

State Ruling

204-590, Tax Topics-- Business and occupation-- Business and occupation tax constitutional limitations-- Apportionment-- Erroneous apportionment to the state

¶204-590. Tax Topics, Washington Department of Revenue, July 23, 2020.

Business and occupation: Business and occupation tax constitutional limitations:

Apportionment: Erroneous apportionment to the state.— The Washington Department of Revenue has responded to the Court of Appeals' decision in *LendingTree LLC v. Department of Revenue*, which concerned how to attribute, for business and occupation (B&O) tax purposes, service income the taxpayer earned from operating a website that matches prospective borrowers with participating lenders.

Under Washington law, the taxpayer's receipts from its referral services are apportionable income attributable to the state where its customer receives the benefit of the service. The court concluded that the benefit of the taxpayer's service was received at the lenders' business locations (not at the borrowers' locations in Washington), where the lenders evaluated the referrals. However, the court's opinion does not suggest that Washington must always attribute receipts to a customer's business location. For example, if a taxpayer provides marketing or advertising services to a customer engaging in selling goods or services, the customer's most directly related activity is "selling" and that activity occurs in the customer's market and receipts will be attributed to that location.

LendingTree decision – what next?

Background

- On March 30, 2020, the Court of Appeals issued a published opinion in *LendingTree, LLC v. Department of Revenue*, reversing the trial court's summary judgment in favor of the department.
- The case concerned how to attribute service income LendingTree LLC (LendingTree) earned from operating a website that matches prospective borrowers with participating lenders.
- Through LendingTree's website, prospective borrowers submit their financial information and type of loan sought, which LendingTree analyzes and then refers to potential lenders.
- The lenders evaluate a borrower's financial information before deciding whether to contact the borrower through LendingTree's website.
- LendingTree receives payments from these lenders for providing such "referral services."

Legal analysis and holding

Under Washington law, LendingTree's receipts from its referral services are apportionable income attributable to the state where its customer receives the benefit of the service. WAC 458-20-19402 (Rule 19402) provides the framework to determine where a taxpayer's customer receives the benefit of the service. On this point, the court cited the department's rule, stating that: "for a service-related business like Lending Tree, 'the benefit is received where the customer's related business activities occur.' WAC 458-20-19402(303)(c)."

In other words, the court applied the analysis in Rule 19402(303)(c), which requires identifying (1) the taxpayer's services, (2) the customer's related business activity, and (3) where the customer's related business activity occurs.

Following this analytical framework, the court said, "we must determine the services performed by LendingTree," and "the [customers'] business activities most directly related to those services." With regard to "taxpayer's services",

- The department argued that LendingTree provided marketing and outreach services to enable

lenders to make loans to borrowers.

- The court disagreed and characterized LendingTree's services as providing referrals of borrower information.

Once the court determined that the service was a “referral,” it then determined that the lender's most directly related business activity was evaluating the referrals and that activity occurred at the lenders' business locations. Accordingly, the court held that LendingTree's income should be attributed to those locations.

Summary

- The court in *LendingTree* followed both the statutory framework on apportionment under RCW 82.04.460 and 82.04.462, and the department's related interpretive guidance under Rule 19402(303)(c).
- The dispute focused on how to apply Rule 19402(303)(c) to the specific facts of *LendingTree*.
- The court concluded that the service was a “referral service” rather than a marketing or outreach service, and therefore, the benefit of LendingTree's service was received at the lenders' business locations, where the lenders evaluated the referrals.
- The court's opinion does not suggest that Washington must always attribute receipts to a customer's business location, nor does the case represent a new legal framework. Thus, for example, if a taxpayer provides marketing or advertising services to a customer engaging in selling goods or services, the customer's most directly related activity is “selling” and that activity occurs in the customer's market and receipts will be attributed to that location.