

Cite as Det. No. 20-0165, 41 WTD 160 (2022)

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. 20-0165
)	
...)	Registration No. . . .
)	

[1] RCW 82.32.070; WAC 458-20-254: RECORDS TO BE PRESERVED. Whether there is a reasonable basis to use a different attribution method for some of the services the taxpayer provided depends on the requisite records.

[2] RCW 82.04.460; RCW 82.04.462; WAC 458-20-19402: APPORTIONABLE INCOME. The taxpayer provided to its affiliates credit card account services and all services necessary for the affiliates to create and maintain a market for their credit card services in Washington. Therefore, the affiliates received the benefit of the taxpayer’s credit card related services at the cardholders’ locations.

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.

Callahan, T.R.O. – A corporation that provided various services to its affiliates, which the parties group into three broad categories (credit card services, administrative services, and database services), protests the assessment of service and other activities business and occupation (B&O) tax on these services. The corporation argues that none of its gross income is attributable to Washington and, therefore, it should have no tax liability in Washington. We deny the petition.¹

ISSUES

1. Whether a corporation that provides different services to its affiliates has provided sufficient documentation under RCW 82.32.070 and WAC 458-20-254 to show that the services it provided should be apportioned separately under RCW 82.04.460, RCW 82.04.462, and WAC 458-20-19402 (Rule 19402).
2. Under RCW 82.04.460, RCW 82.04.462, and Rule 19402, whether for apportionment purposes, the benefit received for [a corporation’s] services that enable its affiliates to extend

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

credit is the location of the corporation's affiliates or where [the affiliates] extend [credit to their customers].

FINDINGS OF FACT

. . . (Taxpayer) is a corporation based [out of state] that provides services to affiliated entities. Taxpayer does not have property or employees in Washington State.

The Department's Audit Division (Audit) examined Taxpayer's records for the period of . . . (Audit Period). During [the Audit Period], Taxpayer and its affiliates, [Affiliate A] and [Affiliate B] (Affiliates), entered into service agreements (Service Agreements) where Taxpayer provided three broad categories of services to Affiliates: credit card account services, administrative services, and database services. . . . Affiliates are headquartered outside of Washington State. . . .

On August 15, 2016, Audit issued an assessment (Assessment) against Taxpayer for the Audit Period for \$. . . . The Assessment consists of service and other activities B&O tax of \$. . . . , a delinquent penalty of \$. . . . , interest of \$. . . . , and a five percent assessment penalty of \$. . . .

Taxpayer did not pay the Assessment. On September 13, 2016, Taxpayer petitioned for correction of the Assessment under WAC 458-20-100. At issue is whether Taxpayer's apportionable income from providing services to Affiliates is attributable to Washington State.

Taxpayer did not provide the Service Agreements to the Department, but did allow Audit to review them during its review. Taxpayer provided Appendix A and Appendix A-1 to the Service Agreements on review, which provide some description of the services it provides the Affiliates. Under the Service Agreements, Taxpayer charged Affiliates a flat monthly fee for each credit card statement Taxpayer issued to Affiliates' customers (Cardholders) on behalf of Affiliates. The monthly flat fees Affiliates paid to Taxpayer encompassed payment for all of the services Taxpayer provided its Affiliates. . . .

Based on the information provided by Taxpayer, it appears that Taxpayer provided the majority of the services necessary for the Affiliates to operate their businesses. As explained above, Taxpayer grouped these services as follows in Appendix A and Appendix A-1:

1) *Credit Card Account Services:*

The credit card account services Taxpayer provided included the following services:

- New Account Processing: receiving and processing Cardholders' applications via mail, fax, or electronic media. Including approving credit scoring and denying credit card applications.
- Application Development: managing and maintaining applications processing and product enhancements.
- Customer Service: processing all customer inquiries, responding to billing inquiries, account disputes and adjustments, and billing error resolution.

- Collections: managing collection of overdue accounts, managing special account processing including bankruptcy and fraud, and managing collection agencies and law firms retained to collect overdue accounts.
- Data Processing: managing processing platforms, including day-to-day operation, backups and maintenance, and disaster recovery.
- Enhancement Services: managing marketing services to Cardholders through periodic communications mediums, such as billing statements and telephone communications.
- Direct Marketing: developing marketing programs to acquire new Cardholders, increasing sales from existing Cardholders, or activating Cardholders who have become inactive.
- Sales Support: providing sales development and support on behalf of Affiliates.
- Credit Relationship Management: providing relationship management staff to support day-to-day management of Affiliates' customer relationship with the Cardholders.
- Credit Operations Support: providing strategic credit operations support for all call center operations.
- Card Embossing and Issuance: including end-to-end processing of card embossing requests.
- Payment Remittance Processing: providing secure processing of Cardholder remittances.
- Statement Issuance: producing and mailing all Cardholder communications from Affiliates.

2) *Administrative Services:*

The administrative services Taxpayer provided included the following services:

- Local Area Network and Telecommunication Support: providing network and telecommunication access.
- Information Security Support: providing technologies to protect client/customer data from illegal acquisition.
- Desktop/PC Support: providing hardware, software and support to ensure continuous functioning.
- Contingency Planning: assisting management in planning for a shut down or disruption in business, as required by Affiliates.
- Accounting Services: providing services similar to financial services provided by an internal accounting department, including but not limited to daily posting of transactions, daily general ledger production, timely account reconciliation within an acceptable materiality factor as determined by Affiliates and timely preparation of monthly financial and quarterly regulatory reports.
- Tax Services: providing services similar to tax related services provided by an internal tax department, including but not limited to computing, paying, and recording all tax obligations of Affiliates; making appropriate filings in the appropriate taxing jurisdictions; and advising Affiliates on how to lawfully reduce its tax obligations.
- Accounts Payable: providing services related to timely payment of invoices.
- Legal and Compliance: providing services related to the interpretation and application of federal, state, and local rules, laws and regulations to activities conducted by

- Affiliates and proactive monitoring of proposed rules, laws, and regulations, and ongoing implementation.
- Audit Services: providing audit services in accordance with Affiliates' Policies.
 - Security: providing physical security for the buildings owned or occupied by Affiliates.
 - Treasury Services: providing certificate of deposit administration, cash management, and funds transfer related services.
 - Disaster Recovery Services: providing disaster recovery services to Affiliates by providing an alternative site for Affiliates' headquarters personnel in the event that Affiliates' locations are inaccessible or inoperable.
 - Human Resources: assisting recruiting, management of staff and management of benefits available to Affiliates' associates.
 - Strategic Planning Support: support in setting Affiliates' direction, as requested.
 - Business Planning Support: support in setting the business Affiliates offered, as requested.
 - Facilities Management: assisting with management of Affiliates' premises and its contents.
 - Mail services, safety services, purchasing Affiliates' office supplies and materials, assisting services related to Affiliates' business travel, project management as requested by Affiliates, and assisting in managing media contact.

3) *Database Services:*

The database services Taxpayer provided included the following services:

- Database Systems: providing a Database System to collect and store Affiliates' data supplied by Affiliates. The data consists of information related to Cardholders, accounts, transactions, billing information, and other data.
- Data Warehouse and Other Sources: housing Affiliates' data warehouse that contains third party data sources.
- Audits: performing data audits and executing process controls to ensure Affiliates' data integrity is maintained.
- Data Mart Maintenance Update and Specialized Data Mart: providing maintenance and weekly updates.
- Support: providing 24/7 production support for the standard processing.
- Campaign Management: providing Cardholder names sorting and selecting to specified criteria for the purpose of performing a direct marketing campaign.
- Data Distribution Reports: completing audit reports after the weekly update process is complete.
- Data Updates: updating data weekly regarding new and changed Cardholders accounts, billing information, and new transactions. Updating data semi-annually regarding accounts that are required by a third party.

Taxpayer did not provide a breakdown of its fees charged for the respective services. The amount charged to the Affiliates for its services is based on operating costs accrued by Taxpayer.¹¹ Taxpayer determined this fee by calculating its budgeted operating costs for the upcoming year and dividing the total by the estimated number of statements that it expected to issue in the

corresponding year. Taxpayer would true up the numbers for the previous year when it reconciled actual and budgeted operating expenses.

Taxpayer did not issue invoices to Affiliates for the monthly fees received, but instead recorded the fees received as intercompany transactions on Taxpayer's books. Taxpayer recognized the monthly fees received from each Affiliate in one revenue account recorded as [Account 1] on Taxpayer's books. Taxpayer did not further breakdown this revenue into the type of service provided to Affiliates. Affiliates recognized the monthly fees paid to Taxpayer as a servicing expense in an expense account recorded as [Account 2] on Affiliates' books. The intercompany service fee calculation worksheets provide the details of Taxpayer's revenue and expense entries on its books, which showed the number of statements Taxpayer generated for each Cardholder, on behalf of Affiliates on a monthly basis.

Audit determined that the benefit of Taxpayer's services was received at the Cardholders' locations and [attributed] Taxpayer's income among the states based on the billing addresses of the Cardholders. Audit decided that since the statements Taxpayer issued to the Cardholders on behalf of Affiliates were an indicator of the number of accounts being serviced, Taxpayer's income pertaining to the administrative services and database services are therefore directly tied to servicing the credit card accounts, as indicated by the fee structure.

Taxpayer argues that the amounts from providing the credit card account services, the administrative services and the database services should be allocated to Affiliates' corporate domicile, where the Affiliates received the benefit of the services. Taxpayer . . . contends that its services to Washington Cardholders are not attributed to Washington under Rule 19402(305) [applicable to services related to extension of credit by nonfinancial institutions,] because Taxpayer did not issue credit cards. Taxpayer relies on *Lutheran Brotherhood Research Corp. v. Comm'r of Revenue*, 656 N.W. 2d 375 (Minn. 2003), and argues that income from providing the credit card account services should be attributed to Affiliates' locations, rather than the location of the Cardholders.

With respect to the administrative services and the database services, Taxpayer argues that Det. No. 17-0210, 37 WTD 076 (2018), and *Lutheran Brotherhood* support its position that income from providing administrative services and database services (which it refers to as back office services) should be attributed to Affiliates' locations as well. Taxpayer asserts that the Department concluded in 37 WTD 076 that attributing income from providing shared corporate officers, support staff, and human resources services, to the taxpayer's affiliates' customer locations was not reasonable. Taxpayer contends that likewise, in *Lutheran Brotherhood*, the Minnesota Supreme Court held that investment management services provided to the investment fund manager should be attributed to the location of the investment managers and not the investors.

Specifically regarding the database services, Taxpayer relies on the examples provided in Rule 19402 to show that the database services are back office services provided to Affiliates and are not related to the credit card account services. Taxpayer relies on Examples 17 and 18, which provide that debt collection service income is attributed to where the debtors are located.¹ The other examples Taxpayer relies on are Examples 24 and 25, where income for providing human resources services or general management services is attributed to the customer's location.

Taxpayer's Proposed Allocation Method:

Taxpayer also argues that the administrative services and the database services represented a substantial portion of the services it provided to Affiliates and are not related to the Cardholders, and therefore should be attributed to Affiliates' locations under Rule 19402. Taxpayer asserts that according to its operating expenses schedules, [half] of its expenses were for performing the administrative services and the database services to Affiliates during [the Audit Period]. In support of its argument, Taxpayer provided summaries of its operating expenses, payroll and benefit details for [the Audit Period] by cost center. These summaries attempt to break down its gross receipts by using its office locations, designated as providing "cardholder facing" versus "non-cardholder facing" expenses, to calculate a percentage. Taxpayer did not provide a further breakdown of its operating expenses for each category of service provided in Appendix A and Appendix A-1 of the Service Agreement.

On review, we asked Taxpayer to produce documents to substantiate its claimed percentages of administrative services and database services provided to Affiliates [during the Audit Period]. However, Taxpayer relies on the summary data explained above, which breaks down the expenses by cost center (or department code), location code, and product code. Audit reviewed this information in detail, but found that the percentage breakdown between the codes was not helpful for several reasons. For example, breaking down expenses between location code and department code yielded different percentages, Taxpayer did not actually provide expense account detail, department code titles were insufficient to determine the nature of that expense, and Taxpayer did not provide its methodology for determining which expenses were cardholder facing and which ones were non-cardholder facing. Audit also notes that Taxpayer, during the course of its review, indicated via email that the majority of its revenue was from credit card servicing.

ANALYSIS

RCW 82.04.220 imposes the B&O tax on every person that has substantial nexus with Washington "for the act or privilege of engaging in business activities." Taxpayers who are engaged in service businesses or businesses that are not specifically taxed under another B&O tax classification are generally required to pay B&O tax under RCW 82.04.290(2) measured by the "gross income of the business." Here, Taxpayer, an out-of-state entity, provided various services that it lumps into three categories: credit card account services, administrative services, and database services. The majority of these services appear to be taxable under RCW 82.04.290(2) at the service and other activities B&O tax rate.² Taxpayer does not contest this classification. . . . At issue is whether Taxpayer's sales of its services to its Affiliates during the Audit Period are attributed to Washington based on the mailing addresses of Affiliates' Cardholders.

Under RCW 82.04.460(1), any person earning apportionable income subject to B&O tax and also taxable in another state must apportion to this state that portion of the person's apportionable income derived from business activities performed within this state under RCW 82.04.462. "Apportionable income" is gross income of the business generated from engaging in apportionable activities. RCW 82.04.460(4)(a). "Apportionable activities" specifically include those taxed under

² We note that some of the services described in Taxpayer's Appendices attached to its Service Agreements could be retail sales under RCW 82.04.050 or subject to a different B&O tax classification in Chapter 82.04 RCW. However, we do not have enough information about each activity to determine how they are taxable.

RCW 82.04.290, which includes the Service and Other Activities B&O Tax Classification under RCW 82.04.290(2). RCW 82.04.460(4)(a)(vi). . . . Taxpayer argues that its income is apportioned entirely outside of Washington.

Here, Taxpayer was engaged in “apportionable activities” in Washington and earned “apportionable income.” Taxpayer is also taxable in other states; therefore, the income Taxpayer earned from rendering its services is subject to apportionment under RCW 82.04.460.

According to RCW 82.04.462, income apportioned to Washington is multiplied by a “receipts factor,” the numerator of which is the gross income of the business attributed to Washington and the denominator of which is the gross income of the business worldwide. RCW 82.04.462(1), (3)(a). The statute provides a series of cascading rules in RCW 82.04.462(3)(b) for purposes of determining to which state to attribute gross income, including, in relevant part, as follows:

Except as otherwise provided in this section, for purposes of computing the receipts factor, gross income of the business generated from each apportionable activity is attributable to the state:

(i) *Where the customer received the benefit of the taxpayer's service or, in the case of gross income from royalties, where the customer used the taxpayer's intangible property. When a customer receives the benefit of the taxpayer's services or uses the taxpayer's intangible property in this and one or more other states and the amount of gross income of the business that was received by the taxpayer in return for the services received or intangible property used by the customer in this state can be reasonably determined by the taxpayer, such amount of gross income must be attributed to this state.*

(ii) *If the customer received the benefit of the service or used the intangible property in more than one state and if the taxpayer is unable to attribute gross income of the business under the provisions of (b)(i) of this subsection (3), gross income of the business must be attributed to the state in which the benefit of the service was primarily received or in which the intangible property was primarily used.*

. . .

RCW 82.04.462(3)(b) (emphasis added).

The “customer” means “a person or entity to whom the taxpayer makes a sale or renders services or from whom the taxpayer otherwise receives gross income of the business.” RCW 82.04.462(3)(b)(viii). Here, Affiliates were the customers for purposes of RCW 82.04.462, because Taxpayer rendered its services to the Affiliates under the Service Agreements. The question before us is where the customers, i.e. Affiliates, received the benefit of the services.

The Department adopted Rule 19402 to implement RCW 82.04.462. Rule 19402(303) explains the framework for determining where the benefit of a service is received depending on the type of services provided. Rule 19402(303) provides, in part:

Benefit of the service explained. The first two steps (subsection (301)(a)(i) and (ii) of this rule) used to attribute apportionable receipts to a state are based on where the taxpayer's customer receives the benefit of the service. This subsection explains the framework for determining where the benefit of a service is received.

[sub-sections (a) & (b) address services related to real property and tangible personal property not applicable here] . . .

(c) If the taxpayer's service does not relate to real or tangible personal property, the service is provided to a customer engaged in business, and the service relates to the customer's business activities, *then the benefit is received where the customer's related business activities occur. The following is a nonexclusive list of business related services:*

- (i) *Developing a business management plan;*
- (ii) *Commission sales (other than sales of real or tangible personal property);*
- (iii) *Debt collection services;*
- (iv) *Legal and accounting services not specific to real or tangible personal property;*
- (v) *Advertising services;* and
- (vi) *Theater presentations.*

Rule 19402(303) (emphasis added).

1. *Has Taxpayer provided sufficient records to separately apportion its various services?*

Taxpayer primarily argues that its various services should be apportioned differently based on the service provided and, without providing the detailed expense records, that many of its services are not related to issuing credit cards for the Affiliates and would be apportioned entirely outside of Washington. In general, neither RCW 82.04.462 nor Rule 19402 limit a taxpayer to one overall attribution for all of their apportionable services. *See* Department's Industry Guide Regarding Apportionment . . .³ But [splitting services for apportionment purposes] requires [both] a legal basis for concluding that the services are severable for apportionment purposes and documentation that would justify applying a different attribution for each service provided.

When considering whether different services should be given different tax treatment, the Department has historically looked first to whether there is a reasonable basis to separately tax the services provided in a single contract or billing. *See, e.g., Chicago Bridge & Iron Co. v. Dep't of Revenue*, 98 Wn.2d 814, 822-23, 659 P.2d 463, 468-69, appeal dismissed, 464 U.S. 1013 (1983) (holding that if services subject to separate contracts are functionally integrated, then the entire price is subject to tax at a single rate for purposes of Washington B&O tax). The Department has been clear that "bifurcation of a contract for taxation will be the unusual case." Det. No. 89-433A, 11 WTD 313 (1992). The Department has disallowed the separate taxation of multiple services in a contract when that work was done in a single, lump sum billing. Det. No. 04-0284, 24 WTD 269

³ [Department's Industry Guide Regarding Apportionment is available on the Department's website at: <https://dor.wa.gov/education/industry-guides/apportionment/attributing-service-income> (accessed May 18, 2020).]

(2005). In Det. No. 05-0172, 25 WTD 138 (2006), we explained the Department's position as follows:

[I]n general, [the Department] does not allow a single billing or contract to be segregated or bifurcated unless there is a reasonable basis to allow it. Det. No. 98-012, 17 WTD 247 (1998); Det. No. 02-0134, 24 WTD 129 (2005). Accordingly, [the Department] has taxed business activities separately where the taxpayers' contracts, which were negotiated before the work was performed, provided a reasonable basis for determining the value of the various activities performed. *See* Det. No. 89-433A, 11 WTD 313, 316 (1992) and [24 WTD 129].

In such cases, when the services are combined, Washington uses a true object test to determine the taxability of the services.⁴ Under the true object test, the Department would need to identify the true object for work completed under that contract. Det. No. 92-183ER, 13 WTD 96 (1993). *See* Det. No. 90-35A, 9 WTD 289 (1990); Det. No. 91-163, 11 WTD 203 (1991). The true object test focuses on the real object of the transaction sought by a taxpayer's customers and not just the transaction's different parts. Det. No. 14-0025, 33 WTD 387 (2014) (citing *Qualcomm, Inc. v. Dep't of Revenue*, 171 Wn.2d 125, 137, 249 P.3d 167 (2011)).

While the Department has historically applied these authorities in the context of determining how to tax multiple activities that are potentially subject to different B&O tax classifications, there is nothing prohibiting their application here where the activities are subject to the same classification, but could require different attribution approaches under RCW 82.04.462 and Rule 19402. Here, Taxpayer did not have any invoices or billing statements for its services. Taxpayer's services were provided via contract and related appendices, which explain the kinds of services Taxpayer provided. While these documents show that Taxpayer negotiated the different services ahead of time with its Affiliates, the records do not provide enough detail for us to apply separate attribution to the different services. Taxpayer charges its Affiliates based on its costs for each service and, while we believe documentation does exist to show how much Taxpayer charged its Affiliates for each service, Taxpayer has not provided that detail to us, other than summary detail that we do not find to be helpful. More importantly, we lack records that would sufficiently describe the services so that we could distinguish what services are integral to credit card services, and are apportioned accordingly, from those services that are unrelated to these activities.

⁴ For transactions that include retail and non-retail components, effective July 1, 2008, the Legislature enacted RCW 82.08.190, 82.08.195, and 82.12.195 to comply with the Streamlined Sales and Use Tax Agreement (or "SSUTA"). Laws of 2007, ch. 6. These provisions apply to "bundled transactions" and explain how to tax transactions that involve both retail and non-retail sales. Before the statute was enacted, the Department looked to the "true object" of the transaction sought by the customer to determine the proper tax classification of a transaction that involved both retail and non-retail services. *See Qualcomm, Inc. v. Dep't of Revenue*, 171 Wn.2d 125, 137-138, 249 P.3d 167 (2011) (citing Det. No. 90-128-1, 9 WTD 280-1, 280-4 (1990) and *Emery Indus., Inc. v. Limbach*, 43 Ohio St. 3d 134, 134-35, 539 N.E.2d 608 (1989)); Det. No. 94-115, 15 WTD 19 (1995); Jerome Hellerstein, *Significant Sales and Use Tax Developments During the Past Half Century*, 39 Vand. L. Rev. 961, 968 (1986). The bundled transaction statutes supersede the true object test for periods after the law change. Thus, for periods prior to July 1, 2008, we apply the true object test. And for periods beginning July 1, 2008, we apply the bundled transaction analysis of RCW 82.08.190. The true object test would still be used for determining how to tax contracts that do not contain a charge for retail sales, but include components that would be taxed differently if provided separately. In this case, though some of the database services could be retail sales under RCW 82.04.050(8), we do not currently have enough information to evaluate this.

RCW 82.32.070 explains the kinds of records that taxpayers doing business in Washington are required to maintain. It provides, in pertinent part:

Every taxpayer liable for any tax collected by the department must keep and preserve, for a period of five years, suitable records as may be necessary to determine the amount of any tax for which the taxpayer may be liable. Such records must include copies of all of the taxpayer's federal income tax and state tax returns and reports. All of the taxpayer's books, records, and invoices must be open for examination at any time by the department of revenue. In the case of an out-of-state taxpayer that does not keep the necessary books and records within this state, it is sufficient if the taxpayer produces within the state such books and records as are required by the department of revenue, or permits the examination by an agent authorized or designated by the department of revenue at the place where such books and records are kept. . . .

RCW 82.32.070(1). WAC 458-20-254 further explains these record keeping requirements and WAC 458-20-254(3) provides more detail on the kinds of records a taxpayer needs to keep:

(b) It is the duty of each taxpayer to prepare and preserve all records in a systematic manner conforming to accepted accounting methods and procedures. Such records are to be kept and preserved. All of the taxpayer's records must be presented upon request by the department or its authorized representatives that will demonstrate:

(i) The amounts of gross receipts . . . from all sources, however derived, . . . , whether or not such receipts . . . are taxable. These amounts must be supported by original source documents or records including but not limited to all purchase invoices, sales invoices, contracts, and such other records as may be necessary to substantiate gross receipts and sales.

(c) The records kept, preserved, and presented must include the normal records maintained by an ordinary prudent business person. Such records may include general ledgers, sales journals, cash receipts journals, bank statements, check registers, and purchase journals, together with all bills, invoices, cash register tapes, and other records or documents of original entry supporting the books of account entries. The records must include all federal and state tax returns and reports and all schedules, work papers, instructions, and other data used in the preparation of the tax reports or returns.

Regarding apportionment specifically, when challenging fair apportionment, taxpayers have the burden of proof. Taxpayers must demonstrate that there is “no rational relationship between the income attributed to the State and the intrastate values of the enterprise,” by proving that the income apportioned to Washington is “out of all appropriate proportion” to the business transacted by taxpayers in Washington. *Container Corporation of America v. Franchise Tax Board*, 463 U.S. 159, 180-81, 103 S. Ct. 2933 (1983).

In this case, Taxpayer has not provided records to, at a minimum, explain how much it charged for each of the activities listed in its Service Agreements and related appendices. Indeed, the Department asked Taxpayer to provide expense detail that would show this. Therefore, we do not have the documentation necessary to apply separate attribution methods to the various services Taxpayer provided here and we apply the true object test to these activities below. Taxpayer needs to provide records of its different revenue sources that would show: (1) the income amounts generated for each activity; and (2) what those activities entailed in more detail than the summary explanation provided in the Service Agreement appendices. If Taxpayer were able to provide these records, we [could better] evaluate whether certain services are severable from Taxpayer's credit card services and subject to a different attribution method.

Based upon the information provided, we conclude that the true object of Taxpayer's activities is to assist its Affiliates in extending credit to Customers. Taxpayer provided Affiliates with all of the services necessary for Affiliates to do so, including soliciting new customers, processing their credit applications, billing Customers once credit is extended, and providing customer support for Customers. While some of the administrative and database services provided could be distinct from credit card services to be apportioned differently, we lack sufficient documentation or information to do so.⁵ We note that certain administrative services and database services, such as services that provide the necessary business environment for Taxpayer to service Customers' credit cards, would nonetheless be so inseparable from credit card services that they would be apportioned in the same manner as credit card services (even if we had more documentation).

Taxpayer argues that Det. No. 17-0210, 37 WTD 076 (2018) applies to this case, enabling it to apportion back office services outside of Washington, separately from its credit card related services. The taxpayer in 37 WTD 076 provided a variety of general and administrative services, such as handling corporate governance or compliance issues, providing CEO and staff, providing human resources services to various affiliated companies. The affiliated companies sold paper and related products. The Audit Division attributed the taxpayer's gross income to Washington based on the destination of paper and related products sales made by the taxpayer's affiliated companies. The taxpayer challenged the Audit Division arguing that a "one-size-fits-all method" was not appropriate in that case. We agreed with the taxpayer that its [CEO and staff] services fit under Example 25 of Rule 19402 and concluded that the taxpayer's CEO and staff services were not related to the affiliated companies' ultimate sales activity to the affiliated companies' customers. [We further concluded the human resource services were attributed consistent with Example 24 of Rule 19402.]

There are some important distinctions between this case and 37 WTD 076. We agree with 37 WTD 076 that Rule 19402 provides that "if a taxpayer provides a variety of services, it follows that, *to the extent that the various services can be reasonably distinguished*, an individual examination of each service is required . . ." 37 WTD at 83 (emphasis added). The main issue here is that the administrative and database services cannot reasonably be distinguished based on the little information that we have about those services. In 37 WTD 076, we felt that there was sufficient

⁵ [For example, one relevant factor would be if the purchaser has the option to purchase the services separately or whether the service provider requires that its customers acquire the services together. This is not the only factor the Department will consider, but when the purchaser must acquire the services together this further supports that the services should be apportioned in the same manner.]

information to separately apportion two of the services: CEO and staff services, and human resource services. We do not have enough information here to do so. This is, in part, because of the nature of Taxpayer's business activities. Rather than providing purely back office type services, like the taxpayer in 37 WTD 076, Taxpayer provided all of the services necessary for the Affiliates to extend credit. Also, it appears, based on the limited information that we have, that the majority of Taxpayer's services directly involve credit card services. Therefore, as we explain above, we cannot determine whether there is a reasonable basis to use a different attribution method for some of the back office services Taxpayer provided.

2. *How are Taxpayer's services apportioned to Washington?*

Having determined that Taxpayer's services are apportioned together and that the true object of those services is extending credit for Affiliates' Customers, we now turn to how to apportion [the receipts from] those services. Taxpayer argues that none of its services are attributable to Washington because those services are provided for Affiliates outside of Washington. For determining where the benefit is received from a nonfinancial [institution's] services related to the extension of credit, special rules for attributing income are described in Rule 19402(305). *See* Rule 19402(303)(e). Rule 19402(305), in relevant part, provides:

(305) Special rules related to extending credit performed by nonfinancial institutions. Businesses not included in the definition of a financial institution under WAC 458-20-19404 that provide services related to the extension of credit must attribute their income from such activities as follows:

...

(b) Activities related to credit cards. Such activities include, but are not limited to, issuing credit cards, servicing, and billing. *Apportionable receipts from these activities are attributed to the billing address of the card holder.*

Rule 19402(305)(b) (emphasis added). Under this provision, any nonfinancial [institution's] activities that are related to credit cards are sourced to the billing address of the cardholders. The rule provides nonexclusive examples of activities related to credit cards, such as issuing credit cards, servicing and billing. *Id.*

Here, the credit card account services Taxpayer provided to Washington Cardholders on behalf of Affiliates included processing new accounts, providing customer service related to the credit cards, collecting credit card payments, issuing credit card statements, processing credit card payments, and embossing credit cards. They also include all other back office services necessary for Affiliates to extend credit. Under Rule 19402(305)(b), income from providing credit card related services is apportioned to the billing address of the credit card holders. Apportioning the credit card account services to the billing addresses of the Cardholders is consistent with RCW 82.04.462, which requires Taxpayer to apportion its credit card account services to where the Affiliates received the benefit of the services.

The credit card account services Taxpayer provided were an obvious benefit to Affiliates in that all of the services were necessary to Affiliates to create and maintain a market for their credit card

services in Washington. The Affiliates received the benefit of Taxpayer's services where the Cardholders are located, which is where the activities in this case were directed. When the Affiliates accepted the Cardholders' credit card applications, Taxpayer provided various credit card account services to the Cardholders on behalf of the Affiliates under the Service Agreements. Under the Service Agreements, Taxpayer created Affiliates' new Washington credit card accounts, performed all the tasks necessary to collect Washington Cardholder payments on behalf of Affiliates, and ensured all of the customer service needs of the Washington Cardholders were met, thereby incurring goodwill with Washington Cardholders. Therefore, the Affiliates received the benefit of Taxpayer's credit card related services at the Cardholders' locations. RCW 82.04.462(3)(b); Rule 19402(305)(b). Accordingly, the services Taxpayer provided to Affiliates are attributed to the billing addresses of the Cardholders. *Id.*

Taxpayer argues that *Lutheran Brotherhood Research Corp. v. Comm'r of Revenue*, 656 N.W. 2d 375 (Minn. 2003) supports finding that its services (or, at a minimum, its back office services) are apportioned to the Affiliates' physical locations outside of Washington. *Lutheran Brotherhood* is not controlling authority in Washington. Furthermore, it is distinguishable here because the relevant Minnesota statute focuses on where the "benefits of the services are consumed" whereas the Washington statute focuses on "where the customer received the benefit." Minn. Stat. § 290.191, subd. 5(j) (1988); RCW 82.04.462(3)(b) (emphasis added). The Supreme Court of Minnesota held that the benefits of mutual fund management services were "consumed" by the investment managers, not the mutual funds' investors, and thus the revenue received by the taxpayer as fees for the mutual fund management services rendered to the mutual funds was properly allocated to where the investment managers were located in Minnesota. *Lutheran Brotherhood*, 656 N.W.2d at 380.

Here, it is not in dispute that Affiliates were the customers for purposes of RCW 82.04.462, because Taxpayer rendered its services to the Cardholders on behalf of Affiliates under the Service Agreements. See RCW 82.04.462(3)(b)(viii). Unlike the Minnesota statute, which focuses on who is the consumer that consumes the benefits of the services, Washington's apportionment statute focuses on where the customer/consumer received the benefit of the services. RCW 82.04.462(3)(b). Affiliates received the benefit of Taxpayer's services where Taxpayer was able to service Affiliate's Cardholders. The services are "related business activities" of Affiliates' credit extension services provided to the Cardholders. Unlike the investment managers in *Lutheran Brotherhood*, who consumed the investment research performed by the investment advisor on the mutual funds in order to be accountable to the investors, Affiliates received the benefit of the subject services where Taxpayer provided the services to the Cardholders on behalf of Affiliates.

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DECISION AND DISPOSITION

We deny the petition.

Dated this 16th day of June 2020.