Cite as 8 WTD 439 (1989)

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. 89-541
. . .	)	Registration No. . . .
	)	. . . /Audit No. . . .
	)	. . . /Audit No. . . .

[1] RULE 211: RETAILING B&O TAX -- SALES TAX -- RENTAL OF PERSONAL PROPERTY -- KILN -- ANNEXED TO REAL ESTATE -- INTENT OF PARTIES TO RENTAL AGREEMENT -- CHARACTERIZATION OF KILN AS PERSONAL PROPERTY. Where parties to rental agreement involving a kiln affixed to real estate characterized the kiln as personal property and to remain so even if affixed to the real estate, the parties intended that the kiln be treated as personal property. The rental payments are subject to Retailing B&O tax and sales tax. Lipsett v. King County, 67 Wn.2d 650 (1965) discussed. ACCORD: Det. 88-342, 6 WTD 361 (1988).

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:

Petition protesting the assessment of Retailing B&O tax and sales tax liability on the rental income earned from leasing a kiln which the taxpayer claims is a fixture/real property, not personal property.

FACTS AND ISSUES:

Krebs, A.L.J. -- . . . (taxpayer) is engaged in business as a lessor of forklifts and a kiln.

The Department of Revenue (Department) examined the business records of the taxpayer for the period from January 1, 1980 through December 31, 1986. As a result of this audit, the Department issued the above captioned tax assessments on June 25, 1987 and August 4, 1987 asserting excise tax liability, interest due and penalties in the respective amounts of $ . . . for the June 25, 1987 assessment and $ . . . for the August 4, 1987 assessment. The taxpayer made payment in full of the June 25, 1987 assessment ($ . . . which included extension interest) on September 4, 1987. The August 4, 1987 assessment remains due with accrued extension interest.

The taxpayer's protest involves Schedules II and III of the (June 25, 1987) audit report where respectively Retailing business and occupation tax (B&O) tax and sales tax liability were assessed on unreported lease income involving the lease of a kiln by the taxpayer/lessor to . . . (lessee). The taxpayer is president of the corporate lessee.

By lease dated June 30, 1982, the taxpayer/lessor leased a 68 foot "double tract lumber dry kiln" to the lessee for a term of 84 months at a monthly rent of $4,300 commencing when the kiln becomes operational. The kiln was constructed upon land owned by the lessee. The lease has the following pertinent provisions:

> 8. SURRENDER. Upon the expiration or earlier termination of this lease, with respect to any item of equipment, the lessee shall...return the same to lessor in good repair, condition and working order,...in the following manner as may be specified by lessor:
>
> > (a) By delivering such item of equipment at lessee's cost and expense to such place as lessor shall specify within the city or county in which the same was delivered to lessee...or (b) By loading such item of equipment at lessee's expense on board such carrier as lessor shall specify and shipping the same, freight collect, to the destination designated by the lessor.
>
> ...

> 14. DEFAULT. If lessee with regard to any item or items of equipment fails to pay any rent...or if lessee...fails to observe, keep or perform any other provision of this lease..., lessor shall have the right to exercise any one or more of the following remedies:
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> ...
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> (c) To take possession of any or all items of equipment...
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> ...
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> 21. PERSONAL PROPERTY. The equipment is, and shall at all times be and remain, personal property notwithstanding that the equipment or any part thereof may now be, or hereafter become, in any manner affixed or attached to, or imbedded in, or permanently resting upon, real property or any building thereon, or attached in any manner to what is permanent as by means of cement, plaster, nails, bolts, screws or otherwise.
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> ...
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> SCHEDULE
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> A. EQUIPMENT LEASED. LSI 68' Double Tract Lumber Dry Kiln...
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> ...
>
> D. LOCATION. The above described equipment shall be located at the . . . Inc. plant in . . . , Washington and shall not be removed therefrom without the prior written consent of the lessor.

The taxpayer asserts that at no time did he have the intention to remove the kiln from the real property, that the kiln is in fact attached to the property, and that its size and nature does not allow for removal from the property.

The taxpayer asserts that the language in the lease referring to "personal property" (see lease provision # 21 above) was written to qualify the kiln for federal investment tax credit (ITC) and that the kiln was specifically identified in (I.R.S.) Rev. Ruling 69-557 as a structure which qualified as ITC property. The taxpayer further asserts that its federal

tax treatment of the kiln as personal property does not change the fact that the kiln was attached to the real property and was a permanent part of the realty. The taxpayer points out that the . . . County Assessor recognizes the kiln to be real property and taxes it as such. The taxpayer asserts that it would be subject to double taxation if the kiln is also taxed as personal property under the excise tax system.

For all of the above reasons, the taxpayer requests that the kiln be treated as real property not subject to the excise tax.

DISCUSSION:

[1] The lease or rental of tangible personal property is subject to Retailing B&O tax and retail sales tax measured by the rental payments. WAC 458-20-211 (Rule 211). Amounts derived from the sale or rental of real estate are exempt from B&O tax, WAC 458-20-118 (Rule 118), and exempt from sales tax which is levied only on the sale or rental of tangible personal property. RCW 82.08.020, RCW 82.04.050 and Rule 211.

In this case, the issue is whether the kiln is real estate or personal property. In the Washington Supreme Court case, Lipsett Steel Products v. King County, 67 Wn.2d 650 (1965), the Court was faced with the same issue with respect to a shear, which cost approximately half a million dollars and was capable of exerting a pressure of 880 tons. The shear was installed on pilings and a reinforced concrete base which was 3 feet thick. A building was erected over and around the huge scrap shear. The Court noted that "the physical nature of the huge scrap shear -- its immense size and weight, the physical aspects of its installation -- could be quite misleading as to whether it is real or personal property."
The Court stated at page 652:

> ...in ascertaining whether or not improvements to buildings or land have become, in legal contemplation, a part of the realty to which they are annexed, the intention of the parties is one of the dominant factors or determinants:
>
> > The true criterion of a fixture is the united application of these requisites: (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. (Emphasis supplied.)

Bethlehem held title to the land on which the shear was installed. Lipsett had bought the shear, had it installed and used it. The lease of the land to Lipsett provided that it would not affect Lipsett's title and ownership of the shear. The Court found that despite great expense and difficulty, the shear could be removed from its location and that the parties had explicitly contracted that there would be no change in title or change in the characterization of the property. The Court concluded that the shear was personal property, not real estate.

Here, in this case, the taxpayer/lessor has title to and owns the kiln which has been installed on the lessee's land and the parties have explicitly contracted that there would be no change in title or change in the characterization of the property. The lease between the parties specifies that the kiln remains "personal property" even if it is affixed or attached to the real property. Article 21 of the lease, supra, is a clear expression of the parties' intent that the kiln remain personal property. The Schedule, supra, to the lease refers specifically to the kiln and allows for removal of the kiln with the prior written consent of the lessor. We conclude that the kiln is personal property and that the taxpayer's lease income is subject to excise taxation.

The Department has previously ruled that where a taxpayer/lessor of a potato storage facility, permanently fixed on the realty owned by the lessee and used for storage of potatoes and crops, declared in the lease that the facility shall remain "personal property" subject to removal at the termination of the lease, then the rental payments were subject to taxes arising from the rental of tangible property. See Determination No. 88-342, 6 WTD 361 (1988).

With respect to the taxpayer's point that the . . . County Assessor recognizes and taxes the kiln as real property and that it would result in double taxation if excise taxes were imposed, it appears to us that there are two different incidents of tax involved: (1) ad valorem taxation of real and personal property based on situs and value, and (2) excise taxation based on business activity gross income from sale/rental by the taxpayer of tangible personal property and consumer activity (purchasing/renting) for sales tax purposes

by the lessee of tangible personal property. In any event, the taxpayer himself is not being subjected to double taxation because he does not pay real estate taxes with respect to the kiln.

DECISION AND DISPOSITION:

The taxpayer's petition is denied.

DATED this 15th day of December 1989.