Cite as Det. No. 92-297, 12 WTD 461 (1992).

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

In the Matter of the Petition For Correction of Assessment of	)	D E T E R M I N A T I O N
	)	No. 92-297
. . .	)	Registration No. . . .
	)	. . ./Audit No. . . .

[1] RCW 82.04.280(4) -- WAC 458-20-182 -- COLD STORAGE WAREHOUSES -- DISTINGUISHED FROM RENTALS. Whether the legal relationship between two parties as to an interest in real property is landlord-tenant or licensor-licensee will be determined by reference to the definitions of those terms in the statute and in the rule, and by the weight of the evidence.

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: . . .

NATURE OF ACTION:

A corporation protests the assessment of B & O tax on its gross receipts under the cold storage warehouse classification. The taxpayer contends the gross receipts are from the rental of real estate and are exempt from the B & O tax.

FACTS AND ISSUES:

Gray, A.L.J. -- The taxpayer is a general partnership that was formed in 1980. The Department audited the taxpayer for the period January 1, 1987 through June 30, 1991, and assessed the taxpayer for B & O tax under the warehousing classification on its gross receipts. The tax rate and classification for cold storage warehouses are found in RCW 82.04.280 and WAC 458-20-182. The taxpayer protests the assessment and argues that cold storage income is exempt from the B & O tax based upon WAC 458-20-118, sale or rental of real estate, license to use real estate.

The taxpayer owns a cold storage warehouse and rents [it] to one tenant . . . . The taxpayer has no employees. [Taxpayer] is a corporation that packs its own fruit as well as the fruit of other growers. [Tenant's] employees operate the cold storage warehouse. [Tenant] is in the fruit storage business; it bills its growers for storage fees and pays B & O tax to the Department at the cold storage warehouse rate. The bulk of [tenant's] business is storing other grower's fruits.

The taxpayer disputes the Department's reasons for assessing tax. The taxpayer argues that costs calculated on the basis of number of bins is the only reasonable way to value what the storage is worth. The taxpayer also represents that calculating storage costs on the basis of number of bins is an industry practice in [the area]. According to the taxpayer, [the tenant] is free to move fruit in and out of the warehouse at its discretion. [The tenant's] employees open and close the warehouse and operate the warehouse. The taxpayer pays the utility costs and its property taxes, but [the tenant's] employees maintain and clean the premises and control access to the warehouse.

The taxpayer explains that the reason there is no lease is because of the identities of the partners in the taxpayer and of the owners in [the tenant]. They apparently relied upon legal advice that the lease was not required to be in writing. The parties are essentially identical. The "certain designated area" that the taxpayer says it leases to [the tenant] is the entire warehouse.

The taxpayer argues that the basis for establishing the annual rent was $ . . . per bin times 12,000 bins, calculated as a flat amount. The taxpayer explained the discrepancy between its explanation and the auditors' conclusion that the amounts paid varied by saying that the taxpayer was on cash accounting basis while [the tenant] was on the accrual accounting basis. Although [the tenant's] records would show a payment of $ . . . to the taxpayer because of its accrual accounting basis, [the tenant] actually paid the amounts over a period of time, and if the payments were made in the taxpayer's subsequent fiscal year, the annual amounts would appear to vary from year to year.

The taxpayer argues that WAC 458-20-118 does not require a written rental agreement, and says "[w]e are aware of no legal requirement that says a lease of real estate must be in writing to be enforceable." The taxpayer argues that the requirement of a written rental agreement exceeds the Department's rule making authority.

The issue is whether the taxpayer leased or rented an interest in real property to [the tenant], so that the rental income is exempt from the B & O tax pursuant to RCW 82.04.390, or whether

the taxpayer was in the cold storage warehouse business as defined in RCW 82.04.280?

DISCUSSION:

RCW 82.04.280 says, in pertinent part:

> Upon every person engaging within this state in the business of: . . . (4) operating a cold storage warehouse or storage warehouse, but not including the rental of cold storage lockers; . . . as to such persons, the amount of tax on such business shall be equal to the gross income of the business multiplied by the rate of forty-four one hundredths of one percent.
>
> As used in this section, "cold storage warehouse" means a storage warehouse used to store fresh and/or frozen perishable fruits or vegetables, meat, seafood, dairy products, or fowl, or any combination thereof, at a desired temperature to maintain the quality of the product for orderly marketing.

WAC 458-20-182(1)(c) repeats the statutory definition and adds that "[t]his term does not include freezer space or frozen food lockers." The rule correctly informs the reader that "[p]ersons engaged in operating any 'storage warehouse' or 'cold storage warehouse,' as defined herein, are subject to tax under the warehousing classification, measured by the gross income of the business. (See RCW 82.04.280.)"

RCW 82.04.390 says:

> This chapter shall not apply to gross proceeds derived from the sale of real estate. This however, shall not be construed to allow a deduction of amounts received as commissions from the sale of real estate, nor as fees, handling charges, discounts, interest or similar financial charges resulting from, or relating to, real estate transactions.

WAC 458-20-118 is the Department's administrative rule regarding income from leases and rentals of real property, and from licenses to use real property. Rule 118 defines a lease or rental of real property:

> (2) A lease or rental of real property conveys an estate or interest in a certain designated area of real property with an exclusive right in the lessee of continuous possession against the world, including the owner, and grants to the lessee the absolute right of control and occupancy during the term of the lease or

> rental agreement. An agreement will not be construed as a lease of real estate unless a relationship of "landlord and tenant" is created thereby.

Rule 118 also defines a "license:"

> (3) A license grants merely a right to use the real property of another but does not confer exclusive control or dominion over the same. Usually, where the grant conveys only a license to use, the owner controls such things as lighting, heating, cleaning, repairing, and opening and closing the premises.

[1] We believe that the taxpayer rented or leased an interest in real property to [the tenant] during the audit period. The subject of the lease was a "certain designated area"; specifically, the entire cold storage warehouse. [Tenant's] employees operated the warehouse. The taxpayer had no employees at all. There is no contention by the Department that the partners themselves operated the warehouse. It stands to reason that the taxpayer as a property owner paid its property taxes; since the county's lien for unpaid taxes runs against the property, any property owner would have an interest in paying the taxes itself and not relying upon a tenant to make the payment (although the rental payment no doubt is calculated to include an amount to cover the property taxes). It is true that the taxpayer paid its own utility bills, but that appears to be the only element that would point toward a relationship of licensor-licensee between the taxpayer and [the tenant]. Otherwise, [the tenant] appeared to have exercised control over the warehouse. Its employees could enter and leave the building at any time without approval from the taxpayer.

The method of calculating the rental payment does not convert the arrangement into a license to use real property. Although the method of calculating cost on the basis of number of bins brought into the warehouse in a year's time does not appear to be inconsistent with how a person in the cold storage warehouse business might charge its customers, its use does not mean that the arrangement is not a lease or rental of real property. Rule 118's definitions of lease or rental of real property and of a license to use real property do not discuss method of calculation of payment as a factor in determining the legal relationship between parties.

The taxpayer does not have a written lease with [the tenant]. Although the taxpayer could have avoided this problem with a

written lease, it does not appear to be necessary for state tax purposes.[1]

DECISION AND DISPOSITION:

The petition is granted.

DATED this 28th day of October, 1992.

[1]The taxpayer is not quite correct when it argues that "[there is] no legal requirement that says a lease of real estate must be in writing to be enforceable." The taxpayer writes in terms of "annual rent," implying that the lease is from year to year. RCW 59.04.010 says that "[t]enancies from year to year are hereby abolished except when the same are created by express written contract." See, Stevenson v. Parker, 25 Wn. App. 639, 608 P.2d 1263 (1980). More generally, RCW 64.04.010 requires that: "[e]very conveyance of real estate, or any interest therein, . . . shall be by deed: . . . ." RCW 64.04.020 requires that every deed be in writing.