Cite as Det. No. 16-0010, 36 WTD 461 (2017)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

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| 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. 16-0010 |
| . . . | ) | Registration No. . . . |

[1] RCW 82.04.4334: BUSINESS AND OCCUPATION TAX DEDUCTION FOR RETAIL SALE OR DISTRIBUTION OF BIOFUEL – RINS. Income from the sale of renewable energy identification numbers does not qualify for the tax deduction for the retail sale or distribution of certain biofuels.

[2] RCW 82.32A.020: SPECIFIC OFFICIAL ADVICE – LETTER RULING. In order to rely on a letter ruling from the Department, the letter ruling must state all the pertinent facts and specifically address the taxation, of the situation at hand.

[3] RCW 82.32.050; RCW 82.04.020: NONCLAIM STATUTE – TAXABLE YEAR. Where a Taxpayer reports on a calendar year basis, rather than on a fiscal year, the taxable year for the nonclaim statute is a calendar year.

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.

Kreger, A.L.J. – A company that blends and sells biodiesel fuels petitions for correction of the assessment of tax on the sale of renewable energy identification numbers, asserting that they should be exempt from tax under RCW 82.04.4334 . . . or alternatively, asserts that tax on all sales for prior periods is precluded by a 2006 letter ruling. The Taxpayer also asserts that the audit exceeded the statute [limiting the time for assessments] due to use of a calendar year rather than the Taxpayer's fiscal year, which ends in September. We conclude that the letter ruling did not specifically address the sale of renewable energy identification numbers or equipment used in processing, and therefore, does not preclude taxation. We also conclude that the deduction from retail sales tax for the sales of biofuels, provided by 82.04.4334, does not apply to the sales of renewable energy identification numbers. . . . Finally, we note that the Taxpayer had not requested or received permission to report on a fiscal year, and accordingly, the calendar year audit was proper and authorized. We sustain the assessments and deny the Taxpayer's petitions.[1]

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

## ISSUES

1. Does the deduction in RCW 82.04.4334, for amounts received from the retail sale or distribution of certain biofuels, also apply to the sale of credits in the form of Renewable Identification Numbers?

2. Does a 2006 letter ruling, issued to the Taxpayer, preclude taxation of these credits or the sale of equipment for prior periods?

. . .

3. Does the fact that the Taxpayer keeps a fiscal year render the initial period of the 2010 calendar year audit outside of statute under RCW 82.32.050, when there is no evidence that the Taxpayer requested to report on a fiscal rather than a calendar year?

## FINDINGS OF FACT

. . . (Taxpayer) is a Washington corporation engaged in the business of blending and selling biodiesel fuel, selling Renewable Identification Numbers (RIN), and offering consulting, office services, and contract work including the sale of equipment. The Audit Division (Audit) of the Department of Revenue (Department) conducted an audit of the Taxpayer's Washington business activities from 2008 through 2013, which resulted in two tax assessments being issued to the Taxpayer. The assessment covering 2008, Document No. . . . in the amount of $ . . . , related to the sale of equipment to . . . .[2] The second assessment covering January 1, 2010, through December 31, 2013, Document No. . . . in the amount of $ . . . , related to the Taxpayer's general business activities.[3] This second assessment was amended and reflects a reduction based on additional information provided by the Taxpayer that supported an adjustment to the apportionment of income for out-of-state sales.[4] The Taxpayer timely filed appeals for both assessments, which are addressed jointly in this determination.

On appeal, the Taxpayer also notes that it maintains a fiscal year running from October 1st through September 30th.

Renewable Identification Numbers:
In addition to the sale of the fuel itself, the Taxpayer also sells RINs. A RIN is a serial number assigned to a batch of biofuel for the purpose of tracking its production, use, and trading as required by the Environmental Protection Agency's (EPA) Renewable Fuel Standard, implemented according to the Energy Policy Act of 2005. The RINs allow for the tracking of the gallons of renewable fuel produced and sold.

[2] This assessment comprised $ . . . in retail sales tax, $ . . . in interest, and a 5% assessment penalty of $ . . . .
[3] This assessment comprised $ . . . in service and other activities (service) business and occupation (B&O) tax, and interest of $ . . . .
[4] Document No. . . . was originally issued in the amount of $ . . ., and consisted of $ . . . in service B&O tax, $ . . . in interest, and a 5% assessment penalty of $ . . . .

RINs are essentially fuel credits, tradable on a market. Oil companies can either buy a quantity of renewable fuel to comply with the Renewable Fuel Standard set by the EPA, or buy a RIN credit on the open market. In other words, RINs represent a mechanism by which the EPA implements the Renewable Fuel Standard:

> When renewable fuels are blended into gasoline and diesel fuel or sold to consumers in neat form (typically 100% biofuel), the RIN representing the renewable attribute of the fuel becomes separated from the physical biofuel and can be used for either compliance purposes or traded. Separated RINs have a market value attached to them and provide flexibility for obligated parties in meeting their [Renewable Volume Obligations]. Obligated parties have the option to either acquire RINs by purchasing and blending physical quantities of biofuels, or by purchasing already separated RINs and submitting them to the EPA for compliance.

U.S. Energy Information Administration, *RINs and RVOs are used to implement the Renewable Fuel Standard* (2013), http://www.eia.gov/todayinenergy/detail.cfm?id=11511 (January 7, 2016).

The Taxpayer tracks and records sales of separate RINs in a different account than the sales of biofuel, which may or may not include a RIN and are tracked and recorded in another account. The creation of the RIN relates to the specific production of a gallon of blended fuel. The Taxpayer asserts that the sale of these RINs should be considered as a component part of the sale of the fuel, and correspondingly, subject to the same deduction as the fuel. However, Audit assessed tax on the RINs sales that were recorded in Account . . . , which only recorded the sale of the RIN as opposed to the biofuel sales, which may or may not have included a RIN, that were tracked and recorded in Account . . . titled Fuel Sales.

Letter Ruling:
In 2006, the Taxpayer requested a ruling on the taxability of purchasing and blending activities. The ruling request noted that "because the fuel at issue is as least 20% biodiesel," the Taxpayer had been informed it was "exempt from B&O." On May 23, 2006, a ruling was issued to the Taxpayer which stated that: "the sale of biodiesel fuel is exempt from B&O tax as long as the fuel meets the American Society of Testing & Materials standard as outlined in specification D6751." The ruling went on to note that because such fuel was subject to the Special Fuel Tax, it was not subject to retail sales tax. The ruling did not mention RINs, any manufacturing activities, or any other project work, but rather, solely addressed the sale of biodiesel fuel.

The Taxpayer responded to this May 23rd message with some additional information and requested further clarification. The Taxpayer stated that it was a "biodiesel distributor" and specifically asked:

> Do we pay the state special road tax on fuel we sell wholesale or retail?
> Do we pay state sales tax on any fuel that we sell wholesale or retail?
> Do we pay B&O on any fuel we sell either wholesale or retail?
> Are there any other taxes we're responsible for collecting?

On May 30, 2006, the Department responded to these specific questions providing additional information and links on the Special Fuel Tax, noting that because the fuel is subject to the Special Fuel Tax, it is not subject to the retail sales tax under RCW 82.08.0255, and repeating that the sale of biodiesel fuel is exempt from B&O tax. [The Department's response] concluded with the statement that: "Based on the limited information provided, you are not responsible for collecting any other taxes."

. . .

## ANALYSIS

Biofuel Deductions/RINs:

A B&O tax deduction for the sale or distribution of biodiesel or alcohol fuels was enacted in 2003 as part of a series of temporary measures benefitting sellers and manufacturers of biofuels.[5] The deduction expired on July 1, 2015, and therefore, is no longer in force. However, during the audit period, RCW 82.04.4334 provided a deduction from B&O tax for amounts received from retail sales or distributions of biodiesel, and E85 motor fuel. Specifically, the statute provided as follows: "In computing tax there may be deducted from the measure of tax amounts received from the retail sale, or for the distribution, of: (a) Biodiesel fuel; or (b) E85 motor fuel." RCW 82.04.4334(1).[6]

Biodiesel, for this purpose, is a chemical derived from vegetable oils and animal fats: "'Biodiesel fuel' means a mono alkyl ester of long chain fatty acids derived from vegetable oils or animal fats for use in compression-ignition engines and that meets the requirements of the American society of testing and materials specification D 6751 in effect as of January 1, 2003." RCW 82.04.4334(1)(a).[7] Because the RINs at issue arise in conjunction with the sale of biodiesel fuel, the Taxpayer asserts that the deduction should also cover their sale.

We begin with the general principle that taxation is the rule, and deductions or exemptions are the exception. *Lacey Nursing Center, Inc. v. Dep't of Revenue*, 128 Wn.2d 40, 49, 905 P.2d 338 (1995). Tax exemptions and deductions must be narrowly construed and the taxpayer bears the burden of proving that it qualifies for a tax deduction. *Budget Rent-A-Car Inc. v. Dep't. of*

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[5] [Other provisions included a] B&O tax deduction for retail sales and distributions of biofuel (RCW 82.04.4334); retail sales tax exemption for sales of machinery, equipment, vehicles, and services related to biofuels (RCW 82.08.955); use tax exemption for the use of machinery, equipment, vehicles, and services related to biofuels (RCW 82.12.955); property tax exemption for property used for the manufacture of biofuels (RCW 84.36.635); leasehold excise tax exemption (RCW 82.29A.135); and reduced B&O tax rate for biofuel manufacturing activity (RCW 82.04.260(1)(e)). These provisions were initially scheduled to expire on July 1, 2009; however, with the exception of the reduced tax rate for biofuel manufacturing, the benefits were subsequently extended.

[6] The sales deduction statute was initially set to expire on July 1, 2009, but was subsequently extended by the legislature to July 1, 2015, during the 2007 legislative session. Laws of 2007, ch. 309, § 3.

[7] According to the National Biodiesel Board, a biodiesel trade association, the term biodiesel "refers to the pure fuel meeting the D 6751 specification before it is blended with petroleum-based diesel fuel." National Biodiesel Board, Biodiesel Basics, http://www.biodiesel.org/what-is-biodiesel/biodiesel-basics (January 7, 2016). Biodiesel blends are symbolized by the notation "BXX," with "XX" representing the percentage of biodiesel contained in the blend. Thus, pure biodiesel is designated as "B100," while fuel designated as B20 is 20% biodiesel and 80% petroleum diesel. The RCW 82.04.4334 deduction only applies to the pure biodiesel portion of the sold fuel. *See* Special Notice, Biofuel Sellers – Update (July 6, 2007).

*Revenue*, 81 Wn.2d 171, 174, 500 P.2d 764 (1972) (citing *Group Health Coop. of Puget Sound, Inc. v. Tax Comm'n*, 72 Wn.2d 422, 443, 433 P.2d 201 (1967)).

As detailed in the fact section, a RIN arises from the production of a gallon of biofuel, but is a separate commodity that trades on its own market and can be sold independent of the fuel that created it. Thus, while initially associated with a specific quantity of biofuel, once it is created, the RIN is a separate product. The Taxpayer asserts that it considers the RIN as part of the sale of the deductible fuel. However, this is inconsistent with separately tracking and recording the sale of the RINs. Audit only assessed tax on the RIN sales that were recorded separate from fuel sales. The deduction at issue is for the sale of biofuel, not any attendant credits such as the RINs that the creation of that biofuel may have generated. We find no basis to read the deduction at issue so broadly so as to include the sale of RINs. Indeed, the plain language of the deduction only addresses specific fuels with no mention of any attendant or associated items or credits. Accordingly, we conclude that the sale of the RINs was not eligible for the deduction provided by RCW 82.04.4334 during the audit period, and sustain Audit's conclusion that this income was subject to tax.

The RIN is a credit, a form of intangible property, which may be separately sold and traded. The Taxpayer recorded and tracked the RINs it sold as part of its business activity. This type of sales activity is not subject to a specific tax classification, and thus, this business activity is taxable under the services and other business activities classification. RCW 82.04.290; WAC 458-20-224. *See also* Det. No. 92-004, 11 WTD 551 (1992) (Income derived from a transfer or sale intangible property interest is subject to the B&O tax for services and other activities.). . . . We conclude that Audit correctly assessed service B&O tax on this sales income and deny the Taxpayer's petition on this issue.

Letter Ruling:

First, we address whether the 2006 letter ruling provided a basis to preclude imposition of tax on the sale of the RINs. RCW 82.32A.020(2) vests the taxpayers of Washington with the right to "rely on specific, official written advice to that taxpayer." RCW 82.32A.020(2). The written advice at issue here is a letter ruling issued in accordance with WAC 458-20-100 (Rule 100). Rule 100 is the administrative rule that addresses letter rulings. It provides in pertinent part:

> Taxpayers may request an opinion on future reporting instructions and tax liability from the department's taxpayer information and education section of the taxpayer services division. The request **must** be in writing**, contain all pertinent facts** concerning the question presented, and may contain a statement of the taxpayer's views concerning the correct application of the law. The department will advise the taxpayer in writing of its opinion in a tax ruling. The **tax ruling must state all pertinent facts** upon which the opinion is based and, if the taxpayer's name has been disclosed, is binding upon both the taxpayer and the department under the facts stated.

Rule 100(2)(b) (emphasis added). In this case, the ruling at issue addresses the purchase and sale of biofuel; there was no mention of or reference to RINs. As the ruling is silent on the taxation of the RINs, it does not provide any binding position on their taxation, and accordingly, no basis to preclude the imposition of the tax at issue in this case. There was no basis for the Taxpayer to rely

on the letter ruling for the proposition that the sale of RINs was exempt from tax, because the ruling does not address or cover such sales. *See* Det. No. 14-0292, 34 WTD 114 (2015).

Similarly, the Taxpayer asserts that the letter ruling should be read to preclude the imposition of tax on the . . . Contract, focusing specifically on the conclusion of the May 30, 2006, which stated: "Based on the limited information provided, you are not responsible for collecting any other taxes." The Taxpayer asserts that it read this provision as indicating that it was only responsible for the taxes addressed in the ruling.

We note initially, as addressed further below, that the assessment of tax on the . . . project is an issue of work that specifically provided for and listed retail sales tax on the contract and invoicing, but where that tax was not remitted. However, we also disagree with the Taxpayer's reading of the final qualifying statement. The Taxpayer reads this sentence as a blanket assertion that only the taxes specifically addressed are due. We rather read this sentence as a limiting qualification, noting that only limited information has been provided and that the ruling is limited to that specific information. The Taxpayer's interpretation of this conclusion is at odds with the requirements that a binding ruling include all pertinent facts. Here, the facts in the ruling only covered sales of fuel at wholesale or retail and only provided summary information about the transactions. There is no reference to equipment used for processing the fuel or any equipment at all. Again, the ruling does not preclude taxation because the ruling does not address the sale of equipment.

Assessment on Calendar Year:
The statute [limiting the time] for tax assessments is detailed in RCW 82.32.050, which provides:

> No assessment or correction of an assessment for additional taxes due may be made by the department more than four years after the close of the tax year, except (1) against a taxpayer who has not registered as required by this chapter, (2) upon a showing of fraud or of misrepresentation of a material fact by the taxpayer, or (3) where a taxpayer has executed a written waiver of such limitation.

RCW 82.32.050(4).

Thus there is a question of whether the "close of the tax year" applies to the calendar year or the Taxpayer's fiscal year. The term tax year is defined by statute as:

> "Tax year" or "taxable year" means either the calendar year, or the taxpayer's fiscal year when permission is obtained from the department of revenue to use a fiscal year in lieu of the calendar year.

RCW 82.04.020.

In this case, there is no record that the Taxpayer ever requested or the Department ever granted permission to use a fiscal year. Thus, for this Taxpayer, the "tax year" under review during the audit period means a calendar year and "close of the tax year" means December 31st of the year in which the tax liability arose. Audit was correct to conduct a calendar year audit and we deny the Taxpayer's petition on this issue. *Accord* Det. No. 92-295, 13 WTD 160 (1993).

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## DECISION AND DISPOSITION

Taxpayer's petitions are denied.

Dated this 7th day of January 2016.