

April 4, 2002

WALLACE, ROBERTS AND TODD

DOCKET NOS: 36BPMERZZ9785 & 36NPMERZZ9883

**STATEMENT OF RECORD:**

1. Wallace, Roberts & Todd (hereafter "Petitioner") filed a petition for review with the Tax Review Board (hereafter "TRB") on March 23, 1998 to challenge a city of Philadelphia audit that resulted in an additional Business Privilege Tax assessment for the years 1995-1997 and an additional Net Profits Tax Assessment for the years 1994-1996.
2. Beginning in June 1998, several public hearings were scheduled and subsequently continued at the requests of the parties. On October 8, 1999, the Tax Review Board granted an open ended continuance to Petitioner pending resolution of a case before the TRB at that time with similar issues captioned Cassway-Albert, Ltd.
3. A public hearing was held before the Tax Review Board on April 24, 2001 and July 10, 2001 following which the matter was taken under advisement pending submission of briefs by the parties. At the public hearing, Petitioner withdrew its challenge to the Net Profits Tax assessment. The hearing thus proceeded only on the Business Privilege Tax issue.
4. On January 22, 2002, the TRB announced its decision to deny the petition on the merits and to abate  $\frac{3}{4}$  of the penalty.
5. Petitioner has appealed to the Philadelphia Court of Common Pleas.

**FINDINGS OF FACT:**

1. WRT is a professional services firm providing architecture, landscape architecture, urban planning, environmental planning and urban design services for its clients. Its principal office is in Philadelphia, Pa.
2. WRT also had offices in Florida and California during the years in question. The receipts generated by these offices were not at issue in this matter.
3. When a current or potential client has a project that needs services in addition to what WRT can provide through its employees, then WRT will reach outside its organization to supplement its own services. For example, the project may need an engineer or some other specialist that WRT does not have in-house. WRT will assemble what it calls a "team" to plan and participate in the project.
4. As the team is assembled, a primary or "prime" consultant is chosen to lead the team through the bidding and negotiation process and, if successful, the project itself. These negotiations and the subsequent contract may identify the other team members and the scope of their contributions to the project as well as the charges for their services.
5. When acting as the prime consultant, WRT will be the entity to execute the contract with the client. The other members of the team are then considered to be sub-consultants who enter into subcontracts directly with WRT.
6. WRT is the responsible party to the client for all work to be performed under the contract, either by its own employees or the subconsultants. The subconsultants may

from time to time deal directly with the clients in the performance of their services but their contractual relationship is with WRT.

7. Once the project is underway, WRT will review and consolidate all subcontractors' bills, consolidate them and send them to the client for review. Payments for these services are to WRT which then disburses the funds to the subcontractors. WRT does not add a commission or profit factor for itself to these subcontractors' fees. It also does not pay the subconsultants from its own funds. The subconsultants are paid when WRT receives the clients' funds.
8. Some of the services performed by WRT or its subconsultants were in Philadelphia and some percentage were outside of the city.
9. There are two basic contracts that Petitioner is likely to enter into with a client. The first is a time and materials contract that provides for Petitioner to bill for actual time or salary expenses, cost of materials and expenses, times a multiplier. Frequently this type of contract has a cap on how much the client is willing to pay. The second type of contract is a lump sum contract where there is a set fee for the project. All expenses, including fees for subconsultants, are paid by Petitioner from this lump sum.
10. The work may take place in the offices of Petitioner, the offices of subconsultants, or at the client's location. The work is coordinated from Petitioner's Philadelphia office.
11. Communication from the client may go directly from the client to the appropriate subconsultant or to Petitioner for communication to a subconsultant.
12. Petitioner has the authority to terminate a team member whose work product does not meet the contract requirements.
13. Petitioner as the prime consultant prepares any final report required of the client. This includes assembling documents from the subconsultants and packaging them into the final report the prime will write.

#### CONCLUSIONS OF LAW:

1. Petitioner seeks to exclude from its gross receipts that portion of its fees that it paid to its subcontractors with no commission or profit taken for itself. The tax years in question are 1995 through 1997. It is the Petitioner's argument that the amounts received from its clients that covered the costs associated with its subconsultants are not "receipts" as defined for purpose of the Business Privilege Tax in The Philadelphia Code Chapter 19-2601.

Petitioner is not entitled to exclude from its gross receipts for Business Privilege Tax purposes the fees received from its clients for work performed by subcontractors even when those fees are passed through to the subconsultants on a dollar for dollar basis.

It is the conclusion of the Tax Review Board that the fees received by Petitioner to cover the services of its subconsultants are taxable receipts within the meaning of The Philadelphia Code Chapter 19-2601. "Receipts" are defined as (c) ash, credits, property of any kind or nature, received from conducting any business or by reason of any sale made, including resales of goods, wares or merchandise taken by a dealer as a trade-in or as part payment for other goods, wares or merchandise or services rendered or commercial or business transactions, without deduction therefrom on account of the cost

of property sold, materials used, labor, service or other cost, interest or discount paid or any other expense.” This broad definition clearly covers all fees paid for services rendered.

Petitioner attempted to characterize its “team” approach as being more in the nature of a joint venture with equal principals rather than a prime contractor who has direct contractual responsibility to the client for a project and then enters into contracts with a variety of subcontractors who can fill in the expertise that Petitioner may not have in its own firm. Petitioner’s theory was that this team concept with its equally participating group of professionals would establish for the TRB that any fees related to work performed by the subconsultants could not be considered receipts of Petitioner but were, instead, receipts of the subconsultants that had merely passed through the hands of Petitioner on their way to the rightful recipients.

However, the facts as developed do not lend themselves to Petitioner’s characterization. It is Petitioner who assembles the “team”, contracts with the client, coordinates the work, has the authority to terminate an unsatisfactory subconsultant, invoices the client, accepts payment from the client, approves the subconsultants’ invoices and disburses those payments to the subconsultants.

Petitioner coordinates the work, verifies the billing, invoices the clients, resolves disputes between client and subconsultant, receives the total fees and then disburses the appropriate amounts to its subconsultants. Petitioner has hiring and firing authority with regard to the subconsultants, even with the understanding that the client will sometimes weigh in on which subconsultant to use for a particular task.

These facts appeared to the TRB to more clearly describe a prime contractor with contractual and primary responsibility to a client to get the job done, with the understanding that subcontractors would be a necessary and acceptable part of the process. The contractual relationships flow between Petitioner and the client, and then between Petitioner and the subconsultants. Therefore, the receipts are attributable to Petitioner.

The ordinance and accompanying regulations provide a list of those items that shall be excluded from a taxpayer’s taxable receipts. The complete list of exclusions is found in Philadelphia Business Privilege Tax Regulation Section 302. Those which could be apposite to this case, and as such were noted by Petitioner, are:

“(1) ( r) reimbursement of expenses, but only if the taxpayer actually incurred such expenses and did so as an agent of another from whom he receives reimbursement in the exact amount he expended.

(2) (t)axes collected as agent for the United States of America, Commonwealth of Pennsylvania, or City of Philadelphia, where the customer or ultimate consumer pays the tax...

(3) (a)n attorney may exclude any fee or portion of a fee paid to another attorney where a matter has been forwarded either from or to the first attorney to or by the second attorney, except where either is an employee of the other.

The fees received by Petitioner for the services of its subconsultants are not excluded from the definition or the express exclusions.

Petitioner, through its attorney, specifically admitted at the hearing that Petitioner did not meet the agency exclusion. See Notes of Testimony, 4-24, Page 18. However, Petitioner went on to argue that it was not relying on an express exclusion in the regulations but on “the fact that the regulations are not exclusive...”. See Notes of Testimony, 4-24, Page 43.

Petitioner argued that, by analogy, it should be regarded as acting in a fiduciary capacity similar to an agent for a governmental body and thus be entitled to the exclusion available to such taxpayers. However, Petitioner admitted that it was not acting as an agent for its subconsultants.

In the alternative, Petitioner argued that by analogy it should be entitled to the exclusion expressly provided to attorneys since its situation of allocating fees is similar. However this exclusion is specifically written and its language does not lend itself to expansion to other professions.

It is the taxpayer who bears the burden of proof in seeking to establish that it falls within an exclusion. Vincent Const., Inc. v. Commonwealth, 668 A.2d 289, 291 (Pa. Commw. 1995).

Petitioner did not establish that it fit within any of the exclusions, nor did it establish to the satisfaction of the TRB that the Revenue Department’s regulations are meant to be advisory or explanatory in nature such that the TRB could expand their definitions or limitations at will.

2. Petitioner is not entitled to apportion its gross receipts when the work performed by subcontractors, who are not employees of Petitioners, is not entirely located within the City of Philadelphia.

Petitioner’s subconsultants are professionals and professional business associations working as independent contractors in a subcontractor capacity and are not employees of the Petitioner. These independent contractors would be responsible for their own Business Privilege Tax filings for work performed within the City of Philadelphia. Therefore the allocation of gross receipts based on the location of services performed by these subconsultants are more appropriately limited to use by these subconsultants in their own Business Privilege Tax filings.

Petitioner’s services were all coordinated from its Philadelphia office and therefore the receipts generated from these services rendered would be subject to the Business Privilege Tax.

The exclusions provided by the Ordinance and Regulations are for the use of the taxpayer based on its business activity and the work performed by its employees.

Concurred:

Daniel Saidel, Esq., Chairman  
Derrick Johnson, Vice Chairman  
Una Vee Bruce  
Wade Stevens  
Joseph Ferla