



COMMONWEALTH of VIRGINIA
Department of Taxation

MEMORANDUM

TO: Lawrence Durbin, Assistant Tax Commissioner
Office of Customer Services

Robert Schultze, Assistant Tax Commissioner
Office of Compliance

FROM: Howard T. Macrae, Jr., Assistant Tax Commissioner
Office of Tax Policy

DATE: December 23, 1998

SUBJECT: *Steuart Petroleum Co. v. Virginia Department of Taxation*

This case stems from a sales and use tax audit assessment. The Richmond Circuit Court found in favor of Steuart Petroleum Co. ("Steuart") in a case concerning the liquidation of a business and the application of the occasional sale exemption. The Virginia Supreme Court denied the department's petition for appeal, thus adversely affecting the department's established policy on liquidation sales.

Facts of the Case

Steuart Petroleum owned and operated 24 service stations/convenience stores located throughout Virginia. Under a plan of liquidation, Steuart sold all of these locations to five separate buyers over a nine month period. Steuart testified that it tried to find one buyer for all of the Virginia locations but was unable to do so. Accordingly, the locations were sold in five geographical blocks to the five buyers. Each of the buyers were themselves established businesses which continued operating the service stations/convenience stores which were purchased from Steuart.

The department assessed Steuart on untaxed sales of fixed assets associated with the sales of the 24 stores. Shortly after the assessment, the department denied Steuart's § 58.1-1821 appeal and upheld the assessment. The determination relied on the department's established policy that the sale of a business over an extended period of time does not qualify as an exempt occasional sale. See Attachment 1.

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Circuit Court's Decision

The court found for Steuart. See Attachment 2. The primary basis for the court's decision was the language of the occasional sale regulation in 23 VAC 10-210-1080. The regulation defines an "occasional sale" to include "the reorganization or liquidation of any business." The court held that:

The defendant's [Dept. of Taxation] over broad application of the "three or fewer" provision to all types of occasional sales ignores the clear construction of the regulation: the term "occasional sale" may **also** be read to include the sale of all the assets of any business and the liquidation of any business.... The number (five) and the time frame (nine months) of sales collides with a single, **alternative** subsection of [TAX's] regulations. This sale/liquidation may not be denied an exemption solely by virtue of the defendant's misguided application of the "three or fewer" provision.

Implications

First, the court's decision is applicable only to liquidation sales. The court's decision does not jeopardize the department's established policy regarding the validity of the occasional sale exemption to other transactions. For example, fund raising sales by a nonprofit organization on more than three occasions within one calendar year remain taxable sales.

Second, the court's decision does not in any way imply that all liquidation sales are exempt occasional sales. Indeed, the court made a clear distinction between the controlled sale of assets in Steuart's case (and found to be exempt sales) and a piecemeal distribution of assets to many buyers over an long period of time (which continue to be taxable).

Ideally, the department's regulation on occasional sales will be revised to address exempt and taxable liquidation sales. In the meantime, the department will have to be very careful when assessing and ruling on liquidation transactions. The distinguishing elements the department will need to look at include:

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- The court noted that Steuart's liquidation was "approved by the unanimous consent of Steuart's Board of Directors." Such approval may prove a good indicator of an exempt occasional sale in subsequent cases;
- sales of assets to the general public (compared with Steuart's sales to established businesses);
- the number of transactions (compared to Steuart's five sales). Other criteria being equal, six or seven sales may not be enough to deny the exemption. Ten or more transactions may be enough to void the exemption;
- the period during which sales were made (compared to Steuart's nine months). Other criteria being equal, a small number of transactions in less than a year may create problems in light of the court's decision;
- other facts which may be used to distinguish cases from *Steuart*. For example, a protective claim has been filed by the buyer of a hotel (who was assessed sales and use tax on the furniture and fixtures associated with that purchase). In that case, the seller sold eight Virginia motels to eight separate buyers in a seven month period. The seller was a partnership established with the express purpose of selling a limited number of hotel properties. This differs from Steuart's case, in which the contested assets were used by Steuart to operate an established business.

The Office of the Attorney General advises that any differences that distinguish other liquidation cases from *Steuart* will have to be thoroughly documented. Further, compliance and customer service staff need to look beyond the "three or fewer" guideline when addressing liquidation sales. Still, the department retains some flexibility in advising taxpayers of the exemption based on individual circumstances.

If you have any questions about this issue, please contact Steven Schwartz in Office of Tax Policy at 367-0959.

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c: Leadership Team