Cite as Det. No. 98-043, 17 WTD 179 (1998)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Refund of	)	D E T E R M I N A T I O N
	)	
	)	No. 98-043
	)	
. . .	)	Registration No. . . .
	)	FY. . . /Audit No. . . .
	)	FY. . ./Audit No. . . .

[1] RULE 211; RCW 82.04.190: RETAIL SALES TAX -- CONSUMER, FINANCING LEASE, AND TRUE LEASE. Where a contractor enters into an agreement with the owner of real property and that agreement is later assigned to a leasing company, the contractor may not accept a resale certificate from the leasing company. This is because either (1) the agreement between the leasing and the owner is a financing lease and the owner is still the consumer of the improvements or (2) the agreement is a true lease and the leasing company is the consumer.

[2] RULE 102; RCW 82.04.470; RETAIL SALES TAX. -- RESALE CERTIFICATES, REASONABLE TIME. Where a contractor treated a transaction as a retail sale, the receipt of a resale certificate more than three years after the completion of the project will not be accepted by the Department because (1) a delay of over three years is not a reasonable time, (2) the purpose of allowing a taxpayer to obtain a resale certificate after-the-fact is to prevent undue hardship which does not exist under the facts here, (3) if the transaction were treated as a wholesale transaction, the taxpayer's tax liability would increase, and (4) the transaction was not a sale for resale.

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.

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NATURE OF ACTION:

A contractor requests that a transaction it previously treated as retailing be reclassified as wholesale and requests specific written instructions concerning the acceptance of resale certificates from leasing companies.[1]

FACTS:

Coffman, A.L.J. -- The taxpayer installs ventilation systems for agricultural storage buildings.[2] The Audit Division (Audit) of the Department of Revenue (Department) reviewed the taxpayer's records for the period January 1, 1991 through June 30, 1995. As a result of that review, the Department issued the above-referenced tax assessment and post assessment adjustment (PAA). The Audit Division's initial review of the taxpayer's records showed that the taxpayer had failed to separately state the retail sales tax. Therefore, the Audit Division included in the measure of the retail sales tax, the entire amount paid to the taxpayer.[3] After the original tax assessment was issued, the taxpayer provided the Audit Division with additional documentation showing that retail sales tax was, in fact, separately stated. In response to these documents, the Audit Division issued the PAA reducing the measure of the retail sales tax and retailing business and occupation (B&O) tax.

This appeal involves only one contract and the taxpayer's request for future reporting instructions. In 1993, the taxpayer entered into a contract with . . . an onion grower (grower), for the installation of a ventilation control system for his onion storage facility. The contract required the taxpayer to install various equipment in the building. The contract stated the purchase price as "$. . . w/tax".[4] Prior to commencement of the construction, the contract was assigned by the grower to a leasing company. We do not have a copy of the agreement between the leasing company and the grower, therefore it is unclear whether the agreement was a financing lease or a true lease. For the reasons stated below, the characterization of the agreement is irrelevant to the decision in this appeal.

The taxpayer reported the gross income (less the retail sales tax) from this contract as a retailing activity and remitted the retail sales tax to the Department. The taxpayer argues that the assignment of the contract to the leasing company converted the sale from retailing to wholesaling. The only documentation supporting the wholesaling classification is a 1996 resale certificate issued to the taxpayer by the leasing company. The taxpayer has not refunded the retail sales tax to either the grower or the leasing company.

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[1] Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.
[2] The taxpayer also sprays sprout inhibiting chemicals on agricultural products. The tax treatment of this activity is not in dispute and therefore will not be addressed further.
[3] See RCW 82.08.050.
[4] As the result of a change order, the contract price was reduced to $. The leasing company paid the taxpayer the full $.

Audit takes the position that resale certificates may not be taken for the ventilation control system because "a resale certificate is only valid when tangible personal property is purchased." Audit further states that the temperature control system is a fixture and therefore, the resale certificate was invalid.

The taxpayer paid the tax assessment in full and now requests a refund for the retail sales tax and retailing business and occupation (B&O) tax relating to the ventilation control system with an offset for the wholesaling B&O tax it believes is properly due.

ISSUES:

1. Under what circumstances may the taxpayer accept a resale certificate from a leasing company?

2. Did the taxpayer, in good faith, accept the resale certificate for the temperature control system?

DISCUSSION:

1. Instructions:

The installation, repair, improvement, or construction of real property for consumers is a retail sale. RCW 82.04.050(1)(b). The grower is owner of the building where the taxpayer installed the ventilation system. As such, the grower is the consumer. RCW 82.04.190(4). Therefore, the sale of the ventilation system to the grower was a retail sale. The complicating factor in this appeal is the involvement of the leasing company.

The taxpayer states that the leasing company enters into two types of leases. Specifically, the taxpayer claims that some of the leases are actually financing leases. See WAC 458-20-211 (Rule 211), subparagraph (2)(g). The remaining leases are true leases. See Rule 211(2)(f). The taxpayer claims that it usually does not know at the time a contract is assigned to the leasing company whether the lease is a financing lease or a true lease. The taxpayer has requested instructions concerning its acceptance of resale certificates from the leasing company.

A. Financing Lease:

A financing lease is defined in Rule 211(2)(g) as:

> The term "financing lease" (often referred to as a "capital lease") typically involves the lease of property for a stated period of time with ownership transferring to the "lessee" at the conclusion of the lease for a nominal or minimal payment. The transaction is structured as a lease, but retains some elements of an installment sale. Financing leases will generally be taxed as if they are installment sales. . . .

Rule 211 addresses the relationship between the leasing company and the grower. It does not address the relationship between the taxpayer and either the lessor or the grower. If the arrangement between the grower and the leasing company is a financing lease, then the leasing company is acting essentially as a lender. Under these circumstances, the purchaser is still the grower. The leasing company's relationship to the taxpayer is merely as the agent for the grower. Because the grower is the consumer, the installation and construction services provided by the taxpayer constitute retail sales.

Thus, if the arrangement between the grower and the leasing company is a financing lease, then the leasing company may not give a resale certificate.

B. True Lease:

A true lease is defined in Rule 211(2)(f) as:

> The term "true lease" (often referred to as an "operating lease") refers to the act of leasing property to another for consideration with the property under the dominion and control of the lessee for the term of the lease with the intent that the property will revert back to the lessor at the conclusion of the lease.

If the arrangement between the grower and leasing company is a true lease, then the leasing company is the real purchaser of the improvements to the building. The leasing company's ownership of the improvements is a determinative factor. The definition of a consumer includes:

> Any person who is an owner, . . .[of] real property which is being constructed, repaired, decorated, improved, or otherwise altered by a person engaged in business, excluding only (a) municipal corporations or political subdivisions of the state in respect to labor and services rendered to their real property which is used or held for public road purposes, and (b) the United States, instrumentalities thereof, and county and city housing authorities created pursuant to chapter 35.82 RCW in respect to labor and services rendered to their real property. Nothing contained in this or any other subsection of this definition shall be construed to modify any other definition of "consumer";

RCW 82.04.190(4). See also WAC 458-20-170.

Paraphrasing Western Ag v. Department of Rev., 43 Wn. App. 167, 169-70, 716 P.2d 310 (1986): "The pivotal issue is whether [the ventilation system is a] fixture rather than personal property for purposes of assessing sales taxes." If the ventilation system is a fixture, then the leasing company, as the consumer, owes retail sales tax on the charge to install it.

Whether an item of property is a fixture is determined

> upon the application of three general tests, all of which must be satisfied:

> (1) Actual annexation to the realty, or something appurtenant thereto; (2) application to the use or purpose to which that part of the realty with which it is connected is appropriated; and (3) the intention of the party making the annexation to make a permanent accession to the freehold.

Western Ag, at 171.

The ventilation system includes, among other items, mounted fans, special doors, exhaust shutters, sensors, and duct work. The purpose for installing the ventilation system is consistent with the purpose of the building. That is -- the storage of onions. Although some of the equipment that the taxpayer installs may be able to be removed without damaging the building, the clear intent is for the annexation was to be permanent.[5]

We find that the ventilation system is a fixture and therefore real property. Under this scenario, the leasing company could not legally give a resale certificate because it is the consumer.

[1] To summarize, the consumer of improvements to real property owes retail sales tax on them.[6] If the agreement between the grower and the leasing company is a financing lease, then the grower is the purchaser-consumer. Thus, payments from the leasing company were made on behalf of the grower. If the agreement was a true lease, then the leasing company is the purchaser-consumer. Thus, we conclude that the taxpayer may not accept resale certificates from leasing companies when it installs equipment in buildings and on real property.

2. Resale Certificate from Leasing Company.

RCW 82.04.470 discusses the effect of obtaining a resale certificate from the buyer of tangible personal property and services. This statute was amended effective July 1, 1993 and read prior to that date as follows:

> Unless a seller has taken from the purchaser a resale certificate signed by, and bearing the name and address and registration number of the purchaser to the effect that the property or service was purchased for resale . . . the burden of proving that a sale . . . was not a sale at retail shall be upon the person who made it.

The actual installation of the ventilation system was scheduled for August 1993. In August 1993, RCW 82.04.470 read:

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[5] It is possible to lease fixtures separately from the real property of which they are a part. See Courtright Cattle Co. v. Dolson Co., 94 Wn.2d 645, 619 P.2d 344 (1980).

[6] Subject to certain exemptions that are not at issue in this appeal.

> (2) If a seller does not receive a resale certificate at the time of the sale, have a resale certificate on file at the time of the sale, or obtain a resale certificate from the buyer within a reasonable time after the sale, the seller shall remain liable for the tax as provided in RCW 82.08.050, unless the seller can demonstrate facts and circumstances according to rules adopted by the department of revenue that show the sale was properly made without payment of sales tax.

(Emphasis added.) See also WAC 458-20-102.

[2] The taxpayer did not receive the resale certificate from the leasing company until September 1996 while the audit was in process. We find that the resale certificate is invalid for four reasons.

First, the taxpayer did not receive the resale certificate within a reasonable time after the sale. A delay of over three years can not be deemed to be reasonable.

Second, the purpose of allowing a taxpayer to obtain a resale certificate after the fact is to prevent undue hardship on taxpayers who treated a transaction as wholesale but had failed to obtain the resale certificate. The taxpayer treated the transaction as a retail sale for all purposes until the audit was almost complete. Thus, we find no hardship on the taxpayer.

Third, acceptance of the resale certificate actually will increase the tax due from the taxpayer. If the sale of the ventilation system was at wholesale, the taxpayer would be required to refund the collected retail sales tax and then pay a higher B&O tax.[7]

Fourth, as discussed above, the leasing company could not give a resale certificate in this transaction. Audit Division's claims that because the ventilation system is a fixture, the purchaser can not give a resale certificate. This position is not completely correct. There are instances when a resale certificate may be given. If a prime contractor is engaged to build an onion storage facility for the grower and subcontracts the ventilation system to the taxpayer, then the taxpayer could have taken a resale certificate from the prime contractor. See WAC 458-20-170(3)(a).

DECISION AND DISPOSITION:

The taxpayer's petition is denied.

Dated this 27th day of March, 1998.

[7] The B&O tax rate for wholesaling is higher than the rate for retailing.