

Cite as Det. No. 17-0197, 38 WTD 126 (2019)

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. 17-0197
)	
...)	Registration No. . . .
)	

[1] RULE 19404; RCW 82.04.060: B&O TAX – SUBSTANTIAL NEXUS – RECEIPTS FROM THIS STATE – LOAN SERVICING FEES. To determine what constitutes “receipts from this state” for determining substantial nexus, the states apportionment rules govern. For loan servicing fees, the fees are attributed to Washington under Rule 19404 if the real property securing the loan being serviced is located in Washington.

[2] RULE 19404(3)(i)(i); RCW 82.04.645; SECTIONS 23A AND 23B OF THE FEDERAL RESERVE ACT: B&O TAX – ARMS LENGTH TRANSACTION – LOAN SERVICING FEES. Amounts are exempt from B&O tax under RCW 82.04.645 if received by a financial institution from an affiliated person in transactions that are required to be at arm’s length under sections 23A or 23B of the Federal Reserve Act. 23A and 23B of the Federal Reserve Act apply only to member banks.

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 loan servicer disputes the calculation of its apportionable income and the resulting assessment of service and other activities business and occupation (“B&O”) tax on several grounds. We deny in part¹

ISSUES

1. Whether certain receipts constitute “loan servicing fees” under WAC 458-20-19404, and were properly apportioned to the locations of the properties securing such loans.
2. Whether the amounts recorded under the account name “I/C Servicing Fee Revenue” (account # . . .) for 2013 and 2014, are exempt from B&O tax under RCW 82.04.645 as amounts received by a financial institution from an affiliated person in transactions that are required to

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

be at arm’s length under sections 23A or 23B of the Federal Reserve Act as existing on June 1, 2010.

FINDINGS OF FACT

. . . (“Taxpayer”) services mortgage loans for loan originators, government-sponsored entities (Fannie Mae, Ginnie Mae, Freddie Mac), and private trusts. It is licensed with the Washington State Department of Financial Institutions under Title 31 RCW and qualifies as a “financial institution” under WAC 458-20-19404. Taxpayer does business nationwide and has a license to service mortgage loans throughout the entire United States, the District of Columbia, and in two United States territories.

Account #	Fee Name	Description	Amount	Taxpayer’s Asserted Apportionment Method under WAC 458-20-19404
. . .	Late Charges Residential	Charges to borrowers when a scheduled payment is not received by the due date/within the courtesy period, defined in the mortgage note. The amounts of the late charges are set by the terms of the loans and can be a set amount or percentage of payment due.	\$. . .	(4)(j) Receipts from services.
. . .	Satisfaction Fees	Charges to borrowers for lien release and assignment recording services, release trustee services, 14 day/bailee note endorsement review services, advance county recording fees for recordation of releases, assignments, and POA.	\$. . .	(4)(j) Receipts from services.
. . .	Satisfaction Fees Recovered from Investors	Satisfaction fees recovered from investors or owners of loans.	\$. . .	(4)(j) Receipts from services.

...	Subordination Processing Fees	Charges to borrower for processing a 2 nd lien subordination request on a loan.	\$...	(4)(j) Receipts from services.
...	NSF Fees	Charges to borrower when a financial institution does not honor a payment, e.g., a check from a closed account or one with inadequate funds.	\$...	(4)(j) Receipts from services.
...	Fee for Service Income	Taxpayer states "Fee for Service Income." Additional information submitted in support of this assertion shows several journal entries for unknown reasons.	\$...	(4)(j) Receipts from services.
...	Disposition Fee Income	Fees earned on the sales of commercial real estate where Taxpayer sub-services the loans. The "disposition fee" is a percentage of the sale price for Taxpayer's help in facilitating the sale of the property.	\$...	(4)(j) Receipts from services.
...	File Fees from Corrs & Brokers	Charges to borrowers or brokers to set up loan servicing.	\$...	(4)(j) Receipts from services.
...	Payoff Quote Fees	Charges to borrowers to calculate and provide a payoff amount.	\$...	(4)(j) Receipts from services.
...	Payoff Fax Fees	Charges to borrowers to fax a payoff quote.	\$...	(4)(j) Receipts from services.
...	Fee for Recovery Services	"Fee for Recovery Services."	\$...	(4)(j) Receipts from services.
...	Deboarding Fees	-	\$...	(4)(j) Receipts from services.
...	HAMP Incentive Fee	See below.	\$...	(4)(j) Receipts from services.
...	HAMP Fee – Current Borrower	See below.	\$...	(4)(j) Receipts from services.
...	HAMP Fee – Pay for Success	See below.	\$...	(4)(j) Receipts from services.

...	[Payment Solution] Fees	See below.	\$. . .	(4)(j) Receipts from services.
...	REALRemit Fees	“REALRemit Fees.”	\$. . .	(4)(j) Receipts from services.

The Department’s Audit Division (“Audit”) reviewed Taxpayer’s books and records from January 1, 2011, to December 31, 2014 (the “Audit Period”). On October 29, 2015, Audit issued a \$. . . assessment against Taxpayer; it is comprised of \$. . . in service and other activities B&O tax, \$. . . in delinquent penalty, \$. . . in assessment penalty, and \$. . . in interest. Taxpayer disputes a majority of the loan servicing fees portion of the assessment (\$. . . in service and other activities B&O tax).

Audit determined that, during the Audit Period, Taxpayer received fees for servicing loans secured by real property, and apportioned such fees to Washington when the real property securing the loan was located in Washington. Audit calculated such apportionment using an apportionment percentage based on loan counts or unpaid principal balances.

Taxpayer disputes Audit’s determination that it received “loan servicing fees” and the apportionment methodology. It points to guidance contained in loan servicing handbooks published by Fannie Mae and Ginnie Mae and regulations published by the Federal Bureau of Consumer Financial Protection that conclude a loan servicing fee is typically a constant rate assessed on the unpaid mortgage balance, paid by the owner of the loan, from the interest portion. “Fannie Mae Servicing Guide” published October 14, 2015, A2-3-02: Servicing Fees for Portfolio and MBS Mortgage Loans; “Ginnie Mae Mortgage-Backed Securities Guide Handbook, 5500.3 Rev. 1, Chapter 6-3: Fees Received By The Issuer;” 12 C.F.R. Part 1026 [Docket No. CFPB-2012-0033] RIN 3170-AA14, Mortgage Servicing Rules under the Truth in Lending Act (Regulation Z).

In general, Taxpayer asserts that the disputed fees are ancillary fees for services, and not loan servicing fees. Dozens of different fees comprise the loan servicing fees portion of the assessment. In many cases, Taxpayer raises objections specific to each type [of fee]. The following are charts of the disputed loan servicing fees (apportioned by loan count and loan unpaid principal balance), that list the account number, name, description, pre-apportionment amount, and Taxpayer’s asserted method of apportionment.

Disputed Loan Servicing Fees Apportioned by Loan Count

HAMP Fees (. . .)

HAMP is an acronym for “Home Affordable Modification Program.” In 2009, the United States Department of the Treasury and the United States Department of Housing and Urban Development developed a program to mitigate the home foreclosure crisis that followed the start of the Great Recession in 2008. Fannie Mae administered the program and provided financial incentives for lenders and loan servicers to adopt federally-designed, default management and loan modification processes, to lower monthly mortgage payments, defaults, and foreclosures. Taxpayer was required to participate, because it serviced loans owned or guaranteed by Fannie Mae and Freddie

Mac and entered into a servicing agreement with Fannie Mae that governed the terms of its participation in the HAMP program.

An eligible borrower, with a documented hardship, could apply for a HAMP modification (to interest rate or other terms) that served to reduce the borrower's monthly payment as a percentage of the borrower's monthly income. If the borrower was eligible for a HAMP modification, the borrower and loan servicer would modify the loan for a three-month trial period. Should the borrower make all trial period payments on time, the HAMP modification became permanent. HAMP prohibits loan servicers from charging borrowers a fee to modify the terms of the loan and restricts the amount of delinquency fees that loan servicers may charge and capitalize as part of the modification.

Taxpayer, as a participating loan servicer, agreed to review every request for HAMP modification consideration from potentially eligible borrowers and not proceed with foreclosure sales on HAMP eligible loans until it evaluated the borrowers for a HAMP modification. Taxpayer also agreed to provide clear and frequent communications to borrowers about the modification process, attain certain financial targets on the loan modification, and make regular reports to Fannie Mae. In turn, Fannie Mae paid Taxpayer the following amounts:

- (1) *HAMP Incentive Fee* (. . .): A one-time payment made in the first month of permanent HAMP modification of a loan. The payment amount is dependent upon the type of entity that owns the loan, the borrower's status when the trial period (for the HAMP modification) begins, and the month in which the trial period [began].
- (2) *HAMP Fee - Current Borrower* (. . .): A one-time payment made when a borrower successfully completes the trial period and that borrower was current on loan payments when the trial period began.
- (3) *HAMP Fee Pay for Success* (. . .): An annual payment, for up to three years, made when a HAMP modification reduced a borrower's monthly housing costs by at least 6% and the borrower remains in good standing while making the HAMP modified payment amount.

Borrowers also receive a financial incentive for participating in HAMP. For the first five years, a borrower in good standing may receive up to \$1,000, annually, towards the balance of the loan at the end of the year, and in the sixth year, the borrower may receive a one-time balance reduction of \$5,000.

Taxpayer asserts that the HAMP incentive payments reward the servicer for creating new internal default management and loan modification systems and are not loan servicing fees because they are predicated on an entirely separate contractual agreement (the HAMP servicing agreement), received from the Federal government, and serve a fundamentally different purpose.

[Payment Solution] Fees (. . .)

Taxpayer partnered with . . . to offer borrowers "[Payment Solution]," an automated ACH bank account withdrawal payment option. Borrowers make [Payment Solution] payments online or via

telephone to avoid the delay of sending payment through the mail. . . . processes and settles all [Payment Solution] payments and then transfers such payments to Taxpayer.

. . . charges borrowers a separate processing fee for making a payment using [Payment Solution]. Taxpayer receives a portion of the separate [Payment Solution] processing fee; these are the amounts at issue.

Taxpayer states that the [Payment Solution] fees are incentives or commissions for marketing and referring borrowers to make payments using [Payment Solution]. Taxpayer asserts that such amounts should not be considered a loan servicing fee because the amounts are not connected to any contract or exchange between the loan owner and Taxpayer and received in exchange for providing separate stand-alone marketing and referral services.

Disputed Loan Servicing Fees Apportioned by Loans' Unpaid Principal Balances

Account #	Fee Name	Description	Total Amount (for entire Audit Period)	Taxpayer's Asserted Apportionment Method under WAC 458-20-19404
. . .	Interest Inc. – Advance Facility	“Interest on advance facility.”	\$. . .	(4)(c) Interest from loans not secured by real property.
. . .	Gain on Sale of LIHTC	Gain on sale of low income housing tax credit.	\$. . .	<i>Excluded</i> (3)(i)(iii) under annual net gain/(loss) calculation.
. . .	Resolution Discount Income	“Resolution Discount Income.”	\$. . .	(4)(j) Receipts from services.
. . .	Gain/(Loss) on Sale of GNMA Repurchases	Gain/loss on sale of GNMA loans that are repurchased and modified before selling.	\$. . .	(4)(d) Net gains from the sales of loans.
. . .	Other Income	“Other income from miscellaneous service activities.”	\$. . .	(4)(j) Receipts from services.
. . .	Commission Income	Referral commissions from brokers for real estate owned properties sold.	\$. . .	(4)(j) Receipts from services.
. . .	Gain/(loss) on Sale of Loans	Gain/loss on sale of mortgage loans.	\$	(4)(d) Net gains from the sales of loans.

...	Misc. Servicing Fee Income	[Payment Solution] commissions (detailed above).	\$	(4)(j) Receipts from services.
...	Fee Income – from Syndicated Projects	“Fee Income – from Syndicated Projects.”	\$. . .	(4)(j) Receipts from services.
...	Interest Income P&I/T&I \$Held At Other	Interest income from [banks] on borrower escrow accounts that hold property taxes and homeowners insurance prior to payment.	\$. . .	(4)(k) Receipts from investment assets and activities and trading assets and activities.
...	Special Serv Fee – Phase I&II	“Special Serv Fee – Phase I&II.”	\$. . .	(4)(j) Receipts from services.
...	Bankruptcy Interest Fees	“Bankruptcy Interest Fees.”	\$. . .	(4)(j) Receipts from services.
...	Other Fees – Servicing	Loan setup fees, deboarding fees, liquidation fees, residual interest, and miscellaneous fees related to [LLC] borrowers that Taxpayer services.	\$. . .	(4)(j) Receipts from services.
...	Service Fee Adjustments	Additional service fee charges from borrowers due to interest rate and date changes from loan modifications.	\$	(4)(j) Receipts from services.
...	MIC/ A/H/L Insurance Fee	“MIC J A/H/L Insurance Fee.”	\$. . .	(4)(j) Receipts from services.
...	Miscellaneous Other Revenue	“Miscellaneous income.”	\$. . .	(4)(j) Receipts from services.
...	I/C Loss on Sale of Advances	Loss on sale of servicing advance rights to affiliated entity.	(\$. .)	<i>Excluded</i> (3)(i)(iii) under annual net gain/(loss) calculation.
...	Gain on debt repurchases	Sales of mortgage servicing rights to third party.	\$. . .	<i>Excluded</i> (3)(i)(iii) under annual net gain/(loss) calculation.

Affiliate Payments

Taxpayer asserts that the 2013 and 2014 amounts (recorded below) are affiliate payments exempt from taxation under RCW 82.04.645.

Account #	Fee Name	2011	2012	2013	2014
...	I/C Servicing Fee Revenue	\$...	\$...	\$...	\$...

... (“[Mortgage Servicing]”) owns Taxpayer, and ... (“[Financial Corp]”) owns [Mortgage Servicing] and ... (“[Mortgage Solution]”).

In 2013, Taxpayer entered into two “Subservicing Agreements” with [Mortgage Solution] whereby Taxpayer agreed to service certain residential mortgage loans on behalf of [Mortgage Solution] in exchange for a percentage (90% for one such agreement and 40% for the other) of [Mortgage Solution’s] servicing fees on such residential mortgage loans. Taxpayer retains the agreed percentage of [Mortgage Solution’s] servicing fees and forwards remaining percentage on to [Mortgage Solution]. Taxpayer states that it records the subservicing fees at arm’s length in accordance with GAAP requirements governing the specific type of subservicing arrangements.

ANALYSIS

“There is levied and collected from every person that has a substantial nexus with this state [Washington] a tax for the act or privilege of engaging in business activities.” RCW 82.04.220.² This is the business and occupation tax (“B&O” as defined above), and it is measured by applying particular rates against the value of the products, gross proceeds of sales, or gross income of the business as the case may be. *Id.*

Persons engaging in business activities not otherwise classified in Chapter 82.04 RCW are subject to the service and other activities B&O tax measured by the gross income or gross proceeds of sales of the business. RCW 82.04.290(2)(a). Here, Taxpayer engages in loan servicing, and this business activity is not otherwise classified in Chapter 82.04 RCW, so Audit assessed service and other activities B&O tax. Taxpayer does not dispute this tax classification but does dispute the amount of its gross income of the business, subject to tax.

RCW 82.04.080 defines “gross income of the business” broadly and reads as follows:

- (1) “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, gains realized from trading in stocks, bonds, or other evidences of indebtedness, interest, discount, rents,

² RCW 82.04.030 defines “person” to include corporations, limited liability companies, associations, and any group individuals acting as a unit, whether nonprofit, or otherwise. “Engaging in business” in Washington means “commencing, conducting, or continuing in business.” RCW 82.04.150. “Business” is defined as including “all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or another person” RCW 82.04.140.

royalties, fees, commissions, dividends, and other emoluments however designated all without 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.

“Gross income of the business” includes “apportionable income.” RCW 82.04.460(1). “Apportionable income” is gross income of the business generated from engaging in apportionable activities inside and outside of Washington, and “apportionable activities” include those business activities taxed under the service and other activities B&O tax classification. RCW 82.04.460(4)(a)(vi). Because Taxpayer engages in business activities taxed under the service and other activities B&O tax classification inside and outside of Washington, it engages in apportionable activities and has apportionable income. Taxpayer disputes the amount of apportionable income included in its gross income of the business during the Audit Period and the resulting assessment [of] service and other activities B&O tax.

WAC 458-20-19404

WAC 458-20-19404 is the Department’s rule that provides the method for apportioning the apportionable income of financial institutions. RCW 82.04.460(2), WAC 458-20-19404.³ It states that a financial institution determines the amount of apportionable income that it must report in Washington by multiplying total (worldwide) apportionable income by the “apportionment percentage.” WAC 458-20-19404(2)(b). The taxpayer’s “receipts factor” determines the apportionment percentage. *Id.*

WAC 458-20-19404(4) explains how to calculate the “receipts factor.” In general:

The receipts factor is a fraction, the numerator of which is the apportionable income of the taxpayer in this state during the taxable period and the denominator of which is the apportionable income of the taxpayer inside and outside this state during the taxable period. The method of calculating receipts for purposes of the denominator is the same as the method used in determining receipts for purposes of the numerator.

WAC 458-20-19404(4)(a). WAC 458-20-19404(4) then applies this general formula and specifically explains how to calculate the receipts factors for the following types of income, common to financial institutions: interest from loans secured by real property; interest from loans not secured by real property; net gains from the sale of loans; receipts from credit card receivables; net gains from the sale of credit card receivables; credit card issuer’s reimbursement fees; receipts from merchant discount; loan servicing fees; receipts from services; and receipts from investment assets and activities and trading assets and activities. WAC 458-20-19404(4)(b)-(k).

³ [The present version of WAC 458-20-19404 applies only to periods beginning January 1, 2016. WAC 458-20-19404A is the current rule that addresses how gross income must be apportioned for financial institutions during the period of June 1, 2010, to December 31, 2015.]

Taxpayer disputes Audit’s apportionment of several fees as loan servicing fees and challenges Audit’s determination that the fees are loan servicing fees. Taxpayer asserts that such fees are other types of income, properly apportioned under different subsections of WAC 458-20-19404(4). The following chart summarizes the differences between relevant receipts factors (those calculated by Audit and those Taxpayer asserts we should substitute for Audit’s apportionment method)[, as set forth under WAC 458-20-19404(4)].

Item of Income	Numerator	Denominator
(b) Interest from loans secured by real property	Interest and fees or penalties in the nature of interest from loans secured by WA real property.	Interest and fees or penalties in the nature of interest from loans secured by all real property.
(c) Interest from loans not secured by real property.	Interest and fees or penalties in the nature of interest from loans not secured by real property where borrower located in WA.	Interest and fees or penalties in the nature of interest from all loans not secured by real property.
(d) Net gains from the sale of loans.	Washington net gains from the sale of loans, calculated by multiplying all net gains from the sale loans by either the receipts factor for, interest from loans secured by real property (subsection b) or interest from loans not secured by real property (subsection c).	Net gains from the sale of loans (both, secured and not secured by real property).
(i) Loan servicing fees.	<p>If Taxpayer is servicing its own loans: Washington loan servicing fees, calculated by multiplying all loan servicing fees by either the receipts factor for, interest from loans secured by real property (subsection b) or interest from loans not secured by real property (subsection c).</p> <p>If Taxpayer is servicing the loans of another: Loans servicing fees of such loans where the borrower is located in Washington.</p>	All loan servicing fees.
(j) Receipts from services.	Receipts from services not otherwise apportioned if the service is performed if WA.	All receipts for services.

We must first determine whether the fees at issue constitute loan servicing fees. If we conclude they do, then our inquiry ends and we sustain Audit's apportionment method using the loan servicing fees receipt factor. If we conclude the fees at issue are not loan servicing fees, then we must categorize the income into one of the other types of income listed in WAC 458-20-19404(4) to determine the proper receipt factor and apportionment.

Loan Servicing Fees

Neither WAC 458-20-19404 nor Title 82 RCW define "loan servicing fees." However, Chapter 31.04 RCW titled "Consumer Loan Act" defines "Service or servicing a loan" to mean:

[O]n behalf of the lender or investor of a residential mortgage loan: (a) Collecting or receiving payments on existing obligations due; (b) collecting fees due to the servicer; (c) working with the borrower and the licensed lender or servicer to collect data and make decisions necessary to modify certain terms of those obligations either temporarily or permanently; (d) otherwise finalizing collection through the foreclosure process; or (e) servicing a reverse mortgage loan.

RCW 31.04.015(28); *see also* RCW 31.04.025(1) ("Each loan made to a resident of this state by a licensee, or persons subject to this chapter, is subject to the authority and restrictions of this chapter.").

The Financial Accounting Standards Board ("FASB") has published accounting and reporting standards for the servicing of financial assets and liabilities. FASB ASC 860-50 states, in pertinent part, as follows:

Servicing of mortgage loans, credit card receivables, or other financial assets commonly includes but is not limited to the following activities:

- a. Collecting principal, interest, and escrow payments from borrowers
- b. Paying taxes and insurance from escrowed funds
- c. Monitoring delinquencies
- d. Executing foreclosure if necessary
- e. Temporarily investing funds pending distribution
- f. Remitting fees to guarantors, trustees, and others providing services
- g. Accounting for and remitting principal and interest payments to the holders of beneficial interests or participating interests in the financial assets

A servicer of financial assets commonly receives the following benefits of servicing:

- a. Revenues from contractually specified servicing fees
- b. A portion of the interest from the financial assets
- c. Late charges
- d. Other ancillary sources, including float.

A servicer is entitled to receive all of those benefits of servicing only if it perform the servicing and incurs the costs of servicing the financial assets.

Taxpayer challenges whether Audit correctly classified the fees above as “loan servicing fees.”

RCW 82.32.070(1) requires a taxpayer to keep and preserve, for a period of five years, those records as may be necessary to determine the amount of any tax for which the taxpayer may be liable. All of a taxpayer’s books, records, and invoices must be open for examination at any time by the Department. *Id.* Should a taxpayer fail or refuse to make such records available for examination, the Department shall proceed in the manner as it may deem best. RCW 82.32.100(1). This means that Taxpayer is required to keep and present the Department with records that show how to apportion the disputed accounts because such apportionment is necessary to determine the amount of tax due.

The disputed accounts fall into two categories: (1) Insufficient records; or (2) sufficient records. We briefly discuss those disputed accounts where Taxpayer has provided insufficient records before weighing Taxpayer’s substantive arguments for those accounts where Taxpayer has provided sufficient records to understand the activity of the account.

Insufficient Records

For the following accounts, Taxpayer provided nothing more than the account title as the description: . . . – Fee for Recovery Services, . . . – Deboarding Fees, . . . – REALRemit Fees, . . . – Interest Inc Advance Facility, . . . Resolution Discount Income, . . . – Other Income, . . . – Gain/(loss) on Sale of Loans, . . . – Fee Income from Syndicated Projects, . . . – Special Serv Fee Phase I&II, . . . – MIC/A/H/L Insurance Fee, . . . – Miscellaneous Other Revenue. The account title is insufficient to determine who is paying Taxpayer, the amounts of the payments, and the reasons for the payments. We conclude these records are insufficient to show that the amounts in such accounts were not loan servicing fees and warrant adjustment.

Taxpayer provided a more detailed description for the following accounts: . . . – Satisfaction Fees Recovered from Investors; . . . – Fee for Service Income; . . . – Disposition Fee Income; . . . – Gain/(Loss) on Sale of GNMA Repurchases; . . . – Commission Income; . . . Gain/(loss) on Sale of Loans; . . . Bankruptcy Interest Fees; . . . – Gain on Sale of LIHTC; . . . – I/C Loss on Sale of Advances; . . . – Gain on debt repurchases. However, even with more details, we are unable to determine who is paying Taxpayer, the amounts of the payments, and the reasons for the payments. For example, it is not clear who are Taxpayer’s investors paying satisfaction fees or why Taxpayer is selling loans when it is a loan servicer or the sources of bankruptcy interest fee. Accordingly, we conclude these records are insufficient to show that the amounts in such accounts were not loan servicing fees and warrant adjustment.

Sufficient Records

We now consider Taxpayer’s substantive assertions with respect to the following accounts where Taxpayer has provided sufficient information for the Department to understand who paid Taxpayer, what amounts, and the reasons for the payments: . . . – Late Charges Residential; . . . – Satisfaction Fees; . . . – Subordination Processing Fees; . . . – NSF Fees; . . . – File Fees from Corrs & Brokers; . . . – Payoff Quote Fees; . . . – Payoff Fax Fees; . . . – Other Fees Servicing; . . . – Service Fee Adjustments; . . . – HAMP Incentive Fee; . . . – HAMP Fee Current Borrower; . . .

HAMP Fee Pay for Success; 853. . .15000 – [Payment Solution] Fees; . . . – Misc. Servicing Fee Income ([Payment Solution]); . . . – Interest Income P&I/T&I \$Held at Other; . . . – Assurant Revenues.

- Late charges, satisfaction fees, subordination processing fees, NSF fees, file fees, payoff quote and fact fees, other servicing fees, and service fee adjustments: This first group of accounts clearly fall under FASB ASC 860-50 as loan servicing fees. FASB ASC 860-50 actually lists late charges as a benefit of loan servicing. The remaining charges for satisfaction, processing, NSF, filing, payoff quotes and faxes, other servicing fees, and service fee adjustments, all fit within the category of other ancillary sources of income from loan servicing because they stem from the listed activities that are included in loan servicing. These fees represent revenues from Taxpayer's activities in collecting principal, interest, and escrow payments and monitoring delinquencies. Thus, we conclude these are loan servicing fees.
- HAMP fees: Taxpayer asserts these fees are to be distinguished from other loan servicing fees because the Federal government paid these fees as part of a government program to modify home loans and meet a policy objective of President Obama. We are unpersuaded. We are unaware and Taxpayer points to no authority that requires borrowers to pay loan servicing fees; thus we are not persuaded that the HAMP fees are to be distinguished from other loan servicing fees on that basis. While we do not doubt that the HAMP program served a government policy objective, this does not take away from the fact that Taxpayer earned these fees for modifying its collection of principal, interest, and escrow payments and monitoring post-modification delinquencies. These are activities that are commonly included in loan servicing. FASB ASC 860-50. Thus, we conclude these HAMP fees are loan servicing fees.
- [Payment Solution] Fees: Taxpayer asserts that it received [Payment Solution] processing fees in exchange for marketing the payment processing platform. We are unpersuaded based on the information currently available. The [Payment Solution] processing fees are a convenience fee – similar to those charged with respect to credit card processing. Taxpayer keeping some of this fee does not change the nature of the charge, and it appears the portion of the fee passed on to Taxpayer serves to compensate Taxpayer for processing a [Payment Solution] payment (instead of simply processing a check). . . . Fees for collecting borrower payments is listed as an activity commonly included in loan servicing; thus, we conclude that [Payment Solution] payments are loan servicing fees.
- Interest income on amounts held for payment of property taxes and insurance: Taxpayer asserts that we should apportion interest received on amounts held in escrow for the payment of borrower's property taxes and insurance as investment assets. We disagree. Trading assets are a collection of securities held by a firm that are held for the purpose of reselling for a profit and recorded in a separate account. <http://www.investopedia.com/terms/t/trading-assets.asp> (August 2, 2017). In contrast, Taxpayer collects payments of borrowers' property taxes and insurance and puts these amounts into an escrow account for a short period of time, until the payment of these items is due. Taxpayer does not hold the escrow accounts for the purposes of making a profit;

[rather,] it charges borrowers the exact amount due to cover property tax and insurance expenses. Further, the escrow accounts are not recorded in a separate account for trading. FASB ASC 860-50 includes paying property taxes and insurance from escrowed funds in those activities commonly included in loan servicing. Because the interest stems from a common loan servicing activity, we conclude the interest income on amounts held for payment of property taxes and insurance are loan servicing fees.

We deny Taxpayer's petition as to this issue.

Amounts Received from Certain Affiliated Persons

Taxpayer asserts that the amounts recorded in "I/C Servicing Fee Revenue" (. . .) are certain affiliate payments exempt from B&O tax under RCW 82.04.645. RCW 82.04.645 reads as follows:

(1) This chapter does not apply to amounts received by a financial institution from an affiliated person if the amounts are received from transactions that are required to be at arm's length under sections 23A or 23B of the federal reserve act as existing on June 1, 2010, or such subsequent dates as may be provided by the department by rule, consistent with the purposes of this section. For purposes of this subsection, "financial institution" has the same meaning as in RCW 82.04.080.

(2) As used in this section, "affiliated" means under common control. "Control" means the possession, directly or indirectly, of more than fifty percent of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting shares, by contract, or otherwise.

Thus, there are three requirements to qualify for the certain affiliate payments exemption: (1) The recipient of the payment is a "financial institution"; (2) the payor is an "affiliated" person; and (3) the recipient receives the payment in a transaction that is required to be at arm's length under section 23A or 23B of the Federal Reserve Act.

Taxpayer is a "financial institution" because it is licensed under Title 31 RCW. [See Rule 19404(3)(i)(i).] OFC owns both Taxpayer (recipient) and [Mortgage Solution] (payor) and this common control means they are "affiliated." We must determine whether Taxpayer's subservicing of [Mortgage Solution's] loans is a transaction that is required to be at arm's length under sections 23A or 23B of the Federal Reserve Act.

The Federal Reserve Act is "An Act to provide for the establishment of Federal reserve banks, to furnish an elastic currency, to afford means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes." <https://www.federalreserve.gov/aboutthefed/officialtitle-preamble.htm> (July 31, 2017). Section 23A concerns relations with affiliates and section 23B concerns restrictions on transactions with affiliates. <https://www.federalreserve.gov/aboutthefed/section23a.htm> (July 31, 2017) codified at 12 U.S.C. §371c, <https://www.federalreserve.gov/aboutthefed/section23b.htm> (July 31, 2017) codified at 12 U.S.C. §371c-1.

Both sections are restricted in their application and apply only to member banks. 12 U.S.C. §371c(a)(1) (“A member bank and its subsidiaries may engage in a covered transaction with an affiliate only if . . .”); 12 U.S.C. §371c-1(a)(1) (“A member bank and its subsidiaries may engage in any of the transactions described in paragraph (2) only . . .”); *see also* 12 U.S.C. §371c(b)(1) (“the term ‘affiliate’ with respect to a member bank means . . .”), (b)(7) (“the term ‘covered transaction’ means with respect to an affiliate of a member bank . . .”). [“Member bank” means “any national bank, State bank, or bank or trust company which has become a member of one of the Federal reserve banks.” 12 U.S.C. § 221.] “The term ‘bank’ includes a State bank, national bank, banking association, and trust company.” 12 U.S.C. §371c(b)(5).

Taxpayer is not a member bank. Therefore, sections 23A and 23B of the Federal Reserve Act do not apply to Taxpayer Accordingly, we conclude that Taxpayer has failed to show that the amounts recorded in “I/C Servicing Fee Revenue” (. . .) are exempt from B&O tax under RCW 82.04.645. We deny Taxpayer’s petition as to this issue.

DECISION AND DISPOSITION

Taxpayer’s petition is denied.

Dated this 3rd day of August 2017.