

Cite as Det. No. 18-0007, 37 WTD 177 (2018)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS 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>
Assessment of)	
)	No. 18-0007
)	
...)	Registration No. . . .
)	Docket No. 201701-0023
)	

RCW 82.32.140; RCW 82.04.180: DEFINITION OF A SUCCESSOR. Where Taxpayer receives more than 50% of its predecessor’s assets, it is a successor for the purposes of successorship liability.

Headnotes are provided as a convenience for the reader and are not in any way part of the decision or in any way to be used in construing or interpreting this Determination.

Lewis, T.R.O. - Taxpayer protests an assessment of successorship liability. We hold that Taxpayer was a successor because Taxpayer received more than 50% of the predecessor’s assets.¹

ISSUE:

Did Taxpayer receive more than 50% of the predecessor’s tangible or intangible assets, which under the provisions of RCW 82.32.140 and RCW 82.04.180, is required for Taxpayer to be a successor?

FINDINGS OF FACT:

The Department of Revenue’s Compliance Division (“Compliance”) assessed Taxpayer, as successor to the tax liability of . . . (“Predecessor”), for the period January 1, 2011, through June 30, 2015. On December 14, 2016, Taxpayer filed a petition requesting cancellation of the assessment.

The Department audited Predecessor’s business records and issued a \$. . . Tax Assessment No. . . /Audit No. . . . against Predecessor.² Predecessor disagreed with the assessment and filed a Petition for Correction of Assessment. On April 13, 2016, the Department issued Determination No. . . . , which remanded the case to the Audit Division for adjustment. Subsequently, on June

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

² The assessment followed an audit of Taxpayer’s business records for the period January 1, 2011, through June 30, 2015. The \$. . . assessment consisted of \$. . . in tax, \$. . . in interest, and a \$. . . assessment penalty.

20, 2016, the Department issued a \$. . . corrected assessment.³ Predecessor disagreed with the post-assessment adjustment and, on July 29, 2016, filed a petition for correction of the assessment. On August 24, 2016, Predecessor's petition for correction of assessment was denied because the petition was filed late.

On August 25, 2016, the Department's Compliance Division ("Compliance") issued Predecessor a demand for payment. On September 15, 2016, during a conversation with Compliance, Predecessor told Compliance it filed an appeal with the Board of Tax Appeals. Compliance informed Taxpayer that the assessment must be paid and that Compliance would pursue collection of the assessment. On September 20, 2016, Compliance issued Tax Warrant No. . . . with a September 30, 2016, due date. On October 4, 2016, Predecessor closed its account with the Department as of September 20, 2016. On October 5, 2016, Compliance filed Tax Warrant No. . . . with . . . Superior court.

The predecessor operated a restaurant that sold [cuisine type "A"]. The restaurant did not prosper. Recognizing the business was in trouble, Predecessor decided to sell the business. On July 6, 2016, Predecessor and Taxpayer signed a purchase and sale agreement. On July 18, 2016, an addendum/amendment to the purchase and sale agreement agreed that the purchase price was \$. . . with the purchase price allocated among the following assets: Leasehold improvements - \$. . . ; Equipment - \$. . . ; Noncompete Agreement - \$. . . ; and Goodwill - \$

The business sale closed on September 20, 2016. The Closing Statement provided that escrow would hold back \$. . . of Seller's equity for a period of thirty days following the date of closing. On September 26, 2016, the escrow company contacted Compliance to inform the Department that Predecessor was selling the business and to determine if Predecessor had paid its tax liability [and] the Department responded that Predecessor had a \$. . . warrant outstanding. On November 15, 2016, Compliance issued a \$. . . successorship assessment against Taxpayer for the unpaid tax due from Predecessor.

In operating the restaurant, Taxpayer changed the name of the restaurant, the food offering, the telephone number, and the décor of the restaurant. Taxpayer paid Predecessor \$. . . for the restaurant assets, not because it wanted to continue the operation of the successor's failed restaurant operation, but because it wanted to open a [cuisine type "B"] restaurant in the location occupied by Predecessor. Taxpayer maintained that there was a minimal value of tangible and intangible assets transferred from Predecessor to Taxpayer. Taxpayer explained that almost all of the equipment purchased from Taxpayer was dumped, and that because Taxpayer changed the cuisine...there was no carry-over of goodwill.

Taxpayer sought review of this assessment. Taxpayer disputed the successorship assessment because: 1) Predecessor was currently under appeal with the Board of Tax Appeals and, until the appeal was decided, the tax was technically not due; 2) Predecessor's tax warrant did not appear on lien searches; and 3) Taxpayer did not purchase a "major part" of the Predecessor's assets, which represented more than 50% of the fair market value of the Predecessor's total assets.

³ The \$. . . assessment consisted of \$. . . in tax, \$. . . in interest, and a \$. . . assessment penalty.

ANALYSIS

Taxpayer's first challenge to the assessment is that Taxpayer should not be held liable for the tax of a predecessor when the amount of tax liability was uncertain at the time of purchase of the business. Taxpayer argued the amount Predecessor owed the Department was uncertain because an appeal of the assessment was pending before the Board of Tax Appeals.

We disagree and find that the amount of tax owed to the Department was fixed and known at the time of purchase of the business. RCW 82.32.160 provides:

Any person having been issued a notice of additional taxes, delinquent taxes, interest, or penalties assessed by the department, may within thirty days after the issuance of the original notice of the amount thereof or within the period covered by any extension of the due date thereof granted by the department petition the department in writing for a correction of the amount of the assessment, and a conference for examination and review of the assessment If no such petition is filed within the thirty-day period the assessment covered by the notice shall become final.

In this instance, Predecessor took advantage of the Department's internal review process and received a determination, which remanded the matter back to Audit for adjustment. Predecessor's tax assessment became final when the Predecessor did not file for review of the amended assessment by the due date, July 20, 2016. Predecessor appealed that decision to the BTA under RCW 82.03.190. This action does not toll the finality of the Department's assessment. There is no provision in Chapter 82.03 RCW that renders an assessment not final during the BTA's appeal process. Indeed, the DOR can take collection action after the assessment is final and nothing prevents the DOR from collecting unpaid taxes due during a BTA proceeding.

Taxpayer also argued that it should not be held liable as a successor because it was unaware of Predecessor's unpaid tax assessment. RCW 82.32.140 provides that if a taxpayer quits doing business and any tax is not paid within ten days from the date of the disposal "the successor [to that business] shall become liable for the payment of the full amount of tax." RCW 82.32.140(2). If the fair market value of the assets transferred is less than fifty thousand dollars, the successor's liability is limited to the fair market value of those assets. "Successor" is defined as:

- (a) 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;

[RCW 82.04.180(1)(a).]

Taxpayer is, therefore, a successor to Predecessor if: (1) Predecessor quit, sold out, exchanged, or disposed of its business; (2) Predecessor sold or otherwise conveyed, directly or indirectly; (3) in bulk or in the ordinary course of Predecessor's business; (4) more than fifty percent of the fair

market value of either tangible or intangible assets; (5) to Taxpayer. *See* Det. No. 05-0313, 26 WTD 27 (2007).

It is noteworthy that there is no requirement that to be a successor the buyer must be aware of the outstanding tax liability of the predecessor. Here, Taxpayer argues that the successorship assessment should be cancelled because Taxpayer was not aware of Predecessor's unpaid assessment. The fact that Predecessor did not disclose the outstanding assessment emphasizes the importance of asking the Department if the seller has outstanding liability with the Department before closing. In this case, the escrow agent on September 20, 2016, the date of closing, faxed the Department a notice that, on or after September 20, 2016, Predecessor was selling the assets of its business to Taxpayer.

On September 26, 2017, the Department's Taxpayer Account Administration ("TAA") replied with a letter that disclosed that Predecessor had a \$. . . outstanding tax warrant.⁴ The closing statement disclosed that \$. . . of the sale proceeds was withheld for thirty days after closing.

The hold back was presumably made to cover payment of Predecessor's liabilities unknown at the time of closing. The date of closing and the amount of Predecessor's equity holdback were decided by Taxpayer and Predecessor. Closing the sale prior to receiving notice from the Department of Predecessor's account status or without a large hold-back of Predecessor's equity funds was done at Taxpayer's and the escrow agent's peril.

Taxpayer also argues that it is not a successor because it did not receive more than 50% of the fair market value of Predecessor's tangible and intangible assets. RCW 82.32.140 provides that a successor to a person going out of business may in some circumstances be liable for the predecessor's unpaid tax liabilities. Specifically, RCW 82.32.140 provides:

(1) 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 hereunder shall become immediately due and payable, and such taxpayer shall, within ten days thereafter, make a return and pay the tax due, unless an extension is granted under RCW 82.32.080.

[(2) 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.]

WAC 458-20-216(3) ("Rule 216") explains what is meant by tangible and intangible assets:

(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

⁴ The tax warrant had a September 20, 2017, due date. At the time of the Department's reply the tax warrant was past due.

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

Taxpayer changed the name of the restaurant, the food offering, the telephone number, and the décor of the restaurant. Taxpayer asserts that it paid Predecessor \$. . . for the restaurant assets, not because it wanted to continue the operation of the successor’s failed [cuisine type “A”] restaurant operation, but because it wanted to open a [cuisine type “B”] restaurant in the location occupied by Predecessor. Taxpayer maintained that there was a minimal value of tangible and intangible assets transferred from Predecessor to Taxpayer. Taxpayer explained that almost all of the equipment purchased from Taxpayer was dumped, and that, because Taxpayer changed the cuisine. . . , there was no carry-over of goodwill.

Taxpayer’s argument is that it is not a successor because it failed to use the tangible and intangible assets it paid for. RCW 82.04.180’s definition of successor does not require that the buyer use the assets acquired. Rather, the definition only requires that the seller “sells or otherwise conveys . . . more than fifty percent of the fair market value of either the (i) tangible assets or (ii) intangible assets of the taxpayer”

The term “fair market value” is not defined in the statute or the rule. Consequently, we use the term’s common and ordinary meaning. *John H. Sellen Constr. Co. v. Dep’t of Revenue*, 87 Wn.2d 878, 882, 558 P. 2d. 1342 (1976). Washington courts have consistently declared that:

[F]air market value has been generally defined as the value for which the property could have been sold in the course of a voluntary sale between a willing buyer and a willing seller, taking into account the use to which the property is adapted or could reasonably be adapted.

Merchant v. Peterson, 38 Wn. App. 855, 858, 690 P.2d 1192 (1984) (citing *Dillon v. O’Conner*, 68 Wn.2d 184, 186, 412 P.2d 126 (1966)); see also *Potter v. Washington State Patrol*, 165 Wn.2d 67, 196 P.3d 691 (2008) (citing *Merchant v. Peterson*).

Therefore, the only measure of the fair market value of the assets Taxpayer acquired is the \$. . . consideration Taxpayer gave Predecessor for the acquisition of the business, which is a “voluntary sale between a willing buyer and a willing seller.” *Id.*

Accordingly, we conclude that Taxpayer is a successor because all five of the elements contained in RCW 82.04.180(1)(a) have been fulfilled. In making this finding, we have also considered and conclude that no adjustment to the assessment is required by RCW 82.32.140(2), which provides for an adjustment on assessments based on the fair value of the amount of assets acquired by the successor:

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.

(Emphasis added.)

In this case, the value of the assets was presumably less than \$. . . because Taxpayer paid \$. . . for the assets of the business in an arm-length transaction. However, the presumed value of the assets purchased exceeds the \$. . . assessment amount. Because Taxpayer has not met the burden of showing that the fair market value of the assets was less than the assessed amount, the limitation on the successor's liability imposed by RCW 82.32.140(2) does require reduction of the assessment.

DECISION AND DISPOSITION:

Taxpayer's petition is denied.

Dated this 11th day of January 2018.