Cite as Det. No. 15-0027, 34 WTD 577 (2015)

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. 15-0027
	)	
. . .	)	Registration No. . . .
	)	

RULE 146; RCW 82.04.4292; B&O TAX – INTEREST INCOME FROM INVESTMENTS – DEFINITION OF "FINANCIAL BUSINESS." A mobile home park that also provided loans on mobile homes in the park, and received interest income from such loans could not qualify as a "financial business" to qualify for a deduction of such income from its measure of tax liability because (1) the mobile home park's primary purpose and objective was not to earn income through the utilization of significant cash outlays, and (2) the mobile home park was not a business comparable to a banking, loan or security business.

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.

Yonker, A.L.J. – The owner of a mobile home park protests the [Department of Revenue's (Department)] denial of a refund request based on the Department's finding that Taxpayer did not qualify as a "financial business" and, therefore, could not deduct from the measure of its tax liability certain amounts it received from interest on mortgage loans. Taxpayer argued that it was a "financial business" because it was the lender on such loans similar to other types of financial businesses. We deny the petition.[1]

ISSUE

May Taxpayer deduct from its measure of taxable income amounts it earned from interest received from loans secured by first mortgages under RCW 82.04.4292?

FINDINGS OF FACT

[Taxpayer] is a Washington limited liability company that owns a mobile home park in . . . Washington. Taxpayer's mobile home park is a " . . . ."[2] Taxpayer rents spaces in the park to individuals that own manufactured homes, which are "stationary and permanent" on the park's land.

[1] Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.
[2] Found at . . . , last visited on January 27, 2015.

Taxpayer has two sources of income. By far, the largest portion of Taxpayer's income is derived from rental payments for the park spaces by the individual renters. The second, smaller source of Taxpayer's income is from interest on loans in which Taxpayer is the lender. Taxpayer explained this process as follows:

> People move into the park and have to leave the park for various reasons. People moving are usually unable to sell as buyers cannot get traditional financing. Also, movers and seller usually have a short time period to move to another area. [Taxpayer and another entity] buy the homes rather than have them abandoned or scrapped on site, and left in an unsightly condition. In many instances [Taxpayer and another entity] have no choice [but] to offer financing. . . . [Taxpayer and another entity] repair, paint, clean and sell the home to a new tenant and provide 1st mortgage financing as there is no other financing available.

In other words, Taxpayer occasionally purchases manufactured homes from individuals who wish to move but cannot easily sell the manufactured homes, and resells those manufactured homes to new individuals who wish to reside in the mobile home park. Taxpayer does this in order to avoid manufactured homes in the park becoming abandoned and detracting from the attractiveness of the park.

As of March 2013, Taxpayer was the lender in eight such loans. A comparison of Taxpayer's income from these two sources, by year as represented by Taxpayer, is as follows:

Year	Income from Rent	Percent of Total Income	Income from Loan Interest	Percent of Total Income
2007	$ . . .	96.5%	$ . . .	3.5%
2008	$ . . .	96.9%	$ . . .	3.1%
2009	$ . . .	96.7%	$ . . .	3.3%
2010	$ . . .	96.9%	$ . . .	3.1%
2011	$ . . .	97.5%	$ . . .	2.5%
2012	$ . . .	98.2%	$ . . .	1.8%
2013	$ . . .	98.8%	$ . . .	1.2%

On February 19, 2013, the Department received a refund request in the form of an amended annual excise tax return for 2011 in which Taxpayer claimed it was entitled to a refund of $ . . . because its income from loans secured by first mortgages should not have been included in its measure of tax liability. On December 11, 2013, TAA denied Taxpayer's refund request after finding that Taxpayer did not qualify for a first mortgage interest deduction. Taxpayer appealed that denial.

ANALYSIS

In Washington, "there is levied and collected from every person that has a substantial nexus with this state a tax for the act or privilege of engaging in business activities." RCW 84.04.220. The [business and occupation (B&O)] tax measure is "the application of rates against value of

products, gross proceeds of sales, or gross income of the business, as the case may be." *Id.* The rate used is determined by the type of activity in which a taxpayer engages. *See generally* Chapter 82.04 RCW.

The B&O tax is a gross receipts tax, meaning that it applies to all value proceeding or accruing to the company, and not only to its profit margins. *Lamtec Corp. v. Dep't of Revenue*, 170 Wn.2d 838, 843, 246 P.3d 788, 791 (2011). By enacting Washington's B&O tax system, the legislature intended to impose the B&O tax on virtually all business activities carried on within the state. *Time Oil Co. v. State*, 79 Wn.2d 143, 146, 483 P.2d 628 (1971). Further, the B&O tax system was meant to "leave practically no business and commerce free of . . . tax." *Budget Rent-A-Car of Washington-Oregon Inc. v. Dep't of Revenue*, 81 Wn.2d 171, 175, 500 P.2d 764 (1972).

RCW 82.04.140 defines "business" broadly and includes "all activities engaged in with the object of gain, benefit, or advantage to the taxpayer or another person or class, directly or indirectly." Generally, all gross income of the business is subject to B&O tax, without any deductions for costs such as labor, materials, taxes, or any other expense. *See* RCW 82.04.080. This holds true unless the legislature has carved out a specific exclusion or deduction.

Here, Taxpayer does not dispute that it is subject to B&O tax generally. Instead, Taxpayer argues that a portion of its gross income during the audit period should be deducted from the measure of its B&O tax liability under RCW 82.04.4292(1), which states the following:

> In computing tax there may be deducted from the measure of tax by those engaged in banking, loan, security or other financial businesses, interest received on investments or loans primarily secured by first mortgages or trust deeds on nontransient residential properties.

See also WAC 458-20-146. We note that when interpreting exemption or deduction provisions, the burden of showing qualification for the tax benefit rests with the taxpayer. *Group Health Coop. of Puget Sound, Inc. v. Washington State Tax Comm'n*, 72 Wn.2d 422, 429, 433 P.2d 201 (1967). In the case of doubt or ambiguity, the provisions of such exemptions or deductions are to be "construed strictly, though fairly and in keeping with the ordinary meaning of their language, against the taxpayer." *Id.*

While the statute contains a number of elements that must be proven in order to qualify for the deduction, the only element at issue in this case is whether Taxpayer is "engaged in banking, loan, security or other financial businesses." Taxpayer stated in its appeal petition that it "need not be a bank to qualify for this deduction as it is open to all businesses doing this financing of 1st mortgages on a regular business." Essentially, Taxpayer argues that it is a "financial business."

The term "financial business" is not defined in statute or rule. Nor have we had the opportunity to define that term in our past determinations in the context of RCW 82.04.4292.[3] While we

[3] In Determination No. 93-023, 12 WTD 575 (1993), we considered whether a taxpayer was entitled to deduct the interest from certain real estate contracts under RCW 82.04.4292, where the taxpayer sold two parcels of land, but

have not had occasion to define "financial businesses" for the purpose of RCW 82.04.4292, we have had occasion to do so for the purpose of another deduction under the former language of RCW 82.04.4281.[4] The Washington courts have similarly had occasion to define "financial businesses" under the former language of RCW 82.04.4281.

In Determination No. 93-269ER, 14 WTD 153 (1995), we relied on two earlier Washington Supreme Court Cases, *John H. Sellen Constr. Co. v. Dep't of Revenue*, 87 Wn.2d 878, 558 P.2d 1342 (1976) and *Rainier Bancorporation v. Dep't of Revenue*, 96 Wn.2d 669, 638 P.2d 575 (1982), to define a "financial business" as the following:

> . . . the common meaning of the phrase ["financial business"] contemplates a business whose primary purpose and object is to earn income through the utilization of significant cash outlays.

Relying on both the *Sellen* and *Rainier* cases, we went on to articulate a two-part inquiry to determine if an entity is a "financial business":

> The first part of the inquiry in determining whether a taxpayer's activities constitute a "financial business" is whether the "primary purpose and objective [of the taxpayer's financial activities] is to earn income through the utilization of significant cash outlays," or whether these activities are merely "incidental" to the taxpayer's other nonfinancial business activities. . . .
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> The second part of the inquiry in determining whether a taxpayer's activities constitute a "financial business" is whether, under the *ejusdem generis* rule of statutory construction, the taxpayer's activities are similar to, or comparable to, those of "banking, loan, [or] security businesses," even though the taxpayer might not technically fall within one of those three categories.

14 WTD 153, pp. 8-10. Similarly, and more recently, the Washington Supreme Court in *Simpson Inv. Co. v. Dep't of Revenue*, 141 Wn.2d 139, 153, 3 P.3d 741 (2000), relied on its earlier decisions in *Sellen* and *Rainier* to declare that determination of whether an entity is a "financial business" under RCW 82.04.4281 depends on whether the answer to the following two questions is "yes": (1) is the entity's "primary purpose and objective to earn income through the utilization of significant cash outlays," and (2) applying the interpretive tool of *ejusdem generis*, is the entity "comparable to a 'banking, loan or security' business."

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primarily was in the business of raising and skinning mink for their fur. In that case, we concluded that the taxpayer was "not engaged in a financial business" and, therefore, did not qualify for the deduction under that statute, but we did not specifically define the term "financial business." *Id.*

[4] The current version of RCW 82.04.4281 allows a deduction from the measure of tax certain amounts derived from certain investments, dividends, and [certain intra-affiliate] interest on loans except for such amounts "received by a banking, lending, or security business." However, in [a] former version of that statute, the deduction was for investments and dividends "derived by person, other than those engaging in banking, loan, security, or *other financial businesses*." RCW 82.04.4281(1980) (emphasis added). [In the present appeal, taxpayer does not argue that the interest income qualifies for the deduction in RCW 82.04.4281.]

We conclude that the same two-part inquiry is appropriate for determining whether Taxpayer here is a "financial business" for the purpose of RCW 82.04.4292. First, we ask whether Taxpayer's "primary purpose and objective" is to earn income through the utilization of significant cash outlays. We conclude the answer to this question is "no." Taxpayer's income from loan interest was never more than four percent of its total gross income during the review period. The vast majority of Taxpayer's income was from rent payments of the park spaces. Clearly, Taxpayer's primary purpose was to rent its park spaces to individuals as opposed to being engaged in lending money to individuals to purchase manufactured homes. Taxpayer only entered into such mortgage arrangements out of necessity to prevent the mobile home park from declining in appearance and appeal to current and potential residents. Essentially, Taxpayer's choice to enter into these agreements was a business choice to protect and cultivate Taxpayer's primary business activity – renting park spaces. Thus, Taxpayer's income from the interest of such loans was merely "incidental" and not Taxpayer's primary purpose or objective.

Second, we ask whether, under the interpretive tool of *ejusdem generis*, Taxpayer is comparable to a banking, loan, or security business. We conclude that the answer to this second question is also "no." The rule of *ejusdem generis* has been explained in the following way by the Washington Supreme Court:

> [G]eneral terms appearing in a statute in connection with precise, specific terms, shall be according meaning and effect only to the extent that the general terms suggest items or things similar to those designated by the precise or specific terms. In other words, the precise terms modify, influence or restrict the interpretation or application of the general terms where both are used in sequence or collocation in legislative enactments.

Sellen, 87 Wn.2d at 883-84 (quoting *State v. Thompson*, 38 Wn.2d 774, 777, 232 P.2d 87, 90 (1951)). Thus, the generic term "financial business" only extends to businesses that are "comparable" to one of the specific categories of banking, loans, and securities. In *Simpson*, the Court stated:

> In applying ejusdem generis the first task is ascertaining what banks, loan companies, and security businesses have in common as a class. These businesses share one principal characteristic; they make money through cash outlays, which generate revenue in the form of interest income, dividends, and appreciation of intangible assets.

Essentially, we must determine if Taxpayer generates its revenue in the same manner as banks, loan companies, and security businesses. We conclude Taxpayer's revenue is not generated "through cash outlays" to any material degree. While Taxpayer receives some income from loan interest, similar to a bank or loan company, that amount is nominal, and not in keeping with the banks, loan companies, and security businesses "as a class." Here, Taxpayer is a mobile home park, which generates revenue primarily from rent payments from individuals. This, we conclude, places Taxpayer outside of the scope of a "financial business."

While Taxpayer argued that allowing Taxpayer the deduction of its loan income is consistent with the legislative intent behind RCW 82.04.4292, we cannot overlook the clear language and

associated case law that control our analysis in this case. As such, we conclude Taxpayer does not qualify for the deduction under RCW 82.04.4292.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 4th day of February, 2015.