

Cite as Det. No. 17-0038, 36 WTD 502 (2017)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS 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. 17-0038
)	
...)	Registration No. . . .
)	

RCW 82.04.3651; WAC 458-20-169: NONPROFIT ORGANIZATION FUND-RAISING ACTIVITIES. A nonprofit organization’s sales of environmental commodity products via phone, email, and web store, do not qualify as tax-exempt fund-raising activities because Taxpayer was operating a regular place of business with regular hours. The ability to instantly purchase environmental commodities in a web store, receive customer service during regular business hours, and request a written response to a purchase inquiry are all characteristics of a regular business in which sales are made during regular hours.

RCW 82.32.105: CANCELLATION OF INTEREST. The Department may only cancel interest when a taxpayer shows either, its failure to timely pay the tax was the direct result of written instructions given to the taxpayer by the Department or the extension of a due date for payment of an assessment of deficiency was not at the request of the taxpayer and was for the sole convenience of the Department. Reliance in good faith on legal counsel is not a circumstance where the Department is authorized to cancel interest.

RCW 82.32.105; WAC 458-20-228: CANCELLATION OF PENALTIES – CIRCUMSTANCES BEYOND THE CONTROL OF THE TAXPAYER. Reliance in good faith on legal counsel does not constitute a circumstance beyond the control of the taxpayer because it is not immediate, unexpected, or in the nature of an emergency. Further, mistakes or misconduct on the part of employees or other persons contracted with the taxpayer are not considered a circumstance beyond the control of the taxpayer.

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.

Anderson, T.R.O. – A nonprofit organization disputes an assessment of service and other activities business and occupation (“B&O”) tax on its sales of environmental commodity products to Washington customers and asserts that such sales constitute “fund-raising activities” that are exempt from B&O tax. The organization also disputes assessments of interest and penalties

because it asserts it did not report and pay B&O tax under the advice of legal counsel. Petition denied.¹

ISSUES

1. Whether a nonprofit organization's sales of environmental commodity products via phone, email, and web store, to Washington customers constitute a fund-raising activity exempt from B&O tax under RCW 82.04.3651 and WAC 458-20-169.
2. Whether RCW 82.32.105 authorizes the Department to cancel assessments of interest or penalties because a nonprofit organization relied in good faith on the advice of legal counsel when it did not report income and pay taxes.

FINDINGS OF FACT

. . . (“Taxpayer”) is a nonprofit organization that is exempt from Federal income tax under section 501(c)(3) of the Internal Revenue Code. Taxpayer's mission . . . is to encourage and fund projects that develop clean, environmentally preferred, renewable energy, and restore and protect fish and wildlife habitat.²

Taxpayer describes itself as an “entrepreneurial 501(c)(3) nonprofit organization” because it receives funds through a combination of revenue-generating products and services and contributions from philanthropic organizations.³ One such revenue-generating product is the sale of environmental commodity products; specifically, renewable energy credits, water restoration certificates, and carbon offsets. Whether Taxpayer's sales of environmental commodity products to Washington customers is subject to B&O tax is at issue here.

Taxpayer's website states as follows on a webpage entitled “Environmental Products”:

. . .

. . . (February 2, 2017) (emphasis in original). Visitors can select environmental commodity products to learn more about and request consultations. Visitors can also immediately purchase a prepackaged environmental commodity product in Taxpayer's web store with secure checkout.⁴ Taxpayer's web store provides a toll-free phone number for customer support, from 7:00 a.m. – 4:00 p.m. PST on Monday through Friday and an inquiry form for contacting Taxpayer outside of the customer support business hours.

The Department's Audit Division (“Audit”) reviewed Taxpayer's books and records from December 1, 2012, through June 30, 2015 (the “Audit Period”). On December 17, 2015, Audit issued an assessment for \$. . . against Taxpayer, [including] \$. . . in service and other activities

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

² . . . (January 27, 2017).

³ . . . (January 27, 2017).

⁴ Taxpayer offers the following prepackaged environmental products for immediate purchase: . . . (February 2, 2017).

B&O tax, \$. . . in interest, \$. . . in delinquent penalty, and \$. . . in 5% assessment penalty.⁵ The entire tax assessment stems from Taxpayer's sales of environmental commodity products to Washington customers.

During the Audit Period, Taxpayer made sales of environmental commodity products to Washington customers in the following years and amounts: 2013 - \$. . . ; 2014 - \$. . . ; and 2015 - \$ Audit determined that these receipts were sufficient to establish economic nexus with Washington under WAC 458-20-19401 and calculated an apportionment percentage for each year (30% in 2013, 50% in 2014, and 49% in 2015). Then Audit multiplied the apportionment percentage by Taxpayer's total income from the sale of environmental commodity products (to determine sales of environmental commodity products attributed to Washington) and assessed service and other B&O tax on the environmental commodity products, along with interest, delinquent penalties, and the 5% assessment penalty.

Taxpayer appeals the assessment. Taxpayer asserts that its receipts from sales of environmental commodity products are exempt from B&O tax under RCW 82.04.3651 because they are amounts from fund-raising activities. Taxpayer states that it sells environmental commodity products to raise funds and support its mission; part of the receipts go to the renewable energy facility generating the products and part go to fund Taxpayer's other activities (renewable energy education, watershed restoration, and renewable energy innovation).

Further, Taxpayer seeks to distinguish its sale of environmental commodity products from the non-qualifying, fund-raising activities in WAC 458-20-169(5)(g). Taxpayer states in its Appeal Petition, in pertinent part, as follows:

Similar to the examples provided in WAC, the examples of nonqualifying fundraising activities all involve a place of business directly related to the fundraising activities being offered.

[Taxpayer] does not maintain a regular place of business within the state of Washington in which the sale, fulfillment, or customer service of environmental commodities (the activities subject to the audit) takes place. [Taxpayer] does not have any physical presence within the State of Washington with respect to the activities subject to the audit. Sales of environmental commodities are made through periodic phone and email solicitations, all of which are conducted [out-of-state]. All business associated with the activities subject to the audit take place solely [out-of-state]. Therefore, the fundraising activities (the sale of environmental commodities) is a qualifying activity within the meaning of RCW 82.04.3651(3) and WAC 458-20-169(5)(g)(ii), and are exempt from B&O tax.

However, should we sustain the assessment of tax, Taxpayer asserts that we should cancel interest and penalties because Taxpayer relied in good faith on legal counsel in not reporting income and paying tax.

⁵ . . .

ANALYSIS

B&O Tax

Washington levies and collects the B&O tax from every person that has substantial nexus with Washington “. . . for the act or privilege of engaging in business activities.” RCW 82.04.220(1). “The tax is measured by the application of rates against value of product, gross proceeds of sales, or gross income of the business, as the case may be.” *Id.*

Persons engaging in service and other activities are subject to a tax rate of 1.5%, applied against the gross income of the business. RCW 82.04.290(2). A person is classified (for tax purposes) as engaging in service and other activities when the business activity is not explicitly taxed under another (B&O) tax classification in Chapter 82.04 RCW. *Id.*

Here, Taxpayer sells environmental commodity products to Washington customers. This business activity is not explicitly taxed under a B&O tax classification in Chapter 82.04 RCW; therefore, it is subject to the service and other activities B&O tax unless a specific exemption applies. RCW 82.04.220.

As relevant here, RCW 82.04.3651 exempts certain amounts received by a nonprofit organization from “fund-raising activities” and reads, in pertinent part:

(1) This chapter does not apply to amounts received from fund-raising activities by nonprofit organizations, as defined in subsection (2) of this section, and libraries defined in RCW 27.12.010.

(2) As used in this section, a “nonprofit organization” means:

(a) An organization exempt from tax under section 501(c)(3), (4), or (10) of the federal internal revenue code (26 U.S.C. Sec. 501(c)(3), (4), or (10));

. . .

(3) As used in this section, the term “fund-raising activity” means soliciting or accepting contributions of money or other property involving the anticipated exchange of goods or services for money between the soliciting organization and the organization or person solicited, for the purpose of furthering the goals of the nonprofit organization. “Fund-raising activity” does not include the operation of a regular place of business in which sales are made during regular hours such as a bookstore, thrift shop, restaurant, or similar business or the operation of a regular place of business from which services are provided or performed during regular hours such as the provision of retail, personal, or professional services. The sale of used books, used videos, used sound recordings, or similar used information products in a library, as defined in RCW 27.12.010, is not the operation of a regular place of business for the purposes of this section, if the proceeds of the sales are used to support the library.

(Emphasis added.) To summarize, RCW 82.04.3651 sets forth two requirements in order to qualify for the nonprofit organization’s fund-raising activity exemption: (1) The taxpayer must be a “nonprofit organization”; and (2) the amounts must be received from fund-raising activities.

Here, Taxpayer is a “nonprofit organization” because it is an organization exempt from Federal income tax under 26 U.S.C. §501(c)(3). At issue is whether its sales of environmental commodity products via phone, e-mail, and web store constitute a “fund-raising activity” under RCW 82.04.3651(3); specifically, whether Taxpayer operated a regular place of business – a non-qualifying activity – to sell the environmental commodity products.

WAC 458-20-169 is the Department’s administrative rule on nonprofit organizations. It discusses the tax exemptions for a nonprofit organization’s fund-raising activities and provides several examples to illustrate the application of the regular place of business exclusion from the definition of “fund-raising activity.” In pertinent part, WAC 458-20-169(5)(g) reads as follows:

(iv) **Nonqualifying activities.** Fund-raising activity does not include the operation of a regular place of business in which services are provided or sales are made during regular hours such as a bookstore, thrift shop, restaurant, legal or health clinic, or similar business. It also does not include the operation of a regular place of business from which services are provided or performed during regular hours such as the provision of retail, personal, or professional services. A regular place of business and the regular hours of that business depend on the type of business being conducted.

...

(B) A nonprofit organization that makes catalog sales throughout the year with a twenty-four hour telephone line for taking orders has a regular place of business at the location where the sales orders are processed and regular hours of twenty-four hours a day. Catalog sales are not exempt as fund-raising amounts even though the funds are raised for a nonprofit purpose.

(C) A nonprofit group organized as a community playhouse has three plays during the year at a leased theatre. The plays run for a total of six weeks and the group provides concessions at each of the performances. The playhouse has a regular place of business with regular hours for that type of business. The concessions are done at that regular place of business during regular hours. The concessions are not exempt as fund-raising activities even though amounts raised from the concessions may be used to further the nonprofit purpose of that group.

(D) A nonprofit student group, that raises money for scholarships and other educational needs, sets up an espresso stand that is open for two hours every morning during the school year. The espresso stand is a regular place of business with regular hours for that type of business. The money earned from the espresso stand is not exempt, even though the amounts are raised to further the student group's nonprofit purpose.

WAC 458-20-169(5)(g). These examples show that a wide variety of business operations can qualify as a regular place of business and, in order to determine whether a nonprofit organization operates a regular place of business, we consider the type of business. For example, a nonprofit organization taking catalog orders over the phone does not need a storefront business location – only a business location at which the nonprofit organization is able to receive telephone orders and process the orders during regular hours for catalog orders. WAC 458-20-169(5)(g)(B).

Here, Taxpayer operates a web store to sell environmental commodity products and provides customer service via telephone and e-mail to support purchases of the environmental commodity products. Customers may purchase prepackaged environmental commodity products at any time in Taxpayer's web store. If a customer has questions or would like to purchase a custom package of environmental commodity products, the customer can request that one of Taxpayer's customer service representatives call or e-mail using an inquiry form or call a customer service representative during published regular business hours (Monday – Friday, 7 a.m. – 4 p.m. Pacific Time.). The ability to instantly purchase items in a web store, receive customer service during regular business hours, and request a written response to a purchase inquiry are all characteristics of a regular business in which sales are made during regular hours.

Taxpayer asserts that it was not operating a regular place of business in selling environmental commodity products because it did not have a location in Washington “. . . in which the sale, fulfillment, or customer service of environmental commodities [took] place.” This assertion implies a requirement that a nonprofit organization's business operations must have a Washington location in order to be a regular place of business. However, neither RCW 82.04.3651 nor WAC 458-20-169 require or even reference the physical location of a nonprofit organization's regular place of business. The examples in WAC 458-20-169(5)(g) make clear that we look to the type of business operations being conducted by the nonprofit organization to determine whether such an operation constitutes a regular place of business.

For the reasons explained above, we conclude that Taxpayer is operating a regular place of business with regular hours to sell environmental commodity products; therefore, Taxpayer's sales of environmental commodity products do not qualify as a fundraising activity that is exempt from B&O tax under RCW 82.04.3651. Accordingly, we sustain Audit's assessment of B&O tax.

Interest and Penalties

When the Department determines that a taxpayer has paid less tax than is properly due, the Department must assess the amount of underpaid tax along with interest. RCW 82.32.050(1). Similarly, the Department is required to assess a delinquent penalty when it has not received tax due by the due date and an assessment penalty where a taxpayer has substantially underpaid tax. RCW 82.32.090(1), (2). Tax is “substantially underpaid” when a taxpayer pays less than 80% of the tax due and the amount of the underpayment is at least \$1,000. RCW 82.32.090(2).

Here, Taxpayer did not pay any B&O tax during the Audit Period and Audit determined that Taxpayer should have paid \$. . . in service and other activities B&O tax. Audit assessed interest on this tax in accordance with RCW 82.32.050(1), delinquent penalties in accordance with RCW 82.32.090(1), and an assessment penalty in accordance with RCW 82.32.090(2). Taxpayer requests we cancel assessments of interest and penalties because Taxpayer relied in good faith on legal counsel in not reporting income and paying tax.

RCW 82.32.105(3) sets forth two criteria that allow the Department to cancel interest. It states:

The department shall waive or cancel interest imposed under this chapter if:

- (a) The failure to timely pay the tax was the direct result of written instructions given the taxpayer by the department; or
- (b) The extension of a due date for payment of an assessment of deficiency was not at the request of the taxpayer and was for the sole convenience of the department.

RCW 82.32.105(3). Here, Taxpayer does not assert and we have no evidence to suggest that Taxpayer's failure to pay B&O tax was the direct result of written instructions from the Department nor that the due date for payment of an assessment of deficiency was extended for the sole convenience of the Department. Accordingly, we sustain the assessments of interest because Taxpayer does not meet either criterion for cancellation in RCW 82.32.105(3).

RCW 82.32.105(1) sets forth the criterion that allows the Department to cancel penalties. It states:

If the department of revenue finds that the payment by a taxpayer of a tax less than properly due or the failure of a taxpayer to pay any tax by the due date was the result of circumstances beyond the control of the taxpayer, the department of revenue shall waive or cancel any penalties imposed under this chapter with respect to such tax.

RCW 82.32.105(1). "Circumstances beyond the control of the taxpayer are generally those which are immediate, unexpected, or in the nature of an emergency." WAC 458-20-228(9)(a)(ii). Mistakes or misconduct on the part of employees or other persons contracted with the taxpayer will generally not be considered a circumstance beyond the control of the taxpayer. WAC 458-20-228(9)(a)(iii)(E). Here, Taxpayer asserts that it relied in good faith upon advice from legal counsel in not reporting income and paying tax. However, this is not a circumstance beyond Taxpayer's control and provides no basis for the Department to cancel assessments of penalties under RCW 82.32.105(1), WAC 458-20-228(9)(a)(iii)(E); *see also* Det. No. 14-0179, 33 WTD 551 (2014) (Taxpayer's reliance on tax advice from a third party that it does not owe Washington taxes is not a basis for waiving the tax or penalties). Accordingly, we sustain the assessments of penalties.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 13th day of February 2017.