

Cite as Det. No. 88-313, 6 WTD 285 (1988)

THIS DETERMINATION HAS BEEN OVERRULED OR MODIFIED IN WHOLE OR PART BY DET. NO. 97-121, 17 WTD 64 (1998)

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 Refund of)	
)	No. 88-313
)	
...)	Registration No. ...
)	
)	
AS SUCCESSORS TO:)	
)	
...)	Registration No. ...
)	
)	

- [1] **RULE 216 and RCW 82.04.180: EXCISE TAXES -- SUCCESSOR LIABILITY -**
- PROPERTY PEACEFULLY REPOSSESSED UNDER SECURITY AGREEMENT. Taxpayer is not liable as a successor if it merely takes possession of tangible personal property pursuant to a security agreement, nor is it liable if it operates the business temporarily as a means of liquidating the property repossessed. Where taxpayer operates the same type of business in the same location as its debtor, it is a successor by virtue of having succeeded to the business.

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 AND PLACE OF CONFERENCE: July 6, 1988; Tacoma, Washington

NATURE OF ACTION:

Taxpayer, who was deemed to be the successor to another business, petitioned for refund of taxes

assessed to it under the successorship statute, RCW 82.32.140.

FACTS AND ISSUES:

Johnson, A.L.J. -- Taxpayer is a corporation, the principal business of which is the operation of a warehouse selling automobile parts. Taxpayer's customers are generally automobile parts stores, which sell to businesses, such as gas stations, on credit and which transact at least some sales with individuals buying for personal use.

In the course of taxpayer's business, it customarily arranges for such automobile parts stores to obtain a line of credit through a local bank. Taxpayer guarantees such loans and secures them with perfected security agreements pursuant to RCW 62A.9, Washington's Uniform Commercial Code statutes.

The debtor in the present case was a chain of auto parts stores, which obtained a line of credit through the taxpayer. The original indebtedness was acquired in 1983 and refinanced in 1985; additional credit was extended in 1986. Taxpayer properly perfected its security interest in all of the debtor's fixtures, accounts receivable, goods, machinery, equipment, inventory and merchandise. Three of the four stores remaining in the chain at the time of default were operated in small towns, and taxpayer notes that the those stores had a loyal clientele because of the stores' good will in the community. On September 5, 1986, the defaulting debtor voluntarily surrendered the collateral without a breach of the peace, pursuant to a surrender agreement. Taxpayer immediately closed the debtor's four auto parts stores for a complete inventory of all property. A substantial percentage of the property was of a kind not sold by the taxpayer in its warehouse operation or was equipment unlikely to be saleable from the warehouse. Two of the debtor's stores, [Store A] and [Store B], were never reopened or operated again. The third store, [Store C], was located in the largest of the four communities. That store was reopened and briefly operated as a means of disposing of the debtor's property, which would not have been easily disposed of in any other manner. The fourth store, [Store D], was operated for fifteen months, until a buyer for the store could be found. At this store, taxpayer sold off the debtor's equipment and stock and then replenished it with its own merchandise.

Taxpayer contends that it is not a successor to the business of the debtor, because it never intended to step into the debtor's shoes and enter the auto parts business in that manner in those locations.

DISCUSSION:

[1] RCW 82.04.180 states that "successor"

means 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, a major part the materials, supplies, merchandise, inventory, fixtures or equipment of the taxpayer. (Emphasis supplied.)

This statute requires that the debtor in the present case have sold or conveyed its merchandise to the creditor-taxpayer in order for successor liability to attach to the creditor. No sale or conveyance

occurred in this instance. The taxpayer was forced by the debtor's default to seize the collateral.

WAC 458-20-216 (Rule 216) is the administrative rule implementing the above statute. It has the same force and effect as law. RCW 82.32.300. That rule provides that "successor" includes persons who acquire the predecessor's business in bulk, whether they operate the business or not

unless the property is acquired through insolvency proceedings or regular legal proceedings to enforce a lien, security interest, judgment, or repossession under a security agreement. (Emphasis added.)

Rule 216 lists factual situations intended to show when successorship liability will attach. Situation 6 expressly declares that when the debtor purchases stock under a security agreement and the property is repossessed by the vendor, the vendor is not a successor. Rule 216's factual situations are not intended to be exclusive. In this case, the debtor purchased goods under a line of credit extended by a bank and guaranteed by the taxpayer, who perfected a security interest in the debtor's property. Upon default, the taxpayer moved to enforce a security interest. Such an action, like the action of a vendor in Situation 6, should not subject the taxpayer to successor liability with regard to the two stores which were immediately closed or to the third store, which was closed as soon as the stock was liquidated.

The creditor-taxpayer in this case was a properly-secured party pursuant to RCW 62A.9, Washington's Uniform Commercial Code statutes. Following the statutory requirements of that section, taxpayer took steps to recover some or all of the value of moneys loaned to the debtor. RCW 62A.9-503 permits the secured party to take possession after default and additionally provides that

[i]n taking possession a secured party may proceed without judicial process if this can be done without a breach of the peace or may proceed by action.

In this case, repossession of the debtor's property was possible without resort to further legal action, because the debtor voluntarily signed a surrender agreement and vacated the premises. Such a surrender facilitating seizure of the debtor's property by the taxpayer was not a sale or conveyance of such property. It simply permitted seizure of the collateral to occur without a breach of the peace.

As its next step, the taxpayer attempted to recover some of its loaned funds by exercising its right under RCW 62A.9-504 to dispose of the debtor's collateral after the default. That statute provides that

[a] secured party after default may sell, lease or otherwise dispose of any or all of the collateral in its then condition or following any commercially reasonable preparation or processing. [Emphasis supplied.]

Further, RCW 60.10.030, governing the rules of sale in summary foreclosure cases, provides that

[s]ale or other disposition may be as a unit or in parcels at any time and place and on any terms but every aspect of the disposition including the method, manner, time, place and terms must be commercially reasonable which shall be construed as provided in RCW 60.10.070. [Emphasis supplied.]

RCW 60.10.070 provides that "commercially reasonable" includes the following conduct:

[i]f a lien holder either sells the collateral in the usual manner in any recognized market therefor or if he sells at the price current in such market at the time of his sale or if he has otherwise sold in conformity with reasonable commercial practices among dealers in the type of property sold he has sold in a commercially reasonable manner. [Emphasis supplied.]

Taxpayer has demonstrated that, with regard to three of the stores, it disposed of the property in the only commercially-reasonable manner available. It closed all four of the stores immediately upon seizure for inventory of the property. Because the property was either of a type not carried by taxpayer in its warehouse operation or was of a type not easily disposed of in a location different from the ones in which it was then located, the taxpayer chose to move the property from the two stores which were then going to remain permanently closed into the store in the largest community in hopes that it would be able to sell the merchandise for a price close to its actual value. That store was closed permanently shortly thereafter. Such behavior is within the definition of "commercially reasonable" and represented a business decision to try and minimize the losses involved. Taxpayer followed the procedures required by the Washington statutes governing secured creditors' rights and summary foreclosure and did not become a successor to the business of the debtor as to [Stores A, B and C].

However, Rule 216 further defines a successor as

any person who shall, through direct or mesne conveyance, purchase or succeed to the business, or portion thereof, or the whole or any part of the stock of goods, wares, merchandise or fixtures or any interest therein of a taxpayer quitting, selling out, exchanging or otherwise disposing of his business. [Emphasis supplied.]

Under Rule 216, taxpayer did "succeed to the business" of the debtor with regard to [Store D]. Taxpayer acknowledges that three of the stores were located in small communities and derived their business largely from repeat customers won by good will. [Store D], which was operated by the taxpayer for fifteen months before a buyer was found, was one of the stores in the small communities. Taxpayer operated [Store D] in the same location under the store's original name, sold the debtor's stock and replaced such stock with its own merchandise from September of 1986 until December of 1987. Taxpayer admits that good will in a small community was certain to be an important part of the attractiveness of the store to a prospective buyer and that it made a business decision to operate the store in the manner chosen. That business decision subjects taxpayer to liability for taxes owed which are attributable to [Store D].

DECISION AND DISPOSITION:

Taxpayer's petition is granted in part and denied in part. As to [Stores A, B, and C], taxpayer is not a successor to the debtor's business. As to [Store D], taxpayer did succeed to the debtor's business. Taxpayer's file will be referred to the Audit Division for determination of the amount of the refund plus statutory interest due.

DATED this 10th day of August 1988.