

Cite as Det. No. 92-029, 12 WTD 333 (1992).

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

In the Matter of the Petition)	<u>D E T E R M I N A T I O N</u>
For Correction of Assessment of)	
Beneficial Liability of)	
)	No. 92-029
)	
. . .)	Registration No. . . .
)	Warrant No. . . . & . . .
)	
)	

- [1] RCW 82.32.020 and 82.04.140: BUSINESS DEFINITION. The definition of business for excise tax purposes is all-encompassing and includes all commercial activity. Budget Rent-A-Car of Washington-Oregon, Inc. v. Department of Revenue, 81 Wn.2d 171 (1972).
- [2] RCW 82.32.210 and WAC 458-20-217: UNPAID TAXES -- LIABILITY OF THIRD PARTIES WHO HAVE A BENEFICIAL INTEREST IN THE BUSINESS. Where an oil company leases convenience stores on a percentage basis and requires as part of the lease that the lessees enter into a separate commission agreement to collect the receipts from the oil company's sale of gasoline from an adjoining filling station and the lessees fail to pay their excise taxes, the personal property of the oil company used in the conduct of the convenience store and filling station is subject to the tax lien. Partial Accord: Det. No. 91-166, 11 WTD 345.
- [3] RCW 82.32.210 and WAC 458-20-217: UNPAID TAXES -- BENEFICIAL INTEREST OF THIRD PARTIES. The attachment of a tax lien to the property of a third party who has a beneficial interest in the delinquent taxpayer's business does not require that the personal property be leased to the delinquent taxpayer.
- [4] RCW 82.32.210 and WAC 458-20-217: UNPAID TAXES -- SECURITY AGREEMENTS -- BENEFICIAL INTEREST OF THIRD PARTIES. The exception from attachment of the tax lien

for bona fide interests of third parties which vested prior to filing a tax warrant does not apply to third parties that have a beneficial interest in the business.

- [5] RCW 82.32.330: SECRECY CLAUSE. Absent the consent of the person primarily liable for the taxes or a specific statutory exception, the Department is prohibited from releasing information concerning that person.

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: . . .

DATE OF HEARING: . . .

NATURE OF ACTION:

The taxpayer appeals the assessment of its liability based on a finding that it had a "beneficial interest" in lessee's business.

FACTS:

Coffman, A.L.J. -- [Taxpayer] is an oil company which leased two . . . convenience stores to . . . (lessees). These leases called for fixed monthly lease payments or 12% of the gross receipts, whichever was greater. In addition, the taxpayer owns the property adjoining each convenience store which was operated as a self service gasoline filling station. Under separate agreements the lessees were paid a commission . . . per gallon for collecting the receipts from the sale of gasoline for the taxpayer. There were two separate leases and two separate commission agreements the terms of which were identical except for the addresses. For clarity purposes each agreement will be referred to in the singular.

The arrangement between the taxpayer and the lessees was the taxpayer's normal method of operation¹. The taxpayer pays all

¹The taxpayer has recently modified its method of operation by entering into franchise agreements and licensing agreements for trade names; however the substance of the arrangements remains the same. That is, the taxpayer leases the convenience store only and operates the filling station under a commission agreement with the appropriate lessee. However, there is some confusion as to the terms of the lease in this case. That confusion will be discussed later.

state and local taxes related to the sale of gasoline and owns and maintains the equipment, owns the fuel, and sets the price to be charged. The taxpayer owns [several] such convenience stores and filling stations in the state of Washington. Customers of either the convenience store or gasoline facility would not be able to determine whose business was whose. In fact, they would probably not know that the taxpayer was involved in the operation at all. The gasoline in this case was not marketed under the taxpayer's name, rather it was marketed under [another]. Customers would pay for their gasoline purchases in the convenience store. The lease required that the lessees maintain a minimum inventory, but did not specify what was to be included in the inventory or from whom it was to be purchased. The lessees were required to maintain a liquor license and have insurance coverage which protected the taxpayer.

The lessees failed to make their lease payments to the taxpayer and were delinquent in paying over the gasoline receipts. [In May 1990], the taxpayer entered into a separate agreement with the lessees whereby the lessees renounced their rights under UCC Article 9, Part 5 in the business personal property of the lessees including the inventory at both locations if certain payments were not made. Further, the lessees failed to pay their state and local retail sales tax and business and occupation taxes. The Department's Compliance Division issued Tax Warrant No. . . . [in June 1990] (for the period of February through April 1990 and balance dues for November 1989 and January 1990) and Tax Warrant No. . . . [in July 1990] (for the period of May and June 1990) against the lessees. These warrants were filed with the [county] Superior Court The lessees ceased operation under the agreements with the taxpayer [in July 1990] and a new operator took over the two convenience stores² [In July 1990] a Notice of Beneficial Interest Liability was issued against the taxpayer directing them to pay \$ The lessees claimed to be liquidating their assets to pay their liability, therefore the Department's Compliance Division agreed to withhold action on the Notice of Beneficial Interest. The lessees filed petition under Chapter 7 of the Bankruptcy Code [in October 1990] and were granted a discharge [in January 1991]. Various conversations and negotiations were conducted between the

²The taxpayer stated at the hearing that a new lease was commenced [seven days earlier]. Further, the taxpayer stated that it foreclosed on its security interest that day, but had no documentation of those actions. However, the statement of the new lessee to the Department's Revenue Officer was that the new operator took over [in July 1990]. This statement was confirmed by the lessees' statement to the same Revenue Officer.

taxpayer and the Compliance Division and extensions to appeal were granted.

The assessed value in 1990 of the taxpayer's personal property located at the two locations was \$ The assessed value in 1990 of the lessees' personal property at both locations was approximately \$

[In October 1991] the taxpayer filed a timely notice of appeal with the Interpretation and Appeals Division of the Department.

TAXPAYER'S EXCEPTIONS:

The taxpayer raises three primary issues in its appeal. Specifically, the taxpayer claims that:

1. The beneficial interest portion of RCW 82.32.210 only applies to the tangible personal property used in the conduct of the convenience store business and cannot apply to the taxpayer's business of selling gasoline.
2. Either the tax lien did not apply to the lessees' personal property or the taxpayer's interest in it had vested prior to the Department's and thus had seniority.
3. The application of the beneficial interest provision to the taxpayer is unconstitutional because it is vague and the taxpayer had no knowledge that the lessees had failed to pay their state taxes.

DISCUSSION:

RCW 82.32.210 specifies that the Department may issue a tax warrant if taxes, increases, or penalties are not paid and further specifies the effect of filing the tax warrant with the Superior Court. RCW 82.32.210 states, in part:

Upon filing, . . . thereupon the amount of the warrant so docketed shall become a specific lien upon all goods, wares, merchandise, fixtures, equipment, or other personal property used in the conduct of the business of the taxpayer against whom the warrant is issued, including property owned by third persons who have a beneficial interest, direct or indirect, in the operation of the business.

(Emphasis added.)

WAC 458-20-217 is the properly adopted rule of the Department which implements the provisions of RCW 82.32.210. This rule states in part:

When a warrant issued under RCW 82.32.210 and 82.32.220 has been filed with the clerk of the superior court and entered in the judgment docket, the warrant becomes a specific lien upon all goods, wares, merchandise, fixtures, equipment or other personal property used in the conduct of the business of the taxpayer, including property owned by third persons who have a beneficial interest, direct or indirect in the operation thereof, and no sale or transfer of such personal property in any way affects the lien. However, the lien is not superior to bona fide interests of third persons which had vested prior to the filing of the warrant when such third persons do not have a beneficial interest, direct or indirect, in the operation of the business, other than securing the payment of a debt or the receiving of a regular rental on equipment. . . .

(a) Thus, where an oil company leases a filling station and other equipment to an operator under conditions whereby the operator is required to sell, or does sell, the products of the lessor, the lien will attach to the personal property leased by the oil company. Likewise, where the owner of a tavern grants to another a concession to operate the lunch counter therein, the lien for unpaid taxes, increases, and penalties with respect to the operation of the lunch counter will attach to any equipment, fixtures, or other personal property owned by the tavern keeper but used by the concessionaire in the conduct of the business. Similarly, the lien attaches to a stock of merchandise supplied to a dealer by a distributor, manufacturer, bank or finance company whether on consignment or under a security agreement where it appears that the distributor, manufacturer, bank or finance company has financed the dealer by means of capital loans or has in any other way aided or assisted in maintaining the dealer in business.

(Emphasis added.)

This rule was originally adopted by the Washington Tax Commission in 1937 as Rule 223. In 1939, the "beneficial interest" provisions were incorporated into Rule 217. The specific language of RCW 82.32.210³ dealing third parties and beneficial interest was adopted in 1949. Section 25, Chapter 228, Laws of

³In 1949 the tax statutes were referred to as the Revenue Act of 1935.

1949. The statute and rule have not changed significantly in the beneficial interest area since 1949.

1. The taxpayer's first argument is:

The beneficial interest portion of RCW 82.32.210 only applies to the tangible personal property used in the conduct of the convenience store business and cannot apply to the taxpayer's business of selling gasoline.

The taxpayer agreed at the hearing that the beneficial interest clause applied to the personal property owned by the taxpayer and used in the operation of the convenience store. The first issue raised by the taxpayer requires that two questions be answered: (1) "What was the business of the lessees?" and (2) "Did the taxpayer have a beneficial interest in the business of the lessees?"

A. What was the business of the lessees?

It is the taxpayer's contention that the sale of gasoline was not the business of the lessees and therefore the personal property connected to the sale of gasoline is not subject to lien created by the tax warrants. However, both activities are indisputably interrelated. The lease stated at paragraph 34:

This lease is made in conjunction with the Commission Agreement of the same date. Compliance with the terms and conditions of said Commission Agreement is of material significance to this lease. Failure of lessee to perform under that Commission Agreement shall constitute a default under this lease.

The term of the Commission Agreement ran "concurrently with the lease entered into between the parties on the adjoining property." The business of the lessees consisted of two distinct functions: the convenience store and the filling station. While the convenience store could operate without the filling station, the filling station could not operate without the convenience store because there would be no method by which the customers could pay for their purchases.

[1] The taxpayer claims that the operative word in the statute and regulation is "business" and not "businesses." RCW 82.32.020 states:

For the purposes of this chapter:
The meaning attributed in chapters 82.01 through 82.27 RCW to the words and phrases "tax year," "taxable year," "person," "company," "gross proceeds of sales," "gross income of the business," "business," "engaging

in business," "successor," "gross operating revenue," "gross income," "taxpayer," and "value of products" shall apply equally to the provisions of this chapter.

(Emphasis added.)

RCW 82.04.140 states:

"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.

The use of the word "activities" in the definition of "business" clearly means that "business" includes both the singular and plural. The term "business" has been interpreted to mean "a broad and virtually all-encompassing commercial activity." Rent-A-Car of Washington-Oregon, Inc. v. The Department of Revenue, 81 Wn.2d 171, 173 (1972), see also O'Leary v. Department of Revenue, 105 Wn.2d 679 (1986) and Keys v. Department of Revenue, BTA Docket No. 31630, 2 WTD 305 (1986). In this case the commercial activities of the lessees included the operation of the convenience store and the collection of receipts from the sale of gasoline (even if the title to the gasoline remained in the taxpayer's name). These activities were clearly performed with object of gain, benefit, or advantage to the lessees.

It is clear that the provisions of RCW 82.32.020 and 82.04.140 require that the term "business" in RCW 82.32.210 be inclusive of all the activities of the lessees. Therefore, the taxpayer's argument that the sale of gasoline was solely the taxpayer's business and not the lessees is erroneous.

RCW 82.32.210 and WAC 458-20-217 state that the tax lien applies to business property and to other property used in the business only if:

1. The property is owned by a third party; and
2. The owner of the property had a beneficial interest in the operation of the business.

The taxpayer agrees that the personal property associated with the gasoline sales facility was its property. Therefore, the issue becomes "Did the taxpayer have a beneficial interest in the business of the lessees?"

B. Did the taxpayer have a beneficial interest in the business of the lessees?

The term "beneficial interest" is not defined in RCW 82.32.210 nor is it defined in WAC 458-20-217. However, the meaning of the term can be determined by reference to the examples in WAC 458-20-217. In the oil company example, the beneficial interest lien applies when a delinquent taxpayer has leased property from a supplier and sells that supplier's products, whether required to do so or not. In this example the supplier is beneficially interested because the success of the business will result in further gains to the supplier. The example dealing with a lunch counter is similar to the first in that the third party derives a benefit from the operation of the lunch counter, i.e. more patrons to the tavern. We note that this example does not require that there be a lease of the personal property. The third example shows where the third party has supported the business of the delinquent taxpayer in some manner and supplied the stock of goods to the delinquent taxpayer. That is, the third party has done more than sold or consigned merchandise to the business.

These examples show that a finding of beneficial interest requires that the third party have a direct or indirect interest in the success of the business that results in the potential for gain to the third party. There is no black letter law that defines "beneficial interest" in this context; rather, it is something that the facts and circumstances will indicate.

In the instant case the taxpayer potentially receives benefits from the success of the lessees' business. Based on information provided by the taxpayer, the lessees sold on average approximately . . . gallons of the taxpayer's gasoline each month. Further, the taxpayer received a percentage of the gross receipts generated by the lessees. The terms of the lease show that the lessees leased the gasoline dispensing facilities, however the taxpayer disputes the express terms of its agreement. For the purposes of this determination, we interpret the lease as the taxpayer suggests⁴. The gross receipts were affected by the

⁴Based purely on the terms of the written lease, the situation in this case is identical to those in the filling station example in Rule 217. If we were to inquire no further the result would be determination of beneficial interest liability. However, the taxpayer explains that the gasoline dispensing equipment was, through clerical error, not marked with an asterisk which would have indicated that it was excluded from the lease. The taxpayer provided copies of schedules from four other leases which show the asterisks next to the gasoline dispensing equipment. These schedules show that there may have been a mistake in the drafting of the lease. Therefore, we will treat the lease as if the asterisks had been placed in the locations indicated by the other schedules. See Berg v. Hudesman, 115 Wn.2d 657 (1990).

availability of gasoline at what appeared to be one business operation. The taxpayer's business success was dependent on the success of the lessees and others similarly situated. The taxpayer was more than a mere creditor of the lessees. The fact that the taxpayer may have lost money in this specific transaction is not determinative, it is the potential for gain that is important.

The taxpayer argues that its beneficial interest, if any, in the lessees' business is limited to the percentage lease payments. Further, the taxpayer points out that percentage leases are commonplace in commercial leasing. The taxpayer states in its petition: "It would be hard to fathom that the Department can pursue as beneficially interested third parties any and all commercial landlords strictly on the basis of a percentage lease." We agree that if the only indication of beneficial interest was a percentage lease there would be insufficient evidence to establish a beneficial interest for the tax lien purposes. However, the taxpayer had more than a pure commercial lease. There was the lease and the mandatory commission agreement. The commission agreement required the lessees to keep the dispensing area clean and remove snow, use their best efforts to sell the taxpayer's gasoline, and not to close the facilities for more than 48 hours. The lessees were responsible for the taxpayer's gasoline that was stolen or otherwise unaccounted for. The lessees were required to have a liquor license, pay property taxes (both real and personal), and provide proof of payment to the taxpayer of all taxes including business and occupation and retail sales.

The only difference between the relationships in this case and the filling station example in Rule 217 would be the existence of a lease of the gasoline dispensing equipment. However, as the second example in Rule 217 shows the existence of a lease is not necessary to show that the tax lien attaches to the personal property used in the business and owned by a beneficially interested third party. In that example, the use by a concessionaire of any equipment in the operation of the concessionaire's business would make that equipment subject to the tax lien. Therefore, we hold that the taxpayer had a beneficial interest in the business of the lessees.

Thus, the tax lien created by the filing of the tax warrants against the lessees attached to the personal property owned by the taxpayer and used in the convenience store and/or gasoline facilities.

2. The taxpayer's second argument is:

Either the tax lien did not apply to the lessees' personal property or the taxpayer's interest in it had vested prior to the Department's and thus had seniority.

The taxpayer took possession [in July 1990] of the personal property of the lessees which was used in the convenience store after the filing of the first tax warrant [of June 1990]. RCW 82.32.210 states that "no sale or transfer of the personal property in any way affects the lien." Thus, the tax lien attached to that personal property prior to the taxpayer foreclosing on its security interest. Therefore, the lien applies to all property (up to the amount necessary to satisfy the warrant) which was acquired by the taxpayer when they took over the convenience store.

[4] The taxpayer claimed to have foreclosed on its security interest the day prior to the filing of the first tax warrant. Thus, the taxpayer relies on the provisions of RCW 82.32.210 and WAC 458-20-217 which state:

However, the lien is not superior to bona fide interests of third persons which had vested prior to the filing of the warrant when such third persons do not have a beneficial interest, direct or indirect, in the operation of the business, other than securing the payment of a debt or the receiving of a regular rental on equipment

(Emphasis added.)

As was discussed above we have held that the taxpayer did indeed have a beneficial interest in the business of the lessees. Therefore, this exception to lien attachment does not apply to the taxpayer, because the property was used in the business and the taxpayer was beneficially interested in the business.

3. The taxpayer's final argument is:

The application of the beneficial interest provision to the taxpayer is unconstitutional because it is vague and the taxpayer had no knowledge that the lessees had failed to pay their state taxes.

The Department of Revenue, as an administrative agency, must presume the constitutionality of the laws it administers. The Department will not and may not rule upon such assertions of unconstitutionality. The Washington State Supreme Court has

directly expressed this position in Bare v. Gorton, 84 Wn.2d 380, 383 (1975) as follows:

An administrative body does not have the authority to determine the constitutionality of the law it administers; only the courts have that power.

Accordingly, we must decline to rule on the constitutionality of Washington's beneficial interest statute. We note however that the statute in question here has been part of the tax laws of Washington for over 40 years and it has not been successfully challenged in court.

For the sake of clarity, it is noted that the taxpayer's principal claim is that it could not obtain information from the Department on the payment status of its lessees, but may be required to pay the taxes that the lessees did not pay. RCW 82.32.330 states that the Department is prohibited from disclosing

any facts or information contained in any return filed by any taxpayer or disclosed in any investigation or examination of the taxpayer's books and records made in connection with the administration hereof. The foregoing, however, shall not be construed to prohibit the department of revenue or a member or employee thereof from:

(2) giving such facts and information to the taxpayer or his duly authorized agent.

[5] This prohibition is for the benefit of the taxpaying public and without a statutory exception is mandatory on the Department and its employees. However, as discussed at the hearing, the taxpayer could obtain consent from its lessees to receive information in the Department's records. The taxpayer acknowledged that it is now aware of this and is requiring such consent from them. Further, we note that the lease between the taxpayer and the lessees states that the lessees shall pay "all state sales taxes, business and occupation and other gross receipts taxes." Paragraph 14(b). Also, Paragraph 14(c) states:

When requested by lessor, lessee shall provide lessor with evidence satisfactory to the lessor that all taxes and other payments for which lessee is responsible, have been paid.

Clearly, these lease terms provided the taxpayer with the means to ascertain whether the taxes had been paid.

DECISION AND DISPOSITION:

The taxpayer's petition is denied. The finding that the taxpayer had a beneficial interest in the business of the lessees is sustained. The file is returned to the Compliance Division for collection action consistent with Chapter 82.32 RCW.

DATED this 7th day of January, 1992.