

Cite as 10 WTD 51

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

In the Matter of the Petition)	<u>D E T E R M I N A T I O N</u>
For Correction of Assessment of)	
)	No. 90-257
)	
. . .)	Registration No. . . .
)	Warrant Nos . . ., . . .
)	

[1] RULE 216: EXCISE TAXES -- SUCCESSOR LIABILITY -- BONA FIDE PURCHASER OF ASSETS -- PARTIAL PAYMENT OF PREDECESSOR'S DEBTS. Taxpayer purchasing assets of a defunct business from the IRS does not become successor notwithstanding the fact that it pays certain dishonored checks or past-due obligations of the predecessor.

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: . . .

NATURE OF ACTION:

Taxpayer petitions for correction of determination of successor liability on grounds it purchased the predecessor's assets from a bona fide third party, the Internal Revenue Service.

FACTS AND ISSUES:

Adler, A.L.J. -- Taxpayer, a corporation, is engaged in the business of selling and servicing office equipment and supplies. The two key parties (H&B) running the corporation previously were employed by another similar or identical business.

The prior business was a corporation owned by a sole shareholder (SH). For numerous years, SH's corporation was in Chapter 11 bankruptcy; SH used the business assets as a debtor in possession; and SH ran the business under at least two similarly-named, properly-registered corporations.

Shortly before disbanding this business in all its forms altogether, SH incorporated again with the Washington Secretary of

State under a new, different name [C]; and SH used a form of incorporation which does not require the naming of the shareholders. This final entity never registered with the Department of Revenue.

An undated Letter of Intent signed sometime before December, 1989, by the sole shareholder (SH) of the three aforementioned entities and by H&B states that SH

agrees to sell to H&B all of the assets of [C] free and clear of all liens, encumbrances, except as may be approved by H&B. . . . in consideration for the expense and investment of effort by H&B to investigate a purchase of the business, [SH] grants to H&B the option to purchase the business, exclusively effective the date of this Agreement, which option shall expire on March 1, 1990, unless theretofore exercised by H&B or its assigns.

The Internal Revenue Service seized the prior corporation or corporations' assets by November 1,

The seized assets were sold to H&B at an IRS auction on November 3,

On December 9, . . . , SH was notified that H&B

have elected to terminate their obligations under the Letter of Intent effective immediately. My clients have discovered numerous and substantial indebtedness to various taxing authorities and business creditors that they are financially unable to assume. Furthermore, their review of the financial condition of the business has resulted in a drastic reappraisal of its worth. As you know, all of the corporate assets were seized by the IRS and resold on an auction basis to pay the delinquent tax of your business.

The Department of Revenue determined that H&B had paid some of the predecessor's past-due obligations and replaced some dishonored paychecks. Taxpayer was notified of successor liability for the full amount of the predecessor's tax debt; or, alternatively, it was determined to be a successor at least up to the amount of the payments for the predecessor's obligations.

DISCUSSION:

[1] A "successor" is one who obtains business assets from a person quitting or disposing of a business. RCW 82.04.180. WAC 458-20-216 (Rule 216) is the administrative rule implementing the statute. It has the force and effect of the law. RCW 82.32.300.

Rule 216 contains several examples of when successorship liability will and will not attach. It is impossible for an administrative rule to furnish examples of every conceivable situation which could arise, so the examples contained in the rule serve as guidelines to be followed in determining whether or not a change of ownership or transfer of stock constitutes a successorship.

The case at hand fits most nearly the principles of illustrations (6)(a) and (7)(b). The Internal Revenue Service possessed a higher-priority tax lien and seized the assets to satisfy all or part of the federal tax debt. As a "repossessor" of the property, the IRS was not a successor. Additionally, persons purchasing from the IRS and continuing the business are not successors. Rule 216(6)(a). The IRS is also in a similar position to an assignee. A purchaser from the assignee is not a successor "unless under the terms of the purchase agreement he assumes and agrees to pay taxes and/or lien claims." Rule 216(7)(b). No such assumption occurred here.

Alternatively, the Department argues that the purchasers should be liable to the state for payment of taxes up to the amount of payments it made to creditors of the predecessor or to employees for dishonored paychecks. We disagree. There are no Washington tax cases directly on point. However, in another successorship case, the Washington Court of Appeals held that voluntary payment of certain debts of a predecessor corporation by its successor does not create an inference that the successor has assumed responsibility for other debts of the predecessor. Long v. Home Health Services, 43 Wn. App. 729 (1986), review denied, 106 Wn.App. 1012 (1986).

We are aware that H&B's attorney advised them to terminate their obligations under the Letter of Intent and to possibly "renew discussions [with the predecessor] regarding the purchase of your interest in whatever assets may remain." December 9 letter. However, the facts indicate that no such purchase or discussions occurred. Although H&B took advantage of events to purchase the business without the liabilities, they exercised business sense and acted legally in doing so. In the absence of an agreement to assume liabilities of the predecessor, either at the time of the IRS sale or through exercise of the option granted in the letter of intent, we find this action does not subject the purchasers to successorship liability.

DECISION AND DISPOSITION:

Taxpayer's petition is granted.

DATED this 25th day of June, 1990.