Cite as Det. No. 87-111, 3 WTD 29 (1987)

THIS DETERMINATION HAS BEEN OVERRULED OR MODIFIED IN WHOLE OR PART BY DET. NO. 91-126, 11 WTD 319 (1991).

BEFORE THE INTERPRETATION AND APPEALS SECTION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

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. 87-111
. . .	)	Registration No. . . .
	)	Tax Assessment Nos. . . .

[1] **RCW 82.29A .020(2) and RCW 36.34.190:** LEASEHOLD EXCISE TAX -- TAXABLE RENT -- COMPUTATION BY DEPARTMENT -- WHEN AUTHORIZED. The Department may calculate the taxable rent in certain, prescribed situations where the actual rent paid for public property is inadequate. It may not do so, however, where the rate is established in accordance with statutory procedures.

[2] **RCW 82.29A.020(2) and RCW 36.34.190:** LEASEHOLD EXCISE TAX -- TAXABLE RENT -- COMPUTATION BY DEPARTMENT -- WHEN AUTHORIZED. The Department may not establish rates for parking spaces on office building premises where statutory rate-making procedures were followed to fix the office rent.

[3] **RCW 82.29A.010:** LEASEHOLD EXCISE TAX -- PURPOSE -- MANAGEMENT CONTRACT -- GOLF PROFESSIONALS. The purpose of leasehold excise tax is to compensate government for services it provides which are otherwise funded by property tax. Golf pros found to be managing golf courses for county rather than leasing them, so no taxable leasehold interest exists.

[4] **RCW 82.29A.020(1):** LEASEHOLD EXCISE TAX -- LEASEHOLD INTEREST -- POSSESSION ELEMENT -- MOBILE HOT DOG VENDOR. A leasehold interest requires possession as well as use. A seller

> of hot dogs from his own trailer at varying sites within a county fairgrounds is deemed as not having possession of public 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.

TAXPAYER REPRESENTED BY: . . .

DATE OF HEARING: March 13, 1986

NATURE OF ACTION:

Petition to cancel several leasehold excise tax assessments and/or revise the basis on which said assessments were calculated.

FACTS AND ISSUES:

Dressel, A.L.J. -- . . . County (taxpayer) had its books and records audited by the Department of Revenue (Department) for the period January 1, 1981 through June 30, 1985. The limited purpose of said audit was to determine if this governmental entity had reported and remitted the proper amount of leasehold excise tax pursuant to RCW 82.29A. The auditor concluded that the county had not done so and caused to be issued the above-captioned tax assessments in the total amount of $14,416.45. Timely appeal of the assessments has been made by the taxpayer.

Four different issues are presented for our determination. The first relates to the rental of a swimming pool by the county to a nonprofit organization known as the . . . (Association). A written lease agreement exists between the two entities whereby the Association agrees to manage and operate a swimming pool within the confines of a county-owned park. The term of the current lease is five years from May 1, 1984 through August 15, 1989. The rent owed by the Association for that period is a total of $10. Under the agreement the Association is responsible for maintenance of the pool and certain appurtenant structures. The Association is also obligated to carry liability and property damage insurance on the pool. Basically, the entire operation is entrusted to the lessee association. Similar one-season lease agreements existed between the parties for 1982 and 1983 which called for similar, nominal rent.

In its audit report the Department asserts that:

> Rental for the lease of [this] county property was not considered in the lease agreement. According to RCW 82.29A.020(2)(b), when rent for publicly owned property has not been negotiated the department may establish a taxable rental. To accomplish the above, we used the construction cost figure plus the land value at a five percent rate of return. (Bracketed inclusion ours.)

That five percent rate became the basis for the Department's determination of the taxable rent which is the measure of the amount of leasehold excise tax due. RCW 82.29A.030. Whether the

assessment of leasehold excise tax is proper under these circumstances is the first question to be answered.

Question number two involves the rent charged for the lease of certain county-owned parking spaces. The county owns the . . . office building which is across the street from the county courthouse in . . . . The county leases office space in that building to the law firm of . . . . With the office space the law firm gets 11 parking spaces adjacent to the building for which it pays two dollars per month per space. In the audit the Department determined that such a rate was below market so it proceeded to determine a more realistic rate and assessed additional leasehold excise tax based on the higher figure. Such action was taken pursuant to RCW 82.29A.020(2)(b). The county objects and says that two dollars per month is representative of the going rate for long-term parking in the vicinity of the courthouse.

Thirdly is the matter of leasehold tax claimed due for the alleged leasehold interest of two golf professionals hired by the county. For the purpose of operating the two golf courses it owns, the taxpayer entered into identical contracts with two different pros. The agreements call for the pros to operate, manage and supervise . . . and . . . golf courses. Among their duties are enforcement of the rules of golf, regulation of the play and conduct of the players, collection of greens and other fees, rental of carts, rental of clubs, selling of golf equipment and accessories through the pro shop on the premises, operation of the restaurant in the clubhouse, the giving of golf instruction, hiring of adequate staff, operation of the driving range, and others. The only significant portion of the golf course for which the pros are not directly responsible is the maintenance of the greens and fairways. As compensation for their services the golf pros receive a $19,200 annual salary plus certain percentages of the income from various sources such as greens fees (two percent), restaurant, driving range and cart rental. The pros receive 90 percent of gross revenue from restaurant sales and all revenue from pro shop sales.

It is contended by the Department that the use and occupancy by the pros of the golf course clubhouse creates a leasehold interest. Each pro owns the food and drink served in the restaurants, the merchandise dispensed from the pro shops and the power carts which are stored on the golf course grounds which are owned by the county. Such an arrangement, it is argued, is a leasehold subject to leasehold excise tax based on the percentage payments to the county from the restaurant and driving range income. The issue, then, is whether the relationship between the taxpayer and the pros is subject to leasehold excise tax and, if so, to what extent.

Lastly is the matter of a mobile vendor at the county-owned fairgrounds. The gentleman under consideration does business under the name . . . . He sells hot dogs, hamburgers, soft drinks and assorted snack items at various events which are staged at the fairgrounds from mid-April through mid-September. Sales are made from a trailer which he moves about the grounds according to the event, be it a horse show or whatever. The vendor pays the county a percentage of his gross sales. There is no written agreement between the parties. The vendor is not confined to a particular space, but he is generally free to locate his trailer wherever he is not interfering with the event in progress. Both the inventory of food and the trailer are owned by the vendor. The Department has taken the position that the vendor enjoys a taxable leasehold interest in the county's property at the fairgrounds. Whether that is true is the fourth question to be answered in this appeal.

DISCUSSION:

The issues will be addressed in the order presented in the previous section which means . . . Pool is first. Leasehold excise tax is imposed under the following authority:

RCW 82.29A.030 Tax imposed---Credit---Additional tax imposed. (1) There is hereby levied and shall be collected a leasehold excise tax on the act or privilege of occupying or using publicly owned real or personal property through a leasehold interest on and after January 1, 1976, at a rate of twelve percent of taxable rent: Provided, That after the computation of the tax there shall be allowed credit for any tax collected pursuant to RCW 82.29A.040.

(2) An additional tax is imposed equal to the rate specified in RCW 82.02.030 multiplied by the tax payable under subsection (1) of this section.

As indicated, the tax is imposed on those holding property through a "leasehold interest" which term is defined thusly:

RCW 82.29A.020 Definitions. As used in this chapter the following terms shall be defined as follows, unless the context otherwise requires:

(1) "Leasehold interest" shall mean an interest in publicly owned real or personal property which exists by virtue of any lease, permit, license, or any other agreement, written or verbal, between the public owner of the property and a person who would not be exempt from property taxes if that person owned the property in fee, granting possession and use, to a degree less than fee simple ownership . . .

"Taxable rent" is the measure of the leasehold excise tax. RCW 82.29A.030. A percentage figure is applied to the "taxable rent" to determine the amount of tax. "Taxable rent" is defined at RCW 82.29A.020 as:

(2) "Taxable rent" shall mean contract rent as defined in subsection (a) of this subsection in all cases where the lease or agreement has been established or renegotiated through competitive bidding, or negotiated or renegotiated in accordance with statutory requirements regarding the rent payable, or negotiated or renegotiated under circumstances, established by public record, clearly showing that the contract rent was the maximum attainable by the lessor: . . .

"Contract rent" is defined in subsection (a) in pertinent part as "the amount of consideration due as payment for a leasehold interest . . ."

Subsection (b) of the same statutory provision states:

(b) If it shall be determined by the department of revenue, upon examination of a lessee's

> accounts or those of a lessor of publicly owned property, that a lessee is occupying or using publicly owned property in such a manner as to create a leasehold interest and that such leasehold interest has not been established through competitive bidding, or negotiated in accordance with statutory requirements regarding the rent payable, or negotiated under circumstances, established by public record, clearly showing that the contract rent was the maximum attainable by the lessor, the department may establish a taxable rent computation for use in determining the tax payable under authority granted in this chapter based upon the following criteria: (i) Consideration shall be given to rental being paid to other lessors by lessees of similar property for similar purposes over similar periods of time; (ii) consideration shall be given to what would be considered a fair rate of return on the market value of the property leased less reasonable deductions for any restrictions on use, special operating requirements or provisions for concurrent use by the lessor, another person or the general public.

Contrary to the auditor's assertion rental was considered in the lease agreement even though, at $10 for five years, it is in a nominal amount. According to the county, that figure was the result of compliance with statutory procedures prescribed in RCW 36.34 which deals with county property. More specifically, the county claims:

> . . . Prior to executing each agreement with the . . . Pool Association, the Board [of County Commissioners] complied with the requirements of RCW 36.68.010 requiring park property be declared surplus to the needs of the County or no longer suitable for park purposes and the provisions of RCW 36.34 et seq. Pursuant to RCW 36.34.160 the Board gave notice of intention to lease the . . . Pool and held a public hearing to consider the lease according to RCW 36.34.180, .190 and .200. RCW 36.34.190 prohibits the Board from making a lease with anyone other than the highest responsible bidder. The . . . Pool Association was the highest responsible bidder at the public hearing. Public records, available to the Department during the audit, which document that all agreements referenced in this petition including the . . . Agreements, were established and negotiated in accord with applicable statutes, will be submitted at the conference. (Bracketed inclusion ours.)

Documentation, submitted as promised at the conference in this matter, confirms adherence by the county to the referenced statutory guidelines. Included is evidence that a formal application to lease the pool was received pursuant to RCW 36.34.150, that notice of a public hearing on the proposed leasing of the pool was published in a county newspaper and the courthouse bulletin board per RCW 36.34.160, that objections to the . . . application were entertained at the hearing per RCW 36.34.170, and that the lease was made to the highest responsible bidder per RCW 36.34.190.

[1] According to RCW 82.29A.020(2)(a) and (b), the Department may compute the taxable rent only if none of the following three situations exist: (1) the leasehold interest has been established through competitive bidding, (2) the rent was set according to statutory requirements, or (3) public records demonstrate that the rent was the maximum attainable. Here, clearly the rent was set according to the statutory requirements of RCW 36.34. The lease was executed with the highest

and, presumably, the only bidder in compliance with RCW 36.34.190. Not only that, but also situations (1) and (3) probably do exist as well. The procedure used by the county provided a forum for competitive bidding even though there may not have been other bidders and public records, at least those supplied by the taxpayer, do not demonstrate that the pool could have been rented for more money. As pointed out by the taxpayer, the costs of maintaining a public pool are considerable, insurance costs are consequential, the swimming pool season in . . . is short, and the potential for making a profit from such an operation is negligible. Those factors considered, it is not particularly surprising that no responsible party bid more than $10 to lease the pool.

In any event, because there was compliance with statutory guidelines regarding the rent payable, the actual amount agreed upon is irrelevant. Also, because of the statutory compliance, the Department is not free to decide upon what it believes to be a reasonable amount and to then use such amount as the measure of the leasehold excise tax. Since there has been the referenced statutory compliance, taxable rent upon which the tax is based is the same as contract rent. RCW 82.29A.020(2). Contract rent is the amount of consideration due as payment for a leasehold interest. RCW 82.29A.020(2)(a). The amount due here is either $10 for $100 depending on the year and those amounts, properly prorated accordingly to the length of the particular contracts in force for the year under consideration, shall be the measure of the leasehold excise tax.

As to issue number one, the . . . swimming pool, the taxpayer's petition is granted.

[2] Issue number two has to do with the parking spaces leased by the county to the law firm of . . . . As with the swimming pool, the auditor has determined that the law firm is paying less than the market rate. Inasmuch as the rental amount is only two dollars per space per month, she is undoubtedly correct. She has calculated a figure she perceives to be more realistic and assessed leasehold tax based on that figure. The problem with that is the same one encountered with the swimming pool. The Department does not have unfettered discretion to disturb a rental rate it regards as unreasonable. It may only do so where none of the three situations cited in RCW 82.29A.020(2)(a) exist. Relative to the parking spaces, the taxpayer has produced the same sort of documents as referenced in the above discussion of the swimming pool issue. These include resolutions by the county commissioners, notices of public hearings, several lease agreements, correspondence with the official county newspaper, etc. Taken together these various documents establish that the office space in the . . . Building was also leased to the highest responsible bidder pursuant to the statutory prescription of RCW 36.34, et seq. The only difference between this situation and the swimming pool is that the various notices and resolutions refer to the office space as opposed to the 11 parking spaces per se. The parking spaces are separately provided for in the lease agreement but were not mentioned in the resolutions or public notices.

This factual variation is not significant enough, however, to cause a different result to be reached here as compared to that reached on the pool issue. It is common knowledge that office buildings frequently provide on-premises parking for tenants, clients, customers, visitors, etc. It is also common that certain spaces are blocked off for use by certain tenants. Such an arrangement provides a significant convenience as well as business advantage to the tenants of the building. In the instant situation, the law firm undoubtedly recognized this fact and reflected it in the amount bid for the office space. Had parking not been part of the bargain, it is presumed the law firm would

have insisted on an office rental rate less than the $23,250 it is presently paying. The upshot of all this is that even though the lease agreement clause says the lessee shall pay two dollars per month each for 11 parking spaces, any inadequacy in that amount is offset in the amount paid for rental of the office space. That amount has been fully subjected to leasehold tax and, when combined with additional tax at the two-dollar rate, fully covers the parking spaces from a leasehold tax point of view.

Furthermore, no need is seen to fragment the statutory rate-making procedure that the county has gone through to find a lessee and rental rate for the office space. It would be illogical and impractical to in effect require the county to conduct a separate notice and hearing procedure on the parking spaces only. It is our finding that the above-mentioned statutory formalities undertaken by the taxpayer are sufficient for the purpose of setting the parking space rate as well as the office space rate and that the Department, therefore, is precluded from rejecting the former for the same reasons indicated in the discussion of the swimming pool issue.

On issue number two, the parking spaces, the taxpayer's petition is granted.

Issue number three concerns the golf professionals and whether they have leasehold interests in the golf course operations with which they are associated. The intent of the legislature in enacting the leasehold excise tax law is expressed statutorily as follows:

> **RCW 82.29A.010 Legislative findings and recognition.** The legislature hereby recognizes that properties of the state of Washington, counties, school districts, and other municipal corporations are exempted by Article 7, section 1 of the state Constitution from property tax obligations, but that private lessees of such public properties receive substantial benefits from governmental services provided by units of government.
>
> The legislature further recognizes that a uniform method of taxation should apply to such leasehold interests in publicly owned property.
>
> The legislature finds that lessees of publicly owned property are entitled to those same governmental services and does hereby provide for a leasehold excise tax to fairly compensate governmental units for services rendered to such lessees of publicly owned property.

[3] We do not believe that the legislature intended that leasehold tax be extended to the kind of situation here being considered.

First, RCW 82.29A.010 can be interpreted to mean that the legislature, in enacting the leasehold excise tax, intended to exact a tax on private users of public property for private purposes. If the private user of the public property is using the property in furtherance of the public owner's purposes, then it is the public owner, not the private user, which benefits from governmental services rendered in respect to such property. Since the tax is intended to compensate units of government for services rendered to private users of public property it would not apply if such services are actually rendered to the public owner. Here, the purpose for which the private parties

are using public property is to run the county's golf course operations. This purpose is an integral part of the county's overall program of providing recreational opportunities for the health and welfare of its citizens through parks, camping and picnicking areas, hiking trails, ski areas and the like. These golf courses are operated as a service to the public. Somebody has to assume the responsibility that that service is rendered, and the golf pros involved in this case are the people the county has hired for that purpose.

Second, we do not believe that the agreements create a leasehold interest. In order for the tax to apply, there must be a leasehold interest. RCW 82.29A.030(1). The agreements create an obligation on the golf pros' part to manage and operate the two courses under the control of the county commissioners and the county's parks and recreation director. Incidental to that obligation golf pros have been provided the use of public property. RCW 82.29A.020(1) provides that a leasehold interest is one which grants "possession and use" of public property. It is clear that the pros have use of public property. However, both possession and use are required for a leasehold interest to arise. Possession is not defined by the statute but must have a meaning beyond that of mere use. In our opinion the pros in this case do not have possessory interest in the public property other than that arising from its use of the property. Such use that it does have is restricted to the purposes of the county and its parks department. The county may displace the golf pros from the areas they use. The pros are obligated to take reasonable care of the equipment they use, but this is only a condition attached to that use. Basically, the agreements provide that the golf pros will manage and operate the two courses and that in the course of performance of the agreements the pros will use public property. Such use is subordinate and incidental to the express purpose of the agreements and in our opinion does not amount to "possession and use" and therefore does not create a leasehold interest. In short, the golf pros run the two courses but they do not rent them.

The auditor has said that the pros have use and occupancy of the golf course clubhouses and that that is a leasehold interest. She then proceeded to assess leasehold tax based on percentages of receipts from the restaurants and the driving ranges. Apparently, she also believes that the pros have use and occupancy of the driving range. We are not sure why she singled out those two aspects of the operation. It could also be said that the pros have use and occupancy of the golf course itself, the golf cart sheds, the outbuildings in which maintenance equipment is housed, the parking lots, the putting greens, etc. Also, what about the pros' use of the "pro shop" portion of the clubhouse in which they stock and sell an inventory of golf equipment owned by them without remitting any percentage of the receipts to the county? It would seem that portion of the business would be a better candidate for leasehold tax than any other in that the pros have more independence in running it than they do other portions of the business and none of the profits from the pro shop flow to the county. The pros have more dominion and control of this department than others, yet it was not subjected to tax.

In reality, we don't think it should have been, but neither do we think the restaurant or driving range should have been. All operations are part of the county's plan in providing a golf program to the public. The agreement between the pros and the county which is labeled "Golf Pro Contract" requires that the pros maintain a quality pro shop, a restaurant and a driving range in addition to a number of other things. In operating those facilities the pros are carrying out the stated wishes and objectives of the county. In other words, a primarily public purpose rather than a private one is

being served. As stated earlier, the theory of the leasehold excise tax is that private users of public property should be monetarily responsible to governmental entities which provide them services. Here, we don't have a private "user" of public property, we have a private "operator" of public property for a public purpose. Thus, governmental services rendered in respect to the property are rendered on behalf of the public party, the county. The fact the governmental services may to some extent also be rendered to the golf pros in that fire departments presumably would also attempt to save their pro shop and restaurant inventories is insignificant. Even though the pros own those inventories the county, like it does in the entire golf course operation, has an interest in them as well in that they are necessary to effectuate the county's stated purposes.

For the above listed reasons, we hold that the arrangement between the taxpayer and the golf pros is a management contract, not a leasehold interest. We also find no valid basis for imposing leasehold tax on selected components of the operation.

On issue number three, the golf professionals, the taxpayer's petition is granted.

Fourthly, the issue of the mobile vendor at the fairgrounds will be considered. As indicated previously, the leasehold statutory scheme contemplates some kind or degree of possessory interest in addition to mere "use" of the premises. In particular, RCW 82.29A.020(1)(a) defines leasehold interest as:

> . . . an interest in publicly owned real or personal property which exists by virtue of any lease, permit, license, or any other agreement, written or verbal, between the public owner of the property and a person who would not be exempt from property taxes if that person owned the property in fee, granting possession and use, to a degree less than fee simple ownership . . . (Emphasis added.)

[4] The vendor has something less than possession of the county's premises. He is not put in control of any real estate at the fairgrounds. He is simply given the right to sell his "food products" somewhere on the grounds. Such a right is more properly termed a "franchise" than a leasehold interest because the necessary element of possession is lacking. In the leading case on leasehold tax the Washington Supreme Court in Mac Amusement Co. v. Department of Revenue, 95 Wn.2d 963, 633 P.2d 68 (1981), quoted with approval Washington Water Power Company v. Rooney, 3 Wn.2d 642, 101 P.2d 580, 127 A.L.R. 1044 (1940), which quoted E. McQuillin Municipal Corporation § 1740 (2 ed. 1943). The court said a franchise is:

> . . . the right granted by the state or a municipality to an existing corporation or to an individual to do certain things which a corporation or individual otherwise cannot do . . .

Accord, Artesian Water Company v. State Department of Highways and Transportation, 330 A.2d 432 (Del. Super. Ct.), aff'd as modified; 330 A.2d 441 (Del. 1974).

Again, the leasehold statutory definitions contemplate some kind or degree of possessory interest in addition to mere "use" of the premises. Here, there was none. The only right granted and paid for

under the oral agreement was the right to make sales on the county's property. For a leasehold interest to be found, a greater degree of dominion and control over a more defined area must be present to satisfy the possession element of the RCW 82.29A.010(1) definition.

Such an interpretation is consistent with RCW 82.29A.020(2)(a) wherein "contract rent" is defined and discussed. Said statute says in part:

> Where the consideration conveyed for the leasehold interest is made in combination with payment for concession or other rights granted by the lessor, only that portion of such payment which represents consideration for the leasehold interest shall be part of contract rent.

The conclusion to be drawn from that sentence is that concession rights are not taxable, and concession rights are all that the vendor received and paid for in the instant case.

On the fourth issue, the fairgrounds vendor, the taxpayer's petition is granted as well.

DECISION AND DISPOSITION:

The taxpayer's petition is granted in its entirety. An amended assessment consistent with this Determination will be issued forthwith. The balance due, if any, will be payable on the date indicated on the new assessment with interest thereon cancelled for the period after June 13, 1986 because the due date will have been extended for the convenience of the Department.

DATED this 14th day of April 1987.