Cite as Det. No. 03-0165R, 24 WTD 336 (2005)

BEFORE THE 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. 03-0165R[1]
	)	
. . .	)	Registration No. . . .
	)	Tax Deferral Certificate No. . . .
	)	Document No. . . .
	)	Audit No. . . .
	)	Docket No. . . .
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[1] RULE 24001(5); RCW 82.60.020(8): TAX DEFERRALS – QUALIFIED BUILDING – APPORTIONMENT OF COSTS. The Department shall apportion the costs of construction if a qualified building is used partly for manufacturing or research and development, and partly for other purposes.

[2] RULE 24001(5); RCW 82.60.020(8): TAX DEFERRALS – APPORTIONMENT OF COSTS – TIME OF APPORTIONMENT. After the taxpayer has notified the Department of Revenue of completion of the eligible investment project, the Department of Revenue shall examine the completed project and, as of the date of examination, determine whether to apportion costs and the percentage of total construction costs eligible for deferral.

[1] The original determination, Det. No. 03-0165, is published at 24 WTD 330.

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.

Two taxpayers seek reconsideration of Det. No. 03-0165. In that determination, we denied the taxpayers' petition to allow a deferral of tax on 100% of the cost of constructing an addition to an existing building under chapter 82.60 RCW (tax deferrals for investment projects in distressed areas), because the addition was used for both qualifying and non-qualifying purposes. The Department of Revenue (DOR) initially approved the taxpayers' applications for deferral of 100% of the addition. After completion of construction, the DOR's Audit Division conducted a partial audit and found that only a portion of the addition qualified for the sales and use tax deferral in ch. 82.60 RCW. We find no error in Det. No. 03-0165 and deny the petition for reconsideration.[2]

ISSUE:

Whether Det. No. 03-0165 relied on repealed statutory language to reach its conclusion.

FACTS:

Gray, A.L.J. – The taxpayers do not assert any factual errors in Det. No. 03-0165. They claim only one legal error, that Det. No. 03-0165 relies upon statutory language repealed by the legislature in 1999. The facts in Det. No. 03-0165 are repeated here for easy reference.

[Owner] owns real estate and buildings in . . . , Washington. [Owner] leases the land and buildings to [Lessee]. [Lessee] manufactures . . . furniture, and sells those items as well as similar items manufactured by others, both at wholesale and retail. [Owner] built an addition to a building in which [Lessee] manufactured furniture. Before construction, the taxpayers used the existing building for some manufacturing purposes. The taxpayers' stated purpose of the expansion was to consolidate all manufacturing in [one city] and to increase the manufacturing capacity there.

On June 6, 1999, the taxpayers met with representatives from DOR, . . . to review the taxpayers' plans for new construction to ensure it would qualify for tax deferral. The taxpayers contend that the DOR representative told the taxpayers, verbally, to wait until after August 1, 1999, to commence construction. The taxpayers said, "the [DOR employee] indicated that after that time, the requirement in RCW 82.60.020 for 'direct utilization' would be repealed."[3] However, the DOR participants in the June 6, 1999, meeting said they were unaware of the taxpayers' plans to place the manufacturing activity in the original structure, not the new addition. The taxpayers began construction after August 1, 1999.

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

[3] Laws of 1999, ch. 164, §301 repealed former RCW 82.60.020(4)(a)(ii), which required that an investment project be "directly utilized to create at least one full-time qualified employment position for each $750,000 of investment."

[Owner] and [Lessee] requested a deferral of state and local sales and use taxes under ch. 82.60 RCW, and they did so before beginning construction or hiring new employees. DOR's Special Programs Division issued a distressed area retail sales and use tax deferral certificate ("certificate") to each taxpayer. [Owner] received certificate number . . . , effective August 1, 1999, for deferral of state and local retail sales and use tax (tax) on construction costs of the building addition. [Lessee] received certificate number . . . , also effective August 1, 1999, for deferral of tax on the purchase of qualified machinery and equipment.[4]

The Audit Division issued a tax assessment against [Lessee] after concluding that retail sales and use tax were due on the acquisition of office furniture and equipment and warehouse equipment, including forklifts. Because [Lessee] failed to present any facts upon which relief could be granted relating to the assessment issued against it, [Lessee's] petition is denied.

The taxpayers completed the addition in 2000, increasing its space by approximately . . . square feet. There is one building: the original building and the addition added by the taxpayers. The taxpayers' applications to . . . County for building permits identify the addition as a warehouse. After completion of construction, the taxpayers notified the Special Programs Division of that fact. On June 27, 2000, the Special Programs Division asked the Audit Division to perform a deferral audit on [Owner] and [Lessee] to determine whether the construction, equipment, and machinery actually qualified for the tax deferral.

On September 12, 2000, the auditor and field audit manager visited the site and toured the original building and the addition. They found, within the original building, approximately 40% of the space was used for manufacturing. All of the manufacturing is done in the original building. No manufacturing takes place in the addition. The addition is taller than the original building. In the addition, as viewed by the auditors, the taxpayers had 14 storage racks for storing furniture and raw materials. Of those 14 racks, only two were used to store the raw materials used in manufacturing or to store the taxpayers' finished goods. The Audit Division apportioned the deferral of tax, calculating the percentage of tax to be deferred at 14.3% (2/14). We note, in the tax year 2000, the taxpayers did not report any income under the manufacturing classification, despite [Lessee's] claim that sales of its own manufactured goods accounted for 47.5% of [Lessee's] total sales.

The Audit Division issued tax assessments against [Owner] after concluding that retail sales tax and use tax on the costs of the new addition were not fully deferred by ch. 82.60 RCW. The taxpayers appeal those tax assessments.

ANALYSIS:

In its original petition, the taxpayers argued that RCW 82.60.020(8) does not require an expanded area itself be directly utilized for manufacturing, and the DOR ignored the legislature's repeal of the "directly utilized" language in RCW 82.60.020(4)(a)(ii):

[4] The Special Programs Division subsequently extended both certificates through January 25, 2000.

> The plain language of RCW 82.60.020(8) is that the expansion of an existing structure for the purpose of increasing floor space or production capacity used for manufacturing is a "qualified building."
>
> The statute does not say that the expanded area itself must be directly utilized for manufacturing. The Auditor, however, is interpreting the statute as if it did have such language. A court may not add language, even if it believes the legislature intended something else but failed to adequately express it. [citation omitted]
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> . . . In 1999, this "directly utilized" language was removed by the legislature. This amendment supports the Taxpayers' position that the expanded area itself does not have to be directly utilized for manufacturing, but, instead, must be for the purpose of increasing floor space for manufacturing in the overall building.

Taxpayers' December 20, 2001, Memorandum of Points and Authorities, page 3.

We issued Det. No. 03-0165 denying relief to the taxpayers because of the uncontradicted findings made by the Audit Division in its on-site inspection of the taxpayer's property that only a part of the property was devoted to manufacturing and our conclusion that only the portion of the expansion that is devoted to manufacturing qualifies for the deferral.

We accepted the petition for reconsideration. The taxpayer wrote, in its December 24, 2003, brief:

> In its determination May 21, 2003, the Appeals Division relies upon the old, "directly utilized" language (page 4). The old, repealed RCW 82.60.020(4)(a)(ii) containing this language is quoted verbatim. The decision goes on to analyze the words "directly" and "utilized." The Determination concludes by stating that the "legislature intended the 'directly utilized' language as a requirement that the tax deferral be granted only if the new construction or expansion clearly produced one new job for every seven hundred fifty thousand dollars of investment."
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> With all respect to the Appeals Division, it is an error of law to rely upon repealed language to decide a case. This is especially so when Washington law presumes that the removal of such language results in a presumption that it was done for a purpose; i.e., in this case to remove that requirement.

The taxpayer has misread Det. No. 03-0165. Det. No. 03-0165 does not rely upon the "directly utilized" language, which the legislature repealed in 1999, to reach its conclusion. Our references to the repealed statutory language were to point out that the taxpayers' interpretation of the repealed language was wrong.

The taxpayer's reference to page 4 of the determination contains this statement: "The phrase 'directly utilized' **is** found in RCW 82.60.020(4)(a)(ii)." (Emphasis supplied.) The sentence would have been better written in the past tense. Nonetheless, after quoting the statute, the determination said that the phrase "directly utilized" was a bridge between the phrases "portion of an investment project" and the number of full-time jobs created. The phrase "directly

utilized" did not refer to the use of a building for a qualifying or nonqualifying use. To put it differently, the repeal of the "directly utilized" language did not improve the taxpayers' positions, because the repealed language did not deal with the amount of building floor space used for manufacturing but was, instead, related to the number of jobs created.

[1] The definition of "qualified building," both before and after the 1999 changes, provides in part:

> If a building is used partly for manufacturing or research and development and partly for other purposes, the applicable tax deferral shall be determined by apportionment of the costs of construction under rules adopted by the department.

The "directly utilized" language was in the definition of "eligible investment project" and required the creation of a certain number of jobs. . . . This was separate and apart from the apportionment that was required for buildings used partly for manufacturing.

[2] The Audit Division apportioned the amount of tax due on the amount of space that qualified for deferral, using the formula provided in Rule 24001(5). It is not enough that, as the taxpayers argue in their petition for reconsideration, "the expansion or renovation of existing structures be for the purpose of increasing floor space or production capacity used in manufacturing activities." Audit must judge the project at the time of its completion, as opposed to judging it on contemplated activity that may never happen.

DECISION AND DISPOSITION:

The petition for reconsideration is denied.

Dated this 9th day of September 2004.