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No. 101794-4

IN THE SUPREME COURT OF THE STATE OF WASHINGTON

PETROGAS PACIFIC LLC and PETROGAS WEST LLC,

Petitioners,

v.

REBECCA XCZAR, Whatcom County Assessor,

Respondent.

MEMORANDUM OF AMICUS CURIAE
COUNCIL ON STATE TAXATION
IN SUPPORT OF PETITION FOR REVIEW

Gregg D. Barton, WSBA 17022
Robert A. Mahon, WSBA 26523
PERKINS COIE LLP
1201 Third Avenue, Suite 4900
Seattle, WA 98101-3099
Telephone: 206.359.8000
Facsimile: 206.359.9000

Attorneys for Amicus Curiae
Council on State Taxation

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I. IDENTITY AND INTEREST OF AMICUS CURIAE

The Council On State Taxation (“COST”) is a nonprofit trade association based in Washington, D.C. COST was organized in 1969 as an advisory committee to the Council of State Chambers of Commerce. Today, COST has an independent membership of over 500 of the largest multistate corporations engaged in interstate and international business. COST represents companies doing business in every state across the country. COST members employ a substantial number of Washingtonians, own extensive property in Washington, and conduct substantial business in Washington.

COST’s objective is to preserve and promote equitable and non-discriminatory state and local taxation of multijurisdictional business entities. In furtherance of this objective, COST has participated as *amicus curiae* in many significant federal and state tax cases since its formation, including cases in which Washington courts have considered important state and local tax issues. Examples include *Lowe’s*

Home Centers, LLC v. Department of Revenue, 195 Wn.2d 27, 455 P.3d 659 (2020); *Express Scripts Inc., v. Department of Revenue*, 193 Wn.2d 1035, 447 P.3d 151 (2019); *Avnet, Inc. v. Department of Revenue*, 187 Wn.2d 44, 384 P.3d 571 (2016); and *Kevin Miller v Department of Revenue*, No. 57112-9-II, argued (Wash. Ct. App., Div. II 2023).

As a matter of longstanding policy, COST seeks fair and equitable property tax systems. Our policy position on property taxes provides that:

State and local property tax systems must be fairly administered and tax burdens equitably distributed among taxpayers. A property tax system that is inefficient or that disproportionately falls upon business is not equitable and will negatively impact a state's business tax climate.

COST, Fair and Equitable Tax Systems,
<https://cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/fair-and-equitable-property-tax-systems.pdf> (last visited May 3, 2023).

Applying the fair and equitable property tax system principle to intangible property, the policy position notes “intangible property, such as trade names, customer relationships and goodwill, should not be included in the property tax base because such property is associated only with the management of business and the measurement of such value is extremely subjective.” *Id.*

Consistent with this policy position, COST, in partnership with the International Property Tax Institute (IPTI), also reviews the states’ (and international) property tax administrative practices and creates a comparison report (“Scorecard”), which we have done for over a decade. The goal of the Scorecard is to improve all jurisdictions’ administrative practices, which includes negatively highlighting the jurisdictions that tax intangible property. In the latest edition, “The Best (and Worst) of International Property Tax Administration” Scorecard, Washington’s overall grade was a “C+” and the grade does not reflect the negative consequence of the Court of Appeals’

decision in this case. COST & IPTI, *The Best (and Worst) of International Property Tax Administration* (June 2019), <https://cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-studies-articles-reports/2019-international-property-tax-scorecard--final-june-20.pdf> (no state or subnational jurisdiction received an overall “A” grade).

Washington’s law explicitly excludes intangible personal property from ad valorem taxation. RCW 84.36.070. COST members are concerned that this case erodes the statutory exclusion of intangible personal property from the property tax base. We respectfully ask this Court to review the underlying decisions to correct any notions that certain intangible personal property values (*e.g.*, goodwill) are included as part of taxable property in the State.

Property taxes should be based on the underlying value of the property used by the taxpayer, and not the business entity’s operations. This Court’s review is needed to address whether assessors and the lower courts (including the State Board of Tax

Appeals) can include intangible values in the taxable property tax base. Certain valuation methods, such as the cost approach, often provide a more accurate reflection of the value of taxable property, as compared to using sales agreements that may not reflect the value of exempt assets that are excluded from property taxation.

II. ISSUES OF CONCERN TO AMICUS

A. Did the Court of Appeals comply with RCW 84.36.070's mandate to exclude intangible property and erroneously include as taxable property "taxable intangible values" in the assessment?

B. Does an overpayment to purchase an asset create taxable tangible property, especially when the transaction is not an arm's length transaction?

III. STATEMENT OF THE CASE

COST adopts the Statement of the Case presented by the Appellants/Petitioners (Petrogas). *See* Pet. For Review at 4–8. Specifically, Petrogas purchased the wharf assets for much more

than they were worth if purchased by a willing seller and willing buyer under no compulsion to sell or purchase the assets.

IV. ARGUMENT

A. Intangible Assets Should Be Excluded From the Property Tax Base.

Under Washington law, intangible assets are excluded from the taxable property tax base.¹ There should be no way to circumvent this, which is the central issue in this case.

Washington, like other states, does not include intangibles in the ad valorem taxation of real property. The International Association of Assessing Officers (IAAO), an organization comprised of state and local property tax assessors, noted in a *Journal of Property Tax Assessment & Administration* article:

In most U.S. jurisdictions, intangible assets are not taxable as part of a real property assessment. For that reason, assessors must ensure the value of intangible assets is excluded. *This is particularly important when properties sell with intangible assets included in a sale price or when business*

¹ While also an important legal issue, the aquatic land lease addressed by Petrogas in its Petition for Review is not discussed in this amicus memorandum.

income is used in an income approach to value a property.

IAAO Special Committee on Intangibles, *Understanding Intangible Assets and Real Estate: A Guide for Real Property Valuation Professionals*, 14 *Journal of Property Tax Assessment & Administration* 41, 65 (2017) (emphasis added). The article also points out “[i]f the assessor determines the price included intangible assets, he or she should determine the value of such intangible assets.” *Id.* at p. 50. We agree with IAAO’s position—adequate steps must be taken to either not include intangible property (such as by using the cost approach valuing tangible assets only) or to remove intangible property from the tax base (such as where the sale price or income approach includes intangibles). Washington is like the vast majority of the other states that have a law, *e.g.*, RCW 84.36.070, that exclude intangibles from property taxation and adequate steps must be taken to remove them from the tax base.

Here, “Petrogas agreed to an overpayment [for the wharf] because the wharf was critical to the integrity of the terminal and Petrogas’s export program as a whole.” *Petrogas Pac. LLC v. Xczar*, 24 Wn. App. 549, 551, 520 P.3d 1077, 1079 (2022). Any overpayment related to the purchase of the wharf constitutes intangible value or goodwill that must be excluded from the property tax base. Nonetheless, even though Petrogas assigned \$100 million to goodwill,² the Court affirmed including that goodwill value in the property tax assessment. *Id.* at 555. Doing so incorrectly focuses on valuing the business rather than valuing the underlying tangible assets used by the business.

Although it is acknowledged that Petrogas overpaid to obtain the wharf, no attempt was made by the assessor to adjust the purchase price to exclude intangible values relating to

² “PwC reviewed and agreed to the allocation for the purposes of financial accounting under U.S. GAAP.” *Id.* As explained in the record in this case, under U.S. GAAP, every dollar of a transaction price must be allocated; by definition, any residual amount not allocated to specific assets is intangible goodwill. CP 2220-21.

Petrogas’s purchase of the wharf from Alcoa. While Petrogas may have valid business reasons to enter into unfavorable terms to obtain full rights to the wharf (given its critical connection to Petrogas’s operations), that does not justify the assessor converting the premium paid for non-taxable intangible personal property into taxable real property.

The Court of Appeals’ and the State Board of Tax Appeals’ decisions, however, broaden what is included in the taxable tangible property tax base, adding murkiness and ambiguity in holding that “[n]onproperty intangible characteristics or attributes are ‘intangible’ but they are not ‘property’ and therefore are not tax exempt intangible personal property.” *Petrogas Pac.*, 24 Wn. App. at 558 (quoting WAC 458-50-160(4)). The Court of Appeals’ reasoning inappropriately narrows what qualifies as “intangible personal property” as though the provision about nonproperty under RCW

84.36.070(3) somehow altered the definition of intangible personal property—which it does not.

The Court of Appeals’ holding also ignores the dual importance of Petrogas’ interconnected rights to both the terminal and wharf, resulting in the assignment of \$100 million of the purchase price as goodwill. The additional purchase made by Petrogas to fully consummate the purchase of the wharf avoided protracted litigation. That fits within the express exclusion for intangibles covered by RCW 84.36.070(2)(c), excluding intangible personal property associated with the “integrity of a business.” Petrogas needed both the wharf and the terminal to effectively operate its business.

B. The Assessor’s Misuse of the Unit Principle Valuation Approach Did Not Properly Account For the Book Value of Petrogas’ Goodwill.

Another problem with the assessment in this case is the use by one of the assessor’s appraisers of a unit valuation

concept.³ This appraisal method is usually limited to utility properties crossing many local government boundaries. Richard Smith⁴ explains the conundrum of excluding goodwill in unitary property taxation:

Case law over the last 50 years has shown a steady recognition that intangible property in general—and goodwill in particular—are important parts of a company’s portfolio of assets. Most states have enacted taxation exemptions for intangible property, usually including goodwill.

The appraisal guidance relied on by states (WSATA and NCUVS) recommend that tax-exempt assets should be deducted at the end of the unit principle valuation process, after the tangible asset value indications from the valuation approaches are reconciled into a final value.

It makes perfect sense to use the accounting book value of goodwill in that process....

Richard G. Smith, *The Continuing Conundrum of How to Exclude Goodwill in Unitary Property Taxation—and a Proposed*

³ *Petrogas Pac.*, 24 Wn. App. at 563.

⁴ Partner, Hawley Troxell, <https://hawleytroxell.com/people/richard-g-smith/> (last accessed May 8, 2023).

Solution, Property Tax Valuation Insights 34, 42 (Summer 2017),
https://willamette.com/insights_journal/17/summer_2017_4.pdf.

Washington is part of the Western States Association of Tax Administrators (WSATA). Even using a unit approach, the appraiser must exclude the recorded book value of Petrogas' goodwill—an essential step that the Court's decision fails to recognize as necessary.

V. CONCLUSION

The lack of clear guidance in the Court of Appeals' and the State Board of Tax Appeals' decisions is of great concern to COST members, whose businesses often include significant intangible value including goodwill. This Court's review of this case would provide both property taxpayers and assessors with needed guidance on how goodwill and other intangible assets are excluded from the property tax base in this State. For the foregoing reasons, COST respectfully asks this Court to review the Court of Appeals' decision.

I certify that this document, excluding the parts exempted from the word count by RAP 18.17, contains 1804 words.

Respectfully submitted,

DATED: May 9, 2023.

PERKINS COIE LLP

By: *s/ Gregg D. Barton*

Gregg D. Barton, WSBA 17022
Robert A. Mahon, WSBA 26523
GBarton@perkinscoie.com
RMahon@perkinscoie.com
PERKINS COIE LLP
1201 Third Avenue, Suite 4900
Seattle, WA 98101-3099
Telephone: 206.359.8000
Facsimile: 206.359.9000

Attorneys for Amicus Curiae
Council on State Taxation

CERTIFICATE OF SERVICE

Today I electronically filed the foregoing document via the Washington State Appellate Courts' Secure Portal, which will automatically cause such filing to be served on counsel for all other parties in this matter via the Court's e-filing platform.

I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED: May 9, 2023, at Seattle, Washington.

s/ Betty Kawagoe _____
Betty Kawagoe
Legal Practice Assistant

PERKINS COIE LLP

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