

# Mortgage brokers

## Mortgage brokers

This tax guide was written to help mortgage brokers understand their tax liability in the state of Washington. For additional information or answers to any questions about Washington excise taxes, please [contact us](#).

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### Types of mortgage brokers

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**Pure mortgage broker:** A pure mortgage broker (PMB) acts solely as a broker. A PMB meets with a potential borrower and gets their financial information. The borrower deposits funds with the PMB to pay third-party costs. This money is placed in a trust account. After getting the necessary information from the potential borrower, the PMB prepares the loan application and “shops” the application with potential lenders. If the application is accepted by a lender and the loan closes, the PMB receives a fee for these services. The fee is usually called a “loan origination fee” for getting the loan for the borrower. The fee received by the PMB is subject to the B&O tax under the Service and Other Activities tax classification.

**Correspondent mortgage broker:** A correspondent mortgage broker (CMB) makes loans in its own name with funds provided by a bank or other entity. The CMB is required to transfer the loan to, or on behalf of, the same entity. The CMB is identified on the closing documents as the lender. In this case, the CMB must transfer the loan to, or on behalf of, the same lender who advanced it the funds. Therefore, the CMB is merely the agent for the lender and does not bear the risk of interest rate fluctuations, etc. The fee, usually the loan origination fee, received by the CMB is subject to the B&O tax under the Service and Other Activities tax classification.

**Lending mortgage broker:** A lending mortgage broker (LMB) uses its line of credit or other funding source without the obligation to sell or assign the loan to the party providing the funding. In this situation, the LMB is the person advancing the funds to the borrower and bears the risk of interest rate fluctuations. As a lending mortgage broker, the net loan origination fees (gross loan origination fees less direct loan origination costs) are interest on its investments or loans. It may be deducted from the B&O tax if the loan is primarily secured by a first mortgage or a trust deed on non-transient residential property.

### Business tax structure in Washington State

#### Business tax structure in Washington State

Washington State does not have a corporate or personal income tax. However, Washington businesses generally are subject to the following:

- Business and occupation (B&O) tax
- Retail sales/use tax
- Personal property tax

#### Business and Occupation tax - State

Virtually all businesses in Washington are subject to the state business and occupation (B&O) tax. This includes businesses formed as corporations, limited liability companies (LLCs), partnerships, and sole proprietors, whether nonprofit or for profit. The B&O tax is calculated on gross income from business activities. Mortgage brokers generally are taxable under the Service and Other Activities B&O tax classification. The rate is 1.5 percent of gross receipts.

## **Retail sales and use tax**

Generally, all sales of tangible personal property to consumers are subject to retail sales tax. Retail sales tax is also due on certain services, such as charges by abstract, title insurance, escrow and credit bureau businesses, including tenant screening services.

Sellers must collect retail sales tax. However, if retail sales tax has not been collected, use tax is due from the in-state consumer. Examples of goods purchased on which use tax may be owed include:

- Computer equipment and fixtures purchased from an out-of-state vendor
- Tangible personal property acquired along with real property when an existing business is transferred
- Promotional items, such as hats, matches, calendars and other items given to customers or other individuals
- Magazine subscriptions
- Artwork

## **Use tax**

- Is due when the goods are first used in Washington.
- Is calculated on the value of the goods and includes any amount paid for freight, delivery, or shipping charges paid to the seller.
- Rates are the same as the retail sales tax rates.
- Rates are calculated on where the buyer first uses the item in Washington (unlike retail sales tax where the rate is based on the location of the sale).

## **Personal property tax**

Most people are aware that property tax applies to real property. Personal property that is used in a business is also subject to property tax. It includes equipment, furniture, and supplies. The tax rate for real and personal property is the same.

Every person who uses personal property in a business or has taxable personal property must complete a personal property tax listing form by April 30 each year. The assessor uses the form to value personal property for taxes due the following year.

County assessors and treasurers levy and collect the property tax. The county assessor mails personal property listing forms in January to persons who have previously listed personal property. If you do not receive a form or have questions about real or personal property taxes, contact your [local county assessor's office](#).

## **Local B&O tax**

Many Washington cities impose a local B&O tax. This tax is separate from the state B&O tax. The Department of Revenue does not administer or collect local B&O taxes. For more information on local B&O tax and licensing, see [License and tax information for cities and towns](#).

## Taxable income

### Taxable income

Mortgage brokers owe B&O tax on their taxable income. Payments made by the brokerage house to independent contractors cannot be deducted.

Fees for specific services directly provided by the mortgage broker, such as document preparation and set up fees, are part of the mortgage broker's gross income. Examples of activities which generate **taxable income** include:

- Fees from closed loans (loan origination fees)
- Amounts billed to independent contractors for B&O tax
- Amounts received for desk or office rental, office services, etc.
- Correspondent fees
- Accrued interest
- Gain on the sale of loans (applies to lending brokers)

### Non-taxable income – Third party costs

The mortgage broker collects amounts from the borrower to cover third party costs for appraisals, title reports, credit reports, etc. that are placed in a trust account.

Mortgage brokers (regardless of type) may charge the borrower various fees for:

- document preparation
- set-up
- title insurance
- credit report

The above third party costs are not subject to the B&O tax and should not be included in the gross income of the mortgage broker.

## Mortgage brokers - allowable deductions

### Mortgage brokers - allowable deductions

No deductions are allowed for the costs of doing business (for example, amounts paid to independent contractors). However, certain income may be deducted including:

**Bad debts:** amounts previously reported and determined to be uncollectible. These amounts must also be written off for IRS purposes.

**Cash and trade discounts:** may be deducted from the gross proceeds of sales if the amount was previously reported. Discounts are typically used as incentives for early payment.

**Interest on certain investments, loans, and/or obligations:** interest received on investments and loans primarily secured by first mortgages or trust deeds on nontransient residential properties. This deduction is only available when **all of the following conditions are met:**

- Taxpayer is engaged in banking, loan, security, or other financial business;
- Amount deducted is from interest received, meaning:
  - It is an obligation of the debtor to pay the creditor;

- Debtor must have made the payment or it was made on his behalf; and
- Payment must not be for specific services such as a finder's fee, document preparation, title examination fees, notary fees, etc.
- Amount deducted received because of a loan or investment (owner of a loan or investment is the person who retains the risk of interest rate fluctuations);
- Loan is primarily secured by a first mortgage or deed of trust; and
- First mortgage or deed of trust is for nontransient real property.

Only lending brokers qualify for this deduction and it is limited to the net loan origination fee and actual interest paid on the loan.

The following interest/fees **do not** qualify for the deduction:

- Interest on equity lines of credit that are subordinate to another loan.
- Interest on second mortgages.

Taxpayers are responsible for maintaining their books and records to support any claimed deductions. If taxpayers are unable to provide supporting documentation, they are not entitled to the deduction.

## Apportionment

Mortgage brokers that conduct business both inside and outside of Washington must apportion their income between Washington and elsewhere.

Lending mortgage brokers are to apportion based on [WAC 458-20-19404](#) for their income from lending.

Other mortgage brokers are to apportion their income under [WAC 458-20-19402](#). For periods prior to June 1, 2010, these mortgage brokers should refer to [WAC 458-20-194](#).

## Independent contractors

### Independent contractors

An independent contractor (loan originator or loan officer) that works in another's mortgage broker business is not considered an employee. Independent contractors are subject to the B&O tax (and other business taxes) - employees are not. Various factors determine whether one is an independent contractor or employee.

Independent contractors generally:

- receive federal 1099 non-employee compensation (NEC) forms from the broker documenting their commissions/fees.
- are entitled to the gross income of the business.
- are liable for business losses and expenses.
- file a statement of business income and expenses (Schedule C) for income tax purposes.
- may employ others.

Independent contractors working with mortgage brokerage firms are taxable under the Service and Other Activities B&O tax classification on their gross commissions.

No deductions are allowed for costs of doing business or for amounts withheld from commissions. Below are examples of amounts commonly withheld from commissions that are not deductible:

- B&O tax
- desk rental

- telephone
- advertising
- office supplies

## **Registering your business**

Independent contractors must register with the Department of Revenue unless they:

- Make less than \$12,000 a year before expenses;
- Do not make retail sales;
- Are not required to pay or collect any taxes administered by the Department of Revenue.

To register your business with the Department of Revenue, complete a [Business License Application](#).

## **For more information**

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Please see the following references:

- [Excise Tax Advisory \(ETA\) 3095](#) (pdf)
- Determination No 98-218 [18 WTD 46](#)
- [RCW 82.04.4292](#)
- [RCW 19.146](#)

## **Mortgage broker licensing – Department of Financial Institutions**

All mortgage brokers in Washington must have a license issued by the [Department of Financial Institutions](#) (DFI).