

Cite as Det. No. 03-0165, 24 WTD 330 (2005)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Correction of)	<u>D E T E R M I N A T I O N</u>
Assessment of)	
)	No. 03-0165 ¹
)	
...)	Registration No. . . .
)	Tax Deferral Certificate No. . . .
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)	Document No. . . . /Audit No. . . .
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RULE 24001(4); RCW 82.60.020(8): TAX DEFERRALS – QUALIFIED BUILDING – APPORTIONMENT OF COSTS. The Department shall apportion the costs of construction if a qualified building is used partly for manufacturing or research and development, and partly for other purposes.

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.

Gray A.L.J. – The taxpayers appeal tax assessments for use tax or deferred retail sales tax on construction costs of an addition to an existing building. The taxpayers argue that the tax is deferred completely under chapter 82.60 RCW (tax deferrals for investment projects in distressed areas). The taxpayers requested and received deferrals. After completion of the project, the Audit Division of the Department of Revenue (DOR) found that only a portion of the

¹ The reconsideration determination, Det. No. 03-0165R, is published at 24 WTD 336 (2005).

construction qualified for the deferral and assessed taxes on the portion that did not qualify. The taxpayers appealed, and we conclude that the Audit Division correctly assessed the tax.²

ISSUES:

1. Whether the taxpayers' building expansion project fully qualified for deferrals of retail sales tax and use tax on construction costs under chapter 82.60 RCW; and
2. Whether DOR is estopped from refusing to defer all retail sales and use taxes on the cost of the addition based upon verbal representations made by a DOR employee.

FACTS:

[Owner] owns real estate and buildings in . . . , Washington. [Owner] leases the land and buildings to [Lessee]. [Lessee] manufactures . . . furniture, and sells those items as well as similar items manufactured by others, both at wholesale and retail. [Owner] built an addition to a building in which [Lessee] manufactured furniture. Before construction, the taxpayers used the existing building for some manufacturing purposes. The taxpayers' stated purpose of the expansion was to consolidate all manufacturing in [one city] and to increase the manufacturing capacity there.

On June 6, 1999, the taxpayers met with representatives from DOR, . . . to review the taxpayers' plans for new construction to ensure it would qualify for tax deferral. The taxpayers contend that the DOR representative told the taxpayers, verbally, to wait until after August 1, 1999, to commence construction. The taxpayers said, "the [DOR employee] indicated that after that time, the requirement in RCW 82.60.020 for 'direct utilization' would be repealed."³ However, the DOR participants in the June 6, 1999, meeting said they were unaware of the taxpayers' plans to place the manufacturing activity in the original structure, not the new addition. The taxpayers began construction after August 1, 1999.

[Owner] and [Lessee] requested a deferral of state and local sales and use taxes under ch. 82.60 RCW, and they did so before beginning construction or hiring new employees. DOR's Special Programs Division issued a distressed area retail sales and use tax deferral certificate ("certificate") to each taxpayer. [Owner] received certificate number . . . , effective August 1, 1999, for deferral of state and local retail sales and use tax (tax) on construction costs of the building addition.

[Lessee] received certificate number . . . , also effective August 1, 1999, for deferral of tax on the purchase of qualified machinery and equipment.⁴

² Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

³ Laws of 1999, ch. 164, §301 repealed former RCW 82.60.020(4)(a)(ii), which required that an investment project be "directly utilized to create at least one full-time qualified employment position for each \$750,000 of investment."

⁴ The Special Programs Division subsequently extended both certificates through January 25, 2000.

The Audit Division issued a tax assessment against [Lessee] after concluding that retail sales and use tax were due on the acquisition of office furniture and equipment and warehouse equipment, including forklifts. Because [Lessee] failed to present any facts upon which relief could be granted relating to the assessment issued against it, [Lessee's] petition is denied.

The taxpayers completed the addition in 2000, increasing its space by approximately . . . square feet. There is one building: the original building and the addition added by the taxpayers. The taxpayers' applications to . . . County, for building permits, identify the addition as a warehouse. After completion of construction, the taxpayers notified the Special Programs Division of that fact. On June 27, 2000, the Special Programs Division asked the Audit Division to perform a deferral audit on [Owner] and [Lessee] to determine whether the construction, equipment, and machinery actually qualified for the tax deferral.

On September 12, 2000, the auditor and field audit manager visited the site and toured the original building and the addition. They found, within the original building, approximately 40% of the space was used for manufacturing. All of the manufacturing is done in the original building. No manufacturing takes place in the addition. The addition is taller than the original building. In the addition, as viewed by the auditors, the taxpayers had 14 storage racks for storing furniture and raw materials. Of those 14 racks, only two were used to store the raw materials used in manufacturing or to store the taxpayers' finished goods. The Audit Division apportioned the deferral of tax, calculating the percentage of tax to be deferred at 14.3% (2/14). We note, in the tax year 2000, the taxpayers did not report any income under the manufacturing classification, despite [Lessee's] claim that sales of its own manufactured goods accounted for 47.5% of [Lessee's] total sales.

The Audit Division issued tax assessments against [Owner] after concluding that retail sales tax and use tax on the costs of the new addition were not fully deferred by ch. 82.60 RCW. The taxpayers appeal those tax assessments.

ANALYSIS:

Chapter 82.60 RCW authorizes deferral of state and local retail sales tax and use tax for qualified buildings in distressed areas and in community empowerment zones. DOR adopted WAC 458-20-24001 (Rule 24001) to administer ch. 82.60 RCW. RCW 82.60.020(8) states:

"Qualified buildings" means construction of new structures, and expansion or renovation of existing structures for the purpose of increasing floor space or production activities, including plant offices and warehouses or other facilities for the storage of raw material or finished goods if such facilities are an essential or an integral part of a factory, mill, plant, or laboratory used for manufacturing or research and development. If a building is used partly for manufacturing or research and development and partly for other purposes, the applicable tax deferral shall be determined by apportionment of the costs of construction under rules adopted by the department.

Rule 24001(5) states that where a building is used for both qualifying and nonqualifying purposes, “the deferral will be determined by apportionment of the total project costs.” This subsection includes the apportionment formula. Based on the apportionment formula in Rule 24001(5), the Audit Division deferred 14.3% of use tax and/or deferred retail sales tax due on the construction costs of the addition. The taxpayers do not dispute the calculation of the apportionment formula under Rule 24001(5). Instead, the taxpayers argue that tax on the entire costs of construction of the addition should be deferred. Their argument is the entire building is a qualified building.

The taxpayer argues that a “qualified building,” under RCW 82.60.020(8), includes “the expansion of an existing structure for the purpose of increasing floor space or production capacity used for manufacturing.” The taxpayer argues that RCW 82.60.020(8) “does not say that the expanded area itself must be directly utilized for manufacturing.” We disagree with the taxpayer’s arguments. The manufacturing must occur in the footprint of the new construction; otherwise, any new construction arguably qualifies for tax deferral. The phrase “directly utilized” is found in RCW 82.60.020(4)(a)(ii):

“Eligible investment project means” . . . [t]hat portion of an investment project in an eligible area as defined in subsection (3)(d) or (g) of this section which is directly utilized to create at least one new full-time qualified employment position for each three hundred thousand dollars of investment on which a deferral is requested in an application approved before July 1, 1994, and for each seven hundred fifty thousand dollars of investment on which a deferral is requested in an application approved after June 30, 1994.

In context, the phrase “directly utilized” tied “portion of an investment project” to “one full-time position.” “Directly utilized” did not refer to the use of a building for a qualifying or nonqualifying use. In determining what a statute means, words should be ascribed their plain and ordinary meanings. *North Coast Air Servs., Ltd. v. Grumman Corp.*, 111 Wn.2d 315, 321, 759 P.2d 405 (1988). When a statute does not define a nontechnical word, the court may look to the dictionary for guidance. *State v. Myers*, 133 Wn.2d 26, 33, 941 P.2d 1102 (1997) (citing *State v. Pacheco*, 125 Wn.2d 150, 154, 882 P.2d 183 (1994)). The ordinary dictionary meaning of “directly” is “in a direct line or way; straight.” The ordinary dictionary meaning of “utilized” is “to put to use.” The legislature intended the “directly utilized” language as a requirement that the tax deferral be granted only if the new construction or expansion clearly produced one new job for every seven hundred fifty thousand dollars of investment.

Chapter 82.60 RCW and Rule 24001 do not allow deferral of retail sales tax or use tax as broadly as urged by taxpayers. We conclude the Audit Division correctly assessed the taxes, which the taxpayer sought to defer. The facts show that only two of fourteen storage racks installed in the new addition were used for raw materials used by the taxpayer in manufacturing furniture or for [Lessee’s] finished furniture. [Lessee] candidly acknowledged that it purchases for resale furniture from other manufacturers and stores that furniture in the addition. Thus, not all of the addition is used for manufacturing or storage related to manufacturing. The deferral is not

intended to apply to building space used for non-manufacturing related purposes. The petitions for correction of assessments are denied on this issue.

The other issue is whether the Department is estopped from assessing retail sales tax or use tax on costs of construction of the addition. We have addressed estoppel issues many times in the past. We begin by noting that the Department's representative denied assuring the taxpayers that their addition would be free from retail sales tax if only they waited to begin construction after August 1, 1999. He was unaware of the taxpayers' plans to place all manufacturing activities in the original building, not the new addition. Further, the taxpayers' estoppel claim is verbal only. ETA 419.32.99 ("ETA 419") addresses the question of whether oral instructions or interpretations by employees of DOR are binding upon DOR. They are not. DOR does not consider claimed misinformation resulting from personal consultations with a DOR employee. ETA 419 cites three reasons for this rule:

- (1) There is no record of the facts which might have been presented to the agent for his consideration.
- (2) There is no record of instructions or information imparted by the agent, which may have been erroneous or incomplete.
- (3) There is no evidence that such instructions were completely understood or followed by the taxpayer.

These reasons apply in the taxpayers' case. We simply do not have a record of what the taxpayers presented to the DOR employee or what the DOR employee told the taxpayers. The State of Washington will not be estopped in its governmental capacity of collecting tax based upon a claim of estoppel that cannot be substantiated:

Application of the doctrine to deprive the state of the power to collect taxes is disfavored. Washington courts have articulated a general rule that courts should be "most reluctant" to find the Department equitably estopped when it is acting in its taxing capacity and for the enforcement and collection of taxes imposed by the Legislature. *Wasem's, Inc. v. State*, 63 Wn.2d 67, 70, 385 P.2d 530 (1963); *Harbor Air Service, Inc. v. Board of Tax Appeals*, 88 Wn.2d 359, 560 P.2d 1145 (1977); *Kitsap-Mason Dairymen's Assoc. v. Tax Comm'n*, 77 Wn.2d 812, 818, 467 P.2d 312 (1970).

Det. No. 99-285, 19 WTD 492 (2000). The petitions for correction of assessments are denied on the estoppel issue.

DECISION AND DISPOSITION:

The petitions for correction of tax assessments are denied.

Dated this 21st day of May 2003.