Cite as 10 WTD 417 (1990).

BEFORE THE INTERPRETATION AND APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Correction of Assessment of	)	D E T E R M I N A T I O N
	)	No. 91-062
. . .	)	Registration No. . . .
	)	. . ./Audit No. . . .
. . .	)	Registration No. . . .
	)	. . ./Audit No. . . .
. . .	)	Registration No. . . .
	)	. . ./Audit No. . . .

[1] RULE 111 -- REIMBURSEMENTS -- OFFICERS' SALARIES -- AFFILIATES. Payments among affiliates for wages and salaries of officers providing services for all corporations are subject to service business and occupation tax. ETB 90.04.203, See also Det. 88-28, 5 WTD 67 (1988)

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.

TAXPAYER REPRESENTED BY: . . .
. . .

DATE OF HEARING: November 27, 1990

NATURE OF ACTION:

The taxpayers petition for the correction of assessment of business and occupation taxes on salaries of corporate officers as well as the interest charges on the assessments.

FACTS AND ISSUES:

Pree, A.L.J. -- The taxpayers are a group of affiliated corporations with common owners. At the time of the audit, each corporation operated several retail . . . stores. All three corporations were managed out of a common, nonretail office.

Expenses of operating that office were divided and paid separately by each corporation. For instance, every month each corporation would write a check directly to the landlord for a portion of the rent. No corporation paid B&O tax regarding payment of these expenses by other corporations. With the exception of payroll, no audit adjustment was made regarding these expenses.

An outside payroll service used a separate, imprest account to pay the salaries and payroll expenses for the personnel in the administrative office. The payroll service would compute the total amount due, and each corporation would remit its share of employee expenses the day before the employees were to be paid to an imprest account. That account was maintained solely for payroll purposes.
The account was not listed as an asset on the balance sheets of any of the taxpayers since its balance was zero at the end of any accounting period. According to the taxpayers, no single corporation "owned" the account.

At the request of, and for the convenience of the payroll service, each employee received a W-2 Form from a single corporation for his/her total salary paid by all the corporations. The taxpayers have provided a copy of an employment agreement with an officer of all the corporations which shows that they are all liable to an employee for his salary. The taxpayers indicate that each employee working at the administrative office understood that he/she worked for and was paid by all the corporations. Employees working at the retail stores understood that they worked only for the corporation which operated the particular retail establishment where they worked and was shown on their W-2.

The Audit Division assessed Service Business and Occupation tax to each corporation shown on a W-2 based on the amount of the salaries for those administrative personnel paid by the W-2 corporation and charged back to the other corporations. The taxpayer disputes those assessments, contending that the employees were working under the control of all three corporations rather than just the corporation listed on the W-

2. Therefore, the W-2 corporations were not providing services to the other corporations.

After the hearing the taxpayer sent a copy of the former president's contract. The contract listed each of the corporations as employer. Their liability was clearly joint. Incentive compensation was computed based on the aggregate profitability of all the corporations.

In addition, the taxpayers dispute the computation as well as sampling method used to arrive at the assessment. The auditor indicates that when he knew an adjustment would be made based on reviewing four two-week periods, he requested the rest of the books from the taxpayer to arrive at the actual amount. He was never provided the books and the assessment was based on a projected figure.

Finally, the taxpayers protest the additional interest added to the assessment, contending that it was due to the unreasonable delay from the time audit fieldwork was completed until the time they received the assessments. The auditor states that he was waiting for the taxpayer to provide the records that he had requested.

DISCUSSION:

RCW 82.04.220 imposes a business and occupation tax on the gross income of a business. For the purposes of the service business and occupation tax, RCW 82.04.080 defines gross income of a business to include the value proceeding or accruing by reason of the transaction of the business without any deduction on account of the expenses of the business.

WAC 458-20-111 (Rule 111) provides an exclusion from gross income for "amounts representing money or credit received by a taxpayer as reimbursement of an advance in accordance with the regular and usual custom of his business or profession." Rule 111 limits the applicability of the exclusion to cases where the taxpayer is not liable for making the payment, stating:

> The words "advance" and "reimbursement" apply only when the customer or client alone is liable for the payment of fees or costs and when the taxpayer making the payment has no personal liability therefor, either primarily or secondarily other than as agent for the customer or client. (emphasis added)

A "common paymaster" is generally a third party entity created solely to pay shared expenses of various principals. Often, it is merely a checking account. Each contributes the amount paid out attributable to it. The separate principals continue to carry on their businesses under their own names and report and pay B & O taxes under their own names. Advances for wages and salaries paid for by others to a common paymaster are excludable.[1]

The issue is whether or not the taxpayer was acting solely as a paymaster and had no personal liability for providing the wages or other services. In the recent case, Rho v. Department of Revenue, 113 Wn2d 561 (1989), the Supreme Court of Washington guides us in making that determination. Resolution of the sole liability issue requires analysis of the control over the employees by the taxpayer as compared with the party making payments through the taxpayer for the services of those employees. It must be determined whether the taxpayer's control over the performers was merely that of paymaster acting as agent for the other corporations. We must look beyond the contract language to factors of control such as hiring, compensation, work assignment, supervision, and termination.

The employees working at the retail outlets were controlled by the corporation running those outlets and were employees of those particular corporations. The auditor did not include their wages and salaries in the adjustment.

However, the auditor did adjust the payments for wages and salaries of the officers and employees performing administrative services for all the corporations. Their control was not limited to any single corporation. All the taxpayers were liable for their full salaries. Their duties were administrative, benefitting all the taxpayers.

WAC 458-20-203 (Rule 203) provides that each separately organized corporation is a "person" within the meaning of the law, notwithstanding its affiliation with or relation to any other corporation through stock ownership by a parent corporation by the same group of individuals. The Department considers management charges from a parent corporation to its subsidiaries subject to business occupation tax under the

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[1] Det. 86-234, 1 WTD 103 (1986); Det. 88-9, 4 WTD 433 (1988)

service classification.[2] Similarly, administrative and personnel charges between affiliated corporations are subject to business occupation tax under the service classification.[3]

The taxpayer relies on one of the department's determinations[4] which also involved a number of affiliates with employees working in different capacities. In that determination, the administrative law judge found that employees working for particular affiliates were not loaned servants and therefore, amounts paid for their services to the paymaster were not subject to service business and occupation tax. Their relationship with particular affiliates was similar to that of the employees working at particular retail outlets in this case for which no assessment was made.

Rather this issue centers around those employees who were officers and whose duties were primarily to coordinate the activities of the affiliates and to provide services to mutually benefit all the affiliates. Each officer was paid by one affiliate, then adjusting entries were made in its books for payments received by the other affiliates.

The duties of the officers at issue in this case were most similar to those of the controller in the determination whose salary was subject to tax. As in that determination, it is not conceivable that any of the affiliates could fire an officer and that he would remain employed by any of the other affiliates.

Unlike the facts in that determination, there was no formal cost sharing agreement here where the affiliates agreed in writing that a particular affiliate was liable. To the contrary, here the affiliates were jointly liable as made clear in the employment agreement. Their bonuses were based on the combined profits of the affiliates. The corporation shown on the W-2 was liable for the full amount of the salary. The requirement in Rule 111 that the taxpayer not be personally liable either primarily or secondarily was not met.

In the determination cited, an officer would be on notice that only one, not all the affiliates were liable for his salary.

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[2] ETB 50.04.203 (. . .)

[3] ETB 90.04.203 (. . .)

[4] Det. 88-28, 5 WTD 67 (1988).

The agreement specified that the taxpayer making the payments was acting in the capacity as agent. Any employee, such as an officer, aware of the agreement would be on notice that the capacity of the taxpayer making payment was that of an agent with liability limited to that capacity.

There is no mention in any agreements that the corporation making payment in this case was doing so in the capacity of agent. That is a key distinction here. Under Rule 111, for a payment to be excluded the following requirement must be met:

> . . . the taxpayer making the payment has no personal liability therefor, either primarily or secondarily other than as agent for the customer or client.

The taxpayers making payment here were liable for the full amount and not merely agents. There is no basis under the rule for excluding those payments from gross income. Therefore, the auditor properly included them in determining the assessment.

[2] Regarding the sampling issue, the auditor offered and still agrees to review the actual records of the taxpayer. The taxpayer must submit all the pertinent records to the auditor within thirty days of this determination.

[3] WAC 458-20-228 (Rule 228) provides in part:

> The following situations will constitute circumstances under which a waiver or cancellation of interest upon assessments pursuant to RCW 82.32.050 will be considered by the department:
>
> 1. The failure to pay the tax prior to issuance of the assessment was the direct result of written instructions given the taxpayer by the department.
>
> 2. Extension of the due date for payment of an assessment was not at the request of the taxpayer and was for the sole convenience of the department.

The issue is whether the delay resulting in the increased interest was for the sole convenience of the department. Much of the delay was the result of the confusion between the taxpayer and the auditor. However, some delay was for the sole convenience of this division of the Department and that interest is hereby waived.

DECISION AND DISPOSITION:

The tax assessment is remanded to the Audit Division for further review. The taxpayer has 30 days to contact the auditor and make available all the records to establish its position regarding actual expenses rather than those developed in the auditor's sample. Interest is waived for the period from [June 1990] to today's date since the delay was for the convenience of the Department.

DATED this 8th day of March 1991.