Cite as 2 WTD 211 (1986)

BEFORE THE INTERPRETATION AND APPEALS SECTION
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. 87-44
. . .	Registration No. . . .
	Real Estate Excise Tax

[1] **REET, RCW 82.45.010 and WAC 458-61-030(11)**: REAL ESTATE EXCISE TAX -- SALE -- CONSIDERATION -- THIRD PARTY BENEFICIARY. Anything of value intended to move directly from the promisee to a third party designated by the promisor as a result of a third party contract is consideration. There is no requirement that consideration move only to the promisor.

[2] **REET AND WAC 458-61-320(3)**: REAL ESTATE EXCISE TAX --EXEMPTIONS --SUBSIDIARY -- CORPORATION AND LIMITED PARTNERSHIP OWNED BY SAME PERSONS. The exemption extended to a transfer between "two or more subsidiary corporations" in WAC 458-61-320(3) will not be extended to a transfer between a corporation and limited partnership, even if ownership of both are identical.

[3] **REET AND WAC 458-61-320(2)**: REAL ESTATE EXCISE TAX --EXEMPTIONS --CORPORATE DISSOLUTION -- PARTIAL LIQUIDATION. The language of WAC 458-61-320(2), which grants exemption to transfers in corporate dissolution, will not be extended to exempt transfers in partial liquidation.

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: September 4, 1986

NATURE OF ACTION:

Real Estate Excise Tax was assessed on the transfer of real property from a corporation to a limited partnership. Partnership units were distributed pro rata to the corporate stockholders of record as of the date of the transfer.

FACTS AND ISSUES:

Burroughs, A.L.J.--The Department of Revenue examined the records of Island, Clallam, Snohomish, Lewis, Whatcom, Jefferson, Kitsap, and Mason Counties regarding the taxpayer's transfer of real property to an existing limited partnership. On its Real Estate Excise Tax Affidavits at the time of the transfers, the taxpayer claimed an exemption from real estate excise tax for "partial dissolution of corporation under WAC 458-61-320(2) with no liabilities assumed." The Property Tax Division, by letter dated April 11, 1986, disallowed the claimed exemption, reasoning that WAC 458-61-320(2) (Rule 320) "refers to an exemption from real estate excise tax on the full or complete dissolution of a corporation, not its partial dissolution." Tax plus delinquent penalties, for a total amount of $667,202.02, were assessed.

Pursuant to a request dated May 21, 1986, the Property Tax Division again considered additional information and arguments submitted by the taxpayer. This petition was rejected by letter dated July 11, 1986. The taxpayer has appealed to this office.

TAXPAYER'S EXCEPTIONS:

The taxpayer has submitted two arguments for our consideration: First, that the tax was wrongfully assessed because the transfer involved the partial liquidation of the taxpayer, and was a transfer without consideration. Second, that the tax was improperly based on values for the property which do not correspond to realistic fair market values.

The taxpayer has described the factual background in its brief submitted at the hearing as follows:

> [The taxpayer] wished to terminate its timber production and land development business in the State of Washington. This was effected in December 1985 by transferring the following assets to [the partnership], a newly formed Delaware limited partnership: (1) certain Timber Development Properties, (3) $1.5 million in cash, and (4) certain Installment Notes. Partnership units of the Partnership were not given to the Corporation in return for these assets. Rather, the partnership units were distributed pro rata to the stockholders of record of the Corporation as of the date of the transfer.[1] Thus, the real properties that were transferred from the Corporation to the partnership were transferred for no consideration. Although the Timber Properties were encumbered by a nonrecourse loan in the amount of $22.5 million, the limited partnership took the Timber Properties "subject to" this nonrecourse loan and did not assume the loan (and in fact no party has any personal liability for the loan). (Bracketed inclusions ours.)

The taxpayer, by extensive briefs and argument, has raised the following points in support of its initial contention that the transfer involved no consideration:

First:

> The transaction between ...[the taxpayer corporation]... and [the limited partnership]... is not taxable because no consideration passed to ...[the taxpayer]... in return for the conveyance of property. The law as developed over the last 30 years has clearly established that a transfer is taxable only when the transferor receives consideration directly from the transferee.
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> . . .
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> The Department of Revenue has thus far held the position that the creation of ...[the limited partnership]... and the distribution of partnership units to ...[the taxpayer's]... shareholders was consideration for the transfer that was "due to"

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[1] Note: Distribution of partnership units was made directly by the limited partnership, an unrelated entity, to the corporate taxpayer's shareholders.

> ...[the taxpayer]... itself. This position misconstrues the facts of the matter and departs from the approach to tax administration that has been mandated and enforced by the courts of the state. The creation of ...[the taxpayer]... was a distinct legal act effected by the ...[taxpayer's]... shareholders. The Corporation did not bargain for the issuance of partnership units. It did not establish the issuance as a condition for the conveyance of the property. Construing the issuance of partnership units as consideration for the Corporation's action is completely unwarranted.
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> . . .
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> ...[The taxpayer]... received no cash for the transferred properties, received no interest in the limited partnership, and received no surrendered or redeemed stock from its own shareholders. ...[The taxpayer]... received nothing whatsoever of value in return for the transfer of the properties. The transfer was therefore not a "sale" and the counties have no authority to impose a tax.
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> (Taxpayer's Memorandum submitted September 3, 1986.) (Bracketed inclusions ours.)

Second:

> The conveyance of real estate in question was merely a transfer, without consideration, from one related entity to another. Since no consideration was given, RCW 82.45 is not applicable. Although there are no Department of Revenue regulations directly on point, this transfer is substantively identical to a transfer between two subsidiary corporations because the shareholders of the Corporation and the partners of the Partnership owned their interests in identical proportions as of the day of the transfer. Consequently, the regulation that states that transfers between two subsidiary corporations are exempt from excise taxation, should be applicable." (Taxpayer's Memorandum dated May 1, 1986.)

Third:

> Partial dissolution of Corporation pursuant to WAC 458-61-320(2).
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> . . .
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> This conveyance is a transfer of real property from a corporation being partially and voluntarily liquidated to all of its shareholders in proportion to their present stock ownership . . ."
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> (Statements in support of claim of exemption on the Real Estate Excise Tax Affidavit dated December 18, 1986.)

Fourth:

> [T]he Department has no power to construe the benefits gained by the third party shareholders as consideration passing to ...[the taxpayer].... The law requires a focus on the transaction between the transferor and the transferee and does not permit a determination of tax based on alternative transactions that the parties might have made. (Taxpayer's Memorandum submitted September 3, 1986.) (Bracketed inclusion ours.)

In support of its contention that the transfer involved no consideration, the taxpayer has cited and discussed the following as authority: Christensen v. Skagit County, 66 Wn.2d 95 (1965); Attorney General Opinion 74-14; WAC 458-61-320(3); Attorney General Opinion 77-6; Estep v. King County, 66 Wn.2d 76 (1965); Weaver v. King County, 73 Wn.2d 183 (1968) (en banc); Ban-Mac, Inc. v. King County, 69 Wn.2d 49 (1966) (per curiam); Doric v. King County, 57 Wn.2d 640 (1961); and Deer Park Pine Industry, Inc. v. Stevens County, 46 Wn.2d 852 (1955).

The taxpayer has further argued that, even if the transfer is found to be taxable, the value which the Department has assigned to the properties (approximately $47.7 million) has no relationship to their true value. For federal tax purposes the lands were valued at $33 million. In addition, the partnership unit value as listed on the Pacific Exchange of roughly $11 per unit is argued to be probative of a lower valuation.

DISCUSSION:

Chapter 82.45 RCW provides for a one percent excise tax upon real estate sales. "Sale" is defined in RCW 82.45.010 as "any conveyance, grant, assignment, quit claim, or transfer of the ownership of or title to real property, including standing timber, or any estate or interest therein for a valuable consideration. . . ." WAC 458-61-030(2) defines "consideration" as "Money or anything of value . . . paid or delivered or contracted to be paid or delivered . . . in return for real property. . . ."

We have considered at great length all of the taxpayer's contentions and authorities. The taxpayer has strenuously argued that, because the corporation itself received nothing of value as a result of the transfer, there was no consideration. We disagree, and hold that real estate at issue was transferred in exchange for valuable consideration.

The court in McDonald v. Murray, 5 Wn.App 68 (1971) summarized the legal principles relating to third-party contracts as follows:

> A third-party beneficiary is one who, though not a party to the contract, will nevertheless receive direct benefits therefrom. In determining whether or not a third-party beneficiary status is created by a contract, the critical question is whether the benefits flow directly from the contract or whether they are merely incidental, indirect or consequential. 17 Am. Jur.2d Contracts, Section 305 (1964). An incidental beneficiary acquires no right to recover damages for nonperformance of the contract. Restatement of Contracts, Section 147 (1932). "[I]t is not sufficient that the performance of the promise may benefit a third person, but that it must have been entered into for his benefit, or at least such benefit must be the direct result of performance and so within the contemplation of the parties." (Footnote omitted.) 17 Am. Jur.2d Contracts, Section 304 (1964). "The question whether a contract is made for the benefit of a third person is one of construction. The intention of the parties in this respect is determined by the terms of the contract as a whole construed in the light of the circumstances under which it was made." Grand Lodge of Scandinavian Fraternity of America v. United States Fid. & Guar. Co., 2 Wn.2d 561, 569, 98 P.2d 971 (1940).

> In regard to the requisite intent, in Vikingstad v. Bagott, 46 Wn.(2d) 494, 282 P. (2d) 824, we recognized the rule stated in 81 A.L.R.1271, 1287, that such "intent" is not a desire or purpose to confer a benefit upon the third person, nor a desire to advance his interests, but an intent that the promisor shall assume a direct obligation to him.

The issue of to whom consideration must move is squarely addressed in 1 Williston on Contracts, Section 113:

> Whether a benefit to the promisor is or is not a sufficient consideration, a detriment to the promisee is. This is equivalent to saying that if the promisee parts with something at the promisor's request, it is immaterial whether the promisor receives anything, and necessarily involves the conclusion that the consideration given by the promisee for a promise need not move to the promisor, but may move to anyone requested by the offer. The commonest illustration of consideration moving to one other than the promisor is the consideration for a guaranty, and a mere reference to this class of cases is sufficient authority. (Footnotes omitted, and emphasis added.)

[1] Thus, anything of value intended to move directly from the promisee to a third party designated by the promisor as a result of a contract is consideration, regardless that it does not move to the promisor.

In this case, the taxpayer corporation (promisor) agreed to transfer its corporate timberlands to an existing limited partnership. As part of the overall plan, the limited partnership (promisee) was to distribute, pro rata, partnership units to the corporation's shareholders of record as of the transfer date. The promisee (the limited partnership) thus parted with something of value which, as a direct and intended result of the contract, flowed to third party beneficiaries, the promisor's shareholders. Such constitutes consideration given in exchange for the conveyance of real estate, and renders the transaction a "sale" for purposes of the real estate excise tax.

Although the taxpayer has strenuously argued that the distribution of partnership units was not bargained-for consideration, we think it unlikely that the taxpayer's shareholders would have maintained this viewpoint had the

partnership failed to distribute the partnership units after receiving the corporate timberlands from the taxpayer. It is even further unlikely that the taxpayer, through its shareholders, would have initially even consented to the transfer of timberlands to the partnership had the transfer of partnership units to the taxpayer's shareholders not been agreed upon.

The taxpayer has further argued that WAC 458-61-320(3), which exempts transfers between two subsidiary corporations from excise taxation, should be applicable, since the shareholders of the Corporation and the partners of the Partnership owned their interests in identical proportions as of the day of the transfer.

[2] The very terms of WAC 458-61-320(3) provide only for transfers between "two or more subsidiary corporations." Not only must the entities be "corporations," they must also be "subsidiaries" of one common corporate parent. The rule merely recognizes that there is no change in value of the corporate parent's net worth when two of its subsidiaries exchange property. In the taxpayer's case, not only are both entities not corporations, they are also not owned by one corporate parent. We decline to extend the rule further than its obvious intent.

As to the taxpayer's original claim on the Tax Affidavit that the transfer was a "[p]artial dissolution of Corporation pursuant to WAC 458-61-320(2)," we must disagree. WAC 458-61-320(2) reads as follows:

> The real estate excise tax applies to all real property transfers between a corporation and its stockholders, officers, corporate affiliates, or other parties, except the following transfers which are not taxable:
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> . . .
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> (2) Corporate dissolution, except in a case where the stockholders assumed or agreed by contract to assume the liabilities of the dissolving corporation. In such event, the real estate excise tax applies to the extent of the liabilities assumed by the stockholder. (Emphasis added.)

Black's Law Dictionary, Revised Fourth Edition (1968), describes corporate dissolution as follows:

> The dissolution of a corporation is the termination of its existence as a body politic. This may take place in several ways; as by act of the legislature, where that is constitutional; by surrender or forfeiture of its charter; by expiration of its charter by lapse of time; by proceedings for winding it up under the law; by loss of all its members or their reduction below the statutory limit. (Emphasis added.)

The taxpayer did not dissolve, and still operates today. Although the taxpayer originally used the term "partial dissolution" on its Tax Affidavit, we are constrained to observe that being "partially dissolved" is as impossible as being "a little bit pregnant." A corporation either does or does not dissolve; it cannot partially dissolve.

[3] The addendum to the tax affidavits and the taxpayer's federal income tax treatment (as disclosed at the hearing) indicate that the transaction was in fact in the nature of a "partial liquidation." There is no provision in the statutes or regulations which exempts a transfer of real property in partial liquidation to all of its shareholders in proportion to their stock ownership. The rule cited by the taxpayer exempts only transfers in corporate dissolution, a circumstance which is not applicable here. Accordingly, the taxpayer's argument on this point must fail.

Because we have determined that there was in fact consideration, we need not further examine the Department's power to "construe the benefits gained by the third party shareholders as consideration passing to [the taxpayer]." (Bracketed inclusion ours.)

The taxpayer lastly contends that the tax was not based on the true value of the properties. We note, however, that the Property Tax Division has not yet had an opportunity to properly examine the taxpayer's arguments as to this issue. Thus, it is appropriate that this case be referred back to that Division for further consideration of the properties' valuation and for the issuance of new assessments, if necessary. If the taxpayer does not agree with the Property Tax Division's determination of valuation, further review by this office would then be appropriate.

DECISION AND DISPOSITION:

The taxpayer's petition for correction of assessment is denied with the following exception: The Property Tax Division will review the taxpayer's contentions regarding the properties' valuation and issue a new assessment, payment of which will be due on the date set forth therein. . . . .

DATED this 10th day of February 1987.