Cite as Det. No. 22-0027, 43 WTD 69 (2024)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of Assessment of	)	D E T E R M I N A T I O N
	)	No. 22-0027
. . .	)	Registration No.. . .

[1] RCW 82.04.080; RCW 82.04.070: GROSS PROCEEDS OF THE BUSINESS. A company using proprietary software to provide sellers of advertising space a market for the space to advertisers must report the income it receives from advertisers as gross proceeds subject to business and occupation tax.

[2] RCW 82.08.010(15)(a): MARKETPLACE FACILITATOR. A company providing a digital platform to sell advertising space is not a marketplace facilitator.

[3] WAC 458-20-218(3)(e); WAC 458-20-111: ADVANCES AND REIMBURSEMENTS. The sale of advertising space cannot be deducted from a business's gross proceeds of sales as an advancement or reimbursement when there is no agency relationship between the parties.

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.

Willette, T.R.O. – A[n out-of-state] corporation ("Taxpayer") that sells digital advertising space through its online exchange protests an assessment by the Department of Revenue ("Department"). The Department disallowed deductions from Taxpayer's gross income subject to Washington's business and occupation ("B&O") tax. Taxpayer contends it is a marketplace facilitator and only the income it classifies as commissions is subject to tax. We deny the petition.[1]

ISSUES

1. Whether Taxpayer correctly reported its gross income as defined by RCW 82.04.080.
2. Whether Taxpayer is a marketplace facilitator, as defined by RCW 82.08.010(15)(a), when it sells advertising space to advertisers using its digital software.

3. Whether Taxpayer can deduct the cost of advertising space from its gross income as advancements or reimbursements under WAC 458-20-218(3)(e) ("Rule 218").

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

FINDINGS OF FACT

Taxpayer is a privately held, for-profit corporation headquartered in . . . . Taxpayer provides an advertising exchange that uses software to auction the advertising space of third-party publishers ("Publishers"), usually mobile-app developers and websites, to advertisers and businesses ("Buyers"). Taxpayer's exchange enables real-time bidding by Buyers on the advertising space of Publishers. Taxpayer's service works, in part, as follows:

> [T]he [ad exchange] uses . . . [digital] technologies to give Publishers the possibility to offer, and Ad Exchange advertisers the ability to show, targeted ads . . . more likely to be relevant . . . because they are based on inferences drawn from location data, web viewing data collected across non-affiliated sites over time, and/or application use data collected across non-affiliated apps over time. This is called "interest-based advertising."

. . . , www.. . . / (last visited Dec. 29, 2021). As such, Taxpayer provides a service to both the Publishers and the Buyers. For Buyers, Taxpayer's digital tools maximize opportunities to reach target audiences by placing the ads most effectively, e.g., based on web viewing data and location data, on Publishers' hosting sites. . . . , www.. . . / (last visited Jan. 21, 2022). Taxpayer's established relationships with Buyers and ability to place ads effectively drives demand for Publishers, maximizing profit on advertising space. . . . , www.. . . / (last visited Jan. 21, 2022).

Under the contract between Taxpayer and Publishers, the service Taxpayer provides to Publishers is contractually defined [as meaning the ad exchange and related services which enable the marketing and selling of digital and mobile advertising inventory, as well as receiving of advertisements for display, by publishers and demand partners. The contract obligates Taxpayer to make "commercially reasonable efforts to fill each impression[2]" according to existing market conditions but does not "ensure that every impression or category of impressions will be filled or filled at a certain price."] Taxpayer Sample Contract[3] at 1 (emphasis added). Publishers have no license or rights with regards to the service, and only Taxpayer can modify or alter the service. *Id.* The cost to Publishers for use of the service is an amount that is deducted from the payment made by Buyers to Taxpayer for the advertising space ("commissions"), and that amount is contractually determined by Taxpayer. The payment terms between Taxpayer and Publishers [provide that Taxpayer will pay Publishers based on the advertisements displayed on the Publisher's inventory and that Taxpayer's impression counts and record of the price per impression are decisive.]

Taxpayer did not provide a contract between it and Buyers. It is not in dispute, however, that Taxpayer provides a service to Buyers that includes making the sale of advertising space. Nothing before us indicates that the cost of the digital and mobile advertising space includes retail sales tax. As such, Taxpayer does not collect retail sales tax from Buyers when it makes the sale of the advertising space, and Taxpayer does not pay retail sales tax on payments to Publishers based on impression counts. Taxpayer promotes its business as offering interest-based advertising and

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[2] Impressions are a metric used in online advertising and quantify the number of views or engagements of a piece of content, and impression counts are integral for measuring performance and setting costs of impressions. *See, e.g.*, *Impression*, INVESTOPEDIA, investopedia.com/terms/i/impression.asp (last visited Dec. 22, 2021).

. . .

acknowledges that advertising services are generally subject to the service and other activities . . . B&O tax.

The Department's Audit Division ("Audit") audited Taxpayer's business activities for the period from January 01, 2015, through December 31, 2019 ("Audit Period"). Audit found that Taxpayer reported only its commissions as part of its gross income on its Washington excise tax returns. Taxpayer classified its income as subject to the service and other activities B&O tax. To calculate its gross income, Taxpayer maintained two data columns for its bookkeeping. One column included the income made from sales of advertising space to Buyers. The contra-account column included the payments to Publishers, essentially sales amounts minus commissions. Taxpayer then deducted the contra-account total from the sales amount total for each return. [4] Thus, Taxpayer's claimed gross income equaled only the commissions during the Audit Period.

The Department disallowed the deductions from Taxpayer's gross income for its payments to Publishers that made up the contra-account. The Department found that the payments to Publishers were a cost of doing business. The Department stated that the definition of gross proceeds under RCW 82.04.070 did not allow for deductions for the cost of doing business. The Department also relied on WAC 458-20-218, the rule for determining the gross income of advertising services.

The Department made the following adjustments to the Taxpayer's returns for the Audit Period:

	2015	2016	2017	2018	2019	AUDIT PERIOD TOTAL
Total Taxable Amount	. . .	. . .	. . .	. . .	. . .	. . .
Amount Reported (less)	. . .	. . .	. . .	. . .	. . .	. . .
Difference/Taxable Amount	. . .	. . .	. . .	. . .	. . .	. . .
Service and Other Activities Tax Rate	. . .	. . .	. . .	. . .	. . .	
Tax Adjustment	**. . .**	**. . .**	**. . .**	**. . .**	**. . .**	**. . .**

The Department also assessed penalties and interest, $. . . and $. . . respectively.

Taxpayer timely filed a petition for administrative review ("Petition"). In its Petition, Taxpayer contends that it is a marketplace facilitator as defined by RCW 82.08.010(15)(a). Taxpayer states that it is a marketplace facilitator because it:

1. Contracts with sellers to sell their products;
2. Communicates directly or indirectly the offer and acceptance of bids on seller's products; and
3. Engages directly in listing seller's products for sale and setting prices on the sales.

[4] Sales to Buyers - Payment to Publishers [Sales to Buyers - commissions] = commissions

Taxpayer Supplemental Briefing at 6. Taxpayer argues that, because it is a marketplace facilitator, an agency relationship between it and Publishers is statutorily created and only the commissions are subject to the service and other activities B&O tax.

ANALYSIS

1. Gross Income

Washington's B&O tax is [generally] calculated based on the "gross income or gross proceeds of sales of the business[.]" RCW 82.04.290(1). "Gross income of the business" is broadly defined and means:

> [T]he value proceeding or accruing by reason of the transaction of the business engaged in and includes gross proceeds of sales, compensation *for the rendition of services*, gains realized from trading in stocks, bonds, or other evidences of indebtedness, interest, discount, rents, royalties, fees, commissions, dividends, and other emoluments however designated, *all without any deduction on account of the cost of tangible property sold, the cost of materials used, labor costs, interest, discount, delivery costs, taxes, or any other expense whatsoever paid or accrued* and without any deduction on account of losses.

RCW 82.04.080(1) (emphasis added); *see also* RCW 82.04.070 (defining gross proceeds of sales). The phrase "value proceeding or accruing" is defined as "the consideration, whether money, credits, rights, or other property expressed in terms of money, actually received or accrued." RCW 82.04.090. "Business" includes "all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or to another person or class, directly or indirectly." RCW 82.04.140. Under the broad definition of gross income of the business, a service provider may not deduct any of its costs of doing business from its gross income. *See Pilcher v. Dep't of Revenue*, 112 Wn. App. 428, 436, 49 P.3d 947, 951 (2002) (citing *Rho Co. Inc. v. Dep't of Revenue,* 113 Wn.2d 561, 566-67, 782 P.2d 986, 989 (1989)).

Although Taxpayer calls its business an exchange, Taxpayer's business operates like an advertising agency because it provides "advertising services." *See* Rule 218(2)(a). "Advertising services" are defined as including, among other things:

- the dissemination of advertisements;
- lead generation optimization;
- rendering advice to a client concerning the best methods of advertising;
- acquisition of advertising space in the internet media; and
- monitoring and evaluation of website traffic for purposes of determining the effectiveness of an advertising campaign.

RCW 82.04.192(3)(b)(xiii); *see also* Rule 218(2)(b). Taxpayer purchases ad space in the internet media from Publishers at a cost per impression. Taxpayer's interest-based advertising collects data over time to monitor and evaluate location data, web-viewing data, and usage data for the purpose of determining the effectiveness of Buyers' advertising campaigns. Taxpayer's service disseminates targeted ads most likely to be relevant to the internet audience, which is essentially

lead generation optimization and providing advice concerning the best methods of advertising. Thus, Taxpayer provides "advertising services."

Taxpayer only reported its commissions; however, because Taxpayer provides advertising services, it is subject to B&O tax on "all gross income and commissions, including amounts received to pay media outlets[.]" Rule 218(3). Here, Taxpayer's gross income includes income received on the sale of advertising space to pay media outlets, Publishers. The income received for purchasing advertising space in a media outlet for a client is subject to the service and other activities B&O tax. Rule 218(3)(a). Thus, unless a specific exemption, deduction, or exclusion applies, Taxpayer's gross income is subject to service and other activities B&O tax without any deduction for its payments to Publishers.

2. Marketplace Facilitator

Taxpayer argues that it is a marketplace facilitator, so an agency relationship is statutorily created.[5] "Marketplace facilitator" is statutorily defined and means, in relevant part, a person that "contracts with sellers to facilitate for consideration, regardless of whether deducted as fees from the transaction, the sale of the seller's products through a marketplace owned or operated by the person[.]" RCW 82.08.010(15)(a)(i).[[6]] Likewise, businesses that provide advertising services are explicitly not marketplace facilitators unless they communicate the "offer acceptance between buyer and *seller*" and engage in certain activities "with respect to the *seller*'s products[.]" RCW 82.08.010(15)(b)(i)(A) (emphasis added). "Seller," as used in the definition of marketplace facilitator, is a defined term, and means "every person, including the state and its departments and institutions, *making sales at retail or retail sales* to a buyer, purchaser, or consumer . . .." RCW 82.08.010(2)(a)(i); *see also* RCW 82.08.010(16) (defining "marketplace seller" as a "*seller that makes retail sales* through any marketplace operated by a marketplace facilitator") (emphasis added).

When interpreting a statute, the fundamental objective is "to ascertain and carry out the Legislature's intent." *Dep't of Ecology v. Campbell & Gwinn, LLC*, 146 Wn.2d 1, 9, 43 P.3d 4, 9 (2002). We begin with the plain language of the statute; although, we may consider the context of

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[5] Marketplace facilitators as agents for sellers pay B&O [tax] on the commission they earn for making retail sales. *See* RCW 82.08.0531(1); WAC 48-20-282(303)(b).

[[6]] RCW 82.08.010(15) became effective as of July 1, 2019 (SSB 5581). The earlier version of the marketplace facilitator statute was enacted per EHB 2163 in 2017. The definition of marketplace facilitator per the EHB 2163 became effective July 7, 2017, and was codified under RCW 82.13.010(3) (which was repealed upon the effective date of SSB 5581). The plain language of the definitions of "marketplace facilitator," "marketplace seller," and "seller" in both EHB 2163 and SSB 5581 read together with RCW 82.08.0531(1) (deeming marketplace facilitator to be an agent of a marketplace seller making retail sales in both EHB 2163 and SSB 5581) restrict sales to strictly retail sales. Therefore, even in the earliest iteration of the statute, the Taxpayer's argument that certain services, like advertising services, that are not retail sales could be included is contrary to the plain language of the definitions and, as such, Taxpayer also cannot be considered a marketplace facilitator under any version of the marketplace facilitator statute. Notably, the Taxpayer is unable to claim they are a marketplace facilitator in Washington for periods before July 7, 2017, as the marketplace facilitator statutes did not exist at that time. Moreover, EHB 2163 explicitly "appl[ied] prospective only" from its July 7, 2017, effective date, and SSB 5581 explicitly "applies prospectively only," except for two portions of the act which apply retroactively to October 1, 2018. Laws of 2017, 3d Spec. Sess., ch.28, §§ 602, 604; Laws of 2019, ch.8, § 803. Thus, neither marketplace facilitator act was operative during the first part of the Audit Period.]

the statute in which the provision is found, related provisions, amendments to the provision, and the statutory scheme as a whole. *Lenander v. Dep't of Ret. Sys.*, 186 Wn.2d 393, 403, 377 P.3d 199, 205 (2016) (citing *Campbell & Gwinn*, 146 Wn.2d at 10-11). Nevertheless, legislative intent should be derived primarily from the statutory language. *Duke v. Boyd*, 133 Wn.2d 80, 87, 942 P.2d 351, 354 (1997).

By the plain language of the statute, Taxpayer cannot be a marketplace facilitator. To be a marketplace facilitator, one must "contract with sellers to sell [the seller's] products." RCW 82.08.010(15)(a)(i). Seller is a statutorily defined term. To be a seller, a person must make retail sales. *See* 82.08.010(2)(a)(i); RCW 82.08.010(16). Taxpayer's contracts are with Publishers. Publishers are not sellers as statutorily defined because they do not make sales at retail. Taxpayer acknowledges that digital advertising is not defined as a sale at retail and that neither it nor Publishers are making retail sales. *Compare* RCW 82.04.257(1) (imposing the retail sales tax on the sale of digital automated services) *with* RCW 82.04.192(3)(b)(xiii) (excluding advertising services from the definition of digital automated service). . . .

Nevertheless, Taxpayer proposes that there is ambiguity in the statutory definition of marketplace facilitator. Specifically, Taxpayer contends ambiguity is created because the definition of marketplace facilitator states that the sales occur "through a marketplace." RCW 82.08.010(15)(a)(1). "Marketplace" is also a defined term and means "a physical or electronic place, including, but not limited to, a store, a booth, an internet website, a catalog or a dedicated sales software application, where tangible personal property, digital codes and digital products, or services are offered for sale." RCW 82.08.010(14). Taxpayer posits that ambiguity arises because the definition of marketplace allows for the sale of services, and certain services, like advertising services, are not retail sales.

A statute is ambiguous if "susceptible to two or more reasonable interpretations," but "a statute is not ambiguous merely because different interpretations are conceivable." *Agrilink Foods, Inc. v. Dep't of Revenue,* 153 Wn.2d 392, 396, 103 P.3d 1226, 1229 (2005) (internal citation omitted). Whether it be an intentional or an inadvertent omission, we cannot read language into a statute where the legislature has omitted it. *Jenkins v. Bellingham Mun. Court*, 95 Wn.2d 574, 579, 627 P.2d 1316, 1319 (1981); *see also State v. Moses,* 145 Wn.2d 370, 374, 37 P.3d 1216, 1218 (2002). Taxpayer's reading of the statute ignores the Legislature's limitation of the definition of marketplace facilitator to those that contract with sellers making retail sales. We have no authority to read into the statute what the Legislature has omitted, whether intentionally or inadvertently. Thus, we find that Taxpayer's interpretation, which requires us to insert language that would allow for the sale of services that are not retail sales, is not a reasonable one. We find the statute is not ambiguous, and so we interpret it by giving effect to its plain language. Taxpayer cannot be classified as a marketplace facilitator because it does not contract with statutorily defined sellers – those making retail sales.

Marketplace facilitator is defined as a three-part analysis, and Taxpayer also proposes that it satisfies the other considerations of the definition of marketplace facilitator. *See* RCW 82.08.010(15)(a)(ii)-(iii). Taxpayer does not satisfy either of the additional elements for the same reason because the second and third elements also require Taxpayer to do certain things with regards to "sellers" and sellers' products. Thus, by the plain language of the statutory definition,

Taxpayer cannot be a marketplace facilitator because it does not contract with sellers to sell its products or meet the additional requirements of the definition.

Because we find that Taxpayer is not a marketplace facilitator, it must report the entirety of its gross income, which includes all consideration actually received without deduction for expenses. *See* RCW 82.04.080(1); RCW 82.04.090.

3. Rule 218(3)(e)

Rule 218, the Department's administrative rule that addresses advertising agencies, details when certain income may be excludable from gross income for advertising agencies. Rule 218(3) states: "Generally, advertising agencies are subject to business and occupation (B&O) tax on all gross income and commissions, including amounts received to pay media outlets, unless the amounts are valid advances and reimbursements under WAC 458-20-111." To be a valid advance or reimbursement, an advertising agency must demonstrate all three of the following requirements:

(i) The amounts are reimbursements or advances *made to pay obligations of a client*;

(ii) *The advertising agency is not performing these services*, either directly or indirectly through independent contractors; and

(iii) The *advertising agency has no liability to pay* the client's obligations, *except as the agent of its clients*.

Rule 218(3)(e)(i-iii) (emphasis added). As indicated in Rule 218(3), the requirements are derived from WAC 458-20-111 ("Rule 111"), which addresses advances and reimbursements, or pass-through income.

We treat exclusions from gross income like exemptions. *See* RCW 43.136.021 (defining deductions, exemptions, exclusions, credits, deferrals, and preferential rates as a tax preference); WAC 458-20-267(1)(b)(ii)(A). Exemptions from a taxing statute must be narrowly construed. *Budget Rent-A-Car, Inc. v. Dep't of Revenue*, 81 Wn.2d 171, 174, 500 P.2d 764, 767 (1972); *State, Dep't of Revenue v. Schaake Packing Co., Inc.*, 100 Wn.2d 79, 83, 666 P.2d 367, 370 (1983) (stating the "strong policy of narrowly construing exemptions" to the B&O tax). Generally, a person claiming a tax exemption, exception, or deduction has the burden of proving he or she qualifies for the tax benefit. *Group Health Cooperative of Puget Sound, Inc. v. State Tax Comm'n*, 72 Wn.2d 422, 429, 433 P.2d 201, 205 (1967).

Taxpayer cannot satisfy its burden under the first element. Taxpayer's payments to Publishers are not obligations of the Buyers (the clients). Taxpayer is responsible for paying Publishers per impression count at a rate that it, Taxpayer, sets. In fact, the contract states that the monies are "related to" the sales to the Buyers, but there are no express terms that . . . the amounts it pays to Publishers are an obligation of the Buyers. Taxpayer Sample Contract at 2.

Taxpayer also cannot satisfy its burden under the second element. Rule 218(e)(ii) requires the advertiser not to be performing the services directly or indirectly through independent contractors.

Taxpayer contracts with Publishers to provide a service that only it can provide, namely, to use its "commercially reasonable efforts" to "fill each impression" with Buyers' advertisements.[7] Taxpayer Sample Contract at 1.

Finally, Rule 218(3)(e)(iii) requires that the "advertising agency has no liability to pay the client's obligations, except as the agent of its clients." Taxpayer does not meet this element because it has liability for the payments to Publishers, and not as the agent of the clients. *See* Taxpayer Sample Contract at 2.

The Department has long recognized and implemented this principle in Rule 111. Rule 111 allows reimbursements to be excluded from gross income only "when the customer or client alone is liable for the payment of the fees or costs and when the taxpayer making the payment has no personal liability therefore, either primarily or secondarily, other than as agent for the customer or client." Courts have interpreted Rule 111 as requiring the taxpayer to prove that the advance in question was made pursuant to an agency relationship and prove that the taxpayer's liability to pay the advance constituted solely agent liability. *Washington Imaging Services, LLC v. Dep't of Revenue*, 171 Wn.2d 548, 561, 252 P.3d 885, 891 (2011); *Rho Co. v. Dep't of Revenue,* 113 Wn.2d at 568; Det. No. 1-0102, 32 WTD 250, 253 (2013).

In other words, by requiring the taxpayer to prove that its liability is solely agent liability, Rule 111 distinguishes payments a taxpayer makes towards its own costs of doing business, from those where it acts solely as an agent in collecting and remitting money to a third party on behalf of its client. *See, e.g., Washington Imaging Services,* 171 Wn.2d 548. Thus, even if agency has been determined, a taxpayer is not entitled to exclude the payments that are owed to a third-party if the taxpayer assumes any liability for the payment, except as an agent. *See* Det. No. 14-0073, 34 WTD 019, 24 (2015). Here, Taxpayer has assumed liability for the payments to Publishers, and there are no facts that indicate it was as an agent. In fact, Taxpayer's contracts with Publishers indicate that it is Taxpayer's sole discretion that determines such compensation to Publishers. Taxpayer Sample Contract at 2 ("[Taxpayer's] impression counts and record of the price per impression will be decisive."). Nothing in Taxpayer's contract with Publishers indicates that Buyers have any liability for the monies owed to Publishers for selling the advertising space. *See generally* Taxpayer Sample Contract.

Taxpayer must meet all three of the requirements set forth in Rule 218(3)(e) for the payments to Publishers to be excluded from its gross income. Taxpayer has failed to meet any of the three requirements. Taxpayer's payments to Publishers, therefore, are a cost of doing business that cannot be deducted from its gross income under Rule 218(3)(e).

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 4th day of February 2022.

[7] Taxpayer also performs the service for Buyers: collecting data over time to monitor and evaluate location data, web-viewing data, and usage data for the purpose of determining the effectiveness of advertising campaigns.