

Cite as Det. No. 03-0316, 24 WTD 16 (2005)

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>
Reporting Instructions and Denial of Refund of	)	
	)	No. 03-0316
	)	
...	)	Registration No. ...
	)	Docket No. ...
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...	)	Registration No. ...
	)	Docket No. ...

RCW 82.08.02567: RETAIL SALES TAX -- EXEMPTION -- MACHINERY AND EQUIPMENT -- ENERGY GENERATION. A public utility district's purchases of machinery and equipment incorporated into an interconnection facility were not exempt from retail sales tax under RCW 82.08.02567 where the interconnection facility was owned and operated by the PUD.

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.

Okimoto, A.L.J. – A public utility district (PUD) that constructed, owned, and operated interconnection facilities enabling a wind farm to connect with a regional electricity grid and the wind farm developer . . . appeal Audit's future reporting instructions. Those instructions state that purchases of equipment incorporated into interconnection facilities are not exempt from retail sales tax under RCW 82.08.02567. In addition, PUD appeals Audit's refusal to refund sales taxes paid on equipment purchased for the interconnection facilities. We deny both . . . appeals.<sup>1</sup>

ISSUE

Are machinery and equipment purchases that are incorporated into an interconnection facility exempt from retail sales tax where the purchases are funded by the wind farm developer but owned by a public utility district?

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

## FINDINGS OF FACT

. . . (Windfarmer) developed and currently operates a wind farm in . . . Washington . . . . A windfarm consists of several rows of wind turbines. The wind-powered turbines generate energy that is connected to a regional energy grid through an interconnection facility. [Windfarmer] originally requested a ruling on September 7, 2001 from the Taxpayer Information and Education section (TI&E) of the Department of Revenue (DOR) on whether Windfarmer's purchases of machinery and equipment in connection with its . . . Project was exempt from retail sales tax under RW 82.08.02567.<sup>2</sup>

Windfarmer's letter asked for a ruling on two separate contracts. The first contract . . . was for the purchase and installation of the wind turbines and associated equipment. The letter also asked that road construction costs necessary to install and maintain the wind turbines be allowed the exemption. TI&E allowed the exemption for the purchase and installation of the wind turbines, towers and associated equipment but denied the exemption for access road construction costs and a building. . . .

Windfarmer's second contract was between Windfarmer and . . . PUD and was for the construction, operation and maintenance of a substation (Interconnection Facilities) necessary to connect the wind turbines to . . . transmission lines. Under the terms of the . . . contract, PUD was obligated to build, operate and maintain an interconnection facility on Windfarmer's land. Windfarmer was obligated to finance the costs of designing, procuring and constructing the Interconnection Facilities out of proceeds of revenue bonds issued by Windfarmer. The agreement provided that, if the generating facility did not achieve commercial operation, PUD's construction costs were not recoverable from Windfarmer or from any bond proceeds. Once commercial operation was achieved, however, Windfarmer was required to reimburse PUD for all of PUD's construction costs for the Interconnection Facilities plus a 10% profit factor. In addition, Windfarmer is required to pay PUD \$ . . . per month as compensation for labor, employee benefits, and administrative and general costs related to operating and maintaining the Interconnection Facilities. Legal ownership of all Interconnection Facilities is vested in the PUD.

TI&E stated that it did not have sufficient information to make a ruling on the PUD Interconnection Facilities contract and the matter remained unresolved. On June 11, 2002 PUD sent a petition to DOR requesting a refund of all retail sales taxes paid by PUD on the Interconnection Facilities contending that it was exempt from tax under RCW 82.08.02567. This petition was referred to DOR's Audit Division (Audit). On August 26, 2002, Audit denied PUD's petition and instructed PUD that, because the Interconnection Facilities were owned and operated by the PUD and not Windfarmer, the exemption did not apply. Consequently, Audit denied PUD's June 11, 2002 refund petition and also instructed PUD to pay retail sales tax on all future purchases of machinery and equipment incorporated into the Interconnection Facilities

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<sup>2</sup> A comparable use tax exemption is contained in RCW 82.12.02567.

project. PUD and Windfarmer . . . appealed the refund denial and future reporting instructions to the Appeals Division (Appeals).

Three days after the petition was filed with Appeals, Windfarmer and PUD executed a supplemental contract to clarify certain aspects of ownership of the Interconnection Facilities. The . . . supplemental contract provides that “the interconnection facilities are to be operated by District for the benefit of the Wind Project . . . .” The supplemental contract states that legal title to the Interconnection Facilities is in PUD whereas Windfarmer is an equitable or beneficial owner of the interconnection facilities.

### ANALYSIS

RCW 82.08.02567 provides a retail sales tax exemption for machinery and equipment used in generating electricity. It provides:

(1) The tax levied by RCW 82.08.020 shall not apply to sales of machinery and equipment used directly in generating electricity using fuel cells, wind, sun, or landfill gas as the principal source of power, or to sales of or charges made for labor and services rendered in respect to installing such machinery and equipment, but only if the purchaser develops with such machinery, equipment, and labor a facility capable of generating not less than two hundred watts of electricity and provides the seller with an exemption certificate in a form and manner prescribed by the department. The seller shall retain a copy of the certificate for the seller's files.

RCW 82.08.02567 provides a tax exemption to the purchaser of machinery and equipment used directly in generating electricity using wind as the principal source of power, “but only if the purchaser develops with such machinery, equipment, and labor a facility capable of generating not less than two hundred watts of electricity . . . .” (Underlining added.) The statute requires that the purchaser of the machinery and the developer of the wind farm facility must be the same. In [this] case, the purchaser of the machinery and equipment for the Interconnection Facilities<sup>3</sup> is the PUD whereas the developer of the wind farm is Windfarmer.

Although [Windfarmer and the PUD] contend that Windfarmer is purchasing the Interconnection Facilities from PUD, we disagree. The . . . (Construction Agreement), dated . . . , clearly delineates that the ownership of the Interconnection Facilities remains with the PUD. Section 4 of the Construction Agreement provides:

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<sup>3</sup> WAC 458 20 163 (Rule 163) (2)(b) provides that the term “used directly” means “the machinery and equipment provides any part of the process that captures the energy of the wind, landfill gas, or solar, converts that energy to electricity, and transforms or transmits that electricity for entry into electric transmission and distribution systems.” Rule 163(2)(a)(ii) also includes substations within the definition of “machinery and equipment.”

4.1 District Ownership. **District shall own all Interconnection Facilities** and other equipment on its side of the Point of Interconnection and all other equipment required to protect the Electric System and the Generating Facility.

(Bolding added.)

We also find [the] argument that Windfarmer is described as the beneficial owner of the Interconnection Facilities in the supplemental contract to be unpersuasive. First, we question whether beneficial ownership of the Interconnection Facilities, alone, would qualify Windfarmer for the exemption under RCW 82.08.02567. However, assuming for the sake of argument that it would, we nevertheless conclude that Windfarmer was not the beneficial owner of the Interconnection Facilities. The manner, in which two parties describe themselves in a contract, although relevant, is not dispositive. It is the facts and conduct of the parties that defines the relationship. *Rho Co. v. Department of Rev.*, 113 Wn.2d 561 (1989).

In *Christiansen, v. Department of Social Security*, 15 Wn.2d 465 (1942), the Washington Supreme Court cited with favor a definition of “beneficial ownership” used by the United States Supreme Court in *Catholic Missions v. Missoula County*, 200 U.S. 118 (1906). That court stated:

The expression, beneficial use or beneficial ownership or interest, in property is quite frequent in the law, and means in this connection such a right to its enjoyment as exists where the legal title is in one person and the right to such beneficial use or interest is in another, and where such right is recognized by law, and can be enforced by the courts, at the suit of such owner or of someone in his behalf.

*Catholic Missions* at 127-8.

*Black’s Law Dictionary* (7<sup>th</sup> ed. 1999) further defines the term “beneficial owner” as:

1. One recognized in equity as the owner of something because use and title belong to that person, even though legal title may belong to someone else; esp.; one for whom property is held in trust.

In this case, the legal title of the Interconnection Facilities is in the PUD. Use and control of the Interconnection Facilities also remain with the PUD. PUD employees run, operate, and maintain the Interconnection Facilities, and the PUD charges Windfarmer a monthly fee for services provided by the Interconnection Facilities. We further note that Section 7.4 of the Construction Agreement allows the PUD to connect additional users to the Interconnection Facilities with the understanding that any new users would reimburse Windfarmer for a pro rata share of future operation and past construction costs. This provision further suggests that it is the PUD that principally enjoys the use and benefits of the Interconnection Facilities. Even though Windfarmer may have originally financed the facilities and has some input on its use, we

conclude that such input is not sufficient to establish Windfarmer as the beneficial owner of the Interconnection Facilities. Accordingly, [the] petition is denied on this issue. . . .

DECISION AND DISPOSITION

[The] petition for correction of future reporting instructions and petition for refund of overpaid retail sales taxes is denied.

Dated this 12th day of November 2003.