Cite as Det. No. 92-277, 12 WTD 451 (1992).

BEFORE THE INTERPRETATION AND APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Ruling of Tax Liability of	)	D E T E R M I N A T I O N
	)	No. 92-277
. . .	)	Registration No. . . .
. . .	)	Registration No. . . .

[1] RULE 211: BAILMENTS -- CONSIDERATION -- DEFINITION -- RECIPROCAL PROMISES. User of chassis does not qualify as bailee where user's right to use the chassis is conditioned on user's promise to permit the chassis owner to use chassis owned by user under similar circumstances. User's promise to permit reciprocal use constitutes "consideration," which precludes the arrangement from qualifying as a bailment under Rule 211. ACCORD: Cook v. Johnson, 37 Wn.2d 19, 23 (1950); Higgins v. Egbert, 28 Wn.2d 313 (1947); Ebling v. Gove's Cove, Inc., 34 Wn. App. 495, 499 (1983); Det. No. 91-44, 10 WTD 395 (1991); Det. No. 87-110, 3 WTD 21 (1987).

[2] MISC. -- JOINT VENTURE -- PROFIT SHARING. An agreement to share the profit resulting from a chassis interchange agreement is essential to the existence of a joint venture. The absence of a profit-sharing agreement thus defeats taxpayers' contention that their chassis interchange agreement was a "de facto" joint venture. ACCORD: Det. No. 90-108, 9 WTD 231 (1990); Det. No. 87-319, 4 WTD 165 (1987); Det. No. 87-93, 2 WTD 411 (1987).

[3] RULES 211 and 247: TRADE-IN -- LIKE-KIND EXCHANGE -- LEASE. User of chassis qualifies as lessee where user's right to use the chassis is conditioned on user's promise to permit the chassis owner to use user's chassis under similar circumstances. User's promise to permit reciprocal use constitutes "consideration," which, coupled with user's dominion

and control over the property, creates a lease under Rule 211. Owner's reciprocal use of user's property constitutes a trade-in of like kind property.

[4] RULE 178: USE TAX -- SALES TAX -- LIABILITY -- PURCHASES FOR RESALE -- INTERVENING USE. Taxpayers are liable for sales or use tax on their purchases of chassis that are contributed to the chassis pool because taxpayers make intervening use of such chassis.

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.

TAXPAYER REPRESENTED BY: . . .

DATES OF TELEPHONE CONFERENCES: . . .
. . .

NATURE OF ACTION:

Two world-wide common carrier transportation companies petition for a ruling of B&O, sales, and use tax liability resulting from an "interchange agreement" in which each taxpayer contributes chassis to a pool. The chassis are removed from the pool and used interchangeably by taxpayers.

FACTS:

Eggen, A.L.J. -- [Taxpayer 1 and taxpayer 2 (taxpayers)] petition for a ruling of prospective tax liability arising from an "interchange agreement." Taxpayers are members of unrelated affiliated groups that provide world-wide common carrier transportation of third-party containerized cargo. Each group operates an independent international transportation network that consists of cargo vessels, cargo containers, ground transportation equipment, and marine and truck terminals.

To increase the groups' efficiency, [taxpayer 1] and an affiliate of [taxpayer 2] entered an agreement ("the coordinated sailing agreement"), which provides for the charter of space between the groups on their respective vessels or on vessels on which they have contracted for space. Thus, vessels operating under the coordinated sailing agreement carry cargo originating from both groups.

In order to successfully operate under the coordinated sailing agreement, taxpayers need to load and unload shipping containers onto and from vessels according to port, weight, and size. The

container slots on each vessel are distributed on that basis and not on the basis of which taxpayer originated the container.

Containers are discharged from vessels onto chassis and are loaded from chassis onto vessels. Only one container is placed on each chassis. Efficiency requires that each container remain on the same chassis while the container is in the terminal. Because of the placement of containers on the vessels, flow of chassis traffic, and chassis availability in the terminal yard, chassis cannot be efficiently lined up in a sequence that will match them to containers owned by the same taxpayer. In other words, chassis owned by both taxpayers must be intermingled for efficient operations.

Therefore, to achieve efficiency, taxpayers entered an "interchange agreement," which established a pool of chassis at the Washington ports of call of the vessels operating under the coordinated sailing agreement. Taxpayers represent that, under the interchange agreement, taxpayers freely interchange their chassis, "without charge," at ports served by the coordinated sailing agreement. Taxpayers further represent that they are obligated to maintain the appropriate balance of chassis in the pool to meet their combined needs. Specifically, each taxpayer is obligated to contribute sufficient chassis to balance its use. If a taxpayer fails to provide sufficient chassis to balance its use, it is required to provide additional chassis to cure that deficiency. Such additional chassis may be, but need not be, leased from the other taxpayer. The lessee of a chassis pays a daily charge for the use of the chassis.

Further, pursuant to the interchange agreement:

1. The user of the chassis is obligated to maintain the chassis at its own expense.

2. The user of the chassis is required to repair damage to the chassis that occurs after delivery to user. If user fails to make such repairs, it is nonetheless liable for the cost of the repairs. If the estimated cost of repairs exceeds $250, the user must obtain the owner's consent prior to repair.

3. The user of the chassis is required to repair the chassis where the need for repair is caused by a defect in the chassis or by ordinary use where the cost of such repair is $50 or less. The owner of the chassis is required to bear the cost of such repairs where the cost of repair is $50 or more.

4. The user of the chassis is required to reimburse the owner of the chassis for the "casualty value" of chassis that are lost or stolen or that become a "total loss."

5. The user of the chassis is responsible for its drayage and is responsible for providing the driver of the vehicle that carries the chassis.

6. The user of the chassis is required to provide evidence of automobile insurance to owner.

7. The user of the chassis is required to pay all expenses of operating the chassis, except as noted above. However, the user of the chassis is not liable for taxes relating to the chassis, except sales and use taxes resulting from the user's use of the chassis.

Taxpayers request a ruling that their use of the chassis under the interchange agreement is not subject to sales, use, or B&O tax. Taxpayers contend: 1) use of the chassis pursuant to the interchange agreement qualifies as use as a bailee for purposes of WAC 458-20-211 (Rule 211); 2) the interchange agreement creates a "de facto" joint venture; and 3) the interchange agreement results in a "random exchange" or "inadvertent use" of the chassis. Taxpayers did not adequately elaborate on their third contention in their petition or during the telephone conferences. This contention will therefore not be addressed in this ruling.

ISSUE:

1. Whether the user of chassis under the interchange agreement is a bailee of the chassis where the user's right to use the chassis is conditioned on its promise to permit the chassis owner to use the user's chassis under similar circumstances.

2. Whether taxpayers qualify as a joint venture where the agreement between taxpayers does not require a sharing of profit.

3. Whether each taxpayer's use of chassis owned by the other results in a lease of tangible personal property, coupled with a trade-in of like kind property.

4. Whether taxpayers are liable for sales or use tax on their purchases or leases of chassis that are contributed to the chassis pool.

DISCUSSION:

As a preliminary matter, we note that taxpayers agree that unless a specific exemption (e.g., use in interstate commerce, RCW 82.12.0254) applies to the daily charges (incurred when one taxpayer leases chassis from the other as the result of the lessee's failure to provide the requisite number of chassis to the pool) such payments are subject to retailing B&O tax and sales or use tax. RCW 82.04.050, .250, .08.020, .12.020. If the charge specified in taxpayers' agreement does not represent the reasonable rental value of the chassis, taxpayers must nonetheless pay sales or use tax based on the reasonable rental value. See RCW 82.08.010, .12.010; WAC 458-20-178.

[1] Taxpayers argue that their use of chassis under the interchange agreement qualifies as a bailment under Rule 211. A bailee is not liable for retail sales or use tax on property if the bailor has already paid either tax on that property. Rule 211.
Rule 211 provides the definition of "bailment" for Washington tax purposes:

> The term "bailment" refers to the act of granting to another the temporary right of possession to and use of tangible personal property for a stated purpose without consideration to the grantor.
>
> A true . . . bailment of personal property does not arise unless the . . . bailee, or employees or independent operators hired by the . . . bailee actually takes possession of the property and exercises dominion and control over it.

(Emphasis added.) Here, one taxpayer (the "user") takes physical possession of and operates a chassis owned by the other taxpayer (the "owner"). The user is responsible for maintenance, certain repairs, and insurance of the chassis in its possession. The user also bears risk of loss, since the user is required to maintain insurance and to pay the owner for the value of the chassis if the chassis is lost, stolen, or a "total loss." Thus, user assumes sufficient dominion and control over the chassis under the interchange agreement.

However, to qualify as a bailment, Rule 211 requires that the use be "without consideration." Here, the user promises to allow the owner to use the user's chassis in exchange for the reciprocal promise by the owner that the user will be permitted to use the owner's chassis. It is hornbook law that reciprocal promises constitute consideration. See, e.g., Cook v. Johnson, 37 Wn.2d 19, 23 (1950); Higgins v. Egbert, 28 Wn.2d 313 (1947); Ebling v. Gove's Cove, Inc., 34 Wn. App. 495, 499 (1983); see also RCW

82.04.090, .08.010 (which include within the definition of "consideration" any "rights" given to the seller); Det. No. 91-44, 10 WTD 395 (1991); Det. No. 87-110, 3 WTD 21 (1987).

Taxpayers' use of the chassis under the interchange agreement thus does not qualify as use under bailment for purposes of Rule 211.

[2] Taxpayers next argue that their interchange agreement qualifies as a "de facto" joint venture. A joint venture requires that the joint venturers share the profit resulting from their joint venture. See, e.g., Det. No. 90-108, 9 WTD 231 (1990); Det. No. 87-319, 4 WTD 165 (1987); Det. No. 87-93, 2 WTD 411 (1987). No such sharing of profit occurs here. Taxpayers do not share the "profit" resulting from the daily charges paid for the leasing of chassis in the case of a shortfall. Nor do taxpayers share the profit derived from customers from that portion of the transportation that involves the use of the chassis. Thus, because taxpayers do not share the profit that results from their interchange agreement, taxpayers' arrangement does not qualify as a joint venture.

[3] Although taxpayers did not raise the issue, we next address whether the interchange agreement resulted in a lease coupled with a trade-in of like kind property.

Rule 211 provides:

> The terms "leasing" and "renting" are used interchangeably and refer generally to the act of granting to another the right of possession to and use of tangible personal property for a consideration.

As with bailments, under a lease it is necessary for the lessee to take actual physical possession of the property and to exercise dominion and control over it. Rule 211. As previously noted, the user of the chassis under the interchange agreement takes actual physical possession of the property and exercises the requisite dominion and control. Further, as previously noted, the user's promise to permit the chassis owner to use user's chassis constitutes consideration. Thus, the owner of the chassis is the lessor of the chassis for Washington tax purposes.

RCW 82.04.050(4) includes within the definition of retail sale the renting or leasing of tangible personal property to consumers. See also RCW 82.04.040. Thus, the owner/lessor of the chassis must pay retail sales tax and retailing B&O tax with

respect to the lease of the chassis to the user/lessee.[1] RCW 82.04.250, .08.010, .020; Rule 211. The measure of the tax is the consideration received by the lessor from the lessee; in this case, the consideration equals the reasonable rental value of the chassis. See RCW 82.04.070, .090, .08.010.

However, for purposes of both the retail sales and use taxes, there may be excluded from the measure of tax the value of like kind property that is traded-in under a lease. RCW 82.08.010, .12.010; Rule 178; WAC 458-20-247 (Rule 247). Specifically, Rule 247 provides:

> [T]he value of "trade-in property" may be excluded from the measure of retail sales tax to be collected and reported by the seller who accepts the trade-in property as payment for new or used property sold.

This same rule applies for purposes of the use tax. Rule 247.

Under Rule 247, property of "like kind" has its "ordinary and common meaning" and means "property of like kind to that acquired in a retail sale which is applied, in whole or in part, toward the selling price" or "property of the same generic classification." The chassis at issue here qualify as like kind property; the chassis are of the same generic classification. In fact, the chassis are basically fungible; there is little or no difference among the chassis each taxpayer contributes to the pool.

Although Rule 247 provides detailed information for purposes of valuing the property traded-in, the value of the chassis exchanged pursuant to the interchange agreement are apparently essentially equal in value.[2] The chassis are apparently of like

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[1]Consumers who rent or lease tangible personal property from others and who have not paid the retail sales tax to their lessors are liable for the use tax on the amount of the rental payments as of the time the payments fall due. RCW 82.12.010, .020; Rules 178 and 211.

[2]Rule 247 provides:

> The seller and buyer establish the value of property traded-in. However, the parties may not overstate the value of the property traded-in in order to artificially lower the amount of sales of use tax due. Absent proof of a higher value, the property traded-in

quality and size and are being used under comparable conditions. Thus, for purposes of this ruling, it is assumed that any difference in value among the chassis that are exchanged is de minimis and need not be reported.

The trade-in exclusion affects only the measure of retail sales tax to be collected and paid. There is no trade-in exclusion for business and occupation tax. Thus, the gross receipts to be reported under the retailing classification of the B&O tax is the total value proceeding or accruing from the lease, including the value of property traded-in. Rule 247.

Rule 211 imposes detailed record keeping requirements for qualification for the like kind exchange exclusion:

> RCW 82.32.070 requires every person liable for any tax to keep and preserve records from which true tax liability can be determined. Before any exclusion from the selling price for the value of property traded-in will be allowed, the property traded-in must be specifically identified and clearly indicated as "trade-in," by model, serial number and year of manufacture where applicable, and the full trade-in value must be shown on the sales agreement or invoice given to the purchaser, with a copy retained in the seller's permanent sales records.

Because of the unusual circumstances in this case, each time there is a lease of chassis, there is, by necessity, a trade-in of like kind property of equal value to that leased.[3] Taxpayers therefore do not track each specific chassis; instead, for each chassis that a taxpayer withdraws from the pool, that taxpayer is simply required to return a chassis to the pool at a later time. Because the chassis are essentially fungible and because each taxpayer's use of the other taxpayer's chassis necessarily results in a reciprocal use, no more elaborate record keeping

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> must be determined by the fair market value of similar property of like quality, quantity, and age, sold or traded under comparable conditions. It is the substance of the actual sale and trade-in transaction which will control the retail sales tax measure, regardless of any subsequent accounting adjustments to the seller's inventory records or books of account.

[3]Under the interchange agreement, each taxpayer is required to contribute to the chassis pool sufficient chassis to balance that taxpayer's chassis use. Thus, when [taxpayer 1] uses chassis owned by [taxpayer 2], [taxpayer 2] must, in turn, use chassis owned by [taxpayer 1].

requirement is needed. Based on the specific facts in this case, we conclude that taxpayers need not track each individual chassis to qualify for the trade-in exemption. However, for B&O tax reporting purposes, taxpayers must keep adequate records to reflect the total time each taxpayer uses chassis belonging to the other taxpayer.

[4] Finally, we address the issue of whether taxpayers are liable for sales or use tax when they purchase or lease chassis for purposes of contributing such chassis to the chassis pool. Taxpayers agree that they are generally obligated to pay sales or use tax on the acquisition of the chassis prior to contribution to the pool, regardless of whether such acquisition is by lease or purchase.

Rule 211 contains a limited exception to this general rule:

> Under unique circumstances when such things are rented for rerent by the lessee, without intervening use, then the original rental is subject to the wholesaling classification of tax and the subsequent rental is subject to the retailing classification.

Under the interchange agreement, prior to the lease of any chassis by a user/lessee, the owner/lessor of the chassis "uses" the chassis by contributing the chassis to the pool; such contribution constitutes an exercise of dominion and control sufficient to support imposition of the use tax. See RCW 82.12.010. Thus, taxpayers are liable for sales or use tax on all chassis contributed to the pool, whether such chassis are acquired by lease or by purchase.

However, where a chassis that is not contributed to the pool is leased by one taxpayer (the "original lessee") from a third party lessor and the original lessee then leases the chassis to the other taxpayer or to others (the "sublessee"), without intervening use by the original lessee, the original lessee is not liable for sales or use tax on its lease payments to the lessor for the period that the chassis is subleased. Similarly, the purchase of a chassis that is not contributed to the chassis pool will not be subject to sales or use tax if the purchaser never itself uses the chassis but instead leases the chassis to the other taxpayer or to others. Rule 211; ETB 481.12.178. Rule 211 provides that retail sales will not apply to sales of tangible personal property to persons who purchase the same solely for the purpose of renting or leasing such property.

This legal opinion may be relied upon for reporting purposes and as support of the reporting method in the event of an audit. This ruling is issued pursuant to WAC 458-20-100(9) and is based

upon only the facts that were disclosed by the taxpayer. In this regard the department has no obligation to ascertain whether the taxpayer has revealed all of the relevant facts or whether the facts disclosed were actually true. This legal opinion shall bind this taxpayer and the department upon those facts. However, it shall not be binding if there are relevant facts which are in existence but not disclosed at the time this opinion was issued; if, subsequently, the disclosed facts are ultimately determined to be false; or if the facts as disclosed subsequently change and no new opinion has been issued which takes into consideration those changes. This opinion may be rescinded or revoked in the future, however, any such rescission or revocation shall not affect prior liability and shall have a prospective application only.

This legal opinion constitutes specific written instructions. RCW 82.32.090(4) specifies:

> If the department finds that all or any part of a deficiency resulted from the disregard of specific written instructions as to reporting or tax liabilities, the department shall add a penalty of ten percent of the amount of the additional tax found due because of the failure to follow the instructions. A taxpayer disregards specific written instructions when the department of revenue has informed the taxpayer in writing of the taxpayer's tax obligations and the taxpayer fails to act in accordance with those instructions unless the department has not issued final instructions because the matter is under appeal pursuant to this chapter or departmental regulations. The department shall not assess the penalty under this section upon any taxpayer who has made a good faith effort to comply with the specific written instructions provided by the department to that taxpayer. Specific written instructions may be given as a part of a tax assessment, audit, determination, or closing agreement, provided that such specific written instructions shall apply only to the taxpayer addressed or referenced on such documents. Any specific written instructions by the department of revenue shall be clearly identified as such and shall inform the taxpayer that failure to follow the instructions may subject the taxpayer to the penalties imposed by this subsection.

DATED this 13th day of October 1992.