

Cite as Det No. 10-0344, 32 WTD 1 (2013)

BEFORE THE APPEALS 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. 10-0344
)	
...)	Registration No. . . .
)	Doc. No. . . ./Audit No. . . .
)	Docket No. . . .

RULE 156; RCW 82.04.050(3)(b) RCW 82.08.020: RETAIL SALES TAX – RETAILING B&O TAX – ESCROW SERVICES. An escrow business’s charges for courier services, reconveyances of deeds of trust, wire transfers, and similar escrow services are subject to retail sales tax and retailing B&O tax when the escrow business orders those services from third parties on its own account and incurs liability for them.

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.

De Luca, A.L.J. – A corporation that provided escrow services protests the assessment of retail sales tax and retailing business and occupation (B&O) tax on fees it charged its customers for services such as courier delivery, reconveyances of deeds of trust, and wire transfers that it purchased in its own name from third parties. Held, we affirm the assessment and deny the taxpayer’s petition.¹

ISSUE

Are costs for courier services, reconveyances of deeds of trust, and wire transfers part of escrow services that are subject to retail sales tax and retailing B&O tax pursuant to RCW 82.04.050(3)(b), RCW 82.08.020, [and] WAC 458-20-156 (Rule 156)... when an escrow agent orders those services in its own name and incurs primary liability for payment of them?

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

FINDINGS OF FACT

The taxpayer was a corporation that provided residential and commercial escrow services in the state of Washington during the audit period. The taxpayer's business is now closed. The Audit

Division of the Department of Revenue (DOR) audited the taxpayer for the period from January 1, 2005, through December 31, 2008, and assessed the taxpayer \$. . . in retail sales tax, retailing B&O tax, interest, and a 5% substantial underpayment penalty. The taxpayer timely appealed the assessment. The assessment remains unpaid.

The taxpayer ordered services in its own name from third parties to provide escrow services to its customers. These third-party services included courier/messenger services for the delivery of documents, reconveyances of deeds of trust by trustees, wire fees, and other related services. The taxpayer charged its customers the amounts it paid the third-party services providers, but it states it did not mark up the charges. The taxpayer also did not add sales tax to these charges when it billed its customers for these services. And it did not report the amounts received from the customers for these charges as part of its gross income. The Audit Division determined that the taxpayer's charges for these third-party services were subject to retail sales tax because they were part of the escrow services provided by the taxpayer. Consequently, the Audit Division included in the taxpayer's gross receipts the amounts received from the customers for the charges for the third-party services and assessed the taxpayer retail sales tax on them.

ANALYSIS

The taxpayer claims it is standard practice in the escrow industry to treat these types of third-party service charges as non-taxable pass-through payments similar to paying utility bills at closing as instructed by the seller and buyer. The taxpayer notes these charges are paid out of its trust fund account at closing and not prior to closing. The taxpayer also contends that DOR is taxing the transaction twice by assessing sales tax on these services when, it alleges, the seller also pays sales tax on the total sales price.

RCW 82.04.050(3) defines "retail sale" to include "(b) Abstract, title insurance, and escrow services."² The retail sales tax is imposed on each retail sale in this state. RCW 82.08.020. "Selling price" or "sales price" for retail sales tax purposes means...

the total amount of consideration, except separately stated trade-in property of like kind, including cash, credit, property, and services, for which tangible personal property, extended warranties, or services defined as a "retail sale" under RCW [82.04.050](#) are sold, leased, or rented, valued in money, whether received in money or otherwise. No deduction from the total amount of consideration is allowed for the following: (i) The seller's cost of the property sold; (ii) the cost of materials used, labor or service cost,

² The statutory definition of "retail sale" in RCW 82.04.050 has included "abstract, title insurance, and escrow services" without change in that wording for several decades. . . .

interest, losses, all costs of transportation to the seller, all taxes imposed on the seller, and any other expense of the seller; (iii) charges by the seller for any services necessary to complete the sale, other than delivery and installation charges; (iv) delivery charges; and (v) installation charges. (Underlining ours.)

RCW 82.08.010(1). Whereas, retailing B&O tax is imposed by RCW 82.04.250 on the gross proceeds of sales, multiplied by the applicable B&O tax rate. "Gross proceeds of sale" is defined in RCW 82.04.070 as...

the value proceeding or accruing from the sale of tangible personal property and/or for services rendered, without any deduction on account of the cost of property sold, the cost of materials used, labor costs, interest, discount paid, delivery costs, taxes, or any other expense whatsoever paid or accrued and without any deduction on account of losses. (Underlining ours.)

DOR adopted Rule 156³ to administer the taxes pertaining to the escrow business. The rule provides in pertinent part:

The gross receipts of..."escrow" businesses include all service charges representing...a charge for...an escrow fee or service charge received by "escrow agents." (Underlining ours.)

Business and Occupation Tax

. . . escrow businesses are taxable under the classification retailing on gross receipts from fees or premiums charged to consumers for...escrow services.

Retail Sales Tax

The retail sales tax must be collected and reported by...escrow businesses on fees or premiums charged for such services. The retail sales tax is applicable to sales to such businesses of forms, office supplies and equipment for use in the conduct of such businesses. (Underlining ours.)

Thus, escrow services are retail sales. Gross receipts, including fees or premiums, received by an escrow agent from its customers for escrow services are subject to retailing B&O tax. And escrow agents must collect and report retail sales tax on fees or premiums charged for such services. *Id.* See Det. No. 91-316, 11 WTD 285 (1991); *see also* Det. No. 90-231A, 12 WTD 305 (1990) (holding that amounts received by an escrow company from activities relating to deeds of trust are subject to the retailing B&O tax and retail sales tax.). Therefore, the disputed charges incurred by the taxpayer are part of its non-deductible costs of doing business for both

³ The current version of Rule 156 was filed on March 15, 1983.

B&O tax and retail sales tax purposes. RCW 82.04.070 and RCW 82.08.010(1)(a), *supra*. Amounts received by the taxpayer from its customers for those charges are subject to sales tax and B&O tax. Rule 156. Failure by a retail seller to collect sales tax makes the seller personally liable to the state for the amount of the tax. RCW 82.08.050(3).

DOR also has held that escrow charges received by an escrow agent from buyers or sellers for third-party messenger services are subject to sales tax and retailing B&O tax. *See* Det. No. 89-237, 7 WTD 316-7 (1989). That determination cited the definition of “gross proceeds of sales” in RCW 82.04.070, *supra*, and the similar definition of “selling price” in RCW 82.08.010(1)(a), *supra*, and concluded that for purposes of calculating the B&O tax and the retail sales tax, respectively, delivery costs are part of the measure of the tax and must be included in the gross proceeds of sale and the selling price whatever the delivery method. *See also* Rule 110(3).

We also conclude that WAC 458-20-111 (Rule 111) does not apply. The rule defines “advance” and “reimbursement” and excludes from the measure of tax money received (pass-through payments) by a taxpayer as a reimbursement of an advance in accordance with the regular and usual custom of the business. . . .

Moreover, . . . the Washington State Supreme Court has ruled that two conditions must be met. The taxpayer must first establish that it received the funds as the agent of the customer or client. If this first condition is satisfied, the taxpayer must also establish that its use of the funds to pay a third party is solely as an agent of the customer or client. *City of Tacoma v. William Rogers Co.*, 149 Wn.2d 169, 60 P.3d 79 (2002).

Therefore, in order for taxpayers to legally take the Rule 111 exclusion, they must first establish that they had an agency relationship with their customers and that they had acted solely in an agency capacity when contracting and paying the third-party service providers.

In 7 WTD 316-7, DOR held that the Rule 111 exclusion did not apply because the taxpayer in that case was not acting solely as an agent for another party, but had contracted with the messenger service in its own name for the services rendered. Likewise, in the present matter, the taxpayer admits it was primarily liable for the disputed third-party services it contracted for in order to provide its escrow services. It was not acting solely as an agent for the buyers or sellers. Consequently, the Rule 111 exclusion does not apply in the present matter. *William Rogers*; ETA 3100.2009

By contrast, DOR has recognized that escrow agents are not liable, other than as an agent, for third-party fees charged to their customers for title insurance, credit reports, and appraisals. Escrow agents can exclude deposits for these customer expenses deposited in the escrow agents’ trust accounts. Det. No. 92-073, 12 WTD 131 (1992); Det. No. 94-092, 14 WTD 251 (1994). These amounts are required by law to be held in trust and never accrue to the benefit of the escrow agent. The escrow agent is not permitted to expend such funds for any purpose other than specific third-party costs or refunds to the customers. *Id.*

Indeed, DOR has adopted ETA 3095 Loan Application Deposits, which explains that loan application deposits are payments made to a lending institution by a person applying for a mortgage loan. They are used by the lending institution to purchase third party services for the applicant that are necessary for the institution to evaluate the loan application. The services purchased with these funds typically include an appraisal of the subject property, a credit report, and a title report. In some cases they may also be used for inspection fees (pest, septic tank,

etc.). Several conditions must exist for a loan application deposit to be considered as an advance that is not included in the definition of "gross income of the business" (RCW 82.04.080). If all of the conditions are present, loan application deposits received by lending institutions should not be reported as gross income subject to the B&O tax. Taxpayers must keep sufficient records to substantiate the existence of each of the conditions listed.

Some of the conditions that must be met for a deposit to be considered a non-taxable advance include...

2. The taxpayer has a signed, written, acknowledgment from the loan applicant at the time of loan application, whereby the loan applicant agrees to be solely liable for payment of the third party services. This acknowledgment must indicate an agreement between the lending institution and the borrower that the lending institution agrees to act solely as the borrower's agent for payment purposes only to third party providers.

5. The taxpayer must notify the third party service providers in writing of the fact that:
a) as a condition of the loan application process the applicant agrees to be solely liable for payment of the third party services; and
b) the taxpayer will not be secondarily liable for payment so long as the taxpayer, acting as agent for the applicant for payment purposes only, has collected funds from the applicant either in advance of, or simultaneous to, ordering services and in fact delivers such funds to the service provider upon request for payment.

ETA 3095.

In the present matter, the taxpayer has provided no evidence that it obtained either written acknowledgement from its customers that they would be solely liable for payment of the third party services, or that it provided written notice to third party service providers that it was acting only as an agent and its customers would be solely liable for payment and the taxpayer would not be secondarily liable for payment. Moreover, the taxpayer admits it was primarily liable to the third parties that provided the disputed services. Therefore, the disputed payments are not non-taxable advances.

We note there is significant difference between contracting for services with third parties in its own name, as the taxpayer did in order to provide its escrow services, and merely paying utility bills at closing for sellers and buyers solely as their agent. In the latter instance, the taxpayer did

not order or receive the benefit of the utilities and would not be liable for the charges other than as an agent.

Finally, there is no double payment of sales taxes by the taxpayer and the sellers of the real properties as the taxpayer suggests. We have explained why the escrow services that the taxpayer provided were retail services subject to retail sales tax and retailing B&O tax. As noted retail sales tax is imposed on each retail sale in this state. RCW 82.08.020(1). A “sales price”

for a retail sale “means the total amount of consideration...for which tangible personal property, extended warranties, or services defined as a “retail sale” under RCW 82.04.050 are sold, leased, or rented” RCW 82.08.010(1)(a), *supra*. Notably, this definition of a sales price for a retail sale does not include the amount of consideration received for the sale of real property. Therefore, the sale of real property is not subject to retail sales tax. Similarly, the sale of real property is not subject to B&O tax. RCW 82.04.390.

By contrast, the sale of real property is subject to real estate excise tax (REET) per RCW 82.45.060. The seller is liable for the payment of REET. RCW 82.45.080. REET is not a retail sales tax imposed by Chapter 82.08 RCW. It is an excise tax imposed by Chapter 82.45 RCW upon each sale of real property in this state at a much lower rate than the sales tax rate. In short, the sale of escrow services is not the sale of real property. They are different transactions. The taxpayer sold escrow services, which were subject to sales tax. But the sellers of real property sold real estate, not escrow services. The sale of real estate is subject to REET.

For the reasons explained above, DOR properly imposed the assessment.

DECISION AND DISPOSITION

Taxpayer's petition is denied

Dated this 10th day of November, 2010.