Cite as Det. No. 88-310, 6 WTD 273 (1988)

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

In the Matter of the Petition For Refund of	)	D E T E R M I N A T I O N
	)	No. 88-310[1]
. . .	)	Registration No. . . .
	)	Tax Assessment Nos. . . .

[1] **RULE 224, RCW 82.04.290 AND RCW 82.04.260**: SERVICE B&O TAX -- TRAVEL AGENT COMMISSION B&O TAX -- TOUR OPERATOR -- TOUR PACKAGES. The amounts received by a tour operator on the sale of its own arranged tour packages where other persons provide the transportation, hotel accommodations, sightseeing, meals, etc., are subject to Service B&O tax. Amounts received by a tour operator as commissions from third party service providers are subject to Travel Agent Commission B&O tax.

[2] **RULE 111**: SERVICE B&O TAX -- DEDUCTION -- ADVANCE/REIMBURSEMENT -- TOUR OPERATOR -- AGENT OF TOURIST -- PAYMENTS TO THIRD PARTY SERVICE PROVIDERS. Where a tour operator has a contractual arrangement with the tourist to be its agent in securing the services of third providers per packaged tours, the tour operator's payments to the service providers are deductible from the measure of the tax under Rule 111's advance/reimbursement principle.

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: . . .
. . .
. . .
. . .
. . .

[1] The reconsideration determination, Det. No. 88-310A, is published at 10 WTD 270 (1990).

DATE OF HEARING: July 9, 1987

NATURE OF ACTION:

Petition for refund of taxes paid on amounts which the auditor did not allow as an advance/reimbursement deduction from the measure of the tax.

FACTS AND ISSUES:

Krebs, A.L.J. -- . . . (taxpayer) is engaged in business as a tour operator and travel agent. . . . .

The taxpayer commenced taxable business activities in October 1979 and was not registered with the Department of Revenue until the Department registered it in March 1985 for purposes of audit and assessment of taxes.

The Department of Revenue examined the taxpayer's business records for the period from October 1, 1979 through December 31, 1984. As a result of this audit, the Department issued Tax Assessment Nos. . . . and . . . on October 22, 1985 asserting excise tax liability in the combined amount of $ . . . plus interest and penalties in the combined amount of $ . . . for a total sum of $ . . . which has been paid in full.

The taxpayer seeks a refund of taxes paid which involves Schedule II of the audit report where Travel Agent Commission business and occupation (B&O) tax was assessed on the taxpayer's gross revenue from the sale of tour packages, the operation of sightseeing tours and commissions received from some hotels.

The taxpayer asserts that the auditor improperly denied the exclusion from the taxpayer's taxable gross income of amounts paid to other service providers such as Amtrak, hotels and cruise lines on tours arranged by the taxpayer for which the tour participants pay a single amount for the total package. The taxpayer contends that such amounts paid to the service providers are excludable pursuant to WAC 458-20-111 (Rule 111), . . ., as advances received by it as agent for the tourist/customer to pay the service providers. The taxpayer further contends it has "no separate liability to pay the third party service providers for the services which they provide as part of tour packages. This is a liability of the tour participants."

The taxpayer cites the Washington Supreme Court case of Walthew v. Department of Revenue, 103 Wn.2d 183 (1984), as holding that Rule 111 excludes amounts received as an agent even though the agent may be liable to a third party, as agent, to remit the funds received.

The taxpayer asserts that the decision in Walthew is directly applicable because (1) the only services which the taxpayer provides and for which it is compensated are the motor coaches and its arrangement of the tour package, and (2) the relationship between the taxpayer and the tour customer is one of agent and principal. The taxpayer points to its brochure and other advertising as stating that it "acts solely in the capacity of an agent on behalf of its clients in arranging for transportation, lodging, sightseeing and other services . . . which are a part of the arrangements requested."

The issue is whether the taxpayer's payments to third party providers of transportation, lodging, and other services to tour participants are deductible from the measure of tax under the advance/reimbursement principle of Rule 111.

DISCUSSION:

[1] The B&O tax is imposed by RCW 82.04.220 which provides:

> There is levied and shall be collected from every person a tax for the act or privilege of engaging in business activities. Such tax shall be measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be. (Emphasis supplied.)

RCW 82.04.260 (10) provides for the travel agent classification as follows:

> Upon every person engaging within this state in the business of acting as a travel agent; as to such persons the amount of the tax with respect to such activities shall be equal to the gross income derived from such activities multiplied by the rate of . . . (Emphasis supplied.)

RCW 82.04.290 provides for the Service classification as follows:

> Upon every person engaging within this state in any business activity other than or in addition to those enumerated in RCW . . . 82.04.260 . . .; as to such persons the amount of tax on account of such activities shall be equal to the gross income of the business multiplied by the rate of . . .

Thus, if the taxpayer acts as a travel agent, it is within the travel agent classification for tax purposes. Otherwise, its business activity is within the Service classification. Neither the statutory law nor the administrative regulations define the term "travel agent." Nor do law and general dictionaries define such term. We believe that the "yellow pages" of the telephone directory (Tacoma and Seattle) which has a separate classification for "travel agencies and bureaus" and their advertisements describing the "business activities" of a travel agent will serve to tell what a travel agent does. Such advertisements stress ticketing and reservations for travel by air, bus, cruise ship and train, and the rendering of other related travel services such as car rental and hotel reservation, and passport and visa assistance.

The "yellow pages" of the Seattle telephone directory have a separate classification for "Tours -- Operators and Promoters" which carries the listing of the taxpayer's business name of " . . . ." The taxpayer has no telephone listing under the classification of "travel agencies and bureaus."

The taxpayer has developed a variety of packaged tours which it sells to tour participants. The tours range from 2 days/1 night to 13 days/12 nights in duration. The package includes such items as overnight hotel accommodations, local transfers between hotels and terminals as

necessary, ferry service and boat rides, transportation between cities, narrated sightseeing of cities and other areas, meals and snacks, . . . , and tours of national parks.

. . . . Where the item involved ticketing for transportation services provided by others, the taxpayer received a travel agent commission. As to the other major item of hotel accommodations, the taxpayer received a preferred rate from the hotels which it viewed as a net price after commission.

The taxpayer does not give an itemization to the tour participant of the actual cost (amounts paid to providers by the taxpayer) of the transportation, lodging, meals, entrance fees, etc. The taxpayer charges a tour package price which is based on its net costs plus a markup. The taxpayer, in effect, operates differently from the conventional and usual travel agent who discloses the provider's charge to the customer for the transportation and lodging and who receives a travel agent commission from the provider.

In unpublished Final Determination No. 85-146A issued April 10, 1986, subsequent to the issuance of the subject assessments on October 22, 1985, the Department clarified its position with respect to tour operators by holding that:

> Persons who produce and provide their own tour packages, excursions, and similar conducted and service provider operated activities are subject to the Service and Other Business Activities classification of tax. . . . The taxpayer's gross receipts from tour sales will be restored to the Service business tax classification.

In this case, the taxpayer produces and provides its own tour packages and excursions. Accordingly, we hold that the amounts received by the taxpayer on its sale of its own tour packages are subject to the Service B&O tax. The amounts received by the taxpayer as commissions from transportation providers and hotels, whether or not the services provided are part of the taxpayer's tour package, are subject to the Travel Agent Commission B&O tax. Where the hotel contracts to give the taxpayer a preferred rate, the amount discounted is not a commission received by the taxpayer.

Having found the taxpayer's gross receipts from the sale of tour packages subject to Service B&O tax, we now turn to the question as to whether the taxpayer's payments to third party providers of transportation, lodging and other services to tour participants are deductible from the measure of the tax under the advance/reimbursement principle of Rule 111.

It should be noted that where a travel agent reports only its receipt of commissions for taxation (indeed, the monthly tax return has it tax classified as "travel agent commissions"), there is a "built-in deduction" for amounts paid by the travel agent to providers. Such amounts are ordinarily part of the gross income of the travel agent's business. But, because the travel agent receives the income as an advance for payment to the provider under the advance/reimbursement principle of Rule 111, it gives rise to the "built-in deduction."

[2] Rule 111 in pertinent part provides:

> The word "advance" as used herein, means money or credits received by a taxpayer from a customer or client with which the taxpayer is to pay costs or fees for the customer or client.
>
> The word "reimbursement" as used herein, means money or credits received from a customer or client to repay the taxpayer for money or credits expended by the taxpayer in payment of costs or fees for the client.
>
> The words "advance" and "reimbursement" apply only when the customer or client alone is liable for the payment of the 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.
>
> There may be excluded from the measure of tax 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.
>
> The foregoing is limited to cases wherein the taxpayer, as an incident to the business, undertakes, on behalf of the customer, guest or client, the payment of money, either upon an obligation owing by the customer, guest or client to a third person, or in procuring a service for the customer, guest or client which the taxpayer does not or cannot render and for which no liability attaches to the taxpayer. It does not apply to cases where the customer, guest or client makes advances to the taxpayer upon services to be rendered by the taxpayer or upon goods to be purchased by the taxpayer in carrying on the business in which the taxpayer engages.

Rule 111 recognizes that "advances" and "reimbursements," as defined therein, may be excluded from the measure of the tax because they are not compensation or consideration for the service rendered which is the basis for the tax. RCW 82.04.080 and RCW 82.04.090, Walthew v. Department of Revenue, supra. Thus, to be excludable from the measure of the tax under Rule 111, the payments received by the taxpayer must (1) be made as part of the regular and usual custom of the taxpayer's business or profession, (2) must be services to the customer which the taxpayer does not or cannot render, and (3) the taxpayer must not be personally liable for paying the customer's fees or costs, either primarily or secondarily, except as agent for its customer.

In this case, the taxpayer meets the first requirement because it is the regular and usual custom of the taxpayer and other tour operators to receive payments for the tour package in advance from the customer before the customer embarks upon the tour. The taxpayer meets the second requirement because it does not and cannot render the services (transportation by air, train and boat, hotel accommodations, meals, etc.) to the customer. . . . .

The taxpayer meets the third requirement because in its contractual arrangement with its tourist-customer it is specifically stated that the taxpayer "acts solely in the capacity of an agent on behalf of its clients in arranging for transportation, lodging, sightseeing and other services."

Furthermore, the service providers are made aware by the taxpayer that it is acting in the capacity of an agent on behalf of its customer. The transportation companies pay travel agent commissions to the taxpayer. The hotels contract to give the taxpayer a preferred rate in recognition of its agency status. The hotels always hold the customer liable per hotel bill presented to the customer if they do not receive payment from the taxpayer, but because the taxpayer as agent always receives payment in advance from the customer it is always in a position to pay the hotels and has done so.

We conclude that the taxpayer's payments to third party service providers who have provided services to tour participants are deductible from the measure of the Service B&O tax.

The holding in this Determination requires that the taxpayer's gross receipts from the sale of tour packages minus the deduction for payments to third party service providers be subjected to Service B&O tax. Amounts received by the taxpayer as travel agent commissions from transportation and hotel service providers are subject to Travel Agent Commission B&O tax which already has the "built-in advance/reimbursement deduction."

Because the auditor's instructions to the taxpayer were that the taxpayer should report revenue from the sale of tour packages and operation of sightseeing tours under the travel agent classification, and generally without an advance/reimbursement deduction, the taxpayer will not be held liable for any tax deficiency caused by following such instructions. However, prospectively from the date of this Determination, the taxpayer is required to follow the holding in this Determination, as set forth in the antecedent paragraph, in the filing of its tax returns.

DECISION AND DISPOSITION:

The taxpayer's petition is partially granted. The matter is being referred to the Department's Audit Section for adjustment of the audit in line with the holding of this Determination. If such adjustment warrants a refund, the Audit Section will authorize a refund which shall include statutory interest. If such adjustment results in a deficiency, the deficiency will be waived because at the time of the audit the Department's position as to tour operators had not been clarified and there would be an inequitable result if enforced against this taxpayer vis-a-vis other taxpayers.

DATED this 5th day of August 1988.