

SYNOPSIS

CONSUMERS' SALES AND SERVICE TAX AND PURCHASERS' USE TAX -- MORTGAGE BROKERS -- NOT PROFESSIONAL SERVICES -- Services provided by mortgage brokers, as well as payments to others (independent contractors) who provided related services, are not "professional" services for purposes of exception from either the consumers' sales and service tax or the purchasers' use tax. The services of a mortgage broker are not explicitly excepted as "professional" by the Legislature, and the minimum (college) education and standards for performance requirements that must be applied have not been satisfied.

FINAL DECISION

The Auditing Division of the State Tax Commissioner's Office issued a consumers' sales and service tax assessment against the Petitioner.

The assessment was for the period of May 21, 1998 through September 30, 2002, for tax and interest, through December 31, 2002.

Also, on December 18, 2002, the Commissioner issued a purchasers' use tax assessment against the Petitioner, under the provisions of Chapter 11, Articles 10 and 15A of the West Virginia Code, for the period of May 21, 1998 through September 30, 2002, for tax and interest, through December 31, 2002.

Written notice of these assessments was served on the Petitioner.

Thereafter, by mail postmarked February 7, 2003, the Petitioner timely filed with this tribunal, the West Virginia Office of Tax Appeals, petitions for reassessment. See W. Va. Code § 11-10A-8(l) [2000].

At the outset of the administrative hearing the presiding administrative law judge noted that counsel for both sides had agreed that the hearing record in a prior consolidated case, would be made part of this record.

DISCUSSION

“PROFESSIONAL” SERVICES

During the assessment period, the Petitioner was engaged in operating a mortgage brokerage business, which is a business that, for a fee or fees, assists borrowers in obtaining mortgages. The issue to be discussed is whether mortgage brokers provide “professional” services for purposes of that exception from the consumers’ sales and service tax (herein “sales tax”) (and from the purchasers’ use tax).

Also, during the audit period Petitioner contracted with an outside individual to provide mortgage brokering services on its behalf. These services were considered to be contract labor by the Commissioner and were assessed purchasers’ use tax. Petitioner again considers same to be “professional” in nature.

The sales tax is imposed on sales of tangible personal property and selected services in this State. See W. Va. Code § 11-15-3. The term “services” or “selected services” includes “all nonprofessional activities engaged in for other persons for a consideration, which involve the rendering of a service as distinguished from the sale of tangible personal property, but shall not include contracting, personal services or the services rendered by an employee to his employer or any service rendered for resale.” See W. Va. Code § 11-15-2 (s) and 110 C.S.R. 15, § 2.7.4. All sales and services are subject to the sales tax unless specifically excepted or exempted. See W. Va. Code § 11-15-6. The services that are excepted from taxation are “professional” services, personal services, and services provided by corporations subject to regulation by the West Virginia Public Service Commission.

See W. Va. Code § 11-15-8. The sales that are exempted from taxation are quite numerous and are listed in West Virginia Code § 11-15-9.

The issue is whether the services provided by Petitioners are “professional” services. To that end, a discussion of mortgage brokers is appropriate.

Mortgage broker activity is regulated by the State Banking Commissioner, who licenses persons engaged in the activity. See W. Va. Code § 31-17-1 et. seq. “Person” is defined to include an individual, partnership, corporation or any other legal entity. See, W. Va. Code § 31-17-1(3). Therefore, both the business and the individual may be licensed.

The requirements for licensing are found in West Virginia Code § 31-17-4. The State Banking Commissioner may refuse to issue a license for reasons specified in West Virginia Code § 31-17-5, and may suspend or revoke a license for reasons specified in West Virginia Code § 31-17-12.

West Virginia Code § 31-17-7 establishes continuing education requirements that must be satisfied on an annual basis. However, a review of West Virginia Code § 31-17-1 et. seq. does not reveal any minimum education requirement that must be satisfied by law in order for the initial license to be issued to an applicant.

West Virginia Legislative Rule 110 C.S.R. 15, Consumers’ Sales and Service Tax and Use Tax, at Section 110-15.2.65 provides the following definition:

2.65. “**Professional service**” means and includes an activity recognized as professional under common law, its natural and logical derivatives, an activity determined by the State Tax Division to be professional, and any activity determined by the West Virginia Legislature in W. Va. Code § 11-15-1 et. seq. to be professional. See Section 8.1.1 of these regulations.

While the foregoing provides the necessary definition of what comprises “professional service,” it is necessary to review Section 110-15-8 to determine just what has transpired relative to legislative determinations of what is a “professional” and what actions the State Tax Division may make in that regard.

8.1.1 Professional Services.

8.1.1.1 Professional services, as defined in Section 2 of these regulations, are rendered by physicians, dentists, lawyers, certified public accountants, public accountants, optometrists, architects, professional engineers, registered professional nurses, veterinarians, licensed physical therapists, ophthalmologists, chiropractors, podiatrists, embalmers, osteopathic physicians and surgeons, registered sanitarians, pharmacists, psychiatrists, psychoanalysts, psychologists, landscape architects, registered professional court reporters, licensed social workers, enrolled agents, professional foresters, licensed real estate appraisers and certified real estate appraisers licensed in accordance with W. Va. Code § 37-14-1 et. seq., nursing home administrators, licensed professional counselors and licensed real estate brokers. Persons who provide services classified as nonprofessional for consumers’ sales and service tax purposes include interior decorators, private detectives/investigators, security guards, bookkeepers, foresters, truck driving schools, hearing aid dealers/fitters, contractors, electricians musicians, and hospital administrators; the foregoing listing is not all-inclusive but intended as containing examples of trades and occupations. The determination as to whether other activities are “professional” in nature will be determined by the State Tax Division on a case-by-case basis unless the Legislature amends W. Va. Code § 11-15-1 et. seq., to provide that a specified activity is “professional.” When making a determination as to whether other activities fall within the “professional” classification, the Tax Department will consider such things as the level of education required for the activity, the nature and extent of nationally recognized standards for performance, licensing requirements on the State and national level, and the extent of continuing education requirements.

The foregoing is rather straightforward. It provides a legislatively approved listing of occupations that have been deemed to fall within the designation of “professional.” Furthermore, it provides the nature of the information the State Tax Division is to consider when making a determination as to whether a service is a professional service. The State, in its brief, reiterated the foregoing and provided the following four-part test to be used when making that determination.

1. Is a State or federal license required to render the service?
2. Is there a level of formal education required to obtain the license and is that education sufficient to result in mastery of a specialized body of knowledge?
3. Are there recognized standards of performance and a body available to discipline licensees who fail to meet those standards?
4. Is continuing education required to maintain the license?

FINDINGS OF FACT

1. Upon application of the foregoing test, this tribunal finds that a license is required to provide mortgage brokerage services and that a license is issued by the State Banking Commission; additionally, this tribunal finds that seven hours of continuing education is required annually in order to retain the license. However, it does not appear that any formal education is required by West Virginia Code § 31-17-1 et. seq.; in fact, one of Petitioner’s witnesses admitted under cross-examination in the prior case that there is not even a requirement that a licensee possess a high school diploma.

2. It may be said that the Banking Commission under the authority of West

Virginia Code § 31-17-12 acts in the capacity of a disciplinary body but no evidence was provided indicating standards of performance that have been promulgated by that agency. This tribunal finds that membership in either the West Virginia Association of Mortgage Brokers or the National Association of Mortgage Brokers for purposes of establishing standards of performance because membership in either of those organizations is discretionary on the part of the licensee.

CONCLUSIONS OF LAW

Therefore, mortgage brokers are not “professionals” for purposes of the sales tax exception.

Based upon the foregoing, the charge for services rendered by mortgage brokers is subject to sales tax.

CHARGES SUBJECT TO TAX

However, there is a question as to whether all charges are subject to sales tax or whether the sales tax only applies to certain ones.

This tribunal therefore turns to a discussion of the various fees charged by mortgage brokers: yield spread fees, and origination or loan origination fees; the latter may also be called broker fees or processing fees. There also are what are referred to as pass-through fees: courier fees, credit report fees, flood report fees and document preparation fees.

FINDINGS OF FACT

1. The origination fee is an amount agreed upon between the broker, the lender and the borrower. While there is not total agreement in the testimony as to just what is included in this fee, it is apparent that the fee is imposed for the different

services provided by the mortgage broker to the borrower. This fee is collected from the borrower.

2. The yield spread fees appear to be based upon the difference between what interest rate the lender would have used and a higher interest rate that the borrower obtained from the mortgage broker. The lender is paying this fee to the mortgage broker because the broker is lending the lender's money to the borrower; the lender will earn revenue off the loan for the life of the loan.

3. Pass-through fees are fees that are collected to pay for charges by the providers of certain services. Some of the charges are not collected unless the loan is closed. However, if the fee is collected, it is collected by the mortgage broker and paid out to the provider of the service for which the charge is rendered.

DISCUSSION

The sales tax is imposed upon the gross proceeds received from the dispensing of services in this State. 110 C.S.R. 15, at Section 110-15-2.35, provides the following definition of the term "gross proceeds."

2.35. **"Gross proceeds"** means the amount received in money, credits, property or other consideration from sales and services within this State, without deduction on account of the cost of property sold, amounts paid for interest or discounts or any other expenses whatsoever. Gross proceeds shall be reduced by the value of an item of tangible personal property which is traded-in for the purpose of reducing the purchase price of the item purchased or the amount of a discount allowed by the vendor for the item at the time the item is purchased. Losses shall not be deducted, but any credit or refund made for goods returned may be deducted.

2.35.1. Gross proceeds shall include the amount of any excise tax or other tax imposed upon the tangible personal property or taxable service sold or used, or the sale thereof, prior to the imposition of the West Virginia consumers' sales and service tax or use tax on such property or taxable service.

2.35.2. Gross proceeds shall include any increase in the amount paid by the ultimate consumer or end user of tangible personal property or a taxable service by reason of shipping charges, postage, handling charges, costs of travel or transportation or any similar cost or charge.

2.35.3. For purposes of these regulations the terms “charge,” “gross sales price,” “sales price,” “purchase price,” “monetary consideration” and “gross receipts” shall be synonymous with the term “gross proceeds.”

2.35.4. Gross proceeds shall not include the amount of federal, state or local tax simultaneously imposed upon the tangible personal property or service purchased.

CONCLUSIONS OF LAW

1. It is quite apparent from the foregoing that expenses may not be deducted from the gross proceeds received for the provision of a service. Pass-through fees are, in actuality, expenses accruing in the provision of a service. If the activities for which the fees are imposed were occurring in a situation other than closing on a loan, the fees would be subject to sales tax. Additionally, there is no statutory exemption for courier fees, flood report fees, document preparation fees and credit report fees that are imposed when a loan is closed. This tribunal therefore is of the opinion that the fees charged for different activities are to be included in the charges that are subject to sales tax.

2. Finally, this tribunal turns to the yield spread fee. Petitioner is of the opinion that even though the bank is purchasing the services of the mortgage broker and paying this fee to the mortgage broker for those services, there is no sales tax involved. 110 C.S.R. 15, at Section 110-15-31, provides a discussion of the application of sales tax to transactions involving banks. Section 110-15-31.1 is rather specific.

31.1 Generally, banks, state and national, are not exempt from the imposition of the consumers sales and service tax or use tax on their purchases, inasmuch as banks are the ultimate consumers of such purchases. Banks are only exempt on purchases of property and services that are resold, subject to tax, to consumers.

It is quite evident from the foregoing that banks are not automatically exempt from sales tax when purchasing services. Therefore, the yield spread fee paid by lenders to mortgage brokers, which is a fee paid for the service of obtaining a borrower for the lender, is subject to the sales tax.

SUMMARY

1. The Petitioner did not present any evidence that there was any minimum education required in order to be licensed as a mortgage broker. As a result, it is determined that neither mortgage brokers nor contract labor performing an identical function satisfies all of the requirements to be classified as a “professional” for purposes of the sales or use tax exception.

2. The evidence presented by the Petitioner relevant to the origination fee was not persuasive in that there was no testimony demonstrating why the fee should not be taxable. As all services are taxable unless the contrary is clearly established, the origination fee is subject to sales or use tax.

3. The Petitioner did not provide any testimony demonstrating why the pass-through fees are exempt. Additionally, the applicable legislative rule clearly states the expenses are not deducted from the charge that is subject to sales tax. Therefore, pass-through fees are to be included in those fees that are subject to sales or use tax.

4. The Petitioner did not provide any evidence demonstrating that the yield spread fee is not subject to tax. The applicable legislative rule clearly states that banks are required to pay sales tax on purchases of services. Therefore, the yield spread fee is subject to sales or use tax.

ANALYSIS GUIDELINES

The issues presented in this matter involve the following important rules of administrative agency authority and statutory construction. Initially, it is important at all times to recognize and to give more than just “lip service” to two general points: (1) rather than utilizing a so-called “de novo” scope of review, deference is to be given to the expertise of the administrative agency, even with respect to an “issue of law,” when that issue of law is one within the peculiar expertise of the administrative agency; and (2) any applicable legislative regulation does not merely reflect the administrative agency’s position but, instead, has been legislatively reviewed and approved, has exactly the same force and effect as a statute, and is, therefore, subject to the usual, deferential rules of statutory construction, *see Feathers v. West v. West Virginia Board of Medicine*, 211 W. Va. 96, 102, 562 S.E.2d 488, 494 (2002).

The following specific points flow from these general points. “[I]f the statute is silent or ambiguous with respect to the specific issue, the question for the [reviewing] court is whether the agency’s answer is based on a permissible construction of the statute.” Syllabus point 4, in part, *Appalachian Power Co. v. State Tax Department*, 195 W. Va. 573, 466 S.E.2d 424 (1995) (emphasis added). Similarly, “the Tax

Commissioner [or the West Virginia Office of Tax Appeals] need not write a rule [or an administrative decision] that serves the statute in the best or most logical manner; he [,or she, or the Office of Tax Appeals] need only write a rule [or a decision] that flows rationally from the statute.” *Id.*, 195 W. Va. at 588, 466 S.E.2d at 439 (emphasis added). Thus, “[i]nterpretations of statutes by bodies charged with their administration are given great weight unless clearly erroneous.” Syllabus point 3, *Shawnee Bank, Inc. v. Paige*, 200 W. Va. 20, 488 S.E.2d 20 (1997) (internal citation omitted) (emphasis added). Finally, “courts will not override administrative agency decisions, of whatever kind, unless the decisions contradict some explicit constitutional provision or right, are the results of a flawed process, or are either fundamentally unfair or arbitrary.” *Appalachian Power*, 195 W. Va. at 589, 466 S.E.2d at 440 (*quoting Frymier-Halloran v. Paige*, 193 W. Va. 687, 694, 458 S.E.2d 780, 787 (1995)).

DISPOSITION

WHEREFORE, it is the **FINAL DECISION** of the **WEST VIRGINIA OFFICE OF TAX APPEALS** that the consumers’ sales and service tax assessment issued against the Petitioner for the period of May 21, 1998 through September 30, 2002, for tax and interest, updated through September 30, 2003, should be and is hereby **AFFIRMED**.

It is **ALSO** the **FINAL DECISION** of the **WEST VIRGINIA OFFICE OF TAX APPEALS** that the purchasers’ use tax assessment issued against the Petitioner for

the period of May 21, 1998, through September 30, 2002, for tax and interest, updated through September 30, 2003, should be and is hereby **AFFIRMED**.