No. 86977-4

SUPREME COURT
OF THE STATE OF WASHINGTON

APL LIMITED, AMERICAN PRESIDENT LINES, LTD. and EAGLE MARINE SERVICES, LTD.,

Plaintiffs-Appellants

v.

WASHINGTON STATE DEPARTMENT OF REVENUE,

Defendant-Appellee

ON APPEAL FROM THURSTON COUNTY SUPERIOR COURT
(Hon. Thomas McPhee)

REPLY BRIEF OF APPELLANTS

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

STATUTES, REGULATIONS AND COURT RULES

OTHER AUTHORITIES

MISCELLANEOUS

I. INTRODUCTION

This appeal does not turn on whether the trial court's findings of fact are supported by substantial evidence; indeed, the facts are largely undisputed. Rather, this appeal turns on whether the trial court properly applied the undisputed facts to the law. It did not. On the issue of annexation, the court erroneously refused to consider the T-5 Cranes' adaptation to Terminal 5. The DOR urges the same flawed approach on appeal, never once acknowledging the well-established doctrine of constructive annexation, the split in authority between *Western Ag* (which was correctly reasoned) and *Glen Park* (which was not) or, amazingly, its own regulation—which expressly *requires* adaptation to be considered when deciding annexation. When the undisputed facts are analyzed under the correct legal standard, it is clear that T-5 Cranes are both constructively and physically annexed to Terminal 5.

On the issue of intent, the trial court also misapplied the facts to the law, beginning with its refusal to apply the presumption of intent in APL's favor. There is no authority to support the DOR's novel argument that the presumption creates a burden of production, not a burden of proof. Further, in considering the facts, the trial court asked the wrong question: the question is not whether the Port subjectively believed the T-5 Cranes were fixtures or personal property, but whether it objectively intended a

permanent annexation. The DOR focuses on the former and ignores the latter—for good reason. All the objective evidence shows that the Port intended the cranes to remain part of Terminal 5 until the end of their useful lives. The Port's ambiguous and subjective "classification" evidence, upon which the trial court relied entirely, cannot overcome that evidence or the presumption of intent. The T-5 Cranes are fixtures.

II. ARGUMENT

A. APL Satisfied Its Burden Of Proving That The T-5 Cranes Are Constructively And Physically Annexed To Terminal 5.

1. The Trial Court Erred As A Matter Of Law In Refusing To Consider Adaptation On The Issue Of Annexation.

The DOR does not dispute that the trial court, relying on Division 2's decision in *Glen Park Assocs. v. Dep't of Revenue*, 119 Wn. App. 481, 82 P.3d 664 (2003), concluded that it could not consider "adaptation" when deciding "annexation." CP 216 (Tr. (10/14/11) at 5-6. Nor does the DOR dispute that, consistent with that conclusion, the trial court's findings on annexation omit all reference to the overwhelming evidence of the T-5 Cranes' adaptation to Terminal 5. CP 200-01 (FF ¶¶ 13-23); CP 219-21 (Tr. (10/18/11) at 9-11). Finally, and further discussed below, the DOR does not dispute that once this overwhelming evidence of adaptation is properly considered, it is clear that the T-5 Cranes were annexed to the realty, and the trial court's conclusion to the contrary must be reversed.

As APL explained in its opening brief, the trial court's refusal to consider "adaptation" when deciding "annexation" was erroneous because *Glen Park*'s dicta to that effect conflicts with settled Washington fixtures law—particularly (a) the doctrine of constructive annexation, (b) Division 3's decision in *Western Ag. Land Partners v. Dep't of Revenue*, 43 Wn. App. 167, 716 P.3d 310 (1986), and (c) WAC 458-12-010(3). APL Br. at 13-17. In response, the DOR simply ignores the conflict, refusing to acknowledge *Glen Park*'s implicit rejection of constructive annexation and explicit repudiation of *Western Ag.* Indeed, and most startling of all, the DOR fails to cite WAC 458-12-010(3) even once in its brief, much less explain how the plain terms of that regulation can be reconciled with the trial court's flawed annexation analysis. It can't. In short, *Glen Park* wrongly decided this issue and the trial court was wrong to follow it.

The DOR argues that adaptation cannot *alone* show annexation. DOR Br. at 23-24. APL has never argued otherwise. What APL has argued, and what the cases hold, is that adaptation must be *considered* when deciding annexation because "constructive annexation" depends, in large part, on an item's use and purpose in relation to the land. *See Chase v. Tacoma Box Co.*, 11 Wash. 377, 380, 39 Pac. 639 (1895); *Western Ag*, 43 Wn. App. at 172. Put simply and stated accurately, "[t]he similarity between constructive annexation and the adaptation test ... makes these

concepts almost indistinguishable in many cases." 2 Wash. State Bar Ass'n, *Wash. Real Property Deskbook: Real Estate Essentials* § 23.2(a)(ii) (4th ed. 2009) (referred to hereafter as the "Real Property Deskbook"). By erecting an artificial wall between annexation and adaptation, *Glen Park* effectively revived the discredited notion that annexation requires absolute physical attachment—an error the trial court perpetuated below.

Certainly, the DOR's own regulation imposes no such wall. On the contrary, WAC 458-12-010—which restates the common law—***requires*** adaptation to be considered when deciding annexation. *APL Ltd. v. Dep't of Revenue*, 2010 WL 264992, *2 n. 7 (Wn. App. Jan. 25, 2010) (regulation restates the common law). It provides that an item is annexed to realty, even if not "securely attached," if it is "permanently situated in one location ... and is adapted to use in the place it is located." WAC 458-12-010(3)(a). Notably, *Western Ag* aptly cited WAC 458-12-010 in holding that adaptation was relevant to annexation; *Glen Park* ignored the regulation entirely. Like *Glen Park*, the trial court ignored WAC 458-12-010 too. If nothing else, the court's refusal to follow the regulation was error. The DOR concedes the point; it cannot explain why WAC 458-12-010 did not apply here or why, on its face, the regulation did not require the trial court to consider adaptation when deciding annexation.

Unable to reconcile *Glen Park* with the doctrine of constructive annexation or WAC 458-12-010, the DOR hardly mentions the case. Instead, it spends pages unsuccessfully trying to distinguish *Western Ag* on the facts, wishfully concluding that, "it is clear that [*Western Ag*] did not hold that Washington law requires consideration of ... adaptation when determining ... annex[ation]." DOR Br. at 27. But that is precisely what *Western Ag* held, consistent with Supreme Court precedent and WAC 458-12-010. *Western Ag*, 43 Wn. App. at 172. The DOR's strained reading of *Western Ag* would certainly come as a surprise to the *Glen Park* court and the trial court—both of which felt compelled to expressly disavow *Western Ag*. *Glen Park*, 119 Wn. App. at 489 ("[w]e decline to follow [*Western Ag*]"); CP 215-216 (Tr. (10/14/11) at 5-6). In sum, there is an irreconcilable conflict between *Western Ag* and *Glen Park*; both cases can't be right. For the reasons explained in the opening brief and here, *Western Ag* accurately states Washington law; *Glen Park* does not.

Lastly, this Court can readily dismiss the DOR's claim that Division 3, in *Union Elevator & Warehouse Co. v. Dep't of Transp.*, 144 Wn. App. 593, 183 P.3d 1097 (2008), "implicitly abandoned" *Western Ag*'s holding that adaptation must be considered when determining annexation. DOR Br. at 27. The annexation prong of the fixtures test was not even an issue in *Union Elevator*; annexation was undisputed. 144 Wn.

App. at 604. The court did not revisit—much less repudiate—*Western Ag*'s annexation analysis. Indeed, *Union Elevator* does not cite *Western Ag* once. Rather, *Union Elevator* turned on intent; the evidence showed that the machinery was not specially adapted to the realty, but, instead, was "designed to be broken down into parts and easily moved." *Id.* at 605-06. As discussed below, the evidence here was precisely the opposite.

2. The Cranes Are Constructively Annexed To Terminal 5 Because They Are Uniquely Adapted To And Specially Fabricated For Use With The Land.

The DOR conceded that the T-5 Cranes were adapted to Terminal 5. CP 207 (CL ¶ 2). The DOR does not dispute that, if the overwhelming evidence of adaptation is considered, as it must, APL amply proved annexation as well. The annexation prong of the fixtures test is satisfied if an item is "attached to the real estate as firmly as it appears to have been reasonably possible to attach it," given its use. *Strong v. Sunset Copper Co.*, 9 Wn.2d 214, 230, 114 P.2d 526 (1941) (citation omitted). The T-5 Cranes are constructively annexed to Terminal 5 because they are attached as "firmly as ... reasonably possible" given the terminal's exclusive use as a cargo container facility. Simply put, if the T-5 Cranes were attached in any other way, the Port's substantial investment in Terminal 5 as a state-of-the-art post-Panamax cargo container facility would be entirely wasted.

Like the trial court, the DOR refuses to recognize adaptation in its annexation analysis, focusing instead on the cranes' movability.[1] That unsupported analysis wrongly assumes that annexation requires absolute physical attachment; as explained above, it doesn't. *Chase*, 11 Wash. at 381; *see also Hall v. Dare*, 142 Wash. 222, 226, 252 Pac. 926 (1927) ("it [is] not necessary that there should be such an absolute physical attachment"). Under the doctrine of constructive annexation, the article's relation to the land—"adaptation"—is the critical inquiry; that is, "whether the article is ... an essential part of the overall use of the property." *Western Ag*, 43 Wn. App. at 172 (internal quotes omitted); Real Property Deskbook, § 23.2(a) (courts "deem ... unattached chattels constructively annexed if they are integral or necessary to the use of the land"). It is the very ability of the T-5 Cranes to move on rails that makes them an essential part of Terminal 5 and, thus, constructively annexed to the land.

The DOR does not dispute that the Port built the T-5 Cranes, and agreed to an unprecedented long-term lease with APL, because the cranes were critical to the Port's strategic plans for Terminal 5. RP (9/27/11) at 86-88, 164-65. The DOR does not dispute that the Port spent millions of dollars to redevelop the terminal to accommodate the cranes—including

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[1] *See* DOR Br. at 11 ("container cranes are ***moveable***"); *id.* ("T5 cranes operate on wheels and ***move*** along rails"); *id.* at 12 (the cranes "***move*** as part of their normal operation").

reinforcing the waterside rail and constructing a new embedded landside rail. *Id.*; RP (9/26/11) at 56, 60-70. And, perhaps most important of all, the DOR does not dispute that the cranes could not service the long post-Panamax ships that dock at Terminal 5 without the ability to move on rails. RP (9/27/11) at 88, 155. As the Port's former executive director testified, the cranes are "an integral part of" Terminal 5 because, without them, "it's not a functioning container facility." RP (9/27/11) at 88.

Further, and also ignored by the DOR and trial court, the T-5 Cranes were specially fabricated for use at Terminal 5. This is equally dispositive on the issue of constructive annexation. *See Western Ag*, 43 Wn. App. at 172 (item "may be constructively annexed because it is specially fabricated for installation"); Real Property Deskbook, § 23.2(a)(ii) (even though not "physically affixed" to land, item "may be constructively annexed because it is specially fabricated for installation"); DOR Det. No. 00-122, 20 WTD 461 (2001) (same). Here too, the DOR does not dispute that the Port designed the cranes to conform to Terminal 5's unique characteristics, including its weight-bearing capacity, seismic and wind conditions. RP (9/26/11) at 55, 73-76; RP (9/27/11) at 88. In short, the T-5 Cranes were not merely adapted to Terminal 5's use as a cargo container facility, they are part and parcel of Terminal 5 itself.

For similar reasons, the T-5 Cranes are constructively annexed to Terminal 5 because they require the terminal's embedded crane rails, dedicated electrical substation and other improvements—all of which are fixtures themselves—to function. It is well-established that, even if not physically attached to the land, an item "may be constructively annexed ... because it is a necessary functioning part of or accessory to an object which is a fixture." *Western Ag*, 43 Wn. App. at 172; Real Property Deskbook, § 23.2(a)(ii) (same). When considered with their necessary components, as they must, the cranes are no less annexed to Terminal 5 than the rotating main arm was to the center pivot system in *Western Ag*; or the trolley was to the monorail in *Nearhoff v. Rucker*, 156 Wash. 621, 287 P. 658 (1930); or the spinning carousel was to the file retrievers in DOR Det. No. 92-218, 14 WTD 145 (1995). All those items were found to be annexed to the realty, and so too should the T-5 Cranes.

The decision in *Seatrain Terminals of Calif., Inc. v. Alameda Cty.*, 83 Cal.App.3d 69, 147 Cal. Rptr. 578, 582 (1978), is compelling on this point. There, the court held that cargo container cranes nearly identical to the T-5 Cranes were fixtures under the same three-prong common law test followed in Washington. *Id.* at 74-75. Like here, the "terminal facility was built specifically for handling cargo containers," "both functionally and physically the cranes were an integral part of the terminal operation,"

and "without them the terminal facility would not function in consonance with its purpose and design." *Id.* at 76-77. On annexation, the court held:

> [T]he cranes in dispute are extremely heavy, weighing 750 tons each. While they are annexed to the wharf facility by weight only, the rails upon which the cranes run are embedded in the wharf and constitute an integral part of the structure. Since the cranes comprise a necessary, integral and working part of the rails which are attached to the property, and since without the cranes the rails the attached part of the structure would lose their significance, the cranes must be deemed to be annexed to the realty within the meaning of the constructive annexation doctrine.

Id. at 76. The same reasoning applies here; the facts and the law are the same. Indeed, *Western Ag* favorably cited *Seatrain* to support its accurate articulation of constructive annexation. 43 Wn. App. at 172.

Finally, that it is possible to physically remove the T-5 Cranes from Terminal 5 is irrelevant. After all, every fixture—even a house—can be severed from the land. For this reason, as discussed below, the cranes' "removability" is relevant to the issue of permanency—*i.e.*, "intent"—not annexation. The DOR's suggestion that the cranes can be easily removed is wildly misleading in any event. Each crane weighs 800 tons and is firmly held to the rails by gravity (CP 200-201 (FF ¶¶ 11, 15), which itself is sufficient for a constructive annexation. *See Hall*, 142 Wash. at 227; *also* WAC 458-12-010(3)(a)(ii) (noting that "a heavy piece of machinery or equipment set upon a foundation without being bolted thereto could be

considered as affixed."). The DOR does not dispute that the cranes were never designed to be removed, and that it took months of engineering work just to temporarily lift one crane off its rails for modification. RP (9/27/11) at 90, 156. To be sure, the rails themselves provide no means for removal; the rails do not extend beyond the boundaries of Terminal 5. RP (9/26/11) at 71. This fact alone shows that the cranes are "permanently situated in one location" and "adapted to use in the place it is located," which is all that is required to demonstrate annexation under the DOR's own regulation. WAC 458-12-010(3)(a)(ii).[2]

3. The Cranes Are Physically Annexed To Terminal 5 By A "Hard-Wired" Electrical Connection.

The trial court also erred in refusing to find annexation by virtue of the dedicated electrical cables that connect the T-5 Cranes to Terminal 5. APL Br. at 23-24. Ignoring APL's authority, but citing none of its own, the DOR argues that this connection is insufficient because the cranes can

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[2] The DOR points to two decisions from the Board of Tax Appeals to support the trial court's annexation ruling. DOR Br. at 11 n. 5. But these decisions highlight the DOR's flawed understanding of the law. In both cases, the Board expressly say what the DOR implicitly argues here: "The common law fixtures test in Washington does not allow for 'constructive' annexation." *Total Terminals Int'l, LLC v. Dep't of Revenue*, 2011 WL 7266153, *11 (Bd. Tax App. 2011); *Hanjin Shipping Co., Ltd. v. Dep't of Revenue*, 2011 WL 823103, *14 (Bd. Tax App. 2011). As discussed above, the Board's conclusion that "[t]here is no such thing as 'constructive' annexation in the law," *Hanjin*, supra, *7, is wrong and inconsistent with Washington law and WAC 458-12-010. The proceedings in both cases are stayed pending the outcome of this appeal.

be "unplugged and moved." DOR Br. at 10-11. But as explained above, annexation, whether physical or constructive, does not require absolute attachment; Washington courts commonly find items to be fixtures despite the fact that they can be "unscrewed" or the like. *See Strong*, 9 Wn.2d at 229-30 (equipment were fixtures where they "could be removed by the mere unscrewing of foundation bolts"); *Amer. Radiator v. Pendleton*, 62 Wash. 56, 58, 112 Pac. 1117 (1911) (appliances were fixtures where they could "be separated and removed without damage to the building"); *Filley v. Christopher*, 39 Wash. 22, 24, 80 Pac. 834 (1905) (pipes were fixtures where they "could be detached from the boiler by unscrewing them").

If an electrical connection was sufficient to show annexation in *Lincoln Ballinger Ltd. P'ship v. Dep't of Revenue*, No. 51253, 1999 WL 1124058 (Bd. Tax App. 1999), the same must be true here. The DOR argues that *Glen Park* "rejected" *Lincoln Ballinger* (DOR Br. at 11 n. 5), but it did not; *Glen Park* did not follow the case citing conflict with an earlier Board of Tax Appeals decision. 119 Wn. App. at 492. The conflict was illusory. Even after *Glen Park*, the Board continues to follow *Lincoln Ballinger*, not the earlier decision. *See Essex Cal-Wa, LP v. King County Assessor*, No. 64956, 2007 WL 3353241 (Bd. Tax App. 2007). In any event, and also ignored by the DOR, *Glen Park* expressly recognized that an electrical connection can be sufficient to show physical annexation:

> We might consider the dishwashers differently because of their annexation to the realty. The dishwashers are hard-wired and more permanently plumbed than the other appliances. But at oral argument, Glen Park asked us to consider the appliances as a group, not separately.

119 Wn. App. at 489 n. 4. The dedicated electrical cables create a "hard-wire" physical connection between the T-5 Cranes and Terminal 5. The trial court erred in refusing to find annexation on this basis as well.[3]

B. The DOR Did Not Overcome The Presumption That The Port Intended To Permanently Annex The Cranes To Terminal 5.

1. The Presumption Of Intent Shifted The Burden Of Proof To The DOR On The Issue Of Intent.

The DOR does not dispute that where, as here, the annexing party is the owner of the land, the owner is legally "presumed to have annexed it with the intention of enriching the freehold." *Western Ag*, 43 Wn. App. at 173; *Nearhoff*, 156 Wash. at 628. Because APL proved that the Port constructively and physically annexed the T-5 Cranes to Terminal 5, the trial court should have applied this presumption of intent in APL's favor, which it erroneously refused to do. CP 203 (FF ¶ 25). As explained in APL's opening brief and below, this error requires reversal because the

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[3] The DOR notes that "APL has not argued that crane number 66 is annexed to Terminal 5 even though it is connected by electric cable to the same substation as the T5 cranes." DOR Br. at 12 n. 6. The DOR's suggestion that the lack of reference to crane number 66 is some sort of concession is utterly disingenuous: APL has not made any arguments regarding crane number 66 because that crane is not at issue in this case.

DOR failed to prove by substantial evidence at trial that the Port had a contrary intent—a point which the DOR apparently concedes.

Instead, and perhaps because it has no alternative, the DOR claims for the first time in this litigation that, despite its well-settled meaning, the presumption of intent does nothing more than create a fleeting and toothless burden of production. DOR Br. at 28. Noting that the presumption is "rebuttable" and citing the so-called "Thayer theory," the DOR argues that the presumption does not actually shift the burden of proof on intent, but rather required it only to produce *some* evidence on the issue, at which point the presumption "disappears"—like a "bursting bubble" or, more colorfully, "bats ... in the sunshine"—forcing APL to "carry on without it." *Id.* at 28-29.

The problem with the DOR's theory is that there is no authority to support it. The fact that recent cases describe the presumption as "rebuttable" is meaningless. "[T]he term is redundant. A presumption is, by definition, rebuttable." Karl B. Tegland, 5 Wash. Prac., *Evidence Law and Prac.* § 301.8 (5th ed. 2012).[4] Thus, the issue is not whether the presumption can be rebutted, but how. Equally misleading is the DOR's

[4] Indeed, it was not until 1986 that Washington cases began to describe the presumption as "rebuttable." *See Western Ag*, 43 Wn. App. at 173. Before that, the cases spoke only in terms of a "presumption." *See, e.g., Nearhoff*, 156 Wash. at 628.

suggestion that presumptions never shift the burden of proof. They do:

> One theory, often attributed to James Thayer, is that a presumption merely shifts the burden of producing contrary evidence to the party against whom it operates. ... The theory obviously minimizes the importance of a presumption. [¶] A second theory, often attributed to Edmund Morgan, gives presumptions far more vitality. ***Under the Morgan theory, a presumption actually shifts the burden of proof as to the presumed fact.***

Tegland, *supra*, § 301.13 (emphasis added). Consistent with the "Morgan theory," many Washington cases hold that the party against whom a presumption applies has the burden of disproving the presumed fact by a preponderance of the evidence. *Id.*, § 301.15 (citing cases); 6 Wash. Prac., Wash. Pattern Jury Instr.—Civ., WPI 24.05 (6th ed. 2012) (model instruction for presumptions that shift the burden of proof).

This is one of those cases. The DOR cannot cite a single fixtures case that holds that the presumption of intent "disappears" upon a showing of some contrary evidence. Rather, consistent with the central role intent plays in fixtures analysis, the cases show that the presumption has real "vitality," and works to shift the burden of proof on the issue. *See Strain v. Green*, 25 Wn.2d 692, 700, 172 P.2d 216 (1946) (presumption must be "overcome" by contrary evidence); *Cutler v. Keller*, 88 Wash. 334, 337, 153 Pac. 15 (1915) (presumption controls in the "absence of evidence of a contemporaneous contrary intention"). Indeed, at least until now, the

Department has applied the presumption in precisely this way. DOR Det. No. 89-55, 7 WTD 151 (1989) (once taxpayer proved annexation by owner, burden was on the "revenue officer" to "rebut this presumption").

Finally, this Court can easily reject the Department's argument that the presumption somehow conflicts with RCW 82.32.180's allocation of the burden of proof in refund cases. DOR Br. at 29. Again, the DOR provides no authority for its argument. Courts are required to apply the common law test to determine whether an item is a fixture for tax purposes. *Western Ag*, 43 Wn. App. at 171; DOR Det. No. 91-317, 12 WTD 51 (1993). The presumption is a critical component of that test, and only applies if the taxpayer successfully proves annexation and adaptation. In all events, the burden rests on the taxpayer to prove "the correct amount of the tax." Just as RCW 82.32.180 does not forbid courts from applying rules of statutory construction against the DOR, *see Agrilink Foods, Inc. v. Dep't of Revenue*, 153 Wn.2d 392, 399 n. 1, 103 P.3d 1226 (2005), the statute does not forbid courts from applying a legal presumption against the DOR either. RCW 82.32.180 does not trump the common law.

2. The DOR Did Not Prove That The Port Intended Only A Temporary Annexation.

The trial court's flawed analysis on annexation doomed its analysis on intent. Because the trial court erred in not finding annexation and

refusing to apply the presumption of intent, at the very minimum, remand is necessary so that the trial court can consider the evidence in light of the DOR's burden on the issue. As APL explained, however, in the interest of judicial efficiency, this Court can and should examine the undisputed evidence itself and conclude that the DOR did not carry its burden of proof. *See* APL Br. at 26-27 (*citing Kunkel v. Fisher*, 106 Wn. App. 599, 23 P.3d 1128 (2001)). Although the DOR complains that this Court should not "re-weigh" the evidence (DOR Br. at 22), it does not dispute the Court's authority to review the record in light of the proper burden of proof and, more conspicuously, does not dispute that—if the element of intent is presumed in APL's favor, as it must—the DOR did not present sufficient evidence to overcome that presumption as a matter of law.

a. There Is No Objective Evidence That The Port Intended A Temporary Annexation.

Throughout its brief, the DOR wrongly frames the issue of intent as whether the Port "treated," "classified" or "considered" the T-5 Cranes to be personal property, not fixtures. DOR Br. at 13, 16-22. The trial court made the same mistake. CP 203 (FF ¶ 27: "the Port intended the T5 Cranes to be equipment in inventory (tangible personal property), not fixtures."). But, as discussed below, for purposes of a fixtures analysis, the only relevant intent is whether, at the time of installation, the Port

intended T-5 Cranes to become a "permanent annexation" to Terminal 5—not whether it subjectively believed the cranes were personal property or characterized them as such. *Dep't of Revenue v. Boeing Co.*, 85 Wn.2d 663, 668, 538 P.2d 505 (1975); *see also Christensen Group, Inc. v. Puget Sound Power & Light Co.*, 44 Wn. App. 778, 783, 723 P.2d 504 (1986) ("the issue of intent to permanently annex cannot be decided as a matter of law simply by considering subjective declarations").

On this key issue, the DOR can point to no objective evidence that the Port intended only a temporary annexation. All the evidence confirms that the Port installed the T-5 Cranes with the intent that they remain at Terminal 5 for their entire useful lives—which, for equipment, is a "permanent annexation." *Reeder v. Smith*, 118 Wash. 505, 510, 203 Pac. 951 (1922). The DOR simply ignores the undisputed evidence that the Port spent millions of dollars rebuilding Terminal 5 to accommodate the T-5 Cranes; that the Port insisted that APL sign a 30-year lease because that was the expected useful life of the T-5 Cranes; that the lease obligates the Port to keep the cranes in "full operating condition" for that entire 30-year term (*see* APL Br. at 28-30); and—most poignantly—that the Port's former executive director provided uncontroverted testimony that, "at the time ... the intent was that those [cranes] were ... the integral part of the container facility and were not going to be moved." RP (9/27/11) at 93.

Indeed, the only objective evidence that the DOR can point to on intent is the fact that it is possible to remove the T-5 Cranes from Terminal 5, a fact the trial court cited as well. DOR Br. at 14-15; CP 203 (FF ¶ 28). As APL has explained, however, the issue is not whether the cranes can be removed, but whether the Port installed them intending to do so. *Strong*, 9 Wn.2d at 229-30 ("that most of that equipment ... could be removed ... [is] not determinative of the particular issue"); *Amer. Radiator*, 62 Wash. at 58 ("[a]though such appliances could ... be separated and removed ..., we do not think they were installed ... with any such purpose in view"). The DOR itself has recognized and applied this principle in the past. DOR Det. No. 89-55, 7 WTD 151 (1989) ("[w]hether the taxpayer could remove the presses without significant damage ... is not a significant factor as to the intent ... to permanently affix the machine to the freehold, unless the equipment was specifically designed to be removable"). But not here.

The DOR is content to ignore the evidence on this point too—for good reason. The testimony was unequivocal that the T-5 Cranes were specially manufactured for use at Terminal 5, with no effort to design them to be disassembled, removed and reassembled somewhere else. RP (9/26/11) at 55, 73-76; RP (9/27/11) at 90, 93. Certainly, the repositioning of one crane in 1999 following modification does not show that the Port intended a temporary annexation when it installed the cranes some 13

years earlier. DOR Br. 15-16. If anything, it shows just the opposite; the crane was modified (to increase its height) at great expense and engineering effort to enhance its *long-term* value to the Port as a container facility. RP (9/26/11) at 73; RP (9/27/11) at 138, 143-46, 155-56. Like everything else, this fact corroborates, rather than refutes, the presumption and evidence that the Port intended to make a permanent annexation.[5]

Boeing does not change the analysis; indeed, as APL explained, it only confirms it. APL Br. at 32-33. In *Boeing*, because the jigs at issue could be used only for manufacturing 747s, they were "designed in such a manner that they [could] be disassembled and moved" if, in the future, Boeing made "changes in the current program." *Boeing*, 85 Wn.2d at 669. In other words, it wasn't the fact that Boeing *could* remove the jigs that proved only a temporary annexation, it was that Boeing *planned* to remove the jigs. Here, the facts are the opposite; from the million dollar rebuild of Terminal 5, to the unprecedented long-term lease with APL, to the unique design of the T-5 Cranes, the evidence shows that the Port never planned

[5] Pointing to Terminal 30, the DOR argues it was "certainly feasible" that the Port could convert Terminal 5 to a different purpose—thereby rendering the T-5 Cranes' annexation something less than "permanent." DOR Br. at 14-15. Unlike Terminal 30, the Port spent tens of millions of dollars rebuilding Terminal 5 and manufacturing the T-5 Cranes to create a state-of-the-art cargo container facility. To suggest that the Port harbored a secret intention to walk away from this massive investment before the end of APL's lease—or, more accurately, the useful lives of the T-5 Cranes—is unsupported by any evidence and pure fantasy.

to remove the cranes. History proves the point: in the 25-plus years since their installation, even as the end of their useful lives approaches, the T-5 Cranes have never been removed from Terminal 5, nor is there any evidence that the Port intends to do so. *Boeing* helps APL, not the DOR.

Again, *Seatrain* is on point. In rejecting the same argument that the DOR makes here, the court concluded correctly that in assessing intent, "permanence is to be distinguished from perpetuity," reasoning:

> While ... it was theoretically possible to transfer the cranes ... to another location and/or [move them to] areas of the wharf where the rails did not extend, the fact remains that in reality none of the suggested measures were carried out. Instead, the record bespeaks that the Agreement accorded Seatrain a long-term lease to use the cranes; and that, availing itself of its contractual rights, Seatrain did use the whole facility, including the cranes, continuously. No evidence was presented that the transfer of the cranes to another port was contemplated or was imminent, much less that any actual step was taken in that direction.

83 Cal.App.3d at 78. All the same is true here; the fact that it is possible to remove the T-5 Cranes is not evidence that the Port intended to do so.

b. The DOR's Subjective Evidence Did Not Overcome The Presumption Of Intent.

Unable to cite *objective* evidence to show that the Port intended only a temporary annexation, the DOR relies on the trial court's findings on the Port's *subjective* belief which, the DOR argues, demonstrates that the Port "considered" the cranes to be personal property. CP 203-207 (FF ¶¶ 29-43). But as APL explained, and the DOR does not dispute, a party's

belief or classification of an item as a fixture or personal property is largely irrelevant to the issue of intent and, by itself, legally insufficient to overcome the presumption of intent. APL Br. at 35 (citing cases); *also Strain*, 25 Wn.2d at 700 ("[t]his presumption is not overcome by evidence of secret intention"). Even in *Boeing*, the Supreme Court recognized that "Boeing's categorization of its equipment certainly is not conclusive as to what is and is not a fixture[.]" *Boeing*, 85 Wn.2d at 670. The Port's purported categorization of the T-5 Cranes is equally inconclusive here too. And, even if the Port's subjective belief mattered, the evidence does not show that the Port considered the cranes to be personal property.

The DOR points to the fact that the Lease does not define the T-5 Cranes as part of the "Premises" or "improvements" leased by APL. DOR Br. at 16-18; CP 203-205 (FF ¶¶ 30-36). Of course, the Lease does not define the cranes as personal property either. Ex. 101. More importantly, the DOR presented no evidence to show that the parties drafted the Lease with an eye towards the cranes' classification as real or personal property. They didn't. The T-5 Cranes were an "instrumental" aspect of the parties' agreement. RP (9/27/11) at 86. The parties owed multiple, unique and specific obligations regarding the cranes—from the Port's duty to install and maintain them, to the APL's duty to pay specially calculated charges to use them; they could not simply treat the cranes like other aspects of the

leased premises. In short, the fact that the Lease contains separate provisions regarding the T-5 Cranes simply reflects a drafting necessity to address rights and obligations specific to the cranes, not proof that the Port intended their annexation to be a temporary one.

The DOR's reliance on the Port's so-called strategy documents—which refer to the cranes as "inventory"—is even more tenuous. DOR Br. at 18-19; CP 203-205 (FF ¶¶ 37-40). Here too, there is no evidence the Port considered the cranes' property status when preparing the documents. That the documents were prepared many years after the Port installed the cranes only reinforces their irrelevance. Moreover, the DOR cannot explain why the term "inventory" is inconsistent with the cranes' status as fixtures. It's not; an inventory is simply a list of property, both real and personal. And, even if the term is more often associated with personal property, it still applies to fixtures; a fixture *is* personal property that is permanently annexed to the realty. For this reason, as APL explained and the DOR ignores, Washington cases and WAC 458-12-010 recognize that equipment and machinery can be—and often are—fixtures. APL Br. at 34. The fact that the Port took "inventory" of its cranes says nothing about whether it intended a permanent or temporary annexation.

Finally, the DOR relies on the Port's supposed tax treatment of the T-5 Cranes to support the trial court's theory of intent. DOR Br. at 19-21.

Pointing to the fact that retail sales tax does not apply to the lease of fixtures (RCW 82.08.020(1) & RCW 82.04.050(4)(a)), the DOR first argues that the Port "always collected tax on the lease of its container cranes." DOR Br. at 19-21. Wrong. Even the trial court made no such finding. While it is undisputed that the Port has collected sales tax from APL, no witness knew whether the Port had "always" done so. The Port's former executive director did not know. RP (9/27/11) at 96. The Port's tax manager began working for the Port in 1999. RP (9/28/11) at 308. APL's controller—whose testimony the DOR quotes—knew only that the Port collected tax from APL "as far as [his] time working there" starting in 2004. RP (9/27/11) at 189-190, 194. In any event, that the Port collected sales tax from APL at some point does not prove it was legally correct in doing so. Put simply, the DOR cannot point to the Port's challenged conduct as some sort of evidence that the conduct itself is proper.

The DOR next relies on the trial court's findings that the Port did not pay sales tax on the T-5 Cranes because the Port considered the cranes personal property subject to the "purchase for resale" exemption. CP 206-207 (FF ¶¶ 41-43). As APL explained, these findings are not supported by substantial evidence. APL Br. at 35-36. The DOR does not dispute that no witness knew whether or not the Port paid sales tax when it purchased the cranes in 1986. RP (9/27/11) at 114-15; RP (9/28/11) at 309-10, 346-

47. Nor does the DOR dispute that the Port could not locate a "resale certificate," which it should have if it did in fact purchase the cranes for resale. RP (9/28/11) at 347-49, 354; RCW 82.04.470. Finally, the DOR ignores the evidence showing that, if the Port did not pay sales tax, it was likely because the cranes' manufacturer was an unregistered out-of-state business at the time. RP (9/28/11) at 346, 350-51. To be sure, the DOR cannot overcome the presumption of intent and overwhelming objective evidence of permanent annexation where, as here, it is entirely speculative whether the Port did or did not pay sales tax on the cranes, or why.

III. CONCLUSION

The trial court should have considered the T-5 Cranes' adaptation when deciding annexation; it should have applied a presumption of intent in APL's favor. This Court should conclude, based on the undisputed evidence, that the T-5 Cranes are fixtures as a matter of law. The judgment below must be reversed and judgment entered in APL's favor.

RESPECTFULLY SUBMITTED this 7th day of December, 2012.

LANE POWELL PC

By _____

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CERTIFICATE OF SERVICE

I hereby certify under penalty of perjury that on December 7th, 2012, I caused to be served a copy of the foregoing **REPLY BRIEF OF APPELLANTS** on the following persons in the manner indicated below at the following address:

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Kathryn Savaria

Kathryn Savaria

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Cc: Docketing-SEA; McBride, Ryan P.; Edwards, Scott M.; Mitchell, Linda; julie@atg.wa.gov
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Dear Clerk, attached for filing is the following document:

Case No.: 86977-4
Case Name: APL Limited, American President Lines, Ltd. and Eagle Marine Services, Ltd., appellants v. Wash. State Dept. of Revenue, appellee.
Pleading: Reply Brief of Appellants
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Thank you.