

Cite as Det. No. 16-0049, 35 WTD 524 (2016)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

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| In the Matter of the Petition for Correction of) | <u>D E T E R M I N A T I O N</u> |
| Assessment of) | |
|) | No. 16-0049 |
|) | |
| ...) | Registration No. . . . |
|) | |

[1] RCW 82.32.140; WAC 458-20-216: SUCCESSORSHIP LIABILITY – INTANGIBLE ASSETS. A contractor is a successor to a defunct corporation when it acquired more than half of the value of the corporation’s intangible assets. Intangible assets include customer testimonials given to a predecessor but used in promoting a successor’s reputation, good name, and integrity.

[2] RCW 82.32.140; WAC 458-20-216: SUCCESSORSHIP LIABILITY – ESTIMATED TAX. A successor is liable for any tax not paid by a predecessor, including a reasonable estimate of tax owed and assessed for failure to file excise tax returns with the Department. A predecessor has the opportunity to challenge an estimated assessment within 30 days of issuance or provide suitable records to show its actual gross sales during the assessment period.

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.

Poley, A.L.J. – A building foundation repair contractor argues that it is not a successor, claiming it acquired less than 50 percent of the predecessor’s intangible assets. We find the contractor is a successor and uphold the assessment of successorship liability.¹

ISSUES

1. Under RCW 82.32.140 and WAC 458-20-216, is a contractor a successor to a defunct corporation when it acquired more than half of the value of the corporation’s intangible assets?
2. Is the [Department of Revenue (Department)] prohibited from assessing successorship liability under RCW 82.32.140 for a predecessor’s estimated taxes?

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

FINDINGS OF FACT

[Corporation], registration number . . . , formed in 2004 and operated a business of waterproofing basements and crawlspaces and remediating damaged building foundations. Corporation recorded business transactions using the cash-basis method of accounting. Since May 2007, [Officer 1] has been identified as a corporate officer for Corporation and the main contact for Corporation's tax reporting account with the Department. [Officer 2] has also been a corporate officer of Corporation since at least May 2014.

Corporation had an agreement with . . . and its related entity, . . . (together, Vendor), to operate as a dealer for Vendor's products and services in As part of their agreement, Vendor would advertise on Corporation's behalf, including creating and maintaining Corporation's websites. Vendor would also funnel potential customers to Corporation. In exchange, Corporation would use techniques and methods developed by Vendor in conjunction with Vendor's patented products, which came with Vendor's transferable, lifetime warranty. Vendor provided marketing materials and product brochures to Corporation, and Corporation was required to use Vendor's proprietary software to manage customer jobs and orders. Vendor also granted to Corporation a non-exclusive, non-sublicensable license to use Vendor's names and trademarks in Corporation's trade name and logo. Corporation paid for the right to be Vendor's dealer.

In 2013, Corporation began having difficulties with Vendor. By the end of May, 2014, Vendor and Corporation ended their business relationship. Corporation no longer received customer leads, advertising, or website support from Vendor, and was unable to order Vendor's products for resale. Vendor also prohibited Corporation from referring to Vendor's products, methods, names, and trademarks, which meant Corporation could no longer use its trade name.

The [Department] assessed \$. . . in unpaid tax against Corporation for various periods between December 2011 and March 2014. When the assessments remained unpaid, the Department issued warrants. On August 1, 2012, the Department issued Warrant No. . . . against Corporation for \$. . . , which included \$. . . of tax. On April 14, 2014, the Department issued Warrant No. . . . against Corporation for \$. . . , which included \$. . . of tax. On June 18, 2014, the Department issued Warrant No. . . . against Corporation for \$. . . , which included \$. . . of tax.

Based on these unpaid warrants, the Department also held a brief adjudicative proceeding to revoke Corporation's certificate of registration.² On September 10, 2014, the Department issued an initial order of revocation against Corporation. On October 30, 2014, revenue agents from the Department visited Corporation's physical location to post the final revocation order and close the business. [Officer 2] was present at the location and indicated she was the office manager. According to Revenue Agent Randy McQuarrie, one of the revenue agents who posted the revocation order, [Officer 2] stated that Corporation had ceased operating in June 2014 after a distributor severed its relationship with Corporation, and the business was now known as ""

Corporation did not file tax returns for the monthly tax reporting periods from April 2014 through October 2014, so on December 12, 2014, the Department issued an estimated assessment

² A business must obtain a certificate of registration from the Department prior to engaging in any taxable activity in Washington. RCW 82.32.030.

based on Corporation's previously reported figures. When Corporation did not pay the assessment, on January 28, 2015, the Department issued Warrant No. . . . against Corporation for \$. . . , which included \$. . . of estimated tax.

Previously, in 2011, [Officer 1] filed a Certificate of Formation of . . . , registration number . . . , with the Washington Secretary of State's Corporations Division and obtained a certificate of registration from the Department. [Officer 1] later changed the name of the entity to [Taxpayer]. [Officer 1] has always been the sole member of Taxpayer.

Taxpayer did not report any business activity to the Department for several years and the Department administratively closed the tax reporting account effective June 30, 2014. In August 2014, [Officer 1] contacted the Department to reopen Taxpayer's account as Taxpayer had obtained a general contractor license and was offering basement waterproofing and building foundation repair services to customers. Taxpayer has since reported gross receipts to the Department at a similar level as Corporation's most recent reported filings.

When Corporation did not pay the four outstanding tax warrants issued against it, the Department investigated and concluded that Taxpayer was Corporation's successor based on the following information:

- Taxpayer and Corporation were both engaged in waterproofing basements and repairing building foundations.
- The Department submitted a demand for payment on Corporation's bond in July 2014, impairing Corporation's contractor license, shortly before Taxpayer obtained its contractor license and began operating.
- Taxpayer's sole member, [Officer 1], was Corporation's longstanding officer and president, lending management experience and business acumen. Taxpayer's office manager, [Officer 2], was also formerly an officer of Corporation.
- Workers, either employees or independent contractors, who previously represented Corporation while on the job with Corporation's customers now represent Taxpayer to Taxpayer's customers. Taxpayer has the advantage of the workers' knowledge, skills, and training.
- Taxpayer and Corporation both reported holding the same contractor's insurance policy, No. . . . , according to the Department of Labor & Industries website.
- Taxpayer and Corporation operated out of the same physical address, . . . , and use the same private mailbox as a mailing address,
- Taxpayer and Corporation have advocated for each other in Departmental actions. Taxpayer was listed as the source of the fax appealing the initial order of revocation of Corporation's business license. Corporation was listed as the source of the fax appealing the denial of Taxpayer's application for a reseller permit.
- Taxpayer uses the same phone number, . . . , that Corporation had listed on its former website. About Us, . . . ; *see* Petitioner's Exhibits, Folder B.
- Between May and December 2014, visitors to one of Corporation's former websites, . . . , were redirected to Taxpayer's current website,
- Taxpayer used Corporation's former website, . . . , and Corporation's email, . . . , when promoting itself as an exhibitor in the . . . RV Show in September 2014.

- Taxpayer relies upon Corporation’s experience to attract new customers. Taxpayer’s website on December 22, 2015, stated:

...

About, . . . (last visited December 31, 2015) (emphasis added). Taxpayer also presents on its website a “case study” of . . . in . . . , who was a customer of Corporation, not Taxpayer. . . . , . . . (last visited December 31, 2015).

- Taxpayer relies upon Corporation’s reputation by publishing testimonials from Corporation’s customers on its website. . . .

On April 16, 2015, the Department issued an Assessment of Successorship Liability against Taxpayer for the unpaid taxes of Corporation for the periods December 2011 through October 2014, in the amount of \$ The Department indicated that if this amount was not paid by May 18, 2015, the Department would amend Corporation’s warrants to name Taxpayer as a legal successor. Taxpayer timely appealed the Assessment of Successorship Liability.

At the hearing, Taxpayer claimed that it did not acquire the majority of Corporation’s intangible assets. Taxpayer asserted that Corporation’s main intangible asset, Corporation’s business relationship with Vendor, was not transferred to Taxpayer. Instead, Taxpayer stated that after Corporation’s relationship with Vendor ended, the business had to “start from scratch” and build a company “from the ground up.” Taxpayer did not provide any information regarding the value of Corporation’s relationship with Vendor other than the relationship was Corporation’s largest intangible asset. Taxpayer also acknowledged that had Corporation attempted to transfer its non-exclusive, non-sublicensable license to use Vendor’s names and trademarks to Taxpayer, Vendor would likely bring legal action against Taxpayer.

Additionally, Taxpayer claimed the insurance policy number shared between it and Corporation is immaterial to a successorship analysis. Taxpayer claimed that the insurance company issued it an insurance policy with the same policy number as Corporation for the insurance company’s internal convenience. Finally, Taxpayer argued that even if it had acquired its workers’ knowledge and skills from Corporation, the value of such expertise is low as many construction workers commonly possess the knowledge and skills to perform Taxpayer’s work.

ANALYSIS

Whenever any taxpayer quits business or sells out, exchanges, or otherwise disposes of more than fifty percent of the fair market value of either its tangible or intangible assets, any tax payable under RCW Ch. 82.32 shall become immediately due and payable. RCW 82.32.140(1). RCW 82.32.140(2) contains the trigger for liability of a successor, and states:

Any person who becomes a successor shall withhold from the purchase price a sum sufficient to pay any tax due from the taxpayer until such time as the taxpayer shall produce a receipt from the department of revenue showing payment in full of any tax due or a certificate that no tax is due. If any tax is not paid by the taxpayer within ten days from the date of such sale, exchange, or disposal, the

successor shall become liable for the payment of the full amount of tax. If the fair market value of the assets acquired by a successor is less than fifty thousand dollars, the successor's liability for payment of the unpaid tax is limited to the fair market value of the assets acquired from the taxpayer. The burden of establishing the fair market value of the assets acquired is on the successor.³

The effect of RCW 82.32.140 is to place on the successor of a business the burden of providing for any outstanding tax liability incurred by its predecessor, and thereby to make the successor secondarily liable for such tax. *Tri-Financial Corp. v. Dep't of Revenue*, 6 Wn. App. 637, 640 (1972). The successor provisions enacted by the legislature are intended to ensure the collection of excise taxes remaining unpaid by a taxpayer who quits, sells out, exchanges, or otherwise disposes of his business or stock of goods. *Id.* at 642. The definition of successorship is not read narrowly. Det. No. 85-215A, 1 WTD 13 (1986), citing *Tri-Financial Corp.*, 6 Wn. App. 637.

A “successor” is defined in RCW 82.04.180(1)(a) as:

Any person to whom a taxpayer quitting, selling out, exchanging, or disposing of a business sells or otherwise conveys, directly or indirectly, in bulk and not in the ordinary course of the taxpayer's business, more than fifty percent of the fair market value of either the (i) tangible assets or (ii) intangible assets of the taxpayer.

Thus, Taxpayer is a successor of Corporation if 1) Corporation quit, sold out, exchanged, or disposed of [its] business; 2) sold or otherwise conveyed, directly or indirectly; 3) in bulk and not in the ordinary course of [its business]; 4) more than fifty percent of the fair market value of either [its] tangible assets or intangible assets; 5) to Taxpayer. *Id.*; Det. No. 05-0313, 26 WTD 27 (2007). Taxpayer's dispute solely relates to the fourth prong.

WAC 458-20-216 (Rule 216) is the Department's administrative rule regarding successor liability. Rule 216(3) [describes] tangible and intangible assets for purposes of the rule, and states:

(a) **Tangible assets.** “Tangible assets” include, but are not limited to, materials, supplies, merchandise, inventory, equipment, or other tangible personal property.

(b) **Intangible assets.** “Intangible assets” include, but are not limited to, all moneys and credits including mortgages, notes, accounts, certificates of deposit; tax certificates; judgments; state, county and municipal bonds; bonds of the United States and of foreign countries; bonds, stocks, or shares of private corporations; personal service contracts; trademarks; trade names; brand names; patents; copyrights; trade secrets; franchise agreements; licenses; permits; core

³ On the other hand, no successor shall be liable for any tax due from the person from whom the successor has acquired a business or stock of goods if the successor gives written notice to the Department of such acquisition, and no assessment is issued by the Department within six months of receipt of such notice against the former operator of the business, and a copy mailed to the successor, or provided electronically to the successor in accordance with RCW 82.32.135. RCW 82.32.140(4). Taxpayer did not comply with this provision so it is not at issue in this appeal.

deposits of financial institutions; noncompete agreements; business name; *telephone numbers and internet addresses; customer . . . lists; favorable contracts and financing agreements; reputation; exceptional management; prestige; good name; integrity of a business*; or other intangible personal property.

(Emphasis added.)

Taxpayer argues that Corporation did not convey its largest intangible asset: Corporation's business relationship with Vendor. However, by the time Taxpayer began operating, Vendor had already severed its relationship with Corporation. Thus, Corporation did not possess a business relationship with Vendor at the time it quit, sold out, exchanged, or disposed of its business. Corporation, therefore, did not have the option to convey or not convey the relationship to Taxpayer as it was no longer an asset of Corporation.

As detailed in Rule 216, "intangibles" include but are not limited to: telephone numbers, internet addresses, customer lists, favorable contracts, reputation, management, prestige, good name, business integrity, or other intangible personal property. Rule 216(3)(b). Here, Taxpayer has acquired the following intangible assets from Corporation:

- Physical address
- Mailing address
- Phone number
- Email address
- Management
- Workers
- Contractor's insurance policy
- Prestige
- Integrity
- Reputation

Taxpayer claims that the value of any expertise obtained from Corporation's management and workers is low as such expertise is not unique. But Taxpayer's website emphasizes the extensive training and certification of its experts and professional teams, indicating that this knowledge is not common or insignificant. While Taxpayer does not have access to Vendor's products or dealer network, Taxpayer's website appears to offer the same contractor services as Corporation; Taxpayer has merely omitted references to trademarked brand names of products previously used. Further, on its website, Taxpayer talks of its "over thirty years combined experience" and company growth, and touts testimonials given to Corporation. Consequently, Taxpayer is relying on Corporation's years in business and customer service for its reputation, good name, and integrity. Taxpayer cannot now disclaim its connection to Corporation to avoid tax liability.

In sum, we conclude that Corporation "directly or indirectly" conveyed the vast majority of its intangible property -- its addresses, telephone numbers, customer list, management experience, contractor expertise, reputation, and goodwill to Taxpayer -- that enhanced Taxpayer's ability to

continue Corporation's business operation and organization with little interruption. Thus, it kept essentially the same business going as a successor.

Further, we do not agree with Taxpayer's contention that the Department should not have assessed estimated tax for the periods after Corporation ceased operating in June 2014. Corporation recognized income on a cash-basis, or when income is actually received by the business. It is foreseeable that a business may receive payments for services up to several months after those services were rendered. Accordingly, the Department acted reasonably when it estimated Corporation's taxes through October 2014.

We also disagree with Taxpayer's argument that the Department cannot assess estimated taxes against a successor. Corporation had an opportunity to contest the estimated assessment when the Department issued the notice of assessment, but did not do so. The statutory consequence is that "[i]f no such petition is filed within the thirty day period the assessment covered by the notice shall become final." RCW 82.32.160. We have no jurisdiction to accept a petition for correction of an assessment once the assessment has become final. Det. No. 15-0115, 34 WTD 537 (2015); Det. No. 03-066R, 23 WTD 243 (2004). RCW 82.32.140(2) explicitly provides, "If any tax is not paid by the taxpayer within ten days from the date of such sale, exchange, or disposal, the successor shall become liable for the payment of the full amount of tax." As a successor, Taxpayer is liable for the amount of tax owed by Corporation with no exception for estimated amounts.

Additionally, because the sole member of Taxpayer is also a corporate officer of Corporation and the sole user of Corporation's electronic filing account, [Officer 1] at all times had the ability to file excise tax returns and provide the Department with actual figures. Taxpayer's member can report Corporation's gross receipts even now, so that the Department may update Corporation's estimated assessment with the actual amount of tax due. It has always been within Taxpayer's member's control to make sure that the estimated assessment reflected Corporation's true tax liability.

For all of the above reasons, we find that Taxpayer is a successor to the business of Corporation and is liable for the taxes assessed against Corporation.

DECISION AND DISPOSITION

Taxpayer's petition is denied and the Assessment of Successorship Liability is upheld.

Dated this 1st day of February, 2016.