

Cite as Det. No. 14-0237R, 34 WTD 515 (2015)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of) D E T E R M I N A T I O N
Assessment of) No. 14-0237R
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)
)
...) Registration No. . . .
)

[1] RCW 82.04.43393: B&O TAX – DEDUCTION – PAYMASTER SERVICES – PROSPECTIVE APPLICATION. The deduction for paymaster services is new law and applies prospectively.

[2] RULE 111; RCW 82.04.080: B&O TAX – GROSS INCOME – ADVANCES AND REIMBURSEMENTS – PAYMASTERS AND EMPLOYERS OF RECORD. Because the taxpayer failed to prove that it has no liability to pay employer obligations except as an agent of its affiliates, it does not qualify for exclusion of income.

[3] RULE 101(14); RCW 82.32.050(4): STATUTORY LIMITATION ON ASSESSMENTS. Where the taxpayer closed its account and rescinded its registration with the Department, we find no basis for limiting the statutory assessment period.

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.

Margolis, A.L.J. – A lessor of employees to affiliated companies (Taxpayer) petitions for reconsideration of Det. No. 14-0237, which held that Taxpayer cannot exclude amounts received for payroll and employee expenses from its measure of business and occupation (B&O) tax, and the Department of Revenue (the Department) can assess Taxpayer for tax periods 2004 through 2006 when it was previously registered but not registered when audited by the Department. Taxpayer’s petition is denied.¹

ISSUES

1. Whether Taxpayer is entitled to the deduction under RCW 82.04.43393, effective October 1, 2013, for periods prior to October 1, 2013.

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

2. Whether, under WAC 458-20-111 and ETA 3181.2013, Taxpayer may exclude amounts received to pay employer obligations absent evidence that it had no liability to pay employer obligations except as an agent of the client.
3. Whether, under RCW 82.32.050(4), the Department can assess Taxpayer for periods beyond the four-year statute.

FINDINGS OF FACT

As explained in Det. No. 14-0237 (in pertinent part),

Taxpayer [a wholly-owned subsidiary of [Parent]] leases employees to Parent's operating companies Per IRS Form 941s, Taxpayer is the employer of record for the employees. It does not file IRS Form 8655 to disclaim that it is an employer. Per IRS Form 1120s, Taxpayer reports the payroll expenses

[T]he employee leasing agreement between Taxpayer and Affiliates, dated January 1, 2001, clearly designates Taxpayer as the employer in control of the employees and states as follows (in pertinent part): . . .

3. All persons employed by [Taxpayer] who render service to the [Affiliates] shall be employees of [Taxpayer] alone and [Taxpayer] may hire, discharge or transfer such employees in such manner as it, in its sole discretion shall deem advisable or appropriate. Such employees shall be entitled to all benefits to their status as [Taxpayer's] employees, including the right to participate in any profit sharing or retirement plan, group insurance, employee's discounts, and other benefits available to [Taxpayer's] employees.

Taxpayer . . . filed a Master Business Application (MBA) on April 27, 2001

Department notes show that Taxpayer contacted the Department on May 17, 2005, and closed its account effective December 31, 2001

On August 9, 2011, the Department of Revenue's Audit Division (Audit) notified Taxpayer that Audit would be examining Taxpayer's books and records, and requested that Taxpayer provide a Washington Business Activities Questionnaire (WBAQ) Taxpayer also signed and returned Statute of Limitations Non-Claim Period Waiver Agreements (Waivers), which cover the periods January 1, 2004 through December 31, 2004 and January 1, 2005 through December 31, 2005, and expire, after extensions, on June 30, 2013

Audit examined Taxpayer's account, and on June 28, 2013, issued two assessments For the period January 1, 2004 through December 31, 2008, . . . [and] [f]or the period January 1, 2009 through March 31, 2013 Taxpayer appeals these assessments.

We issued Det. No. 14-0237 on July 25, 2014. Taxpayer asked for reconsideration, arguing, in addition to its previous arguments raised in Det. No. 14-0237, that RCW 82.04.43393 requires the exclusion of payroll costs for all tax periods at issue; ETA 3181.2013 was misinterpreted, has no substantive authority, and cannot be applied to the tax periods at issue; and, the assessment was issued beyond the statute of limitations and is therefore invalid.

ANALYSIS

In Det. No. 14-0237, FN 4, we explained that because the deduction for paymaster services under RCW 82.04.43393 does not apply to the audit period, the determination does not address whether Taxpayer qualifies for the deduction. Taxpayer asserts that it does apply, arguing that the statute was intended to correct the Department's alleged misapplication of *City of Tacoma v. Wm. Rogers Co.*, 148 Wn.2d 169, 60 P.3d 79 (2002), and is an affirmation of an established practice, applicable absent retroactivity, or *arguendo*, remedial and retroactive.

Courts "presume that a statute applies prospectively, unless the legislation intends otherwise, or unless the amendment is remedial in nature." *Loeffelholz v. Univ. of Wash.*, 175 Wn.2d 264, 285 P.3d 854 (2012). ESSB 5882 (Laws of 2013, 2d Spec. Sess., ch. 13, §101(4)) explains the implementation of RCW 82.04.43393 as follows (in pertinent part):

The legislature adopts the historical tax policy of allowing exclusions for payroll cost reimbursements within a centralized payroll reporting system of an affiliated group and requires the implementation of such tax policy from the effective date of this section . . . The legislature does not intend for part I of this act to retroactively create a right of refund for taxes paid on payroll cost reimbursements prior to the enactment of this statute.

The legislation took effect October 1, 2013. *Id.* at § 1904. It adopts an historical policy, but is not merely an affirmation of a previous practice. It is a new law, and the legislation shows no intent for retroactive application. Consequently, the deduction can be applied retroactively only if it is "remedial" in nature. A remedial statute "relates to practice, procedures, and remedies" and "will generally be applied retroactively, unless it affects a substantive or vested right." *Densley v. Dep't of Ret. Sys.*, 162 Wn.2d 210, 173 P.2d 885 (2007). A tax deduction affects a substantive right – it provides taxpayers the right to take a deduction under specified circumstances. Therefore, the remedial exception to the usual presumption does not apply. Moreover, the legislation explicitly requires implementation from the effective date, and we find no grounds to apply the deduction in this matter.² See also Excise Tax Advisory (ETA) 3181.2013 ("For periods beginning on or after October 1, 2013, certain taxpayers may qualify

² The deduction under RCW 82.04.43393 applies to "amounts that a qualified employer of record engaged in providing paymaster services receives from an affiliated business to cover employee costs of a qualified employee." "Qualified employee" means an employee with whom the affiliated business has a functional employment relationship. RCW 82.04.43393(2)(e). "Functional employment relationship" means "having control over the work schedule and activities of the employees *and control over all employment decisions* such as salary, discipline, hiring, or layoffs." RCW 82.04.43393(2)(c) (Emphasis added.) In this matter, per the employee leasing agreement, Taxpayer "may hire, discharge, or transfer such employees in such manner as it, in its sole discretion shall deem advisable or appropriate." Even were we to apply the statute in this case, because Taxpayer has control over employment decisions, it does not qualify for the deduction.

for the new deduction created by ESSB 5882."); Special Notice titled, "Paymaster Deduction," dated September 27, 2013 ("No deduction is allowed for periods prior to October 1, 2013.")

In finding that Taxpayer does not qualify for the exclusion, we applied ETA 3181.2013 (ETA 3181), which explains that in order to exclude amounts received, taxpayers must meet the requirements of WAC 458-20-111 (Rule 111). In Det. No. 14-0237, we stated as follows (in pertinent part):

In the present case, the taxpayer is the employer of record. . . . Employers of record generally have primary or secondary liability to the employees to pay the employer obligations. However, with respect to employers of record, ETA 3181 provides a bright line test for satisfying the third requirement:

An employer of record may have liability for certain employer obligations under common law and state and federal statutes. However, for purposes of this ETA, a taxpayer that is an employer of record will be deemed to satisfy this element when either:

- Each employee agrees in writing that the paymaster has no liability to the employee to pay any employer obligation; or
- In the case of a captive paymaster, the paymaster is a Form 2678 Agent for the clients under 26 USC Sec. 3504 and the employees are provided with written notice of the paymaster arrangement, including the client's status as employer liable to the employees for all employer obligations.

We found that Taxpayer did not satisfy this test, and concluded that amounts Taxpayer received from Affiliates are not reimbursements under Rule 111 and Taxpayer cannot exclude the amounts from the measure of gross income under this rule.

Excise tax advisories (ETAs) are interpretative statements that are advisory only under RCW34.05.230. In this case, we apply ETA 3181's guidance regarding the application of Rule 111, [which provides authority under which Taxpayer's income could be excluded from its "gross income of the business" for measuring the B&O tax. See RCW 82.04.080(1).] Taxpayer asserts that ETA 3181 holds no substantive authority and cannot be applied to this matter because it was issued after the tax periods and assessments at issue and violates due process by imposing after-the-fact requirements. However, ETA 3181 reflects the Department's interpretation of how Rule 111 applies with regards to paymasters and employers of record, and does not create new requirements that we applied retroactively in the determination. Thus, we find no error in applying ETA 3181 to this matter.

Taxpayer also argues that ETA 3181 does not provide a bright-line test, and instead merely provides one method of proof to satisfy the requirement that taxpayers have no liability to pay employer obligations except as agent of the client. As we explained in Det. No. 14-0237, Pages 4-5, when we interpret [Rule 111], the burden is upon the taxpayer to show the exemption applies. Regardless of whether the test provided in ETA 3181 is the only test, Taxpayer has not

proven that it has no liability to pay employer obligations except as an agent of its affiliates. Indeed, the employee leasing agreement, which states that the employees “shall be employees of [Taxpayer] alone” and “shall be entitled to all benefits to their status as [Taxpayer’s] employees,” indicates otherwise. Thus, we sustain our conclusion that Taxpayer does not qualify under Rule 111.

Taxpayer asserts that the assessments were issued beyond the statute of limitations and are therefore invalid. RCW 82.32.050(4) provides limitations on tax assessments as follows (in pertinent part):

No assessment or correction of an assessment for additional taxes, penalties, or interest due may be made by the department more than four years after the close of the tax year, except (a) against a taxpayer who has not registered as required by this chapter, (b) upon a showing of fraud or of misrepresentation of a material fact by the taxpayer, or (c) where a taxpayer has executed a written waiver of such limitation.

Under RCW 82.32.030, the taxpayer was required to apply for and obtain a registration certificate from the Department. WAC 458-20-101(14) recognizes that closing a taxpayer’s account has the effect of rescinding the taxpayer’s tax registration. Accordingly, under the plain meaning of RCW 82.32.050, the period for an assessment was not limited to four years after the close of the tax year for a taxpayer that was not registered as required by RCW Chapter 82.32.

DECISION AND DISPOSITION

Taxpayer’s petition is denied.

Dated this 19th day of February, 2015.