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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. 90-226
. . .	)	Registration No. . . .
	)	. . ./Audit No. . . .
. . .	)	Registration No. . . .
	)	. . ./Audit No. . . .

[1] RULE 128, RULE 111 & RULE 201 -- B&O TAX - EXCLUSION - ADVANCE AND REIMBURSEMENTS - REAL ESTATE BROKERAGE - EXPENSES REIMBURSED BY AGENTS. A real estate brokerage may not exclude reimbursements received from its salespersons for services provided by third parties (such as telephone, multiple listings) from gross income if it is either primarily or secondarily liable for the charges, unless solely as agent.

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.

NATURE OF ACTION:

Two taxpayers protest additional taxes and interest assessed in their audit reports. Because of the close affiliation of the two taxpayers involved and the identical nature of the issues involved, the petitions have been consolidated for purposes of appeal.

Because the taxpayer's petition and the audit reports clearly explain the issue in controversy, we have determined that a further conference is not required for the proper disposition of this case.

FACTS:

Okimoto, A.L.J. -- . . . , Inc., and . . . , Inc. (hereinafter referred to as " . . . " and " . . . " respectively, or "taxpayer" collectively) are real estate brokerage offices conducting business in . . ., Washington. . . . and . . . 's business records were examined by a Department of Revenue (Department) auditor for the period . . . through . . . . The Department issued the above-referenced tax assessments for additional taxes and interest on . . . in the amounts of $ . . . and $ . . . , respectively. Both taxpayers have paid the tax assessments in full, and now petition for refunds.

All of the corporate taxpayer's income is derived from real estate commissions. The taxpayer uses real estate salespersons, each of whom is an independent contractor, to facilitate the buying and selling of real property. The taxpayer pays B&O taxes on the entire gross commission income (including the salesperson's portion) received from its clients for the sale of the property.

After the commission on the sale is split in accordance with the negotiated percentage, the taxpayer receives additional amounts as reimbursements for certain expenses attributable to its salespersons. The auditor included in the taxpayer's gross income reimbursements received for multiple listing expenses, telephone charges, and other miscellaneous expenses billed to the taxpayer but attributable to its salespersons. Although requested sample invoices have not been submitted by the taxpayer, it appears that the third party providers billed the taxpayer directly for these expenses. After receiving the bill, the taxpayer then paid the bills and collected the money from its salespersons through a reduction of the salesperson's commission account.

TAXPAYER'S EXCEPTIONS:

First, the taxpayer claims that taxing income from salesperson reimbursements constitutes a double taxation of the commission income which is precluded by Davenport, Inc. v. Department of Revenue, 6 Wash. App. 581, 494 P.2d 1376 (1972). The taxpayer argues that the state is taxing the same dollar twice: first, as a commission received by the corporation, and again when the salesperson uses his or her portion of the commission to reimburse the corporation for expenses.

Second, the taxpayer contends that the payments should be excluded as an "advance and reimbursement" under WAC 458-20-111 (Rule 111). The taxpayer argues that it does not have "sole responsibility" for payment of the expenses, because the contract between the salespersons and the taxpayer provides that the salespersons "must" reimburse the taxpayer for these expenses. Therefore, the taxpayer contends that the primary liability for payment of these expenses lies on the salespersons and not the taxpayer. The taxpayer also contends that these payments are merely passed through to the salespersons.

Finally, the taxpayer argues that the reimbursements are exempt from taxation as "Inter-Departmental" charges. The taxpayer contends that the Washington Court recognized a real estate brokerage office as a "group of individuals acting as a unit for purposes of tax assessments against commissions" in Davenport, supra. The taxpayer believes that this single unit analysis is equally applicable to other B&O tax assessments.

ISSUE:

May a real estate brokerage office exclude from gross income amounts received from its salespersons as reimbursements for services billed directly to the taxpayer but performed by third parties?

DISCUSSION:

[1] We believe that the Davenport case is clearly distinguishable from the taxpayer's situation. In Davenport, the Department attempted to tax commission income earned on a single sale of real estate on successive distributions to the parties involved in earning that commission. First, the Department taxed the 100% of the total commission earned on the sale when it was paid to the brokerage, and second, the Department taxed that portion of the commission earned by the agent when it was distributed to the agent by the brokerage. The Court held that the Legislature only intended to tax the activity of earning that commission (sale of property) one time, and that the subsequent distribution to the agent was not taxable. In the taxpayer's case, however, we have two separate taxable activities. First, there is the sale of the property from which the commission is earned, and second, the paying, consolidating and allocating of various overhead expenses between the different salespersons.

Nor do we believe that the income is entitled to be excluded as an advance and reimbursement. Rule 111 provides in part as follows:

> 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. . . . [Emphasis ours.]

Therefore, a real estate brokerage may not exclude reimbursements for services provided by third parties (such as telephone and multiple listing) from gross income when it is either primarily or secondarily liable to the third party provider, unless solely as agent.

In this case, it appears that the taxpayer contracted with third party providers and was billed directly for the expenses involved. Therefore, the third party providers had a contractual right to look to the taxpayer for payment and had no such right with the taxpayer's salespersons. The mere fact that the taxpayer could contractually recover those expenses from its salespersons, simply does not relegate its own status to one of agency. In addition, the Department has consistently held that:

> ... Any person who claims to be acting merely as agent ... in making purchases for a buyer, will have such claim recognized only when the contract or agreement between such persons clearly establishes the relationship of principal and agent and when the following conditions are complied with:
>
> (1) The books and records of the broker or agent show the transactions were made in the name and for the account of the principal, and show the name of the actual owner of the property for whom the sale was made, or the actual buyer for whom the purchase was made.
>
> (2) The books and records show the amount of gross sales, the amount of commissions and any other incidental income derived by the broker or agent from such sales. WAC 458-20-159 [Emphasis ours]

The taxpayer has presented no such evidence to clearly establish its status, and we therefore conclude that the taxpayer contracted with the third party providers in its own capacity, and not as an agent.

Finally, we do not believe that the transactions are exempt as interdepartmental charges. The definition of a real estate brokerage office cited in the Davenport case is applicable only for "purposes of tax assessments against commissions" and has no application in respect to other transactions.

Furthermore, although WAC 458-20-201, (Rule 201) allows an exemption for "interdepartmental charges," it "does not permit the exclusion or deduction of charges against or income derived from an affiliated corporation or other affiliated association." The contract between the taxpayer and its salespersons clearly identifies the salespersons as independent contractors. The contract provides:

> The parties agree that Associate is an independent contractor for federal tax and all other purposes, and is not an employee of, or partner with the Broker.

As an independent contractor, each salesperson is a legal entity separately engaged in business within the state. Therefore, transactions between the taxpayer and its affiliated independent contractors may not be deducted. Accordingly, we must deny the taxpayer's petition on this issue.

DECISION AND DISPOSITION:

The taxpayer's petition for refund is denied.

DATED this 31st day of May, 1990.