Cite as 3 WTD 195 (1987)

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

In the Matter of the Petition For Ruling of Tax Liability of	D E T E R M I N A T I O N
	No. 87-186
. . .	Registration No. . . .
	Tax Assessment No. . . .

[1] **RULE 194, RCW 82.04.460 AND RCW 82.04.4286:** APPORTIONMENT -- PLACE OF BUSINESS -- DUE PROCESS CLAUSE -- COMMERCE CLAUSE. Apportionment may not be denied solely because a taxpayer does not maintain a place of business outside this state.

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: March 18, 1986

NATURE OF ACTION:

Taxpayer, a voluntary association of Northwest auto dealers organized as a Washington non-profit corporation, requests a ruling on whether it may apportion gross income derived from directing cooperative advertising for its members in various northwest states.

FACTS:

Rosenbloom, A.L.J. (successor to Chandler, A.L.J.) -- The taxpayer is a Washington non-profit corporation whose members are . . . dealers located in Washington, [and other northwest states]. The taxpayer's revenue is derived from assessments upon its members based upon the number of new cars each

receives from the manufacturer. The assessments are paid directly to the manufacturer. The manufacturer in turn passes these revenues on to the taxpayer. The manufacturer issues only one check, but provides the taxpayer with an itemization of each member's contribution.

The taxpayer uses these revenues to finance regional advertising in the geographical areas in which its members are located. Advertising expenditures are distributed among the various areas in the same proportion as assessment revenues are received from each area. Decisions regarding the purchasing of advertising are made by the taxpayer's Board of Directors at its monthly meetings.

The Board of Directors holds its meetings alternately within and outside the state at temporary locations. The taxpayer has no office or regular place of business in any state. The taxpayer's books and records are maintained in this state in the office of its Certified Public Accountant, but the taxpayer does not hold Board meetings or otherwise engage in any business activities at that address.

The taxpayer has been the subject of numerous audits by the Department. In each prior audit, the Department has acknowledged the taxpayer's right to apportion its gross income, paying B&O tax only upon gross income derived from assessments upon members located in Washington. In the most recent audit, however, the taxpayer was provided with instructions for future reporting to the effect that all of its gross receipts are subject to tax without apportionment. The taxpayer has petitioned for a ruling of tax liability. Specifically, the taxpayer requests a ruling that it be allowed to continue paying B&O tax only upon gross income derived from assessments upon its members located in Washington.

DISCUSSION:

The auditor takes the position that the taxpayer's gross receipts are subject to tax without apportionment because: (1) The taxpayer is a Washington corporation, and its books and records are maintained in this state; (2) the taxpayer maintains no place of business outside this state; and (3) no portion of the taxpayer's gross receipts appears to be subject to tax by any other state. We disagree.

Tax liability does not result merely because the taxpayer is incorporated under the laws of this state, or because the

taxpayer's books and records are maintained in the office of a certified public accountant within this state. The taxpayer is liable for Washington B&O tax only to the extent that it engages in taxable business activities within this state. Here, the taxpayer engages in taxable business activities within this state; however, the taxpayer also engages in substantial business activities without the state. This state has no power to levy a tax upon activities that occur outside its territorial limits. Dravo Corp. v. Tacoma, 80 Wn.2d 500 (1972).

[1] Apportionment may not be denied solely because the taxpayer does not maintain a place of business outside this state. RCW 82.04.460 prescribes alternative methods of apportionment for "person(s) rendering services taxable under RCW 82.04.290 and maintaining places of business both within and without this state which contribute to the rendition of such services." Plainly the statute does not apply in this case since the taxpayer maintains no regular place of business, either within or outside this state. This does not mean, however, that all of the taxpayer's gross receipts are subject to Washington tax. RCW 82.04.4286 allows a B&O tax deduction for amounts derived from business which the state is prohibited from taxing under the Constitution of the United States. A recent Washington Supreme Court decision contains the following discussion of the due process clause of the federal Constitution:

> Due process focuses on whether a state is taxing beyond its jurisdictional reach. (citation omitted.) The test applied to state taxation of interstate business under the due process clause has two prongs: (1) There must be a "minimal connection" or "nexus" between the interstate taxing activities and the taxing state; and (2) the income attributed to the state for tax purposes must be rationally related to "'values connected with the taxing state.'" (Citations omitted.) Nexus is established if the corporation "avails itself of the 'substantial privilege of carrying on business' within the state." (Citation omitted.)

Chicago Bridge and Iron Co. v. Dept. of Revenue, 98 Wn.2d 814, 820 (1983).

Clearly, the taxpayer has availed itself of the substantial privilege of carrying on business within this state. It is

incorporated under the laws of this state and engages in business within this state. Thus, nexus is established.

However, the taxpayer also engages in substantial business activities outside this state. A Washington tax on gross income derived from activities substantially performed both within and outside this state would be a tax "out of all proportion to the business transacted" in this state, 98 Wn.2d at 823, thus running afoul of the second prong of the due process clause.

Moreover, the commerce clause requirements of a state tax on interstate business are as follows: (1) There must be a sufficient connection or nexus between the interstate activities and the taxing state; (2) the tax must be fairly apportioned; (3) the tax must not discriminate against interstate commerce; and (4) the tax must be fairly related to the services provided by the state. Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 51 L.Ed.2d 326, 97 S. Ct. 1076 (1977).

The auditor's conclusion that apportionment is not available may have been based on the following language of WAC 458-20-194 (Rule 194):

> When the business involves a transaction taxable under the classification service and other business activities, . . . the tax applies upon the income received for services incidentally rendered to persons outside this state by a person domiciled herein who does not maintain a place of business within the jurisdiction of the place of domicile of the person to whom the service is rendered.

However, this provision is not controlling in this case. The key word is incidentally. Where, as here, services are substantially rendered to persons outside this state, the provision has no application.

Thus, irrespective of whether the taxpayer meets the precise terms of RCW 82.04.460, the United States Constitution, and thus RCW 82.04.4286, requires apportionment of gross receipts derived from business activities which are substantially performed both within and outside the state.

Finally, it is irrelevant whether any other state imposes a tax on any portion of the taxpayer's gross receipts. Washington may assert B&O tax only to the extent that the

taxpayer engages in taxable business activities within the territorial limits of this state, Dravo Corp. v. Tacoma, supra. And gross receipts derived from services substantially rendered both within and outside this state are entitled to apportionment, regardless of whether any other state chooses to tax any portion of such receipts.

DECISION AND DISPOSITION:

The instructions for future reporting included in Tax Assessment No. . . . are withdrawn. The taxpayer may continue to apportion gross receipts and pay B&O tax only upon gross income derived from assessments upon members located in Washington.

DATED this 2nd day of June 1987.