IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

DIVISION II

DONALD R. WATTS, DONALD L. ODEGARD, and STEPHEN D. BANNWORTH, Appellants, v. WASHINGTON STATE DEPARTMENT OF REVENUE, Respondent.	No. 42159-3-II UNPUBLISHED OPINION

Armstrong, J. — Donald Watts, Donald Odegard, and Stephen Bannworth (collectively Watts) owned 50.01 percent of 100 Circles Farms. After selling their interest in 100 Circles Farms to ConAgra, Watts paid the Washington real estate excise tax on the fair market value of all the real estate 100 Circles Farms owned. Watts now seeks a partial refund, arguing it should pay tax on only 50.01 percent of the real estate 100 Circles Farms owned, corresponding to its 50.01 percent ownership interest in the property. RCW 82.45.030(2) requires the seller of a "controlling interest" in an entity to pay the real estate excise tax on "the true and fair value of the real property owned by the entity." Under this statute, the Department of Revenue required Watts to pay an excise tax on the full value of the realty. The superior court granted summary judgment in favor of the Department.

Watts argues that the real estate excise tax is a property tax that violates the uniformity requirement of article VII, section 1 of the Washington Constitution; that the tax is invalid because it taxes (1) an involuntary act, (2) the value of the entire property, and (3) the right to own or hold property. Finally, Watts argues that the real estate excise tax violates equal protection and due process. We affirm.

FACTS

Watts, Odegard, and Bannworth owned Watts Brothers Farms LLC, which owned a 50.01 percent interest in 100 Circles Farms LLC; ConAgra Lamb Weston Inc. (ConAgra) owned the remaining 49.9 percent interest. The parties stipulated that 100 Circles Farms owned approximately 19,400 acres of farm land in Benton County, Washington.

In February 2008, Watts sold its interest in Watts Brothers Farms to ConAgra. The sale transferred Watts' 50.01 percent interest in 100 Circles Farms to ConAgra. ConAgra then held a 100 percent interest in 100 Circles Farms.

In March 2008, Watts filed a controlling interest transfer tax return with the Department of Revenue, reporting the sale of Watts Brothers Farms. The parties agreed that the fair market value of the Benton County farm property was $62,626,074.79. Watts then paid the Washington real estate excise tax of $1,320,643.60, based on the fair market value of all the farm property 100 Circles Farms owned.

Refund Claim

In January 2009, Watts filed for a refund from the Department for $478,993.65, representing ConAgra's 49.99 percent real estate portion, plus interest. The Department denied Watts' request for a refund. Watts appealed the Department's denial. After an informal hearing, an Administrative Law Judge denied Watts' refund request. In March 2010, Watts appealed to the Thurston County Superior Court, which granted the Department's motion for summary judgment.

ANALYSIS

I. Standard of Review

We review a summary judgment de novo. *Flight Options LLC v. Dep't of Revenue*, 172 Wn.2d 487, 495, 259 P.3d 234 (2011). Summary judgment is appropriate only if there is no genuine issue of material fact in the pleadings, affidavits, depositions, and admissions on file, and the moving party is entitled to judgment as a matter of law. CR 56(c); *Hisle v. Todd Pac. Shipyards Corp.*, 151 Wn.2d 853, 861, 93 P.3d 108 (2004). A party who challenges the constitutionality of a statute has the burden of establishing its unconstitutionality beyond a reasonable doubt. *Wash. State Grange v. Locke*, 153 Wn.2d 475, 486, 105 P.3d 9 (2005). We resolve any reasonable doubt in favor of constitutionality. *Wash. State Grange*, 153 Wn.2d at 486.

II. Uniform Tax Under the Washington Constitution

Watts contends that the real estate excise tax is not uniform because it taxes the full value of 100 Circles Farms' real property, even though Watts transferred only its 50.01 percent

interest. Stated differently, Watts argues that the Department improperly taxed it on the 49.9 percent ownership interest ConAgra had in 100 Circles Farms before the sale.

Article VII, section 1 of the Washington Constitution applies only to property taxes and provides, in relevant part:

> All taxes shall be uniform upon the same class of property within the territorial limits of the authority levying the tax and shall be levied and collected for public purposes only. The word "property" as used herein shall mean and include everything, whether tangible or intangible, subject to ownership. All real estate shall constitute one class. . . .

Constitutional provisions requiring uniformity do not apply to excise taxes. *Dean v. Lehman*, 143 Wn.2d 12, 25-26, 18 P.3d 523 (2001).

A. <u>Excise Tax</u>

Watts argues that the real estate excise tax as applied in this case is actually a property tax. Thus, according to Watts, applying the real estate excise tax to the full value of the 100 Circles Farms' property violates the uniform taxation requirement of the Washington Constitution. The Department responds that the excise tax applies to the voluntary sale of a controlling interest in an entity and is not a property tax triggering the uniformity requirement of article VII, section 1 of the Washington Constitution. We agree with the Department.

Our Supreme Court explained the distinction between a property tax and an excise tax in *Covell v. City of Seattle*, 127 Wn.2d 874, 905 P.2d 324 (1995). An excise tax is defined as:

> [An] obligation . . . based upon the voluntary action of the person taxed in performing the act, enjoying the privilege or engaging in the occupation which is the subject of the excise, and the element of absolute and unavoidable demand, as in the case of a property tax, is lacking.

Covell, 127 Wn.2d at 889 (quoting *High Tide Seafoods v. State*, 106 Wn.2d 695, 699, 725 P.2d

411 (1986)). To be clear, an excise tax applies to the right to use or transfer things. *High Tide Seafoods*, 106 Wn.2d at 699. The tax applies to the sale of an interest in real property, including the transfer of a controlling interest in any entity with an interest in real property[1] for valuable consideration.[2] RCW 82.45.010(2)(a).

In support of its argument, Watts relies on *Harbour Village Apartments v. City of Mukilteo*, 139 Wn.2d 604, 989 P.2d 542 (1999), to argue that the tax at issue here is a property tax. But *Harbour Village* is distinguishable. The issue there was whether a residential dwelling unit fee the city charged to the apartment owners was an excise tax or a property tax. *Harbour Vill.*, 139 Wn.2d at 605. The flat rate fee was based on each rental unit and it was due regardless of whether the apartment owner rented out the unit. *Harbour Vill.*, 139 Wn.2d at 606. It was simply an annual flat fee on each unit rented or offered for rent. *Harbour Vill.*, 139 Wn.2d at 606. The court held that the tax applied based on "the mere ownership of that subclass of real property defined by its rental use." *Harbour Vill.*, 139 Wn.2d at 607. The court explained that "the character of a tax is determined by its incidents, not by its name." *Harbour Vill.*, 139 Wn.2d at 607 (citations omitted). The court concluded that the residential dwelling unit fee was unconstitutional because it applied only to rental property, thereby violating the constitutional

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[1] Real estate and real property are statutorily defined as "any interest, estate, or beneficial interest in land or anything affixed to land, including the ownership interest or beneficial interest in any entity which itself owns land or anything affixed to land." RCW 82.45.032(1).

[2] The legislative intent of the real estate excise tax is to apply "chapter 82.45 RCW to transfers of entity ownership when the transfer of entity ownership is comparable to the sale of real property. The legislature intends to equate the excise tax burdens on all sales of real property and transfers of entity ownership essentially equivalent to a sale of real property under chapter 82.45 RCW." Laws of Washington 1993, 1st Spec. Sess., ch. 25, § 501(2).

requirement that taxes on real property must be uniform. *Harbour Vill.*, 139 Wn.2d at 608.[3]

The real estate excise tax is not a property tax that is imposed on mere ownership.[4] Here, the real estate excise tax applies to Watts' act of transferring a controlling interest in 100 Circles Farms. *See High Tide Seafoods*, 106 Wn.2d at 699-700. It is measured by the value of the real property the entity owned. RCW 82.45.030(2). Thus, when Watts transferred its controlling interest, 50.01 percent of 100 Circles Farms, to ConAgra, Watts owed the tax on the full value of the real estate under RCW 82.45.010(2)(a).

B. <u>Nonuniform Rate of Taxation</u>

Watts challenges the constitutionality of the real estate excise tax, arguing that it is not imposed at a uniform rate or by a uniform measure. Watts states that this is a nonuniform tax because the tax rate is higher for an entity that sells a controlling but fractional interest in the property than for a tenant in common. The Department responds that there is no constitutional reason requiring the excise tax to be prorated based on the ownership percentage of the entity sold, contrary to Watts' assertion. The Department further explains that because this is an excise tax, not a property tax, there is no merit to Watts' claim that the tax is unconstitutional.

The real estate excise tax is the seller's obligation at the time of sale. RCW 82.45.080, .100. The selling price used to determine the tax to be paid where "[t]he sale is a transfer of a

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[3] The *Harbour Village* court compared the residential fee to the sales tax fee in *Black v. State*, 67 Wn.2d 97, 406 P.2d 761 (1965), a case Watts also cites. Black was subjected to a $17,000 sales tax on a $425,000 ship lease payment, which the court held was "'an excise tax on the transaction of leasing tangible personal property . . . not a tax on property.'" *Harbour Vill.*, 139 Wn.2d at 608 (quoting *Black*, 67 Wn.2d at 99).

[4] Watts' assertion that this is a property tax imposed on mere ownership is further discussed below in the section titled, "Right to Own and Hold Property."

controlling interest in an entity with an interest in real property located in this state" is "the true and fair value of the real property owned by the entity." RCW 82.45.030(2); *see McFreeze Corp. v. Dep't of Revenue*, 102 Wn. App. 196, 201, 6 P.3d 1187 (2000) ("[t]he value taxed is not the consideration paid, but the value of the real estate owned by the entity.").

Watts appears to argue that the tax should apply only to the extent of the transferred interest or the value of the 50.01 percent interest in 100 Circles Farms that was actually transferred. Watts further argues that all forms of property ownership should be taxed the same.[5] But Watts does not support its argument that the "tax must be prorated in order to be constitutional" with any authority. Br. of Resp. at 10-11. And as we have discussed, because the real estate excise tax is imposed on a transaction and not on property ownership, it does not trigger the uniformity provision of the Washington Constitution. *See Dean*, 143 Wn.2d at 25-26.[6]

III. Validity as an Excise Tax

Watts argues that the real estate excise tax is invalid because it is imposed without a voluntary act of a transfer and is not based on the extent to which taxpayers enjoy the privilege of transferring the property. The Department responds that Watts does not identify the constitutional provision to support its claim that the real estate excise tax is "invalid." Br. of Resp't at 17. Moreover, the Department contends that this argument merely repeats Watts'

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[5] The merits of Watts' argument that an excise tax can only be collected on the extent of the value of what is at issue is addressed below under the section titled "Validity of the Excise Tax" because Watts does not assert a constitutional basis for this argument.

[6] Watts refers in passing to "article 7 § 1" but provides no persuasive argument based thereon. Moreover, its reliance on the New York Real Estate Transfer Tax, which apportions that tax based on the amount of the entity transferred, is misplaced. As Watts concedes, the "Washington statute intentionally omits any such apportionment." Br. of Appellant at 40.

argument that the real estate excise tax is a "nonuniform property tax." Br. of Resp't at 18.

"'The legislature's power to enact a statute is unrestrained except where, either expressly or by fair inference, it is prohibited by the state and federal constitutions.'" *Wash. State Farm Bureau Fed'n v. Gregoire*, 162 Wn.2d 284, 300-01, 174 P.3d 1142 (2007) (quoting *State ex rel. Citizens Against Tolls v. Murphy*, 151 Wn.2d 226, 248, 88 P.3d 375 (2004)). The party asserting that the legislation violates the state constitution has the burden of establishing the unconstitutionality beyond a reasonable doubt. *See Wash. State Grange*, 153 Wn.2d at 486.

The real estate excise tax is imposed "upon each sale of real property." RCW 82.45.060. To be valid, an excise tax must tax a voluntary act of the taxpayer. This affords the taxpayer the benefits of the occupation, business, or activity that triggers the taxable event. In addition, an excise tax must be proportional to the benefit the taxpayer enjoys from the taxable privilege. *Sheehan v. Cent. Puget Sound Reg'l Transit Auth.*, 155 Wn.2d 790, 800, 123 P.3d 88 (2005).

A. Voluntary Act

Watts argues that the excise tax is invalid because Watts did not voluntarily act to transfer the ConAgra portion of the property and the excise tax was not based on the extent to which Watts received consideration for the property transfer. The Department responds that the excise tax is imposed on the voluntary act of Watts selling its controlling interest in 100 Circles Farms.

In *Sheehan*, 155 Wn.2d at 801, the court affirmed the motor vehicle tax on the privilege to relicense a motor vehicle for use on public roadways and the method of using the value of the vehicle to measure that privilege. The court concluded that the voluntary act was the resident choosing to drive her vehicle on the public roadway, stating, "There is no inherent requirement that residents of the taxing districts own or continue to own a motor vehicle." *Sheehan*, 155

Wn.2d at 800. Similarly, the act taxed here is sufficiently voluntary—the transfer of Watts' controlling interest in the property.

Watts also cites *Mahler v. Tremper*, 40 Wn.2d 405, 243 P.2d 627 (1952) and *Morrow v. Henneford*, 182 Wash. 625, 47 P.2d 1016 (1935), to argue that the tax rate applied to the value of the asset transferred in those cases, unlike here where the Department based the tax base on the entire property. In *Mahler*, 40 Wn.2d at 409-10, the court held that the real estate excise tax applied on the sale of the property and did not need to be apportioned because it was an indirect tax on a limited exercise of a property right. The imposition of the excise tax was "not upon each and every owner merely because he is the owner of the property involved." *Mahler*, 40 Wn.2d at 410. And in *Morrow*, 182 Wash. at 630, the court upheld a sales tax imposed on prepared foods, stating that the excise tax "laid only upon the exercise of a single one of those powers incident to ownership, the power to give the property owned to another." Here, the tax applies to Watts' voluntary act of selling the property: it did not apply because of mere ownership.

Watts also asserts that the excise tax "was a tax on the transfer of real property, not a tax on the transfer of an interest in an entity." Br. of Appellant at 18. Watts did, however, transfer a 50.01 percent interest in 100 Circles Farms, and Watts owed the excise tax because of its transfer of a controlling interest in the entity under RCW 82.45.030(2). We conclude that the real estate excise tax applied to Watts' voluntary act of transferring its controlling interest.

B. Taxable Privilege

Watts argues that RCW 82.45.010 and RCW 82.45.030 are valid as to direct transfers of real property but invalid as applied to a transfer of control. The Department contends that the decision to tax the sale of a controlling interest and the measure of the tax is sufficient because it

applies to the real property value only when the seller transfers control of the entity. Watts offers no persuasive argument that our constitution requires the excise tax to distinguish between a transfer of control of entity ownership and the direct sale of real property.

Watts attempts to distinguish its case from *McFreeze Corp.*, 102 Wn. App. 196, in which we upheld the statute at issue here. In *McFreeze Corp.*, 102 Wn. App. at 198, the McCollums owned 50 percent of stock in the McFreeze Corporation. The Department of Revenue required the McCollums to pay the real estate excise tax on the full value of the realty after they purchased the remaining 50 percent of stock. *McFreeze Corp.*, 102 Wn. App. at 198. The McCollums challenged the real estate excise statute for being ambiguous and argued that RCW 82.45.030(1) defined "selling price" as "total consideration paid in an arm's length transaction" and that RCW 82.45.030(2) defined the "selling price" as the "true and fair value of the real property owned by the entity" leading to odd results. *McFreeze Corp.*, 102 Wn. App. at 199-201. "For example, if the McCollums had purchased both halves of the corporation in separate sales, they would be taxed twice on the full value of the corporation." *McFreeze Corp.*, 102 Wn. App. at 201. We recognized that "in the sale of an entity, the value taxed is not the consideration paid, but the value of the real estate owned by the entity." *McFreeze Corp.*, 102 Wn. App. at 201. The same concept applies to Watts' challenge.

We hold that the Department properly imposed the tax on Watts' transfer of its controlling interest in 100 Circles Farm. Watts fails to provide persuasive argument or authority suggesting that this violates the constitution or is otherwise invalid.

C. Right to Own or Hold Property

Watts next challenges the real estate excise tax, arguing that it was "a tax on the right to

own and hold property." Br. of Appellant at 28. The Department replies that this is a simple rehashing of Watts' previous argument that this is not a uniform property tax. Br. of Resp't at 20.

An excise tax may not be imposed on the right to own and hold property because "'to tax by reason of ownership of property is to tax the property itself.'" *Harbour Vill.*, 139 Wn.2d at 608 (quoting *Jensen v. Henneford*, 185 Wash. 209, 218, 53 P.2d 607 (1936)). The real estate excise tax here is imposed on the voluntary act of transferring a controlling interest in an entity, rather than on a right to own and hold property. *See* RCW 82.45.030.

The cases Watts relies on simply do not support its argument that the Department imposed the real estate excise tax on its "right to own [or] hold property." Br. of Appellant at 28; *see Dawson v. Kentucky Distilleries & Warehouse Co.*, 255 U.S. 288, 294, 41 S. Ct. 272, 65 L. Ed. 638 (1921) (annual tax on business of owning and storing whiskey in bonded warehouse was a property tax subject to uniformity requirement of Kentucky Constitution); *Harbour Vill.*, 139 Wn.2d at 607 (residential dwelling unit fee was a property tax that applied based on "the mere ownership of that subclass of real property defined by its rental use"); *Apartment Operators Ass'n of Seattle, Inc. v. Schumacher*, 56 Wn.2d 46, 351 P.2d 124 (1960) (taxing rental income was a tax on property, which violated the uniformity requirement); *Jensen*, 185 Wash. 209 (personal income is property and therefore, the personal net income tax was a property tax and not an excise tax).

Watts asserts that the real estate excise tax was imposed on the ownership of the 100 Circles Farms property. However, the tax was imposed because of the controlling interest transfer. For Watts to prevail with this argument, it would have to convince us that the real estate

excise tax as applied here is a property tax and, thus, must be uniformly imposed. Because Watts fails to do so, we affirm.

IV. Equal Protection Clause

Watts next argues that the real estate excise tax violates the equal protection and due process clauses of both the United States and Washington constitutions. Watts provides no citation to legal authority or to the record to support these arguments. Thus, we decline to review them. RAP 10.3(a)(6).

Affirmed.

A majority of the panel having determined that this opinion will not be printed in the Washington Appellate Reports, but will be filed for public record in accordance with RCW 2.06.040, it is so ordered.

Armstrong, J.

We concur:

Penoyar, J.

Johanson, A.C.J.