

Cite as Det. No. 14-0306, 34 WTD 129 (2015)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of) Letter Ruling of)) . . .)))	<u>D E T E R M I N A T I O N</u> No. 14-0306 Registration No. . . .
---	---

[1] RULE 19401; RULE 19405; RCW 82.04.067: B&O TAX – SUBSTANTIAL NEXUS – PAYROLL THRESHOLD. During each calendar year at issue, Taxpayer paid more than the threshold amount in payroll expenses to its one Washington employee, and, therefore, created substantial nexus with Washington during those years.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

Yonker, A.L.J. – An out-of-state web development company (Taxpayer) appeals a letter ruling finding that Taxpayer established nexus in Washington in 2013 because Taxpayer had payroll of more than \$53,000 in Washington during that year. Taxpayer argues that a portion of the amount of payroll it paid in 2013 was attributable to 2012. Taxpayer also argues for a waiver of any tax liability because its payroll was only slightly above the \$53,000 threshold. We deny Taxpayer’s petition.¹

ISSUE

Pursuant to RCW 82.04.067(c)(iii), and WACs 458-20-19401 and 458-20-19405, did Taxpayer have more than \$53,000 of payroll in Washington in 2013, thereby establishing nexus in Washington and subjecting Taxpayer to tax liability in this state?

FINDINGS OF FACT

[Taxpayer] is an [out of state] corporation . . . that provides web development services primarily to law firms. In October 2012, Taxpayer hired an employee that resided and worked remotely in Washington. On November 13, 2012, Taxpayer opened a business account in Washington, and was placed on an annual tax reporting schedule. For 2012, Taxpayer reported “no income” in Washington. In 2013, Taxpayer paid its one Washington employee a total of \$53,740.25, according to that employee’s 2013 W-2 form.

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

On February 24, 2014, Taxpayer requested a “waiver” of its 2013 Washington tax liability, stating the following in relevant part:

It appears that through the hiring of [one employee located in Washington] caused the company to reach and establish Nexus as their wages reported was \$53,740.25 which is just slightly over the 2013 threshold limit set at \$53,000k. At this stage, we do not intend to rehire within the State of Washington. Based on this information presented, I request that you reconsider our position as a small business employer and grant our request for waiver of the 2013 WA State Business Excise Tax.

On March 6, 2014, the Department’s Taxpayer Information and Education section (TI&E) issued a letter ruling stating the following:

For purposes of business and occupation (B&O) tax, you must continue to pay B&O tax on all Washington sales for *one* year after the year in which the nexus creating activity ceases. Therefore, if you have nexus in Washington in 2013, B&O tax still applies to the income you receive from Washington customers through at least December 31, 2014.

(Emphasis in original). Taxpayer timely appealed this letter ruling.

ANALYSIS

Washington imposes upon “every person that has a substantial nexus with this state” a business and occupation (“B&O”) tax “for the act or privilege of engaging in business activities” in Washington. RCW 82.04.220(1). The B&O tax measure and rate are determined by the type of business in which a person engages, and the statute provides numerous classifications of activities. [*Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971); RCW 82.04.290(2)].

A state cannot tax business activity that does not have sufficient connection or “nexus” with the state. *See Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 97 S. Ct. 1076 (1977); *Tyler Pipe Indus., Inc. v. Dep’t of Revenue*, 483 U.S. 232, 107 S.Ct. 2810 (1987); *Quill Corp. v. North Dakota*, 504 U.S.298, 112 S.Ct. 1904 (1992); Det. No. 05-0376, 26 WTD 40 (2007). The idea of “nexus” flows from limits on a state’s jurisdiction to tax found in the Due Process and Commerce Clause Provisions of the United States Constitution. Det. No. 01-188, 21 WTD 289 (2002); *see also* RCW 82.04.4286. The U.S. Supreme Court has held that the Commerce Clause requires that the transaction being taxed have “substantial nexus” with the taxing state. *Complete Auto Transit, Inc.*, 430 U.S. at 279. In *Complete Auto Transit*, the Court articulated a four-pronged test that a state must satisfy to withstand a Commerce Clause challenge to its jurisdiction to tax. The Court held that the Commerce Clause requires that the tax: (1) be applied to an activity with “substantial nexus” with the taxing state, (2) be fairly apportioned, (3) not discriminate against interstate commerce, and (4) be fairly related to the services provided by the state. *Complete Auto Transit, Inc.*, 430 U.S. at 279.

On June 1, 2010, the legislature enacted RCW 82.04.067, which codified the definition of “substantial nexus” in Washington. Laws of 2010, ch. 23, § 1709. RCW 82.04.067(1) provides

that a person engaging in service business activity is deemed to have substantial nexus with Washington if the person is:

- (a) An individual and is a resident or domiciliary of this state;
- (b) A business entity and is organized or commercially domiciled in this state; or
- (c) A nonresident individual or a business entity that is organized or commercially domiciled outside this state, and in any tax year the person has:
 - (i) More than fifty-three thousand dollars of property in this state²;
 - (ii) More than fifty-three thousand dollars of payroll in this state³;
 - (iii) More than two hundred sixty-seven thousand dollars of receipts from this state⁴;
or
 - (iv) At least twenty-five percent of the person's total property, total payroll, or total receipts in this state.RCW 82.04.067(1).

See also WAC 458-20-19401(3). Here, Taxpayer concedes that it had one employee in Washington during 2013, and paid that employee a total of \$53,740.25 during that year. While this amount is only slightly above the \$53,000 payroll threshold, it is, nevertheless, above that threshold. We have no authority to “waive” tax liability for any taxpayer that meets any of the thresholds identified in RCW 82.04.067.

Taxpayer argued at hearing that \$5,489.73 of the total it paid to its Washington employee in 2013 was paid on January 15, 2013, for work done between December 1, 2012 and December 31, 2012. According to Taxpayer, it follows that the remaining \$48,250.52 is below the \$53,000 payroll threshold. We disagree. RCW 82.04.067(1)(c) makes clear that the payroll threshold is based on the payroll that Taxpayer has “in” the tax year. Further, WAC 458-20-19401(5) defines “payroll” as “the total compensation . . . **paid during the calendar year.**” (Emphasis added). These authorities make clear that all compensation paid “in” or “during” the calendar year in question is the basis for determining whether the payroll threshold is met. Here, there is no dispute that Taxpayer paid the entire \$53,740.25 “in” and “during” 2013. As such, we conclude that Taxpayer met the payroll threshold for 2013. Therefore, Taxpayer established nexus with Washington in 2013. We affirm the letter ruling accordingly.

² RCW 82.04.067(1)(c)(i) states that this amount is \$50,000; however, RCW 82.04.067(5)(a) directs the Department to adjust the thresholds for determining substantial nexus. WAC 458-20-19405 adjusted that original threshold amount to \$53,000 for the 2013 calendar year.

³ RCW 82.04.067(1)(c)(ii) states that this amount is \$50,000; however, RCW 82.04.067(5)(a) directs the Department to adjust the thresholds for determining substantial nexus. WAC 458-20-19405 adjusted that original threshold amount to \$53,000 for the 2013 calendar year.

⁴RCW 82.04.067(1)(c)(iii) states that this amount is \$250,000; however, RCW 82.04.067(5)(a) directs the Department to adjust the thresholds for determining substantial nexus. WAC 458-20-19405 adjusted that original threshold amount to \$267,000 for the 2013 calendar year.

DECISION AND DISPOSITION

[Taxpayer's petition is denied.]

Dated this 23rd day of September 2014.