TAX APPEAL BOARD OF THE STATE OF DELAWARE

EHM PENCADER VII LLLP and PENCADER , V LIMITED PARTNERSHIP LLLP	)	
Petitioners,	)	
v.	)	Docket Nos. 1538 and 1541
DIRECTOR OF REVENUE,	)	
Respondent.	)	

BEFORE: Todd C. Schiltz, Esq., Chairman, Joan M. Winters, CPA, and Sindy Rodriquez and Robert Slavin, Members

Michael F. Bonkowski, Esq., Therese A. Scheuer, Esq., Cole, Schotz, Meisel, Forman & Leonard, P.A. for Petitioners.

Jennifer R. Noel, Esq., Deputy Attorney General, for Respondent.

DECISION AND ORDER

The issue before the Board is whether non-party Pencader IV LLC ("Pencader 4"), petitioner Pencader V Limited Partnership LLLP ("Pencader 5") and petitioner EHM Pencader VII LLLP ("Pencader 7", and together with Pencader 4 and Pencader 5, the "Entities") comprised an enterprise with common ownership or common direction and control within the meaning of 30 *Del. C.* § 2301(d) during the period January 1, 2008 through March 31, 2010 ("Tax Period"). If the Entities comprised such an enterprise, then, collectively, they were entitled to just one periodic deduction for gross receipts tax purposes during the Tax Period. If they did not, then each of the Entities was entitled to its own periodic deduction for gross receipts tax purposes (and their collective gross receipts tax burden would diminish).

For the reasons set forth below, the Board concludes that the Entities comprised an enterprise and that the enterprise had common ownership and common direction and control

within the meaning of Section 2301(d) during the Tax Period. As a result, the Entities were entitled to just one periodic deduction for gross receipts tax purposes during the Tax Period.

Pertinent Statutory Provisions

Delaware taxpayers licensed as commercial lessors under 30 *Del. C.* § 2301(a)(6) are required to pay a tax on their gross receipts pursuant to 30 *Del. C.* § 2301(d). In pertinent part, Sections 2301(d) states that:

> (1) In addition to the license fee required by subsection[] (a) … of this section, every person [licensed as a commercial lessor] shall also pay a license fee at the rate of 0.307% of the aggregate gross receipts paid to such person attributable to activities licensable under this chapter ..., which fee shall be payable monthly on or before the twentieth day of each month with respect to the aggregate gross receipts for the immediately preceding month.[1] In computing the fee due on such aggregate gross receipts for each month, there shall be allowed a deduction of $80,000. *For purposes of this subsection, all branches or entities comprising an enterprise with common ownership or common direction and control shall be allowed only 1 monthly deduction from the aggregate gross receipts of the entire enterprise.* The monthly returns shall be accompanied by a certified statement on such forms as the Department of Finance shall require in computing this fee due.
>
> (2) Notwithstanding paragraph (d)(1) of this section, if the taxable gross receipts prescribed by paragraph (d)(1) of this section during the lookback period as defined in § 2122 of this title do not exceed $750,000, the return and payment of the additional license fee imposed for such month shall be due on or before the last day of the first month following the close of the quarter. In the case of such return, in computing the fee due on such aggregate gross receipts for each quarter, there shall be allowed a deduction of $240,000. *For purposes of this paragraph, all branches or entities comprising an enterprise with common ownership or common direction and control shall be allowed only 1 quarterly deduction from the aggregate gross receipts of the entire enterprise.* The quarterly return shall be accompanied by a certified statement on such forms as the Department of Finance shall require in computing this fee due.

30 *Del. C.* § 2301(d) (emphasis added). Thus, regardless of whether gross receipts taxes are paid on a monthly or quarterly basis, if several entities "compris[e] an enterprise with common

[1] The gross receipts tax rate changed twice during the Tax Period. For calendar year 2008, the applicable rate was 0.307%. For calendar year 2009, the applicable rate was 0.384%. For the remainder of the Tax Period, the applicable rate was 0.4147%.

ownership or common direction and control," then the entities that comprise that enterprise are entitled to just one periodic gross receipts deduction. *Id.*

Statement of Facts

Unless otherwise noted, the following facts are derived from the stipulation of facts submitted in Docket Nos. 1538 and 1541, the supplemental stipulation of facts filed on September 2, 2014, and the emails from the parties dated October 30, 2014 and November 4, 2014.

The Entities' Business Activities

Pencader 4 is a Delaware limited liability company that operated in Delaware and was licensed as a commercial lessor pursuant to 30 *Del. C.* § 2301(a)(6) during the Tax Period. Pencader 4 owns two parcels of real property together with the improvement thereon located at the Pencader Corporate Center. The two parcels are knows as Parcels 5 and 7. During the Tax Period, Pencader 4 owned Parcels 5 and 7, leased Parcels 5 and 7 to third parties, and received rental income from its third party renters.

Pencader 5 is a Delaware limited liability limited partnership that operated in Delaware and was licensed as a commercial lessor pursuant to 30 *Del. C.* § 2301(a)(6) during the Tax Period. Pencader 5 owns a parcel of real property together with the improvement thereon located at the Pencader Corporate Center. The parcel is knows as Parcel 2. During the Tax Period, Pencader 5 owned Parcel 2, leased Parcel 2 to third parties, and received rental income from its third party renters. Pencader 5's business and purpose consist solely of the acquisition, ownership, development, operation and management, including, without limitation, leasing or selling, of Parcel 2.

Pencader 7 is a Delaware limited liability limited partnership that operated in Delaware and was licensed as a commercial lessor pursuant to 30 *Del. C.* § 2301(a)(6) during the Tax Period. Pencader 7 owns a parcel of real property together with the improvement thereon located at the Pencader Corporate Center. The parcel is knows as Parcel 13. During the Tax Period, Pencader 7 owned Parcel 13, leased Parcel 13 to third parties, and received rental income from its third party renters. Pencader 7's business and purpose consist solely of the acquisition, ownership, development, operation and management, including, without limitation, leasing or selling, of Parcel 13.

During the Tax Period, each of Pencader 4, Pencader 5 and Pencader 7 held a separate gross receipts license, filed separate federal and state income tax returns, had separate bank accounts, and maintained separate contracts with vendors.

The assets of each of the Entities are subject to mortgage loans that impose restrictions on each entity's operations, including, in some instances, requiring a single purpose and single asset structure. The respective lenders have certain other rights, for example the right to approve or not approve certain types of leases.

As Pencader 4, Pencader 5 and Pencader 7 each owned real property located in the Pencader Corporate Center and as each leased its property to third parties during the Tax Period, they competed for tenants.[2] The Entities used the same property management company, an entity that manages and provides services to many properties other than the four owned by the Entities.

[2] The Entities compete for tenants to the extent the parcels they own are similar. The record before the Board does not contain any facts detailing the similarities or differences between Parcels 2, 5, 7 and 13.

Ownership of the Entities

The following chart identifies the owners of Pencader 4, Pencader 5 and Pencader 7 and each owner's respective ownership interest in each of the Entities during the Tax Period.

Owner	Ownership Interest		
	Pencader 4	Pencader 5	Pencader 7
Emory Holdings II[3]	20%	18%	32.5%
Robert Hill	20%	18%	16.25%
Paul McConnell	20%	18%	25%
Carmen Facciolo	20%	18%	16.25%
Linda Rowe-McConnell	10%	10%	5%
Joseph Fox	10%		5%
J. Richard Latini		18%	

All of the owners of Pencader 4, Pencader 5 and Pencader 7 are unrelated individuals or entities, except that Paul McConnell and Linda Rowe-McConnell are husband and wife. Emory Holdings II is owned by R. Clayton Emory, Davis Emory, John Emory and Georgia Emory Smith, all of whom are members of the same family.

Each of the owners identified above are or have been involved with real estate development projects, co-owned in certain circumstances with third parties who have no ownership interest in the Entities. In the past, certain of the owners or their affiliates have been adverse to one another in litigation. *See McConnell v. Emory Holdings, L.P.*, C.A. No. 16584 (Del. Ch.).

[3] The full name of this entity is Emory Holdings II Limited Partnership LLLP.

Governance of the Entities

The individuals and entities responsible for managing the affairs of the Entities during the Tax Period are:

	Managers/General Partners
Pencader 4	Emory Holdings II Robert Hill Carmen Facciolo
Pencader 5	Emory Holdings II Robert Hill Carmen Facciolo
Pencader 7	Emory Holdings II Robert Hill Carmen Facciolo

The partnership agreements for Pencader 5 and Pencader 7 give the general partners of each partnership the authority to manage its affairs, including the authority to develop, maintain, lease or sell the property the partnership owns.

The Gross Receipts Tax Returns

Each of the Entities filed gross receipts tax returns on a quarterly basis during the Tax Period reporting income from their leasing activities. Each one of the Entities claimed a deduction on its returns pursuant to 30 *Del. C.* § 2301(d).

The Director of Revenue's staff audited the Entities' returns for the Tax Period and determined that, during the Tax Period, Pencader 4, Pencader 5 and Pencader 7 comprised an enterprise with common ownership or common direction and control, and, therefore, that the Entities were allowed just one quarterly deduction.

Thereafter, the Director of Revenue issued notices of assessment notifying Pencader 5 and Pencader 7 that their claimed deductions during the Tax Period had been disallowed and

seeking the payment of additional gross receipts tax and the imposition of penalties and interest. The Director of Revenue allowed Pencader 4 to claim a quarterly deduction for the Entities. Pencader 5 and Pencader 7 filed timely protests of the notices of assessment. The protests were disallowed in a notice of determination and this timely appeal followed.

Analysis

As stated above, the issue in the case is whether the Entities "compris[ed] an enterprise with common ownership or common direction and control . . ." under Section 2301(d) during the Tax Period.

A. An Enterprise

Under Section 2301(d), two or more entities comprise an enterprise if the entities are pursuing a profit in the same line of business. *Music Service & Investment Co., LLC v. Director of Revenue*, Dkt. No. 1439 (Del. Tax App. Bd. June 13, 2007); *Bear-Season's Pizza & Restaurant, Inc. v. Director of Revenue*, Dkt. No. 1286 (Del. Tax App. Bd. March 9, 2001); *Del. Motor Sales, Inc. v. Director of Revenue*, Dkt. No. 1270 (Del. Tax App. Bd. Feb. 9, 2001); *Valueline Foods of Delaware, Inc. v. Director of Revenue*, Dkt. No. 850 (Del. Tax App. Bd. Dec. 10, 1993). Each of the Entities was a commercial landlord who leased the real property and improvements it owned to third parties for a profit during the Tax Period. As a result, the Entities comprised an enterprise under Section 2301(d) during the Tax Period. *Music Service*, opinion at 5 ("As Musico and Lanco are both landlords who lease commercial property for a profit, we conclude that they properly are viewed as a single enterprise.").

The Entities argue that the standard of "two or more entities pursuing a profit in the same line of business" employed by the Board to determine when entities comprise an enterprise is overly broad. The Entities contend that the Board should narrow the standard so that only two or

more "entities that are part of the same business organization pursuing profit in the same line of business" (Opening Brief at 15 (emphasis added)) comprise an enterprise. The Entities point to no case law or legislative history to support their narrow standard. Moreover, Section 2301(d) provides that "all branches or entities comprising an enterprise" are entitled to one deduction from gross receipts and thereby recognizes that an enterprise may be comprised of multiple separate entities or branches. The Entities' proposed standard is inconsistent with this mandate and effectively attempts to rewrite the statute so that it reads: "all branches or entities that are part of the same business organization comprising an enterprise" are entitled to one deduction from gross receipts. By advocating a construction that requires the insertion of language into Section 2301(d), the Entities violate a basic interpretive principle: judicial and administrative bodies are not free to "rewrite clear statutory provisions under the guise of 'interpretation.'" *Scattered Corp. v. Chicago Stock Exchange, Inc.*, 671 A.2d 874, 879 (Del. Ch. 1994), *aff'd*, 676 A.2d 907 (Del. 1996). The Entities' proposed standard must be rejected.

The Entities also contend that they do not comprise an enterprise because they competed with each other for tenants during the Tax Period. Yet, any competition between the Entities arose because the Entities were engaged in the same line of business – ownership and leasing of commercial property – owned real property and improvements located in the same business park and utilized the same property manager. While these circumstances caused the Entities to compete with each other at some level, they also support a finding that the Entities comprised an enterprise. Indeed, the standard utilized by the Board requires the entities to be in the same line of business and, therefore, to some degree, to be competitors. The fact the Entities competed with each other for tenants during the Tax Period does not prevent them from comprising an enterprise under Section 2301(d).

B. Common Ownership

The Entities were under common ownership during the Tax Period. As set forth above, the same five owners owned between 82% and 95% of the Entities during the Tax Period. The fact these five owners were not related by birth or marriage does not mean the Entities did not have common ownership during the Tax Period. Under any reasonable definition of common ownership, the Entities were under common ownership during the Tax Period for purposes of Section 2301(d).[4]

C. Common Direction and Control

The Entities were under common direction and control during the Tax Period. The same three individuals and entity served as the managers/general partners of each of the Entities during the Tax Period. In addition, the partnership and operating agreements give these managers/ general partners the authority to manage the affairs of each of the Entities, including the authority to develop, maintain, lease or sell the property each of the Entities owned. Under these circumstances, the Entities were under common direction and control during the Tax Period.

---

[4] The Entities rely on 30 *Del. C.* § 2120 to contend that there was no common ownership during the Tax Period. Section 2120 exempts payments from "related entities" from taxable gross receipts and provides that "[e]ntities are related whenever: (1) more than 80 percent in value of the stock . . . interests of each entity is owned directly, indirectly or beneficially by the same 5 or fewer individuals . . . ." 30 *Del. C.* § 2120(b). The Entities contend that Emory Holdings II is not an "individual" as that term is used in Section 2120 and, as a result, five owners did not own more than 80% of each of the Entities during the Tax Period and, as a result, there is no "common ownership of the Entities under Section 2301(d).

The fundamental flaw in the Entities' argument is that nothing indicates that the General Assembly intended for the "related entities" definition set forth in Section 2120 to serve as the definition for "common ownership" in Section 2301(d). The General Assembly frequently amends Section 2301(d) and if it had intended for Section 2120 to articulate the standard for "common ownership" in Section 2301(d), it could have amended Section 2301(d) to so provide. It did not and this suggests the General Assembly meant for the terms to have different meanings. As a result, this Board will not use the definition of "related entities" in Section 2120 as a proxy definition for "common ownership" in Section 2301(d). *See Official Committee of Unsecured Creditors of Motors Liquidation Co., v. JP Morgan Chase Bank, N.A.*, 2014 WL 5305937, at *3 (Del. Oct. 17, 2014) (inappropriate for court to engraft a condition into a statute when General Assembly could have written the statute to provide the claimed right but did not); *Freeman v. X-Ray Assocs., P.A.*, 3 A.3d 224 229 (Del. 2010) (a "commonly accepted rule of statutory interpretation . . . requires [courts] to give each distinctive term an independent meaning").

The Entities contend they were not under common direction and control during the Tax Period because: (a) they were competitors during the Tax Period, (b) the members and partners are not related by birth or marriage, (c) the members and partners have been involved in real estate development projects with persons not holding an ownership interest in the Entities, (d) certain of the members or partners have been adverse to one another in litigation in the past, (e) each of the Entities is subject to a mortgage loan which requires each entity to have a single purpose and hold a single asset, and (f) each of the Entities held a separate gross receipts tax license, filed separate federal and state tax returns, had separate bank accounts, and maintained separate contracts with vendors. These facts reflect individual business decisions by the Entities and their members or partners and do not overcome the fact that the same three individuals and entity were the managers or general partners of the Entities and these individuals and entity have complete managerial control over the Entities during the Tax Period.

D. The Entities' Other Arguments

The Entities contend that any ruling in favor of the Director of Revenue would be tantamount to disregarding their separate corporate existence. This is incorrect. The Board is not disregarding the separate existence of the Entities. Rather, the Board is concluding that, notwithstanding their separate corporate existence, the Entities must be viewed as an enterprise with common ownership or common direction and control for purposes of Section 2301(d). The statute expressly contemplates treating multiple entities as a single enterprise for purposes of calculating the applicable gross receipts tax deduction and that is all the Board is doing here.

The Entities also contend that any ruling in favor of the Director of Revenue will subject them to double taxation. Specifically, the Entities argue that a ruling for the Director will result

in each of the Entities having to pay both an annual franchise tax and gross receipts taxes during the Tax Period. The Entities are again incorrect.

Delaware imposes a franchise tax on almost all entities created under Delaware law.[5] The franchise tax is imposed for the privilege of operating as a Delaware entity. *See State v. Surety Corp. of America*, 162 A. 852, 854 (Del. Ch. 1932) (franchise taxes are imposed upon a corporation "for its privilege to exist" under Delaware law). The annual franchise tax is not dependent upon or related to an entity's gross receipts, income, company activity or whether the entity is a "franchise." Rather, it is a fixed rate tax, currently set at $300 for limited partnerships and limited liability companies, and must be paid in order for the entity to remain in good standing.

The gross receipts tax, in comparison, imposes a tax based on an entity's gross receipts, as that term is defined by statute. *See* 30 *Del. C.* § 2301. The amount of gross receipts tax an entity must pay is dependent upon three things: (a) the type of business license held by the entity, (b) the gross receipts/income generated by the entity, and (c) the gross receipts deduction that the entity can claim. 30 *Del. C.* § 2301.

As the franchise tax and the gross receipts tax do not tax the same thing, there is no double taxation.[6] As explained in *Lehman Brothers Bank, FSB v. State Bank Commissioner*, 2006 WL 345649 (Del. Super. Nov. 30, 2006), *aff'd in part and rev'd in part on other grounds*, 937 A.2d 95 (Del. 2007):

---

[5] As limited partnerships formed under Delaware law, the Entities must pay "an annual tax, for the use of the State of Delaware, in the amount of $300." 6 *Del. C.* § 17-1109(a). *See also* 6 *Del. C.* § 15-208(a) (requiring every partnership that has filed a statement of partnership existence to pay an annual franchise tax); 6 *Del. C.* § 18-1107(b) (requiring all domestic limited liability company to pay an annual franchise tax); 8 *Del. C.* § 503(a) (requiring most Delaware corporations to pay an annual franchise tax).

[6] 84 *C.J.S Taxation* § 58 ("In order to constitute double taxation . . . both taxes must be imposed on the same property or subject matter"); *id.* § 67 ("The imposition of franchise taxes, license fees or excises on corporations is not duplicative of taxes levied on their . . . income").

> A franchise tax generally is a tax on an entity for the right or privilege of doing business or exercising its franchise in a state. . . . Franchise taxes "are not placed upon a particular corporate business or transaction, but upon the privilege of doing business as a corporation and exercising corporate powers for the purpose of producing a profit." . . . .
>
> A franchise tax is different from other taxes, including income taxes, as it is imposed for different purposes. "The [franchise] tax is not laid on property or on income, though both are regarded in measuring it." A state can tax the entity's income and also impose a franchise tax since "income taxes are based on taxing individuals and entities on monies made whereas franchise taxes stem from the notion that a company should pay for the privilege of operating its business in this state."

2006 WL 345649, at *4 (citations omitted).[7]

Finally, the Entities contend that the Director of Revenue lacks the authority to allocate the periodic deduction to Pencader 4 and deny the deduction to Pencader 5 and Pencader 7. According to the Entities, "Title 30 does not grant the Director the authority to pick and choose among the entities as to how the deduction should be allocated. Should this Board determine that the Entities are entitled to only one deduction, this Board should hold that [the] Director cannot himself allocate the deduction." The Board disagrees.

Title 30, Section 521 gives the Director of Revenue the authority to examine any return and determine the correct amount of tax due. 30 *Del. C.* § 521(a). If the Director of Revenue determines the taxpayer owes additional tax, he is required to send the taxpayer a notice of assessment advising the taxpayer of the additional tax, interest and penalty owed. 30 *Del. C.* § 521(a), (c).

[7] A finding in favor of the Entities would not eliminate their obligation to pay either franchise taxes or gross receipts taxes. Rather, a finding for the Entities would reduce the amount of gross receipts tax they must pay (by increasing the number of periodic deductions they can claim on their returns) while a finding for the Director will increase the amount of gross receipts tax the Entities must pay (by decreasing the number of periodic deductions they can claim on their returns). Regardless of how this matter is resolved, however, the Entities will be subject to both franchise taxes and gross receipts taxes.

Here, the Director of Revenue reviewed the Entities' tax returns for the Tax Period, determined that they had impermissibly claimed multiple deductions, permitted Pencader 4 to claim the one deduction the Entities were entitled to claim and sent Pencader 5 and Pencader 7 notices of assessment. The Director has the power to take these steps pursuant to Section 521. In particular, pursuant to his authority to examine tax returns and assess unpaid taxes pursuant to Section 521, the Director has the authority to allow one of several entities that comprise an enterprise under common ownership or common direction and control to claim a periodic gross receipts tax deduction and to disallow any deduction claimed by any other entity that is part of the enterprise.[8] Any other result would impermissibly impair or prevent the Director of Revenue from enforcing Section 2301(d) and exercising his authority under Section 521.

Conclusion

For the reasons stated, the Board concludes that the Entities comprised an enterprise with common ownership or common direction and control within the meaning Section 2301(d) during the Tax Period and judgment is rendered in favor of the Director of Revenue.

The Director of Revenue is instructed to circulate a proposed form of order to Pencader 5 and Pencader 7 for review within fourteen (14) days of the date of this opinion. The proposed form of order shall detail the total tax, penalty and interest that Pencader 5 and Pencader 7 owe as of the date of this opinion for the Tax Period, as well as a per diem calculation for each additional day the amounts due pursuant to the order remain unpaid. Tax Appeal Board Rules 19(e) and 20. The parties shall file a joint proposed order for signature by the Board, or, if

[8] The fact that the Director of Revenue has the authority to allocate the periodic deduction to one of several entities that comprise an enterprise with common ownership or common direction and control does not prevent the entities from agreeing to allocate the deduction and/or tax liability in a different manner. Indeed, related entities often enter tax sharing agreements which allocate tax liability among the parties to the agreement. Nothing prevents the Entities from entering such an agreement here.

necessary, separate proposed forms of order, within thirty (30) days of the date of this opinion. Tax Appeal Board Rule 20.

Date: Dec. 10, 2014