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State and Local Taxation—County-Imposed Real Estate Sales Tax—Applicabilty to Corporate Transfers in Dissolution

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have indicated her belief that some rights or interest still remained in the vendee even after declaration of forfeiture. It is more likely, however, that the quitclaim deed was taken in order to increase the marketability of Palmer's title by destroying any possible cloud which the vendee's interest would create. In that case any inconsistency in conduct would obviously disappear as would the above possibility of relief from forfeiture.

Conceivably a third rationalization may be founded on the theory that the declaration of forfeiture was more closely analogous to a mutual rescission. This conclusion would result if the declaration of forfeiture were converted into an acceptance of the vendee's offer to rescind implied from his default. Even though Norlin accepted the mortgage knowing that it was subject to the vulnerability of a forfeitable contract, the fact that Palmer took an assignment of the vendor's interest with notice of the mortgage could result in her having less freedom to declare a forfeiture than the original vendor had. The element of *wilfulness* in the vendee's ability to destroy the security for the mortgage by defaulting in payment of installments, combined with the *voluntary* exercise of Palmer's *option* to declare a forfeiture on default, could have been considered so unfair that an equity court was unwilling to recognize the strict forfeiture *as between Norlin and Palmer*.

Balancing all the equities and considerations discussed above it is at least arguable that relief from strict forfeiture should not have resulted from the court's decree recognizing the survival of the mortgage as a lien. The complete absence of judicial discussion of the forfeiture issue directs the conclusion that the result should at least be re-examined when the opportunity next arises. HARTLEY PAUL

STATE AND LOCAL TAXATION

County-imposed Real Estate Sales Tax—Applicability to Corporate Transfers in Dissolution. Extending the reasoning in *Deer Park Pine Indus., Inc. v. Stevens County*,[1] *Doric Co. v. King County*[2] holds that a distribution of a dissolved corporation's sole asset to its sole shareholder, who does not assume an existing debt of the corporation,

[1] 46 Wn.2d 852, 286 P.2d 98 (1955).
[2] 57 Wn.2d 640, 358 P.2d 972 (1961).

is not a sale within the meaning of RCW 28.45.050, which authorizes counties to levy a tax on the sale of real estate.[3]

The plaintiff corporation instituted voluntary dissolution proceedings and a trustee was appointed according to law.[4] The only corporate asset was an apartment building, valued at $5,100,000 and encumbered by a mortgage securing an installment note with an outstanding balance of about $2,350,000. The trustee executed a warranty deed, conveying all of the corporation's interest in the apartment house to the sole shareholder. The deed stated that the property was conveyed subject to the lien; the shareholder did not assume the obligation secured by the mortgage. Subsequent to the distribution plaintiff paid all installments on the note as they came due out of the income from the building. The plaintiff paid the county real estate sales tax of one per cent of the obligation owing on the note under protest and brought an action for refund. The trial court entered summary judgment dismissing the suit.

The county real estate sales tax is not a tax upon property itself, but rather an excise upon the sale of property.[5] An excise tax could be levied upon *any* conveyance of property, even by gift,[6] but the statutes purport to authorize a tax only upon the sale of real property within the levying county.[7] The term "sale" is defined to "have its ordinary meaning and . . . [to] include any conveyance . . . or transfer of the ownership of or title to real property . . . or any estate or interest therein for a valuable consideration . . . ."[8] A lengthy list of exceptions then follows. Determining what constitutes a conveyance of an interest in real property for valuable consideration, the problem considered by the court in the *Doric* case, has been a prime problem in administering the tax.

This county-imposed (although state-authorized) real estate sales tax should not be confused with the state documentary stamp tax imposed by RCW chapter 82.20. The stamp tax is an excise tax on conveyancing instruments levied "upon . . . any . . . writing . . .

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[3] "The county commissioners of any county are authorized by ordinance to levy an excise tax upon sales of real estate not exceeding one per cent of the selling price." All Washington counties have implemented the tax. 1 CCH WASH. TAX REP. ¶ 56,542.

[4] RCW 23.01.530.

[5] Mahler v. Tremper, 40 Wn.2d 405, 243 P.2d 627 (1952) (construing the tax as being upon one of the incidents of ownership).

[6] *Id.* at 408, 243 P.2d at 628-29. The court quoted extensively from Bromley v. McCaughn, 280 U.S. 124, 136-38 (1929). See also Sablosky v. Messner, 372 Pa. 47, 92 A.2d 411 (1952).

[7] RCW 28.45.050, .060.

[8] RCW 28.45.010.

whereby any . . . realty sold shall be . . . conveyed to, or vested in, the purchaser . . . when the consideration or value of the interest . . . conveyed . . . exceeds one hundred dollars."[9] The term "realty sold" is not defined by this statute. This excise is very similar to the county tax; generally both will apply to the same transaction. The county tax is levied at the rate of one per cent of the consideration or selling price, while the state tax is roughly one-tenth of one per cent of the consideration.[10]

The applicability of the county tax to a corporate dissolution was first litigated in *Deer Park Pine Indus., Inc. v. Stevens County*.[11] Two corporations owned all of the stock in a third corporation, whose assets included a considerable amount of timber land. The jointly-owned corporation was dissolved and the trustee in dissolution distributed the land to the shareholder corporations who assumed the dissolved corporation's obligations. Stevens County sought to impose the tax based on the market value of the property situated in the county. It argued that: (1) to make the tax appropriate the only requirements are a transfer of an interest in real property and consideration, (2) the consideration here was the surrender and extinguishment of the rights in the dissolved corporation represented by the stock, and (3) the value of the stock surrendered was the value of the land so the tax should be assessed on that value.[12] The taxpayer argued that a distribution pursuant to a corporate dissolution is not a sale within the ordinary meaning of the word and thus should not be taxed. The taxpayer made the alternative argument that if the conveyance was made for valuable consideration, the only value given was the assumption of the corporate liabilities by the distributees. Thus, the tax, if imposed, should be measured by the amount of the liabilities assumed rather than the total value of the property distributed.[13]

A lengthy amici curiae brief was filed by a number of law firms, in which it was argued that the dissolution distribution was not a conveyance for valuable consideration inasmuch as nothing given by the distributees had been bargained for. It was further argued that because the distribution was in satisfaction of pre-existing rights of the

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[9] RCW 82.20.010.

[10] The definition of consideration differs slightly. The county tax includes the amount of a prior lien remaining after the sale, RCW 28.45.030, while the state tax excludes this amount. Wash. Rev. Act, Rule 184 (rev. 1960).

[11] 46 Wn.2d 852, 286 P.2d 98 (1955).

[12] See Brief for Respondent.

[13] See Brief for Appellant.

shareholders, title vested in them automatically after certain unilateral acts on the part of the corporation.[14]

The court concluded that "the science of semantics would be stretched beyond permissible limits to conclude that the transaction . . . constitute(d) a sale in 'its ordinary meaning,' "[15] but that still, it might be a conveyance for a valuable consideration. However, the shareholders' loss of their rights was not valuable consideration.

> The fact that the dissolution of the corporation is the act which terminates the right to participate in the management of the corporation, and makes operative the right to share in the distribution of assets, does not make the termination of the first, the consideration for the execution of the second. There is no conveyance for a valuable consideration, taxable under the ordinance and statutes we are considering, where a change of title to real property is effected solely as a result of its distribution to stockholders of a solvent corporation in the process of dissolution, except as hereafter noted.[16]

Neither did the court consider the actual surrender of the stock certificates to be valuable consideration; "their surrender is, at this stage of the proceeding, a matter of form and not of substance. The stockholder neither gained nor lost anything thereby."[17]

The court did determine, however, relying upon two federal cases[18] interpreting the federal documentary stamp tax,[19] that the voluntary assumption of the corporation liabilities by the distributee stockholders constituted giving valuable consideration, and that the tax was properly levied on the amount of the liabilities assumed. The underlying theory is that the net equity of the corporation in the assets was conveyed without consideration, but because the corporation's creditors have first claim on the distributed assets,[20] the distributees' assumption of the obligations is in effect a purchase of the creditor's interest. However, if the conceptual approach to the transaction is that the corporation can convey only its net equity in the property, then the result becomes anomalous in that the tax is imposed upon what *is not*

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[14] See Brief for Amici Curiae.

[15] Deer Park Pine Indus., Inc. v. Stevens County, 46 Wn.2d 852, 855, 286 P.2nd 98, 100 (1955).

[16] *Id.* at 857, 286 P.2d at 100-01.

[17] *Ibid.*

[18] Greyhound Corp. v. United States, 208 F.2d 858 (7th Cir. 1954); R. H. Macy & Co. v. United States, 107 F. Supp. 883 (S.D.N.Y. 1952).

[19] "There is hereby imposed, on each deed, instrument, or writing by which any lands, tenements, or other realty sold shall be granted... or otherwise conveyed to... any... person... when the consideration or value of the interest... conveyed... exceeds $100...." 26 U.S.C. § 4361 (1955).

[20] Taylor v. Interstate Inv. Co., 75 Wash. 490, 135 Pac. 240 (1913).

conveyed, rather than what *is* conveyed. A further criticism concerns the requirement that consideration be bargained for.[21] It is difficult to conceive that the assumption of debts is the inducement for the conveyance in the corporate dissolution.

The taxpayer in the *Doric* case, no doubt with an eye to the *Deer Park* decision, did not assume the debt of the corporation, but took the asset subject to the security interest, thus removing this factor as possible consideration for the conveyance. The county still sought to impose the tax, arguing that where the asset is valued at more than twice the amount of the debt secured, taking "subject to" is tantamount to "assuming," so that the taxpayer implicitly assumed the obligation.[22] Thus the county sought to apply the excise tax to all corporate dissolutions involving the distribution of real property which exceeds in value the debts secured by it, whether any liabilities are actually assumed or not. To this the court answered, "We disagree. . . . We did not find that, as a matter of law, stockholders agree to assume the corporate liabilities when they seek a voluntary dissolution of the corporation."[23] The court concluded that because there was no express assumption of the corporate debts by the distributee shareholder, the conveyance was not for valuable consideration, and thus no excise tax should be imposed. The same reasoning should be applied to a partial liquidation, for no substantial distinction exists. Florida has taken this position.[24]

Taken together, *Doric* and *Deer Park* have clear meaning for corporate shareholders contemplating dissolution. If all corporate obligations are satisfied prior to distribution, or if the distributees do not assume them, there is no argument—no tax is assessable.

But there is little guidance for solving similar but not analagous problems. Because the tax, though burdensome, rarely exceeds the cost of trying and appealing a case, litigation seldom reaches the appellate level at which definitive answers are given. The language of the statute, although becoming more explicit with each new amendment, is still so broad that in many circumstances the taxpayer is

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[21] "Consideration must actually be bargained for as the exchange for the promise." RESTATEMENT, CONTRACTS § 75 comment b (1932). See also Universal C.I.T. Credit Corp. v. DeLisle, 47 Wn.2d 318, 287 P.2d 302 (1955); Snyder v. Roberts, 45 Wn.2d 865, 278 P.2d 348 (1955).

[22] Brief for Respondent, pp. 2-10, 21-23, The Doric Co. v. King County, 57 Wn.2d 640, 358 P.2d 972 (1961).

[23] The Doric Co. v. King County, 57 Wn.2d 640, 645-46, 358 P.2d 972, 975 (1961).

[24] State *ex rel.* Palmer-Florida Corp. v. Green, 88 So. 2d 493 (Fla. 1956). *Contra,* OPS. ATT'Y GEN. 490 (Wash. 1951-53) (rendered before either *Deer Park* or *Doric*).

uncertain as to his obligations. For instance, if a taxpayer organizes a corporation for the purpose of conveying his real property to it, taking in return stock of that corporation, is this a "sale" within the meaning of the statute and ordinances? What of a merger or consolidation of two corporations involving real property? These situations are not covered by the statute.

Opinions of the Washington Attorney General on the question of what is a taxable sale are numerous. However, the Attorney General's position as counsel for the State Tax Division, and the comparable agencies of the counties, makes objectivity in interpreting the tax statute difficult.[25] Thus it appears that the prime purpose of these opinions is not to give impartial interpretations of the law, but rather to indicate the position of the State in a given situation. The taxpayer then knows only that he must litigate if he is to establish his contention. To predict the outcome of that litigation with any measure of reliability the practitioner must look elsewhere.

The Washington State Tax Commission has promulgated rules relating to the state documentary stamp tax. They do not necessarily apply to the county real estate sales tax, because of differences in language, but may be helpful by analogy. The state tax is phrased much like the federal documentary stamp tax; therefore the Tax Commission has promulgated a rule that "in situations not specifically covered by this rule, the Tax Commission will be guided by any covering regulation of the United States Bureau of Internal Revenue relating to federal documentary stamps."[26] In *Deer Park* the court indicates that these regulations may also be applied to the county tax by its statement that, "analogous to the (county) tax . . . is the Federal documentary stamp tax . . ."[27] and by its reliance on federal cases construing the federal tax.[28] Further, because the state and the federal tax statutes are worded similarly, the county tax apparently may be analogized to the state tax.

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[25] OPS. ATT'Y GEN. 98 (Wash. 1951-53), to the effect that deeds by which tenants in common partition their land in accordance with their respective undivided interests therein are taxable, was nullified by legislative amendment in 1955. Wash. Sess. Laws 1955, ch. 132, § 1. The *Deer Park* case similarly nullified the most recent opinion on the subject. OPS. ATT'Y GEN. 116 (Wash. 1953-55).

[26] Wash. Rev. Act, Rule 184 (rev. 1960). The comparable federal regulation may be found at Treas. Reg. § 43.4361 (1961).

[27] Deer Park Pine Indus., Inc. v. Stevens County, 46 Wn.2d 852, 857, 286 P.2d 98, 101 (1955). This conclusion is open to attack, because the former is levied upon a sale of realty (an act), while the latter is levied upon an instrument of conveyance (a document). Hence, the incidents taxed are totally different, although the one may normally accompany the other.

[28] See note 18, *supra*.

No other jurisdiction appears to have a statute phrased in the terms of the county provision, but several have taxes similar to the federal documentary stamp tax.[29] Litigation interpreting these acts may be of some assistance, but because of the uniformly low rates of these taxes, appellate decisions are rare.

These sources, although limited, do yield some helpful information regarding the problems previously alluded to: conveyance of property to a corporation upon its organization by its sole owner[30] and corporation mergers or consolidations.[31] Beyond this, one may only attempt to develop some basic principles from the applicable Washington decisions. An initial premise in Washington, and generally, in the construction of any tax statute is that its provisions should not be extended by implication beyond the clear import of the language used, and in cases of doubt the statute should be construed most strongly

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[29] Alabama, Colorado, Florida, Maryland, Massachusetts, Minnesota, Pennsylvania, South Carolina, Tennessee, Virginia, West Virginia, and District of Columbia.

[30] The Attorney General of Washington takes the position that a transfer of realty to a corporation by the sole shareholder, the consideration returned being the issuance of common stock, constitutes a sale. OPS. ATT'Y GEN. 100 (Wash. 1959-60). This follows a series of "precedents." See OPS. ATT'Y GEN. 11 (Wash. 1957-58); OPS. ATT'Y GEN. 29 (Wash. 1955-57); OPS. ATT'Y GEN. 25 (Wash. 1955-57) (transfer by a husband and wife under court order pursuant to a property settlement in a divorce proceeding); OPS. ATT'Y GEN. 225 (Wash. 1953-55); OPS. ATT'Y GEN. 313 (Wash. 1951-53). The latest opinion does not, however, take the *Doric* case into consideration, for although the opinion was issued two weeks after the *Doric* decision was rendered, the court's opinion did not appear in advance sheet form until a week after the opinion was issued.

The Federal Regulation states that a conveyance to a corporation in return for its stock is taxable, Treas. Reg. § 43.4361-2 (a) (7) (1961), but does not cover the "sole shareholder upon organization problem." One federal case has held such a transfer not taxable. Murray v. Hoey, 32 F. Supp. 1008 (S.D.N.Y. 1940) (the taxpayer was a non-stock corporation). Connecticut has held that such a transfer of personal property is a sale under a sales and use tax. Frank Amodio Moving & Storage Co., Inc. v. Connelly, 144 Conn. 569, 135 A.2d 737 (1957).

It was decided in *Deer Park* that when a corporation is dissolved, the termination of the rights incident to the ownership of stock was not "consideration" for the right to direct ownership of the asset by distribution. (See text accompanying note 16, *supra*.) The court may well determine, based upon this that the reverse procedure should be treated in the same fashion: that is, that the termination of direct ownership in an asset is not "consideration" for the rights incident to the ownership of stock received by the individual, and thus that no taxable "sale" occurred.

It would seem, however, that an organizer could build a stronger case for himself by paying cash for a few shares of stock; then conveying the realty to the corporation, taking nothing in return. He would still have sole ownership of the asset, through the corporation, but it would be extremely difficult to find consideration for the conveyance.

[31] The universal feeling seems to be that a corporate merger or consolidation does not involve a conveyance of property for consideration. OPS. ATT'Y GEN. 158 (Wash. 1951-53); Treas. Reg. § 43.4361-2 (b) (12). Courts generally agree. United States v. Seattle-First National Bank, 321 U.S. 583, 589-90 (1944); United States v. Niagara Hudson Power Corp., 53 F. Supp. 796 (S.D.N.Y. 1944); Rochelle Inv. Corp. v. Fontenot, 34 F. Supp. 118 (D. La. 1940); National Dairy Prods. Corp. v. Carpenter, 326 S.W.2d 87 (Mo. 1959) (under personal property sales and use tax).

against the government and in favor of the citizen.[32] A second basic principle is that a political subdivision has no inherent power to levy taxes, and thus cannot exceed the power delegated to it by the state.[33] Thus the counties of the state can never go beyond the statutory framework of RCW chapter 28.45.

The county real estate excise tax is dependent on (1) a conveyance (2) for valuable consideration.[34] Neither *Doric* nor *Deer Park* specifically hold that a conveyance occurs when a corporation is dissolved. In both the court assumed this premise. It may not, however, be so clear. Dissolution itself is a volitional act, but the transfer of the property interest automatically results.

> On dissolution, the legal title to land passes to the stockholders, and title to the corporate property vests in the stockholders as tenants in common and is subject to their contract if all debts have been paid and no receiver has been appointed. The sole stockholder in a dissolved corporation has such an interest in its property as may pass by will.[35]

This argument was made (although not very articulately) to the court by the amici curiae in the *Deer Park case*,[36] but apparently without persuasive effect.

As has been seen, the Washington cases establish that the surrender of stock certificates, or loss of the rights of stock ownership in a dissolution process, are not "valuable consideration." It should be noticed, however, that either surrender of certificates or loss of rights would constitute sufficient consideration in the contract sense to make a counter promise enforceable.[37] Hence, it appears that the court will require something more than the traditional "pepper-corn." The con-

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[32] Thys v. State, 31 Wn.2d 739, 199 P.2d 68 (1948); Pacific First Fed. Sav. & Loan Ass'n v. Pierce County, 27 Wn.2d 347, 178 P.2d 351 (1947); State v. Lawton, 25 Wn.2d 750, 172 P.2d 465 (1946); State v. Pacific Tel. & Tel. Co., 195 Wash. 244, 80 P.2d 780 (1938); Weyerhaeuser Timber Co. v. Henneford, 185 Wash. 46, 53 P.2d 308 (1936); Denny v. Wooster, 175 Wash. 272, 27 P.2d 328 (1933); Union Trust Co. v. Spokane County, 145 Wash. 193, 259 Pac. 9 (1927).

[33] Great No. R.R. v. Stevens County, 108 Wash. 238, 183 Pac. 65 (1919). See also Pacific First Fed. Sav. & Loan Ass'n v. Pierce County, 27 Wn.2d 347, 178 P.2d 351 (1947) (and cases cited therein); State *ex rel.* Hansen v. Salter, 190 Wash. 703, 70 P.2d 1056 (1937) (and cases cited therein).

[34] Required also under the federal documentary tax. See Treas. Reg. § 43.4361-1 (a) (4) (ii).

[35] 16 FLETCHER, CORPORATIONS § 8134 at p. 878 (1942). See also Cohen v. L. & G. Inv. Co., 186 Wash. 308, 57 P.2d 1042 (1936); Taylor v. Interstate Inv. Co., 75 Wash. 490, 135 Pac. 240 (1913).

[36] Brief of Amici Curiae, pp. 14-15, Deer Park Pine Indus., Inc. v. Stevens County, 46 Wn.2d 852, 286 P.2d 98 (1955).

[37] RESTATEMENT, CONTRACTS § 75 (1932).

cept of valuable consideration is often used in a conveyancing context to determine whether one taking a conveyance without notice of an outstanding interest will be protected by a recording statute. In this context it has been explained thus:

> Although there is authority to the contrary, generally the term "valuable consideration" is used in contradistinction to a good, valid, or sufficient consideration. The term means something of substantial value, such as money, or something that is worth money, as, for example, legal or other services. Moreover, to constitute a consideration the thing of value which is given must be in respect of the contract of sale.[38]

At least one other jurisdiction has required such consideration under a comparable statute: "actual monetary consideration or . . . considerations which have a reasonably determinable pecuniary value."[39]

If the county taxing authorities cannot be convinced of the justice of one's position on the basis of the sources and principles above discussed, then the taxpayer must become reconciled to payment of the tax although convinced that it is unjustly levied, unless he is prepared to sacrifice for the sake of principle. Only in rare instances, such as the *Doric* case, are sufficient amounts involved as to make an eventual victory worth the cost of the battle.

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[38] 92 C.J.S. *Vendor & Purchaser* § 323 at p. 225 (1955). See also 55 AM. JUR. *Vendor & Purchaser* § 736 (1946); Annot., 59 A.L.R. 632, 636 (1929).

[39] DeVore v. Gay, 39 So. 2d 796, 797 (Fla. 1949) (holding that promises to pay rent in the future and perform other covenants were not valuable consideration).

TORTS

Evidence of Lack of Malice by Defendant to Mitigate Damages in Defamation Action. Prior to the appearance of *Farrar v. Tribune Publishing Co.*,[1] it appeared reasonably clear that in defamation actions,[2] evidence of the defendant's malice or good faith was not admissible for the purpose of enhancing or mitigating damages. Since

[1] For a survey of the law of libel in Washington see Comment, 30 WASH. L. REV. 36 (1955).

[2] 57 Wn.2d 549, 358 P.2d 792 (1961).