BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Refund of
Assessment of )
) DETRMINATION
) No. 17-0210
)
)
)
...
)

Registration No. . . .

ESTIMATING GROSS INCOME OF THE BUSINESS BASED ON TAXPAYER
RECORDS. The Department may estimate a taxpayer’s gross income of the business
based on the records that Taxpayer provides to the Department if it appears that the
amounts at issue are in exchange for the rendition of services.

REASONABLE METHOD OF PROPORTIONALLY ATTRIBUTING GROSS
INCOME. Determining a reasonable method of proportionally attributing gross income is
a service-by-service analysis and examples provided in Rule 19402 may be used as
guidance in determining a reasonable method for such services. Specifically, “CEO and
Staff Services” may be attributed to the location of the corporate domiciles where the CEO
and associated staff provided service consistent with Example 25 in Rule 19402. Likewise,
“Human Resources Services” may be attributed to employee locations consistent with
Example 24 in Rule 19402.

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, T.R.O. – A parent company (Taxpayer) that provides a variety of “general and
administrative services” to various affiliated companies protests the method used by the
Department’s Audit Division to calculate an assessment of business and occupation tax [(B&O)].
Specifically, Taxpayer argues that (1) the Audit Division included amounts that do not constitute
gross income in Taxpayer’s tax base, (2) the Audit Division used an unreasonable method of
proportionally attributing Taxpayer’s income from certain categories of services, and (3) it is
entitled to a waiver of penalties. We grant the petition in part, deny in part, and remand for
adjustment to the tax assessment.¹

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

1. When estimating Taxpayer’s income under RCW 82.32.100(1), did the Audit Division include amounts that did not constitute “gross income of the business” under RCW 82.04.080?

2. Under RCW 82.04.462 and WAC 458-20-19402, did the Audit Division use a reasonable method of proportionally attributing gross income for all categories of Taxpayer’s services when calculating Taxpayer’s Washington tax liability?

3. Under RCW 82.32A.020, RCW 82.32.105, and WAC 458-20-228, is Taxpayer entitled to a waiver of penalties?

FINDINGS OF FACT

. . . (Taxpayer) is [an out-of-state] limited liability company that provides “general and administrative services” to various affiliated companies (collectively, Affiliates), which sell paper and related products. Taxpayer and all of the Affiliates are domiciled outside of Washington, but the Affiliates each make retail and/or wholesale sales in Washington.

Specifically, Taxpayer represented that in exchange for recovery of its service costs, through “intercompany transactions,” Taxpayer provided the following broad categories of service to its Affiliates during the relevant time period:

- **Corporate Governance/Compliance** – Taxpayer represented its staff handled various compliance issues, such as ethics training, environmental regulatory matters, and documentation retention, for the Affiliates.
- **CEO & Staff** – Taxpayer represented that Taxpayer and the Affiliates had common corporate officers and support staff, and that Taxpayer and the Affiliates shared in the expense of paying corporate officers and support staff salaries, and other related expenses.
- **Finance and Accounting (Including Tax)** – Taxpayer represented that its staff provided centralized financial and accounting services for the Affiliates, including the filing of tax returns and other financial management duties. Taxpayer also represented that some Affiliates maintained a small “skeleton crew” of staff that provided some localized finance and accounting services to those Affiliates.
- **Government/Public Affairs** – Taxpayer represented that its staff oversaw, on behalf of the Affiliates, state legislative and lobbying efforts. Taxpayer also represented that its staff provided centralized media and communications services for the Affiliates.
- **Human Resources** – Taxpayer represented that its staff provided traditional human resource services, such as hiring employees and medical benefit counseling, for the Affiliates. Taxpayer also represented that some Affiliates maintained a small “skeleton crew” of staff that provided some localized human resources services to those Affiliates.
- **Procurement** – Taxpayer represented that its staff provided centralized purchasing services for the Affiliates. Taxpayer represented that some larger Affiliates may have procurement staff for local purchases in addition to the centralized services Taxpayer’s staff provided to the Affiliates.
Other Corporate Services – Taxpayer represented that it did not have complete information on all the services that fell into this category. Taxpayer speculated that such things as centralized mailroom services, the company car program, the corporate aircraft program, and other miscellaneous services were all included in this service category.

Corporate Strategy & Development – Taxpayer represented that its staff provided centralized business planning, corporate organization and reorganization services, and helped develop nationwide sales strategies for the Affiliates.

Legal – Taxpayer represented that its legal staff, including attorneys and legal support staff, provided legal support and advice to the Affiliates in a wide range of legal issues. Taxpayer also represented that the income from this category of service also included recovery of Taxpayer’s costs for seeking the services of outside legal services.

Beginning with its September 2007 combined excise tax return, Taxpayer began reporting “no business,” and, as a result, reported no tax liability in Washington from that time. On October 3, 2011, the Department issued a letter to Taxpayer stating the following:

Your Washington State Department of Revenue tax reporting account was closed effective June 30, 2011.

The account was closed because you did not report any gross income or file a return in the last two years. Accounts with no indication of taxable activity occurring in the last two years are administratively closed. (WAC 458-20-101(14)).

In 2016, the Department’s Audit Division found that Taxpayer had taxable business activity in Washington after the administrative closure of Taxpayer’s tax reporting account. The Audit Division then commenced a review of Taxpayer’s books and records for the time period of January 1, 2012, through June 30, 2016, (audit period) to determine Taxpayer’s tax liability in Washington. Taxpayer provided limited documentation to the Audit Division during that review. The Audit Division derived Taxpayer’s gross income amount from a document, referred to as “Schedule M,” which Taxpayer represented was a list of intercompany transaction amounts Taxpayer received from the Affiliates during the audit period, separated into various categories of services. The Audit Division then took that gross income amount and employed one method of proportionally attributing all of Taxpayer’s gross income from all services to Washington based on the proportion of the Affiliates’ product sales that were delivered to Washington.

On October 17, 2016, as a result of the Audit Division’s review, the Department issued a tax assessment for $ . . . , which included $ . . . in service and other activities B&O tax, a $ . . . delinquent penalty, a $ . . . five-percent assessment penalty, and $ . . . in interest. Taxpayer subsequently requested review of the tax assessment.
ANALYSIS

In Washington, “there is levied and collected from every person that has a substantial nexus with this state a tax for the act or privilege of engaging in business activities.” RCW 82.04.220. Taxpayer does not dispute that it has nexus with Washington, and is, therefore, generally subject to B&O tax in Washington. The B&O tax measure is “the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be.” Id. The rate used is determined by the type of activity in which a taxpayer engages. See generally chapter 82.04 RCW. Income from any business activity that is not expressly classified in Chapter 82.04 RCW is taxed under the service and other activities B&O tax classification. RCW 82.04.290(2). There is no dispute that Taxpayer’s business activity is subject to service and other activities B&O tax. There is also no dispute that Taxpayer’s business activity is also taxable in other states.

RCW 82.04.460, which addresses when income is taxable in both Washington and another state, requires that income from business activity taxable under the service and other activities B&O tax classification be apportioned “to this state, in accordance with RCW 82.04.462, that portion of the [taxpayer’s] apportionable income derived from business activities performed within this state.”

To determine taxable income in such cases, a taxpayer’s total apportionable income is multiplied by a fraction referred to as the “receipts factor.” RCW 82.04.462(3)(a). The numerator of the receipts factor is Washington apportionable receipts and the denominator is the worldwide apportionable receipts minus any “throw-out income”. See id.; WAC 458-20-19402(402). In essence, the receipts factor becomes the percentage by which a taxpayer’s gross income is multiplied to derive the portion of that taxpayer’s total gross income that is taxable in Washington. Taxpayer challenges (1) the total gross income that the Audit Division used to calculate Taxpayer’s taxable income in Washington, and (2) the method used by the Audit Division to determine the receipts factor that was applied to that total gross income. We address each issue in turn.

1. Amount of Gross Income of the Business

RCW 82.04.290(2)(a) states that service and other activities B&O tax is equal to the “gross income of the business multiplied by the rate of 1.5 percent.” RCW 82.04.080(1) defines “gross income of the business” to mean the following:

[T]he 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, royalties, fees, commissions, dividends, and other emoluments however designated, all without any 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.

(Emphasis added). Essentially, a taxpayer’s tax liability is based on its gross income without any deduction for its business costs. Here, during the Audit Division’s review, Taxpayer provided one document, Schedule M, that included total amounts, by category of service, received by Taxpayer
as “intercompany transfers” from the Affiliates. The Audit Division relied on these amounts as Taxpayer’s “gross income of the business” when it calculated Taxpayer’s tax liability. RCW 82.32.100(1) authorizes the Department to “proceed, in such manner as it may deem best, to obtain facts and information on which to base its estimate of the tax” when a taxpayer does not provide complete documentation. Therefore, the Audit Division was authorized to proceed with estimating Taxpayer’s tax liability based on the available information contained in Schedule M in the absence of complete documentation.

On review, Taxpayer argues that the amounts contained in Schedule M did not accurately represent the Taxpayer’s gross income. In support of its argument, Taxpayer provided an updated Schedule M. Taxpayer explained that the difference between the amounts in the original Schedule M and the reduced amounts in its updated Schedule M is due to the removal of intercompany transaction amounts related to (1) the “CEO & Staff” category of service, and (2) amounts recorded under the business description “Corporate” that Taxpayer allocated to itself – as opposed to one of the Affiliates – for Taxpayer’s own share of the intercompany corporate expenses.

Regarding the first category of “CEO & Staff” intercompany transactions, we conclude that such amounts are properly included in Taxpayer’s “gross income of the business” as defined under RCW 82.04.080. This is because such “CEO & Staff” intercompany transactions are “compensation for the rendition of services” performed by Taxpayer for the Affiliates. Therefore, the Audit Division correctly included such amounts in Taxpayer’s gross income of the business for calculating Taxpayer’s tax liability.²

Regarding the second category of “Corporate” amounts, the Audit Division stated on review that Taxpayer’s explanation of that category of “Corporate” amounts was reasonable, and we have no reason to question that explanation. Accordingly, we conclude that such amounts are not “intercompany transactions” since they represent Taxpayer’s own share of the intercompany corporate expenses, as opposed to amounts received from the other Affiliates to cover such intercompany corporate expenses. Therefore, these amounts should not be included as part of Taxpayer’s estimated “gross income of the business” under RCW 82.32.100(1) and RCW 82.04.080, and should be removed from Taxpayer’s tax base before calculating its tax liability.³ We remand to the Audit Division to adjust Taxpayer’s tax base to remove such amounts.

2. Receipts Factor

RCW 82.04.462(3)(b) provides for the following series of cascading steps for attributing apportionable income to Washington for the purpose of determining the numerator of the receipts factor:

² However, as we discuss later in this determination, the “CEO & Staff” intercompany transactions are ultimately subject to a receipts factor of zero, resulting in no Washington B&O tax liability on the intercompany transactions associated with that category of service.
³ It is unclear where Taxpayer obtains funds to pay for its own portion of shared expenses as Taxpayer represented that it receives no mark up on the intercompany transactions that Taxpayer receives from the Affiliates for their portion of the shared expenses.
[F]or 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.

WAC 458-20-19402 (Rule 19402) is the Department’s administrative rule implementing RCW 82.04.462. Rule 19402(301) provides the following additional information regarding the attribution of apportionable income:

Receipts are attributed to states based on a cascading method or series of steps. The department expects that most taxpayers will attribute apportionable receipts based on (a)(i) of this subsection because the department believes that either the taxpayer will know where the benefit is actually received or a “reasonable method of proportionally attributing receipts” will generally be available. These steps are:

(a) Where the customer received the benefit of the taxpayer’s service . . . ;

(i) If a taxpayer can reasonably determine the amount of a specific apportionable receipt that relates to a specific benefit of the services received in a state, that apportionable receipt is attributable to the state in which the benefit is received. When a customer receives the benefit of the taxpayer's services 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 by the customer in this state can be reasonably determined by the taxpayer, such amount of gross income must be attributed to this state. This may be shown by application of a reasonable method of proportionally attributing the benefit among states. The result determines the receipts attributed to each state. Under certain situations, the use of data based on an attribution method specified in (b) through (f) of this subsection may also be a reasonable method of proportionally attributing receipts among states (see Examples 4 and 5 below).

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4 Rule 19402 was originally issued on an emergency basis on June 2, 2010. It was later amended a number of times on an emergency basis until [the first permanent version of the rule was filed on September 17, 2012].
(ii) If a taxpayer is unable to separately determine or use a reasonable method of proportionally attributing the benefit of the services in specific states under (a)(i) of this subsection, and the customer received the benefit of the service in multiple states, the apportionable receipt is attributed to the state in which the benefit of the service was primarily received. Primarily means, in this case, more than fifty percent.

(Emphasis added.) Rule 19402(301) goes on to describe additional cascading steps in the series that a taxpayer is to follow if either (a)(i) or (a)(ii) are not feasible. These additional steps mirror the steps described in RCW 82.04.462(3)(b)(iii) – (vii).

Here, Taxpayer and the Audit Division both agree that Taxpayer’s gross income should be attributed consistent with RCW 82.04.462(3)(b)(i) and Rule 19402(301)(a)(i) to where Taxpayer’s customers received the benefit of Taxpayer’s services. Taxpayer and the Audit Division also agree that a “reasonable method of proportionally attributing” must be employed here to determine where the Affiliates received the benefit of Taxpayer’s services. Rule 19402(106)(f) defines “reasonable method of proportionally attributing” as “a method of determining where the benefit of an activity is received and where the receipts are attributed that is uniform, consistent, and accurately reflects the market, and does not distort the taxpayer’s market.”

The “benefit of the taxpayer’s service” is not defined in statute. Rule 19402(303), however, defines that term in a variety of ways, depending on the factual circumstances:

**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.

(a) **If the taxpayer's service relates to real property, then the benefit is received where the real property is located.** The following is a nonexclusive list of services that relate to real property:

   (i) Architectural;
   (ii) Surveying;
   (iii) Janitorial;
   (iv) Security;
   (v) Appraisals; and
   (vi) Real estate brokerage.

(b) **If the taxpayer's service relates to tangible personal property, then the benefit is received where the tangible personal property is located or intended/expected to be located.**

   (i) Tangible personal property is generally treated as located where the place of principal use occurs. If the tangible personal property is subject to state licensing (e.g., motor vehicles), the principal place of use is presumed to be where the property is licensed; or
   (ii) If the tangible personal property will be created or delivered in the future, the principal place of use is where it is expected to be used or delivered.
(iii) The following is a nonexclusive list of services that relate to tangible personal property:
   (A) Designing specific/unique tangible personal property;
   (B) Appraisals;
   (C) Inspections of the tangible personal property;
   (D) Testing of the tangible personal property;
   (E) Veterinary services; and
   (F) Commission sales of tangible personal property.

(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.

(Emphasis in original.) Thus, determining where the Affiliates receive the benefit of Taxpayer’s services depends on the nature of the specific service, of which there are many categories in this case.

Here, the Audit Division attributed gross income to Washington based on the destination of sales made by the Affiliates. The Audit Division used this method for every category of service provided by Taxpayer to the Affiliates. In the Audit Division’s words, “the services performed are in support of the overall affiliate business activity (sales of paper products). The services that they provide support product sales activity of affiliates, including some that don’t have employees in WA.” Taxpayer disagrees with this reasoning, stating that the Audit Division “has applied an overly simplistic and expansive interpretation” of Rule 19402. Taxpayer argues that a one-size-fits-all method is not appropriate in its case. We agree with Taxpayer.

Rule 19402(303) requires that the method for determining where a customer receives the benefit of a taxpayer’s service depends on the specific service. Thus, 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 under Rule 19402 to determine where the benefit of each discrete service is received by the customer. Here, Taxpayer asserts this argument with respect to only [two] categories of services: (1) CEO & Staff, [and] (2) Human Resources. We address each category of service separately herein.
a. CEO & Staff Services

As discussed earlier, Taxpayer’s CEO & Staff services consist of providing shared corporate officers and support staff to the Affiliates. We conclude that such services are not related to real property or tangible personal property. Therefore, both Rule 19402(303)(a) and (b) are inapplicable here, and, instead, the determination of where the benefit of such services is received by the Affiliates is determined under Rule 19402(303)(c), which calls for the benefit of a taxpayer’s services to be attributed to where the customer’s “related business activity” occurs.

Here, the Audit Division found that the Affiliates’ “related business activity” was the sale of their products to consumers throughout the country. However, Rule 19402(304) provides an example that is relevant here, and defines the related business activity in a similar situation more narrowly:

Example 25. Director serves on the board of directors for DEF, Inc. Director's services relate to the general management of DEF, Inc. DEF, Inc. is Director's customer and receives the benefit of Director's services at its corporate domicile. Therefore, Director must attribute the receipts earned from Director's services to DEF to DEF's corporate domicile.

Here, Taxpayer, similar to Director in Example 25, provided CEO services to Affiliates. Such services are similar to the service in Example 25 of serving on the board of directors for DEF, Inc. Further, Example 25 identifies Director’s services as relating to “the general management of DEF, Inc.” We note that Example 25 does not expand DEF, Inc.’s related business activity to include any ultimate sales activity to consumers. Likewise, here, we conclude that Taxpayer’s CEO and Staff services relate to “the general management” of each Affiliate. Accordingly, we conclude that Example 25 is instructive here, and, consistent with that example, conclude that amounts of intercompany transactions associated with Taxpayer’s CEO and Staff services should be attributed to Affiliates’ corporate domiciles.

In light of the guidance provided under Example 25, we conclude that the Audit Division’s method of proportionally attributing intercompany transactions related to Taxpayer’s CEO and Staff services based on the location of sales of the Affiliates’ products to consumers is not reasonable. Under Rule 19402(106)(f), discussed earlier, a method is only reasonable if it “does not distort the taxpayer’s market.” Here, Taxpayer’s “market” for its CEO and Staff services is not the same as the Affiliates’ market for the sale of paper products. Instead, Taxpayer’s market is more properly described as being confined to the Affiliates. Expanding Taxpayer’s market for this specific service to the larger general market of the Affiliates’ sales, as the Audit Division’s method does, improperly distorts Taxpayer’s market. To conclude otherwise would be inconsistent with Example 25. Therefore, we conclude that the Audit Division’s method, as applied to Taxpayer’s CEO and Staffing services, is not reasonable under Rule 19402(106)(f).

Since none of the Affiliates have a corporate domicile in Washington, no intercompany transactions associated with Taxpayer’s CEO and Staff services are attributed to Washington, and, thus, none of the CEO and Staff service amounts are taxable in Washington. We remand to the Audit Division accordingly for appropriate adjustment to the receipts factor for the intercompany transfers associated with Taxpayer’s CEO and Staff services.
b. **Human Resources Services**

As discussed earlier, Taxpayer’s Human Resources Services consist of providing such services as hiring employees and medical benefit counseling for the Affiliates. We conclude that such services are not related to real property or tangible personal property. Therefore, both Rule 19402(303)(a) and (b) are inapplicable here, and, instead, the determination of where the benefit of such services is received by the Affiliates is determined under Rule 19402(303)(c), which calls for the benefit of a taxpayer’s services to be attributed to where the customer’s “related business activity” occurs. Once again, we look to the examples in Rule 19402(304)(c) for guidance:

**Example 24.** Company A provides human resources services to Racko, Inc. which has three offices that use those services in Washington, Oregon, and Idaho. Racko sells widgets and has customers for its widgets in all 50 states. The benefit of the service performed by Company A is received at Racko’s locations in Washington, Oregon, and Idaho. Assuming that each office is approximately the same size and uses the services to approximately the same extent, then attributing 1/3 of the receipts to each of the states in which Racko has locations using the services is a reasonable method of proportionally attributing Company A’s receipts from Racko.

Here, Taxpayer, similar to Company A in Example 24, provided Human Resources services to the Affiliates. Accordingly, we conclude that Example 24 is applicable here. As Example 24 makes clear, even though the customer in Example 24 sold widgets in all 50 states, the reasonable method of proportionally attributing the Company A’s receipts from Racko, Inc. for human resources services was to divide the receipts amount among the states where Racko, Inc.’s offices were located, and the location of widget sales was irrelevant. Thus, consistent with Example 24, a reasonable method here would be to divide the amount of intercompany transactions related to Taxpayer’s Human Resources services between the various locations around the country where the Affiliates have offices.

In light of the guidance provided under Example 24, we again conclude that the Audit Division’s method of proportionally attributing intercompany transactions related to Taxpayer’s Human Resources services based on the location of sales of the Affiliates’ products to consumers is not reasonable. Taxpayer’s “market” for its Human Resources services is confined to the Affiliates and expanding Taxpayer’s market for this specific service to the larger general market of the Affiliates’ consumer sales improperly distorts Taxpayer’s market. Further, any relationship that Taxpayer’s Human Resources services has to the Affiliates’ products sales is secondary at best. This is made clear from Example 24, which implies that Racko, Inc.’s “related business activity” is not its consumer sales of widgets, but something more administrative focused at the office locations. Therefore, we conclude that the Audit Division’s method, as applied to Taxpayer’s Human Resources services, is not reasonable under Rule 19402(106)(f).

Having concluded that the Audit Division’s method is unreasonable, we turn to Taxpayer’s suggested method of using Affiliates’ staff location. We conclude that such a method is reasonable under Rule 19402(106)(f) as it is consistent with Example 24, being based on the location of where the subjects of Human Resources services – the Affiliates’ employees – are likely concentrated, very similar to attributing based on office location described in Example 24. Therefore, we remand
to the Audit Division accordingly for appropriate adjustment to the receipts factor for the intercompany transactions associated with Taxpayer’s Human Resources services.

3. **Penalty Waiver**

Taxpayer also requests a waiver of the delinquent penalty and the five-percent assessment penalty that were assessed in the tax assessment, arguing that because the Department administratively closed its account, thereby providing Taxpayer “with a confirmation that our zero-dollar filing position taken on prior filings was appropriately filed.” We note that the notice that the Department sent to Taxpayer in 2011 regarding the administrative closure indicates that the closure was based on “no indication of taxable activity” because Taxpayer “did not report any gross income or file a return in the last two years.” There is nothing in that notice indicating that the Department had reviewed and approved of Taxpayer’s position regarding its Washington tax liability.

RCW 82.32A.020(2) gives taxpayers the right to a waiver of penalties where they have detrimentally relied on “specific, official written advice and written tax reporting instructions” from the Department. In Determination No. 05-0040, 24 WTD 407 (2005), we held that the Department’s administrative closure of a taxpayer’s account did not trigger a penalty waiver under RCW 82.32A.020(2), reasoning as follows:

All taxpayers have an obligation to “[k]now their tax reporting obligations, and when they are uncertain about their obligations, seek instructions from the department of revenue.” RCW 82.32A.030. A taxpayer who is notified that DOR has administratively closed its account thus has an obligation to know whether it still has a tax reporting obligation. If the account should remain active, the taxpayer may request that it remain open. WAC 458-20-101(14) (Rule 101(14)). If an account is closed, a taxpayer may request that it be reopened when its business activities require the taxpayer to report. Rule 101(15).

Consistent with our past holding, we conclude that the Department’s administrative closure of Taxpayer’s account did not constitute “specific, official written advice and written tax reporting instructions,” and was merely an administrative response to Taxpayer’s reporting of no business activity up to that point. That closure, however, did not relieve Taxpayer of its ongoing obligation to know its tax reporting obligations.

RCW 82.32.105 provides the only other circumstances under which the Department may waive penalties. Waiver of penalties is required when the Department finds that a taxpayer’s failure to pay the proper amount or to pay timely was the result of “circumstances beyond the taxpayer’s control.” RCW 82.32.105(1). “Circumstances beyond the control of the taxpayer,” in turn, is defined in WAC 458-20-228 (Rule 228), which states the following:

Circumstances beyond the control of the taxpayer are generally those which are immediate, unexpected, or in the nature of an emergency. Such circumstances result in the taxpayer not having reasonable time or opportunity to obtain an extension of the due date or otherwise timely file and pay.
Rule 228(9)(a)(ii). Rule 228(9)(a) goes on to provide examples of what circumstances generally qualify as “circumstances beyond the taxpayer’s control,” and what circumstances generally do not qualify as such. Rule 228(9)(a)(iii)(B) specifically states that “[a] misunderstanding or lack of knowledge of a tax liability” is generally not a circumstance beyond the taxpayer’s control. Taxpayer’s failure to report to the Department was due to its misunderstanding or lack of knowledge of its tax liability. Therefore, we conclude that Taxpayer has failed to offer a circumstance beyond its control under Rule 228(9)(a) that would allow us to grant a penalty waiver. See 24 WTD 407.

RCW 83.32.105(2) provides another means, commonly known as the “24-Month Rule,” by which the Department will waive a delinquent penalty. This second means, however, does not apply to the five-percent assessment penalty. As described more fully in Rule 228(9)(b), the 24-Month Rule provides that a delinquent penalty will be waived when (1) the taxpayer requests the waiver for a return required to be filed and the taxpayer has timely filed and (2) paid all tax returns due for a period of 24 months immediately preceding the period covered by the return for which the waiver is being requested. In addition, a taxpayer is only eligible for waiver under the 24-Month Rule if that taxpayer “has obtained a tax registration endorsement with the department prior to engaging in business” in Washington. Id.

It is undisputed that Taxpayer’s account was administratively closed in 2011, and Taxpayer was, therefore, not registered while it continued to engage in business that was taxable in Washington. Thus, we have no authority to waive any portion of the delinquent penalty under RCW 82.32.105(2) and Rule 228(9)(b). Accordingly, we affirm the assessment of both the delinquent penalty and the five-percent assessment penalty, subject to appropriate reductions based on other adjustments ordered elsewhere in this determination.

DECISION AND DISPOSITION

Taxpayer’s petition is denied in part and granted in part. We deny the petition with respect to Taxpayer’s arguments that (1) amounts of intercompany transactions related to Taxpayer’s CEO and Staff services are not part of Taxpayer’s gross income of the business, and (2) Taxpayer is entitled to a penalty waiver. We grant the petition with respect to Taxpayer’s arguments that (1) amounts booked to itself for its own share of corporate expenses is not part of Taxpayer’s gross income of the business, (2) amounts intercompany transactions related to Taxpayer’s CEO and Staff services should be proportionally attributed to the Affiliates’ domicile location, (3) amounts of intercompany transactions related to Taxpayer Human Resources should be proportionally attributed based on Affiliates’ staff locations.

Dated this 17th day of August 2017.