includes all "value proceeding or accruing from" such sales at retail without any deduction for any business costs. RCW 82.04.070. In addition, Washington imposes a retail sales tax on each sale at retail in this state, unless there is a specific exemption. RCW 82.08.020; RCW.04.050.

RCW 82.04.050(2) defines "sale at retail" as including charges made for labor and services rendered in respect to the following:

(a) The installing, repairing, cleaning, altering, imprinting, or improving of tangible personal property of or for consumers . . .

(b) The constructing, repairing, decorating, or improving of new or existing buildings or other structures under, upon, or above real property of or for consumers, including the installing or attaching of any article of tangible personal property therein or thereto, whether or not such personal property becomes a part of the realty by virtue of installation . . .

RCW 82.04.050(3) further defines "sale at retail" as including charges made for labor and services rendered in respect to "[l]andscape maintenance." Thus, any income Taxpayer received during the review period for performing any of these retail services is subject to retailing B&O tax and retail sales tax. Further, in the case of retail sales tax, while such tax "must be paid by the buyer to the seller," it is the seller's obligation to collect such retail sales tax, and if a seller fails to collect the retail sales tax, the seller is "personally liable to the state for the amount of the tax." RCW 82.08.050(3).

Here, during TAA's original review, TAA discovered that in addition to receiving payment for its payroll administration services, Taxpayer also received income from retail services such as "improvements, installations and maintenance" performed by Taxpayer's employees at the mobile home parks. TAA requested from Taxpayer information regarding "[g]ross income received from improvements, installations and maintenance." In response, Taxpayer submitted two . . . lists of "maintenance wages," one list for each mobile home park. Taxpayer did not provide any other documentation of the income it received as a result of its retail services performed during the review period.

RCW 82.32.100 states the following:

> (1) If any person fails or refuses to make any return or to make available for examination the records required by this chapter, the department shall proceed, in such manner as it may deem best, to obtain facts and information on which to base its estimate of the tax; and to this end the department may examine the records of any such person . . .
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> (2) As soon as the department procures such facts and information as it is able to obtain upon which to base the assessment of any tax payable by any person who has failed or refused to make a return, it shall proceed to determine and assess against such person the tax and an applicable penalties or interest due, but such action shall not deprive such person from appealing the assessment as provided in this chapter.

Here, TAA used these lists of "maintenance wages" that Taxpayer submitted as the basis for estimating the amount of Taxpayer's gross income from retail services. TAA also used the lists of "maintenance wages" for estimating the amount of Taxpayer's income that was subject to retail sales tax but on which Taxpayer had failed to collect retail sales tax from its customers, the mobile home parks, at the time Taxpayer's employees provided the retail services. We conclude that, pursuant to RCW 82.32.100, TAA was authorized to estimate those amounts in the absence of actual records. We find nothing unreasonable in TAA's reliance on Taxpayer's own reported "maintenance wages" as an appropriate measure for determining the amount of income Taxpayer had from such retail services. Further, Taxpayer has made no argument that such reliance led to a higher estimated tax liability than Taxpayer's actual tax liability for the performance of its retail services during the review period.

To the extent that Taxpayer argues on appeal that employee wages themselves should not be subject to retail sales tax, we do not disagree with Taxpayer. However, that is not what TAA did here. As discussed above, TAA merely used the "maintenance wages" amounts for two things: (1) as the measure for determining Taxpayer's estimated retailing B&O tax liability for performing retail services during the review period, and (2) for determining Taxpayer's estimated retail sales tax liability for those retail services for which Taxpayer should have, but failed to, collect retail sales tax from the mobile home parks. Thus, the assessment of retail sales tax is the result of Taxpayer's failure to charge its customers, the mobile home parks, retail sales tax at the time the retail services were provided. We conclude that TAA's actions were appropriate here, and find no basis for adjustment on this issue.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 4th day of February, 2015.