

Cite as Det. No. 16-0337, 37 WTD 015 (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. 16-0337
)	
... )	Registration No. . . .
)	

[1] RULE 216; RCW 82.04.180; RCW 82.32.140: SUCCESSOR – SUCCESSORSHIP LIABILITY – ACQUISITION OF PREDECESSOR ASSETS – BASIS FOR DETERMINING SUCCESSORSHIP. The determination of whether a person is a successor under RCW 82.04.180(1)(a) is based on the percentage of the fair market value of predecessor’s tangible or intangible assets acquired, notwithstanding the predecessor’s liabilities.

[2] RULE 216; RCW 82.04.180; RCW 82.32.140: SUCCESSOR – SUCCESSORSHIP LIABILITY – LIMITATION OF SUCCESSORSHIP LIABILITY – BURDEN OF PROOF ON SUCCESSOR TO ESTABLISH FAIR MARKET VALUE OF ACQUIRED ASSETS. To limit the amount of successorship liability to the value of the assets acquired from its predecessor, pursuant to RCW 82.32.140(2), a successor has the burden of showing that the fair market value of the assets it acquired was less than \$50,000, notwithstanding predecessor’s liabilities. Assets include both “tangible assets” and “intangible assets.” Tangible assets include, but are not limited to inventory, supplies, equipment, or other tangible personal property. Intangible assets include, but are not limited to, all moneys and credits, accounts receivable, goodwill, customer lists, favorable contracts and financing agreements, intellectual property, and other intangible property.

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.

LaMarche, T.R.O. – A Washington state corporation disputes the Department’s assessment of successorship liability for the unpaid taxes of a defunct business, based on Taxpayer’s acquisition of the business’s assets. We conclude that Taxpayer is a successor and is liable for the unpaid taxes of its predecessor. We further conclude that Taxpayer has not met its burden of proving that the fair market value of the assets it acquired from its predecessor is less than \$50,000. Therefore,

Taxpayer may not limit its successorship liability to the fair market value of the acquired assets. We deny the petition.<sup>1</sup>

### ISSUES

1. Under RCW 82.32.140(1), RCW 82.04.180(1), and WAC 458-20-216 (Rule 216), is Taxpayer liable as a successor for the unpaid taxes of a business whose assets it acquired?
2. If Taxpayer is a successor pursuant to RCW 82.04.180(1) and Rule 216, has it established that the fair market value of the assets it acquired from its predecessor is less than \$50,000, thereby limiting the amount of successorship liability to the value of those assets, pursuant to RCW 82.32.140(2) and Rule 216(5)(c)?

### FINDINGS OF FACT

. . . (Taxpayer) is a Washington corporation that provides telephone answering, messaging, and dispatch services. The Compliance Division (Compliance) of the Department of Revenue (Department) assessed Taxpayer as a successor to the tax liability of . . . (Predecessor), for the periods of January 1, 2006, through March 31, 2010, and January 1, 2011, through July 31, 2015.

Predecessor owned and operated a sole proprietorship, registered with the Department on April 1, 1988, with Tax Registration Account No. . . . , which provided telephone answering and messaging services. Predecessor closed her tax registration account on January 8, 2015. (Compliance Response to Petition (Compliance Response), Exhibit A.) The Department issued Tax Warrant No. . . . in the amount of \$ . . . against Predecessor, filed with . . . Court on November 16, 2011, for the tax periods from January 1, 2006, through March 31, 2010. (*Id.*, Exhibit B.) The Department issued a second warrant, Tax Warrant No. . . . in the amount of \$ . . . against Predecessor, filed with . . . Court on September 15, 2015, for the tax periods from January 1, 2011, through July 31, 2015. (*Id.*, Exhibit C.)

Taxpayer was formed in January 2015, and filed its registration with the Washington Secretary of State on January 6, 2015, listing . . . , Predecessor, as registered agent and president of the company. (*Id.*, Exhibit D.)

On January 8, 2015, [Predecessor] submitted a Business License Application (BLA) to the Department on behalf of Taxpayer, listing herself as the president and sole officer with 100% ownership. (*Id.*, Exhibit E.) The BLA listed the same business address and phone number as Predecessor and indicated that Taxpayer performed the same kind of services as Predecessor. (*Id.*, Exhibits E & F.) The BLA also lists Predecessor's Tax Registration Account No. . . . as a previous business. (*Id.*, Exhibit E.)

On March 3, 2015, the electronic banking information used by Predecessor to make payments toward the Predecessor's tax warrant was changed to that of Taxpayer. (*Id.*, Exhibit G.) Using that

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

account, Taxpayer made \$ . . . in payments from March 3, 2015, through August 21, 2015, towards Predecessor's tax warrant.

Compliance issued a successorship liability assessment against Taxpayer on October 13, 2015, in the amount of \$ . . . , representing tax due, excluding penalties and interest, with a due date of November 12, 2015. Taxpayer filed a petition for correction on October 21, 2015.

In a letter dated December 10, 2015, . . . (President), who succeeded [Predecessor] as Taxpayer's president in January 2015, described the circumstances surrounding Taxpayer's acquisition of Predecessor's assets. *See* Compliance Response, Exhibit M. He explained that [Predecessor] was his grandmother, and that he previously worked for Predecessor for four years writing invoices, but did not have financial decision-making authority or authority to write checks for Predecessor during that time. *Id.* It became apparent to him that there were significant problems with Predecessor's financial affairs and that the business was not being run well. *Id.* He and his grandmother, . . . , jointly decided that he would take over the business, with the goal of making it viable. *Id.*

President stated, in part, "There was no written or verbal understanding that I would provide [Predecessor] with any compensation for transferring the business to me." *Id.* President indicated that his intent was only that Taxpayer would manage the business and satisfy Predecessor's outstanding accounts payable to its contractors, but that Taxpayer would not assume Predecessor's tax liability. *Id.* President stated that when Taxpayer acquired Predecessor, Predecessor had little to no net value, with outstanding lease payments for Predecessor's computer server totaling \$ . . . , outstanding telephone bills of \$ . . . , and an unpaid bill for an information technology technician of \$ . . . . *Id.*

President assumed management of Taxpayer on January 8, 2015, and initially held 20% ownership, while [Predecessor] held 80%. *Id.* President stated that in conjunction with a later business license renewal, his mother, . . . , succeeded him as president. *Id.* He became vice-president, and [Predecessor's] ownership was reduced to 10%. *Id.* He stated that [Predecessor] is part-owner of Taxpayer in name only, and that since the inception of Taxpayer in January 2015, she has not signed any checks and is in no way involved in financial decision-making for Taxpayer. *Id.* He stated that [Predecessor] now works as an employee of the company, but only answers service calls for customers. *Id.*

A telephone hearing was held on January 21, 2016, in which Taxpayer indicated that it acquired the assets of Predecessor in January 2015, that there was no exchange of money, and that there was no written sales contract for the transaction.

In email correspondence dated April 16, 2016, Taxpayer provided a desk appraisal conducted by . . . (Appraiser), an auctioneer and appraiser located [out-of-state], which stated that the fair market value of Predecessor's tangible assets, including telephones, computers, computer peripherals, office furniture and other items, was \$ . . . . Appraiser included his professional profile with the appraisal, which indicated he was a graduate of the Certified Appraiser's Guild of America, was versed in the Uniform Standards of Professional Appraisal Practice, and indicated other bona fides to support his qualification to conduct appraisals. However, the appraisal does not detail the

valuation methodology used, or discuss comparable assets or other information used by Appraiser to value the tangible assets.

Appraiser did not address Predecessor's intangible assets in the appraisal.

In its April 16, 2016, correspondence, Taxpayer also provided a copy of [Predecessor's] 2013 federal form 1040 tax return, showing gross business receipts of \$ . . . , and expenses of \$ . . . . Taxpayer also provided a summary through December 2013, of all of Predecessor's accounts receivable.

Gross annual income for Predecessor for 2014 was \$ . . . . The gross annual income for Taxpayer for 2015, after it acquired Predecessor's assets, was \$ . . . .

### ANALYSIS

RCW 82.04.180 sets out the definition of a "successor" as follows:

(1) "Successor" means:

(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; . . . .

(Emphasis added.) Rule 216, the Department's rule administering successorship, mirrors the statute. *See* Rule 216(2). Here, Taxpayer acquired all of Predecessor's assets, including both tangible assets and intangible assets, which constitutes "more than fifty percent of the fair market value" of either Predecessor's tangible assets or intangible assets. Although Predecessor had significant debt in the form of her own tax liability as a sole proprietor, as well as unpaid leases and other business expenses, RCW 82.04.180(1)(a) is clear on its face, and indicates that the basis for determining whether a person is a successor is based solely on the percentage of assets acquired, notwithstanding the predecessor's liabilities.

RCW 82.32.140 addresses the tax liability of successors, and states as follows:

(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) 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.) *See also* Rule 216.

We address the legislative intent underlying RCW 82.32.140 in Det. No. 14-0153, 33 WTD 534 (2014), and explain,

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.

Here, Predecessor owed taxes to Washington State that she did not pay before her business assets were acquired by Taxpayer. Taxpayer has not shown that Predecessor paid her state taxes within ten days after the date of acquisition. Therefore, notwithstanding President's assertions that Taxpayer did not intend to become liable for Predecessor's taxes, Taxpayer became liable for the payment of the full amount of tax after ten days from the date of its acquisition of Predecessor's assets. RCW 82.32.140. However, because Taxpayer is a "successor" as defined in RCW 82.04.180, Taxpayer is *not* liable for interest or penalties associated with Predecessor's tax liability. RCW 82.32.140; Rule 216(5)(a).

Although we have concluded that Taxpayer is liable as a successor for Predecessor's unpaid tax liability, in certain circumstances successors may limit the amount of their liability for a predecessor's taxes. If a taxpayer proves that the assets it acquired from its predecessor had a fair market value less than \$50,000 at the time of acquisition, the taxpayer's successorship liability for its predecessor's unpaid tax is limited to the fair market value of those assets. RCW 82.32.140(2); Rule 216(5)(c). We note that for purposes of RCW 82.32.140(2) and Rule 216(5)(c), Taxpayer has the burden of establishing the fair market value of the assets it acquired from Predecessor.

Rule 216 defines tangible and intangible assets as follows:

### 3) What are tangible and intangible assets for purposes of this rule?

- (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 deposits of financial institutions; noncompete 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.

Here, Taxpayer produced evidence of the value of Predecessor's assets in the form of an appraisal of tangible personal property, an accounts receivable summary, and a copy of Predecessor's 2013 form 1040 tax return. However, these documents are insufficient to meet Taxpayer's burden of proving the fair market value of all assets it acquired from Predecessor, as required by RCW 82.32.140(2) and Rule 216(5)(c).

First, although Taxpayer provided a statement of value for Predecessor's tangible personal property, the appraisal does not detail the valuation methodology used, or discuss comparable assets or other information used by Appraiser to value the assets. . . . [Under the circumstances, we have not given much weight to the appraisal] in determining the value of the tangible assets it addressed.

Second, although Taxpayer provided evidence of some intangible assets in the form of a summary of Predecessor's accounts receivable, Taxpayer failed to provide evidence of other intangible assets, such as goodwill, customer lists, bank accounts, and contracts existing at the time of acquisition. We note that the gross annual income for Predecessor for 2014 was \$ . . . , and the gross annual income for Taxpayer for 2015, after it acquired Predecessor's assets, was \$ . . . . This indicates that there was significant value in the intangible assets that Taxpayer acquired from Predecessor.

We conclude, therefore, that Taxpayer has not provided complete and reliable proof of the total value of both tangible and intangible property it acquired from Predecessor, as required by RCW 82.32.140(2) and Rule 216(5)(c). Therefore, Taxpayer has not met its burden of establishing that the fair market value of the assets it acquired from Predecessor was less than \$50,000. Accordingly, Taxpayer is liable for the full amount of tax due pursuant to RCW 82.32.140(2). *See also* Rule 216(5)(a). Accordingly, we deny the petition.

#### DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 20th day of October 2016.