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BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS 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. 18-0327
	)	
. . .	)	. . .
	)	

RCW 82.04.260; RCW 82.04.460: APPORTIONMENT – STEVEDORING. Income a business receives from stevedoring activities is not subject to apportionment if the stevedoring activities occur exclusively in Washington.

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.

Peña, T.R.O. – A Washington company that engages in stevedoring and associated activities exclusively in the state of Washington disputes the Department's denial of its refund request to apportion its gross income under the stevedoring business and occupation (B&O) tax classification to states other than Washington. The petition is denied.[1]

ISSUE

Is a Washington business' gross income from stevedoring and associated activities classified under RCW 82.04.260(7) subject to apportionment under RCW 82.04.460 if the business activity was conducted exclusively in Washington?

FINDINGS OF FACT

. . .(Taxpayer) is a Washington corporation with its business operations at the Port of . . . in . . . , Washington. On December . . . , 2016, Taxpayer submitted a refund request in the amount of $. . . for amounts attributable to the tax period January 1, 2011, through October 31, 2016. Taxpayer asserted that income from certain activities which were previously reported under the service and other activities business and occupation tax classification should be reclassified under the stevedoring B&O tax classification. Taxpayer also requested the reclassified income be eligible for apportionment outside of Washington.

Taxpayer's taxable business activity is to privately operate a portion of the Port of . . . which includes: loading, unloading, monitoring and storing cargo, demurrage and storage guarantees, demurrage commissions, and storing empty storage containers and chassis. Taxpayer provides

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

these services for shipping companies using the Port. The Department's Audit Division (Audit) conducted a review of Taxpayer's activities and records and determined that all of the activities qualified for the reclassification to the stevedoring B&O tax classification except for fees collected for the storage for empty chassis. Taxpayer initially reported both the empty container storage and empty chassis storage activities under one line item on its combined excise tax returns. Audit requested documentation showing the allocated amounts for each activity, however, Taxpayer elected not to provide the documentation and instead withdrew the refund request related to empty container storage. Taxpayer also agreed with Audit's determination regarding its refusal to reclassify the income for the storage of empty chassis.

Audit also determined that the gross receipts reclassified to the stevedoring B&O tax classification were not subject to apportionment under RCW 82.04.460(4). Taxpayer disagreed and timely filed its petition for review on December 12, 2017. In its petition, Taxpayer asserted that since the service provided by Taxpayer relates to tangible personal property and the cargo will eventually be delivered to some point outside of Washington, all income received from Taxpayer's stevedoring activities should be apportioned according to the cargo's final delivery point.

ANALYSIS

Washington imposes a business and occupation (B&O) tax "for the act or privilege of engaging in business" in this state. RCW 82.04.220. The B&O tax "is measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be." *Id.* The B&O tax rate used is determined by the nature of the business activity in which a taxpayer engages. *See generally* Chapter 82.04 RCW.

A B&O tax is imposed "[u]pon every person engaging within this state in the business of stevedoring and associated activities pertinent to the movement of goods and commodities in waterborne interstate or foreign commerce . . . ." RCW 82.04.260(7). Taxpayer does not dispute that income from its business activities are subject to the stevedoring B&O tax classification. Taxpayer does, however, assert that its income received from these activities is subject to apportionment.

Under RCW 82.04.460(1), "any person earning apportionable income under this chapter and also taxable in another state must, for purpose of computing tax liability under this chapter, apportion to this state, in accordance with RCW 82.04.462, that portion of the person's apportionable income derived from business activities performed within this state." Taxpayers who earn apportionable income under RCW 82.04.460(1) are entitled to apportion income to Washington "by multiplying [their] apportionable income by the receipts factor." RCW 82.04.462(1). RCW 82.04.462(3)(a), (b) explains how to calculate the receipts factor, the numerator of which is a taxpayer's "total gross income of the business . . . attributable to this state during the tax year from engaging in an apportionable activity;" the denominator is a taxpayer's "total gross income of the business . . . from engaging in an apportionable activity everywhere in the world during the tax year."

"Apportionable income" is defined as "gross income of the business generated from engaging in apportionable activities, including income received from apportionable activities performed outside this state if the income would be taxable under this chapter if received from activities in

this state . . . ." RCW 82.04.460(4)(a). This definition specifically includes income subject to the stevedoring B&O tax classification under RCW 82.04.260(7). *See* RCW 82.04.460(4)(a)(ii).

Gross income is attributed to Washington based on a series of cascading rules set forth in RCW 82.04.462(3)(b). The first rule attributes receipts to the location where the customer received the benefit of the taxpayer's service. RCW 82.04.462(3)(b)(i), WAC 458-20-19402(301) (Rule 19402)(301)).

Taxpayer asserts that though it provides stevedoring services for its shipping company customers, its stevedoring activities are performed for the benefit of third parties (owners of the cargo) and relate to the tangible personal property being transported and, therefore, any tax levied on those activities should be taxed at the tangible personal property's final destination. We disagree.

Rule 19402 is the Department's rule implementing RCW 82.04.462. Rule 19402(301) explains how to attribute apportionable receipts and provides that the Department expects most taxpayers will be able to attribute apportionable receipts to the *location where the customer received the benefit of the taxpayer's service,* because either the taxpayer will know where the benefit is actually received or a "reasonable method of proportionally attributing receipts" will generally be available. Rule 19402(301)(a)(i). "Reasonable method of proportionally attributing" means "a method of determining where the benefit of an activity is received and where the receipts are attributed that is uniform, consistent, and accurately reflects the market, and does not distort the taxpayer's market." Rule 19402(106)(f).

Rule 19402(303) explains how to determine where a taxpayer's customer receives the benefit of the taxpayer's service. Rule 19402(303)(b) addresses situations where the taxpayer's service relates to tangible personal property. Here, cargo, storage containers, and chassis are clearly tangible personal property[,] and the service being provided relates to the tangible personal property involved. Rule 19402(303) states, in pertinent part:

> (b) If the taxpayer's service relates to tangible personal property, then the benefit is received where the tangible personal property is located or intended/expected to be located.
>
> (i) Tangible personal property is generally treated as located where the place of principal use occurs. If the tangible personal property is subject to state licensing (e.g., motor vehicles), the principal place of use is presumed to be where the property is licensed; or
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> (ii) If the tangible personal property will be created or delivered in the future, the principal place of use is where it is expected to be used or delivered.
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> (iii) The following is a nonexclusive list of services that relate to tangible personal property:
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> (A) Designing specific/unique tangible personal property;
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> (B) Appraisals;
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> (C) Inspections of the tangible personal property;
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> (D) Testing of the tangible personal property;
>
> (E) Veterinary services; and

(F) Commission sales of tangible personal property.[2]

(Emphasis in original.)

Here, the benefit for Taxpayer's customers occurs at the Port of . . . . Taxpayer is either loading or unloading the tangible personal property (cargo) here in Washington. Taxpayer's customers are contracting with Taxpayer to provide its services in Washington. Its customers are not contracting with Taxpayer to provide its services anywhere else. Taxpayer's customers receive the benefit of Taxpayer's services in Washington, because [the principal use for the customer occurs in Washington].

"Customers" can be "third party beneficiaries" under Rule 19402(106)(e) ("[i]f the *taxpayer performs apportionable services for the benefit of a third party*, the term 'customer' means the third party beneficiary.").[3] A "third party beneficiary" is not defined in the statute or rule. However, the term as used in the rule is ultimately referring to a third party for whom the taxpayer's apportionable services directly benefit. "Third party beneficiary" is defined as "a person who, though not a party to a contract, stands to benefit from the contract's performance." Black's Law Dictionary 149 (7th edition, 1999).

Even though third parties can be considered customers as "third party beneficiaries" in some contexts, that is not the case in this matter. For example, under Example 1 of Rule 19402(106)(e), a child is a third party beneficiary and benefits directly from a contract when a parent buys an apportionable service for that child. Taxpayer's business is to load and unload cargo (i.e., tangible personal property) for shipping companies who contracted with Taxpayer to do so. While the owners of the cargo tangentially benefit from Taxpayer's services, since they have previously contracted with the shipping companies to transport their goods, they cannot be determined to be Taxpayer's customers as "third party beneficiaries" under Rule 19402(106)(e).

The United States Supreme Court determined that the B&O tax levied under the stevedoring classification did not ". . . fall on the good[s] themselves. The levy reaches only the business of loading and unloading ships or, in other words, the business of transporting cargo within the State of Washington." *Dep't of Revenue v. Ass'n of Washington Stevedoring Companies*, *et al.*, 435 U.S. 734, 755, 98 S. Ct. 1388, 55 L. Ed. 2d 682 (1978).

The tax levied under the B&O tax stevedoring classification does not fall on the cargo that is being loaded and unloaded from the ships. Instead, the proper taxing jurisdiction is where the customer receives the benefit. Here, all of Taxpayer's taxable activity under the stevedoring classification is being conducted in Washington. Therefore, all of Taxpayer's stevedoring activities are taxable in Washington.

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[2] Subsections (a) and (c) of Rule 19402(303) address services related to real property and when services do not relate to either real property or tangible personal property and are not applicable here.

[3] "Customer" means "a person or entity to whom the taxpayer makes a sale, grants the right to use intangible property, or renders services or from whom the taxpayer otherwise directly or indirectly receives gross income of the business. If the taxpayer performs apportionable services for the benefit of a third party, the term 'customer' means the third party beneficiary." Rule 19402(106)(e).

Additionally, RCW 82.04.460(1) requires "any person earning apportionable income taxable under this chapter and *also taxable in another state* must, for the purpose of computing tax liability under this chapter, apportion to this state, in accordance with RCW 82.04.462, that portion of the person's apportionable income derived from business activities performed within this state." (Emphasis added.) Rule 19402(106)(h)(i) defines "taxable in another state" to mean either:

> (A) The taxpayer is subject to a business activities tax by another state on the taxpayer's income received from engaging in apportionable activity; or
> (B) The taxpayer is not subject to a business activities tax by another state on the taxpayer's income received from engaging in apportionable activity, but the taxpayer meets the substantial nexus thresholds described in WAC 458-20-19401 for that state.

Substantial nexus exists where, in the current or immediately preceding calendar year, a person is:

> (i) An individual and is a resident or domiciliary of this state;
> (ii) A business entity and is organized or commercially domiciled in this state; or
> (iii) A nonresident individual or a business entity that is organized and commercially domiciled outside this state, and the person had:
> (A) More than fifty-three thousand dollars of property in this state;
> (B) More than fifty-three thousand dollars of payroll in this state;
> (C) More than two hundred sixty-seven thousand dollars of receipts from this state from apportionable activities, from selling activities, or from a combination of both . . . .

WAC 458-20-19401(3).

Here, Taxpayer has not shown it has substantial nexus with any other state besides Washington. Taxpayer is a business entity that is organized and commercially domiciled in Washington; it has not shown it has any payroll or property outside of Washington; nor has it received any income within any other state for its stevedoring activities. Taxpayer's taxable activity, stevedoring, is exclusively conducted in the state of Washington. Therefore, none of Taxpayer's stevedoring income can be apportioned outside of Washington.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 27th day of December 2018.