

Cite as Det. No. 93-166, 14 WTD 022 (1994).

BEFORE THE INTERPRETATION AND APPEALS DIVISION  
DEPARTMENT OF REVENUE  
STATE OF WASHINGTON

In the Matter of the Petition	)	<u>D E T E R M I N A T I O N</u>
For Correction of Assessment of	)	
	)	No. 93-166
	)	
. . .	)	Registration No. . . .
	)	FY. . ./Audit No. . . .

- [1] RULE 170: RETAILING B&O TAX -- PRIME CONTRACTOR. Taxpayer corporation which contracted with a real property owners and subcontractors to construct buildings was a prime contractor when the taxpayer provided construction supervision, labor and accounting services; issued resale certificates as a general contractor; required subcontractors to provide it insurance coverage as contractor; and identified itself in contracts and correspondence as the contractor with contractor duties.
- [2] RULE 170, RULE 111 AND RULE 223; RCW 82.04.070 AND RCW 82.04.080: RETAILING B&O TAX -- PRIME CONTRACTOR -- PAYMENT TO THIRD PARTIES BY OWNER -- GROSS INCOME. Taxpayer is a prime contractor subject to assessment based on the total amount of construction costs even if the owner paid the third party suppliers and subcontractors directly. The taxpayer benefitted from such payments because they reduced or eliminated the taxpayer's personal liability from the debts. The owner's payments were part of the contract's consideration received by the taxpayer and are considered gross income to the taxpayer.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

NATURE OF ACTION:

The taxpayer appeals an assessment of tax based on a finding that it acted as a prime contractor.

## FACTS:

De Luca, A.L.J. -- The Department of Revenue audited the taxpayer for the period January 1, 1988 through December 31, 1991, and assessed retailing business and occupation (B&O) taxes, retail sales tax and interest. The Department credited the taxpayer for reporting part of the construction income under the service B&O classification.

The taxpayer is a corporation based in Washington. In 1988, the taxpayer's president signed on its behalf two construction contracts which describe the taxpayer as "the Contractor." The contract form used in both instances was the "Abbreviated Form of Agreement Between Owner and Contractor," AIA Document A107 (1978 ed.). The first contract pertained to the construction of the [City A] Inn, whose owner was a limited partnership. One of the limited partners was also the taxpayer's president. The contract specifically states that "the Contractor shall perform all work required by the contract documents for the [City A] Inn." The contract also declares "the Owner shall pay the Contractor . . . the contract sum of \$. . . .", subject to additions and deductions by change orders. Article 10 of the contract describes in detail the duties of the contractor. In short, those duties included ones normally performed by a prime contractor, such as ". . . supervise and direct the work . . . and be solely responsible for all construction means, methods, . . . and for coordinating all portions of the work under the contract."

Article 11 of the primary contract permits the contractor to contract with subcontractors for the project. The taxpayer used the AIA Document A401 (1978 ed.) form for the contractor-subcontractor agreements for both projects. The subcontract sample, included in the audit report for the first project, refers to the taxpayer as "the Contractor" and was signed by one of the taxpayer's officers and by the subcontractor. The subcontractor agreement specifically states in its Article 4 that "the Contractor shall pay the Subcontractor in current funds for the performance of the work, . . . the contract sum of \$. . . ." Under Article 9 the parties inserted that the subcontractor was required to "furnish the contractor with a certificate of insurance naming the contractor as additional insured." Article 12 of the subcontractor agreement details the rights and responsibilities of the contractor to the subcontractor, including payment.

Additional documents for the [City A] project show a bid from the same subcontractor which lists the taxpayer as the contractor.

Furthermore, the taxpayer provided signed resale certificates to subcontractors and suppliers which describe the taxpayer as a "general contractor" for the project.

The second construction project involved the [City B] Inn. Its owner was another limited partnership. The contract between the owner and the taxpayer likewise refers to the taxpayer as "the Contractor." The contract similarly states "the contractor shall perform all the work required by the contract documents for construction of the [City B] Inn." The contract reveals the owner would pay the contractor the contract sum of \$. . . . The contract specifically declares that sales tax is in addition to the contract sum.

We note the contract states it is ". . . for administration only to [taxpayer's president]." The contract also provides that "all expenses attributed to the building will be reimbursed to [taxpayer] or paid directly by [the owner]." Apparently the owner did pay many of the expenses because the audit report states the owner reported use taxes for most of the construction contracts.

Similarly, the taxpayer entered into agreements with the project's subcontractors. The first page of the subcontractor agreement sample in the audit report refers to the taxpayer as "the Contractor." The subcontractor was [a plumbing & heating company]. Accordingly, the taxpayer's president signed the agreement on behalf of the taxpayer, who is identified as the "Contractor." Article 4 declares "the Contractor shall pay the Subcontractor . . . the Contract Sum of \$. . . ." Whereas, Article 5 adds that "all payments will be the responsibility of the owner . . . and not [taxpayer]. Payments when due will not be released until approved by both [taxpayer] and the owner." The parties also inserted under Article 9 the provision that "the Subcontractor shall furnish the Contractor with a Certificate of Insurance naming the Contractor as additional insured."

The audit report contains as well an August 14, 1989, letter from the taxpayer's president to another subcontractor, [a framing company], concerning a payment dispute. The letter refers to the subcontract agreement and asserts that payment was the responsibility of the project owner and not the contractor. The taxpayer's president signed the letter on behalf of the taxpayer as the "contractor."<sup>1</sup>

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<sup>1</sup>Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

## ISSUE:

Was the taxpayer a prime contractor subject to an assessment of retailing B&O tax against either the full contract price or the total amount of construction costs?

## DISCUSSION:

The taxpayer argues that it did not act as a prime contractor for either project and should not be subject to such an assessment. Yet, it does not claim it was a speculative builder because it lacked ownership in the two real properties. Instead, it claims it was administering the projects for the owner by "consultation and management."

Despite the tangible evidence, the taxpayer denies it had a written contract for the [City A] project. Rather, it claims the [City A] contract was between the owner and the taxpayer's president. The taxpayer asserts it did not construct that project, but "was used for accounting purposes, and received no payment from the [owner] except to reimburse it for the job superintendent and laborers." The taxpayer admits elsewhere in its petition it did provide some construction labor for the [City A] project.

The taxpayer concedes it had a written contract for the [City B] project. However, the taxpayer declares it merely managed the [City B] project's construction for the flat fee and did not provide construction labor. The taxpayer adds that the laborers and the job superintendent in [City B] were on the owner's payroll. Furthermore, the taxpayer contends it acted only as an agent for the owner when it signed contracts with subcontractors and suppliers. The taxpayer claims the owner itself paid such third parties directly and did not use the taxpayer even as a conduit for payment. The taxpayer states the only money it received for the project was the flat fee.

RCW 82.04.050 (2) defines retail sales for building construction. WAC 458-20-170 (Rule 170) implements the statute regarding such construction activities. The rule defines a "prime contractor" as a person engaged in the business of constructing buildings for consumers. A "subcontractor" means a person in business performing a similar service for persons other than consumers. A "speculative builder" means one who constructs buildings for sale or rental upon real estate owned by him. Persons, including corporations, who perform construction upon land owned by their corporate officers are constructing upon land owned by others, and are taxable as sellers under the rule, and not as "speculative builders."

The rule provides that prime contractors are taxable under the retailing B&O classification upon the gross contract price. Where no gross contract price is stated in any contract or agreement between the builder and the property owner, then the measure of B&O tax is the total amount of construction costs required for the construction and paid by the builder.

[1] We will discuss the [City A] contract first. Not only does that contract with the owner describe the taxpayer as the "Contractor," it specifically lists the duties the taxpayer is required to perform. As noted above, those duties are ones normally performed by a contractor. For example, the taxpayer even admits it received payments from the owner for accounting services, job supervision and labor. We also note the taxpayer's president signed the agreement on behalf of the taxpayer which is designated as the "Contractor" above his signature. Additionally, the taxpayer gave resale certificates to subcontractors and materials suppliers naming itself as the "General Contractor" on those certificates.

Furthermore, the taxpayer entered into agreements with subcontractors. Those agreements list the taxpayer as "the Contractor" and require the taxpayer to pay the subcontractors for their services. The taxpayer inserted into the subcontractor agreements a provision that the subcontractor would furnish the taxpayer, as the "Contractor," a certificate of insurance naming it as an insured party. The subcontractor agreement also identifies the taxpayer as the "Contractor" where the taxpayer's officer signed the document. The agreement does not identify the taxpayer as the owner's agent.

We find the taxpayer was acting as a prime contractor for the [City A] project in light of these facts and Rule 170's definition of a prime contractor. See Det. No. 90-4, 9 WTD 45 (1990). The assessment was correctly based on the gross contract price plus or minus work order changes.

We next consider the [City B] project. Like the [City A] project, the contract between the owner and the taxpayer identifies the taxpayer as "the Contractor." The taxpayer also signed agreements with subcontractors identifying itself as the contractor with provisions in those agreements obligating it to pay the subcontractors. Similarly, the taxpayer demanded the subcontractors provide it with insurance coverage as the project's "contractor." The taxpayer's officers signed those subcontractor agreements in the taxpayer's name and not as an agent for the owner. The taxpayer also gave subcontractors and suppliers resale certificates listing itself as the general

contractor. The taxpayer's president in a letter to a subcontractor identifies the taxpayer as the contractor for the project. Furthermore, the agreement with the owner states that sales tax is in addition to the flat fee. All of these facts are persuasive evidence that the taxpayer and the many parties it dealt with considered it the prime contractor. In sum, the taxpayer assumed the contractual obligations and benefits of a contractor. 9 WTD 45, supra.

There are a few differences between the [City A] and [City B] contracts. The [City B] contract does not have a gross contract price. The contract merely lists the flat fee payable for "administration only" to the taxpayer's president. Thus, the assessment was based on construction costs. This contract provision, however, is in addition to other provisions in the agreement obligating the taxpayer to provide contractor services such as supervision and coordination of the work. The taxpayer has not explained the difference between construction supervision as a prime contractor and construction administration as a manager. Nor do we find a difference when considering the taxpayer issued resale certificates, signed agreements as a contractor, and corresponded with subcontractors as the contractor while demanding that it be insured as the contractor.

The taxpayer's agreements with subcontractors do state all payments to them will be the responsibility of the owner and not the taxpayer. However, this provision is in addition to other provisions in the agreements obligating the taxpayer to pay the subcontractors. Furthermore, the taxpayer's officers did not sign the subcontractor agreements as agents for the owner. Rather, they signed them while representing the taxpayer as contractor. 9 WTD 45, supra.

[2] The taxpayer also claims that, unlike [City A], it did not provide labor and supervision at [City B]. It states it did not even act as a conduit for payment of the construction costs at [City B] because the owner itself directly paid the costs. However, the taxpayer as the contractor directly entered into agreements with the subcontractors and suppliers and it provided them resale certificates. These facts show that the taxpayer was either primarily or secondarily liable to those parties. Thus, payments to those parties could not qualify as exempt pass-through income for the taxpayer under WAC 458-20-111 (Rule 111).

In fact, the suppliers and subcontractors billed the taxpayer because, one, the contracts personally obligated the taxpayer to pay them and, two, the taxpayer issued resale certificates to them. The taxpayer cannot escape the tax assessment merely because the owner paid the bills directly to the third parties.

When the owner paid such bills, the taxpayer benefitted because the payments relieved the taxpayer of personal liability for those debts. Indeed, part of the consideration which formed the contract between the owner and the taxpayer was that the owner would either reimburse the taxpayer for construction costs paid or pay the costs directly to the third parties. Under RCW 82.04.080 " `gross income of the business' means the value proceeding or accruing by reason of the transaction of the business engaged in . . . ." RCW 82.04.090 defines "value proceeding or accruing" as "the consideration, whether money, credits, rights, or other property expressed in terms of money, actually received or accrued." Thus, payments by the owner to the third parties were part of the taxpayer's gross income.

See also WAC 458-20-223 (Rule 223) which provides that persons who perform contracts on a cost-plus-fixed-fee basis are subject to tax

As to constructing and repairing of new or existing buildings, [under] WAC 458-20-170; . . .

The measure of the tax under each of the foregoing types of contracts is the amount of profit or fixed fee received, plus the amount of reimbursements or prepayments received on account of sales of materials and supplies, on account of labor costs, on account of taxes paid, on account of payments made to subcontractors, and on account of all other costs and expenses incurred by the contractor, plus all payments made by his principal direct to a creditor of the contractor in payment of a liability incurred by the latter.

Under this rule, direct payments by the owner to the third parties who contracted with the taxpayer to provide services and/or supplies were properly assessed against the taxpayer as gross income. Det. No. 89-248, 10 WTD 264 (1988).

#### DECISION AND DISPOSITION:

The taxpayer's petition for correction of assessment is denied.  
DATED this 14th day of June, 1993.