

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>
Notice of Successorship Liability of	)	
	)	
	)	No. 97-121
	)	
	)	As successor to:
	)	...
...	)	Registration No. ...
	)	Tax Warrant Number: ...
	)	

- [1] RULE 216; RCW 82.04.180 AND 82.32.140: -- SUCCESSORSHIP -- ELEMENTS. The five elements of a statutorily defined successor are: (1) The successor must acquire from a taxpayer; (2) who is selling out, exchanging, or disposing of a business; (3) in bulk and not in the ordinary course of business; (4) by sale or conveyance; (5) a major part of the materials, supplies, merchandise, inventory, fixtures, or equipment of the delinquent taxpayer.
- [2] RULE 216; RCW 82.04.180, 82.32.140, AND 60.72.010: -- SUCCESSORSHIP - - LANDLORD'S LIEN. The holder of landlord's lien has the same rights as a secured creditor and is entitled to same defenses against an assessment of successorship liability.
- [3] RULE 216; RCW 82.04.180 AND 82.32.140: -- SUCCESSORSHIP -- ENFORCEMENT OF A LIEN -- PEACEFUL REPOSSESSION. A secured party's acquisition of property by "regular legal proceedings to enforce a lien" does not subject it to successorship liability. Peaceful repossession qualifies as a regular legal proceeding. Acceptance of a bill of sale in satisfaction of a lien is a peaceful repossession.
- [4] MISCELLANEOUS -- AUTHORITY TO INVALIDATE A PROPERLY ADOPTED RULE. Generally, the Department must follow its own rules.

- [5] MISCELLANEOUS -- AUTHORITY TO REACH CONCLUSIONS CONTRARY TO THE LANGUAGE OF A PROPERLY ADOPTED RULE. When a rule substantially quotes a statute that has been amended and the rule is not amended to reflect the new statutory language, the Department must interpret the rule as if the new statutory language were included therein and ignore those portions of the rule that are inconsistent with the new statutory language. **Partially Overruling Det. No. 88-313, 6 WTD 285 (1988) to the extent that it reached a conclusion contrary to the statutory language.**

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:

A lessor protests the assessment of successorship liability claiming that the exercise of summary foreclosure of a landlord's lien pursuant to RCW 60.72.010 and 60.10.030 is not a purchase of assets.<sup>1</sup>

#### FACTS:

Coffman, A.L.J. -- The taxpayer is a partner in a partnership that owns a strip mall. One of the tenants of the strip mall failed to pay its rent and was evicted by the partnership. In lieu of formal foreclosure of the landlord's lien, the tenant executed a bill of sale in favor of the landlord for the equipment and supplies located on the premises. The bill of sale is dated August 28, 1996. The partnership immediately leased the premises to a similar business and allowed the new lessee to use the equipment and supplies.

The taxpayer claims that in addition to the bill of sale the partnership utilized the summary foreclosure procedure authorized by RCW 60.10.030. The partnership sent a notice of sale to the tenant on September 17, 1996, stating that public sale would be held at the leased premises on October 1, 1996.

The Department of Revenue's (Department) Compliance Division issued a tax warrant against the tenant on October 10, 1996, and filed it with the Superior Court on October 24, 1996. The same day, the Department issued an Assessment of Successorship Liability to the taxpayer for the taxes owed by the tenant.

#### ISSUES:

Is the landlord's acquisition of the tangible personal property of the delinquent tenant by means of the summary foreclosure of a landlord's lien a sale or other conveyance so that the landlord becomes a successor as defined in RCW 82.04.180?

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<sup>1</sup> Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

## DISCUSSION:

If a taxpayer quits, sells out, or otherwise ceases to operate a business, the taxpayer must pay its excise taxes within 10 days of the closure of the business. If the taxes are not paid within those 10 days, any successor to the taxpayer is personally liable for the delinquent taxes. To the extent that the successor pays the delinquent taxes, the payments are treated as payments to the delinquent taxpayer. RCW 82.32.180.

Successor is defined in RCW 82.04.180:

"Successor" means any person to whom a taxpayer quitting, selling out, exchanging, or disposing of a business sells or otherwise conveys, directly or indirectly, in bulk and not in the ordinary course of the taxpayer's business, a major part of the materials, supplies, merchandise, inventory, fixtures, or equipment of the taxpayer. Any person obligated to fulfill the terms of a contract shall be deemed a successor to any contractor defaulting in the performance of any contract as to which such person is a surety or guarantor.

[1] This definition has five elements: (1) The successor must acquire from a taxpayer; (2) who is selling out, exchanging, or disposing of a business; (3) in bulk and not in the ordinary course of business; (4) by sale or conveyance; (5) a major part of the materials, supplies, merchandise, inventory, fixtures, or equipment of the delinquent taxpayer.

All five of these elements must be present before an assessment of successorship liability will be sustained. The taxpayer agrees that the business equipment was acquired from the tenant, the tenant was going out of business, the acquisition was in bulk and not in the ordinary course of business, and that the property acquired constituted a major part of the supplies, inventory, and equipment used by the tenant. The only element in dispute is whether the acquisition was by sale or conveyance.

[2] In Palmer v. Department of Rev., 82 Wn.App. 367, 917 P.2d 1120 (1996), the Court of Appeals discussed the terms "sell" and "convey". The court stated at 374:

Palmer's exercise of his rights as a secured creditor to possession of his collateral did not constitute either a sale or conveyance by definition. Because a sale or conveyance did not occur, Palmer was not a successor pursuant to RCW 82.04.180 and is not subject to the assessed tax liability.

The landlord's lien created by RCW 60.72.010 is:

paramount to, and [has] preference over, all other liens except liens for taxes, general and special liens of labor, and liens of mortgages duly recorded prior to the tenancy.

In Paris American Corp. v. McCausland, 52 Wn.App. 434, 759 P.2d 1210 (1988), the court held that a security interest created after the commencement of the tenancy is inferior to the landlord's lien. Thus, we find that the holder of a landlord's lien is a secured party and has at least the same rights as a purchase money secured creditor like Palmer.<sup>2</sup>

There are differences between the facts in Palmer and here. Palmer held the Manufacturer's Statements of Origin, which were the only documents of title for the boats at issue in the case. In the present case, the property did not have certificates of title. Because of the lack of title documents the partnership took a bill of sale. The bill of sale states that it is in "satisfaction of the lien for rent created by RCW 60.72.010". This is the same as a deed in lieu of foreclosure or peaceful repossession.

[3] We ruled in Det. No. 88-313, 6 WTD 285 (1988) that acquisition by peaceful repossession does not result in the secured party becoming a successor. Here, we find that the partnership's acceptance of the bill of sale was the same as a peaceful repossession and, therefore, that the taxpayer is not a successor.

We note that Rule 216 states:

The work (sic) "successor" includes all persons who acquire the taxpayer's equipment or merchandise in bulk, whether they operate the business or not, unless the property is acquired through insolvency proceedings or regular legal proceedings to enforce a lien, security interest, judgment, or repossession under a security agreement. The following factual situations illustrate the application of the foregoing: ...

5) Taxpayer leaves business, including fixtures and stock of goods, which his landlord holds for unpaid rent. The landlord will be a successor unless he proceeds to foreclose his landlord's lien by posting notice and holding a sale by the sheriff.

There is no statutory requirement that a landlord foreclose its lien for rent by a sheriff's sale. A sheriff's sale is one of several methods that can be used. The landlord may also use the summary foreclosure process authorized by RCW 60.10.030 to sell the property by public or private sale. The landlord can bid on the property at the sale.<sup>3</sup> RCW 60.10.030(3). The taxpayer used a regular proceeding to dispose of the property. Because peaceful repossession does not result in successorship liability, we also find that successorship liability cannot be imposed merely because the partnership did not incur the expense of a sheriff's to foreclose its landlord lien.

We incorrectly ruled that the secured party in Det No. 88-313 was a successor to a portion of the business because it continued to operate that portion. This part of Det No. 88-313 relied on language contained in WAC 458-20-216 (Rule 216) that states:

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<sup>2</sup> The landlord is a secured party only for the period when its landlord lien is valid.

<sup>3</sup> After taking the bill of sale, the partnership followed the summary foreclosure procedure.

The word "successor" means any person who shall, through direct or mesne conveyance, purchase or succeed to the business, or portion thereof, or the whole or any part of the stock of goods, wares, merchandise or fixtures or any interest therein of a taxpayer quitting, selling out, exchanging or otherwise disposing of his business.

(Emphasis added.) This definition substantially quotes the former version of RCW 82.04.180 which stated:

"Successor" means any person who, through direct or mesne conveyance, purchases or succeeds to the business, or portion thereof, or the whole or any part of the stock of goods, wares, merchandise, or fixtures or any interest therein of a taxpayer quitting, selling out, exchanging, or otherwise disposing of his business.

[4,5] (Emphasis added.) The statutory definition of a successor was substantially amended in 1985 and removed the emphasized language. The Department has not amended Rule 216 to reflect the statutory change. Generally, the Department must follow a properly adopted administrative rule in an informal administrative appeal. Det. No. 96-135, 16 WTD 112 (1996). However, when a rule substantially mirrors the language of the statute and the statute is amended, the rule is deemed to have been amended consistent with the new statutory language. Thus, until the rule is amended, the Department must interpret the rule as if the new statutory language were included therein and ignore those portions of the rule that are inconsistent with the new language of the statute. For the reasons stated above, Det. No. 88-313, 6 WTD 285 (1988) is overruled to the extent that it found the secured party to be a successor.

#### DECISION AND DISPOSITION:

The taxpayer's petition is granted. The assessment of successorship liability is hereby canceled.

Dated this 6th day of June, 1997.