Cite as Det. No. 94-108, 15 WTD 10 (1995).

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

In the Matter of the Petition for Tax Ruling of	)	D E T E R M I N A T I O N
	)	No. 94-108
. . .	)	Registration No. . . .
	)	FY. . ./Audit No. . . .

RCW 82.04.050(4): DEFINITION OF RETAIL SALE -- APPLICATION TO EXISTING CONTRACTS. Where a taxpayer enters into a fixed price contract which requires it to rent equipment with an operator prior to the passage of legislation including the rental within the definition of a retail sale, the application of the retail sales tax to the rental is not an unconstitutional impairment of contract.

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.

NATURE OF ACTION:

The taxpayer requests an interpretation clarifying whether the inclusion of the rental of equipment with an operator to the definition of a retail sale applies to a fixed price contract entered into prior to the change and partially performed afterwards.[1]

FACTS:

Coffman, A.L.J. -- The taxpayer is a demolition subcontractor. The taxpayer entered into a fixed price subcontract with a contractor (Prime Contractor) to perform certain demolition work

[1]Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

on a major highway construction project. The subcontract was entered into on April 8, 1993.[2]

The taxpayer states it considered the estimated cost of subcontracting for the provision of heavy equipment with operators when making its bid. However, the bid did not state this fact. The taxpayer assumed that there would be no retail sales tax on its subcontract. The taxpayer later contracted with a subcontractor (Subcontractor) to provide certain equipment and the operators. No written contract existed between the taxpayer and Subcontractor.
On May 6, 1993, after the taxpayer entered into its agreement with Prime Contractor, the definition of a retail sale was expanded, by our legislature, to include the "rental of equipment with operator".[3] The taxpayer claims, at the time of executing its contract with Prime Contractor, it had no ability to foresee the change in the definition of a retail sale to include the rental of equipment with an operator.

The billings from Subcontractor for periods prior to July 1, 1993 did not include retail sales tax as did the original billings for July and early August 1993. However, Subcontractor later billed the taxpayer for retail sales tax for all services provided after June 30, 1993.

ISSUE:

Does the expanded definition of a retail sale apply to a contract entered into prior to passage of the 1993 Act, but not fully performed until after the effective date?

DISCUSSION:

The 1993 Act changed the definition of a retail sale by adding "the rental of equipment with an operator." The taxpayer states that the agreement with the Subcontractor constitutes a retail sale under this new definition. Further, there is no reason to believe that the treatment of the arrangement as a service prior to July 1, 1993, was erroneous. Essentially, the taxpayer is

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[2] The contract document actually states the date as April 8, 1992. We have confirmed that a typographical error was made in the date on the contract.

[3] Second Engrossed Substitute Senate Bill 5967 (1993 Act) amended many sections in Title 82 RCW including RCW 82.04.050 which defines a retail sale. The effective date of the 1993 Act was July 1, 1993. The bill was originally introduced on March 27, 1993.

arguing that applying the new definition to a contract entered into prior to the passage of the 1993 Act is an impairment of contract. U.S. Const., art. 1, § 10 and the Wash. State Const., art. 1, §.23.

The Department does not have the authority to determine the constitutionality of the statutes it administers. Bare v. Gorton, 84 Wn.2d 380, 383, 526 P.2d 379 (1974). We can, however, address the question of whether the application of the 1993 Act unconstitutionally impairs the taxpayer's contract. RCW 82.08.0254.

1. Historical Perspective.

Generally, the term "impairment of contract" has been interpreted as a lessening of value. It could be said that the change in the law lessened the value of the taxpayer's contract with the Prime Contractor because the taxpayer is now required to pay more to the Subcontractor. However, when the alleged impairment relates to the power to impose taxes, the considerations are more complex.

Three Washington Supreme Court cases are directly applicable to the taxpayer's situation. In City of Tacoma v. State Tax Comm., 177 Wash. 604, 33 P.2d 899 (1934), the court discussed the relationship of new taxes and the prohibition on the impairment of contracts. The court, at 611, stated:

> The power to tax is the basic principle upon which government is founded. Without that right, no government worthy of the name can long exist. The lack of power to tax was one of the main causes of the complete breakdown of the association which the thirteen colonies attempted to establish by virtue of the articles of confederation, and rendered necessary the "more perfect union" which was formed under the constitution. The right to tax underlies and adheres in all of our legislative enactments.

The court, at 615, quoted with approval the decision of the Oregon Supreme stating:

> The supreme court of Oregon, in the case of Portland v. Portland Railway, Light & Power Co., 80 Ore. 271, 156 Pac. 1058, used the following language:
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> "The defendant is not denied the equal protection of the law merely because it has made contracts to furnish electricity at prescribed rates and the tax will diminish the profits of these contracts. Section 1 of the Fourteenth Amendment to the federal Constitution is not violated. Contracts must always be entered into with full knowledge that the government may at any time draw upon its extensive

> powers of taxation; and when the company made contracts to furnish light it did so subject to the right of the municipality to exercise its taxing power in all its fullness; 8 Cyc. 997.
>
> "Nor are the obligations of contracts impaired, and Article I of Section 10 of the national Constitution is not violated, by the collection of taxes which are imposed by a law passed subsequent to the making of a contract. The ordinance does not strike at the terms of the contracts; the agreements are preserved, and are enforceable now the same as before by both parties; the obligation of the contracts still binds to the same extent as before the passage of the ordinance, and there is no impairment of any obligations."

Second, the decision in H&B Communications Corp. v. Richland, 79 Wn.2d 312, 484 P.2d 1141 (1971) is of interest. In 1953 the City of Richland granted a franchise to H&B's predecessor to provide a community antenna television system (cable television). In 1960, the City of Richland imposed a business and occupation on the operation of cable television services. H&B made several constitutional arguments against the imposition of the tax including that the tax impaired its franchise agreement. The franchise agreement provided that H&B would "pay any and all taxes imposed by the federal government, the State or any political subdivision thereof." The State Supreme Court summarily dismissed the impairment of contract argument with the statement: "There is no unconstitutional impairment of contract by levying of the respondent's business and occupation tax." at 317.

Finally, in Aetna Life Ins. Co. v. Washington Life and Disability Ins. Guaranty Ass'n, 83 Wn.2d 523, 520 P.2d 162 (1974), the court was again asked to address the application of the constitutional prohibition on impairing existing contracts. Here, the state passed a law in 1971, that required all insurance companies licensed to sell life and disability insurance in this state to be members of the guaranty association. The court, at 525, stated:

> The purpose of the Guaranty Association, in part, is to accumulate funds arising from assessments upon all insurers authorized to transact life or disability insurance business in the state of Washington. These are used to assure the performance of contractual insurance obligations of insurers becoming insolvent to residents of this state.

An insurance company became insolvent less than six months after the effective date of the new statute. The Insurance Commissioner was named the statutory receiver and issued an assessment in 1972, to cover the insurance contracts of the

insolvent insurer. The policies assessed included policies issued in 1970, prior to the effective date of the new statute. Even though the Court found that the assessments were not taxes, it found that the assessments did not violate the prohibition on impairment of contracts.

2. Application to Taxpayer.

The taxpayer's contract with the Prime Contractor included a provision on taxes. It states: "Unless specifically provided otherwise, all prices include all Federal, state and local sales or other taxes, and the costs of all licenses and permits." This language parallels the language quoted in H&B Communications Corp. v. Richland, supra.

[1] The fact that the taxpayer had entered into a contract prior to the change in the tax law does not protect the taxpayer from the tax. The contracts entered into by the taxpayer have not been changed or altered in any respect. Rather, the tax due on the subcontract has been altered. The taxpayer retained the right to compensation from the Prime Contractor and the right to have the Subcontractor provide equipment to perform the demolition project.

3. Equitable Argument.

Finally, the taxpayer argues that it had no knowledge of the proposed change in the tax laws and no means by which it could have become aware.[4] However, we note that the in Aetna Life Ins. Co., supra, the insurance companies had no advance knowledge nor did the cable company in H&B Communications, supra.

DECISION AND DISPOSITION:

The taxpayer's petition is denied. The taxpayer is required to pay retail sales on its rental of equipment with an operator after July 1, 1993. It is the period of use of the equipment that determines the taxation of the use.

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.

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[4] Although not determinative to our decision, we note that the original bill introduced in the legislature prior to entering into the contract with the Prime Contractor included language which would have subjected construction equipment rentals with operator to the retail sales tax.

DATED this 10th day of June, 1994.