

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

In the Matter of the Petition)	<u>D</u> <u>E</u> <u>T</u> <u>E</u> <u>R</u> <u>M</u> <u>I</u> <u>N</u> <u>A</u> <u>T</u> <u>I</u> <u>O</u> <u>N</u>
For Correction of Assessment of)	
)	No. 88-199
)	
. . .)	Registration No. . . .
)	
)	

[1] **RULE 170:** RETAIL SALES TAX -- SPECULATIVE BUILDER --
WHAT CONSTITUTES -- JOINT VENTURERS -- ETB 275.08.170. A
"speculative builder" means a person who constructs
buildings for sale or rental upon real estate owned by
the builder. The deeding of a half interest in land
owned by one joint venturer to a co-venturer, a
contractor, for security purposes only did not make the
contractor or their joint venture the owner of the land.

[2] **RULE 170:** RETAIL SALES TAX -- CONSTRUCTION CONTRACT --
JOINT VENTURE -- FACTORS DETERMINING. The tax
consequences applicable to joint venturers are proper
when:

- 1) the joint venture was specifically formed
to perform the contract work,
- 2) the formation of the joint venture
occurred before any of the work required by
the contract had been undertaken,
- 3) the contract work was in fact performed by
the joint venture,
- 4) the funds were handled as a joint venture
rather than as separate funds of any party to
the joint venture agreement, and
- 5) there is a contribution of money, property
and/or labor so that any profit or loss
incurred by the joint venture is
proportionately shared by all joint venturers.

Sale treated as retail sale between a contractor joint venturer to a co-venturer where the funds were not handled as joint venture funds and the contractor was guaranteed payment from the co-venturer.

- [3] **RULE 178 AND RCW 82.08.050:** RETAIL SALES TAX -- USE TAX -- COLLECTION OF. RCW 82.08.050 provides that the Department has discretion to proceed directly against the buyer or the seller for collection of retail sales tax that is due. The use tax supplements the retail sales tax by imposing a tax of like amount upon the use within this state as a consumer of tangible personal property on which the retail sales tax was not paid.

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.

TAXPAYER REPRESENTED BY: . . .

DATE OF HEARING: September 15, 1987

NATURE OF ACTION:

The taxpayer, a construction company, protests the assessment of retailing B&O and retail sales tax on the amount received as a member of a joint venture for the construction of a home. The taxpayer contends the construction and sale of the home was done by the joint venture as a speculative builder.

FACTS AND ISSUES:

Frankel, A.L.J. -- The taxpayer's records were examined for the period January 1, 1982 through December 31, 1985. The audit disclosed taxes and interest owing in the amount of \$ Assessment No. . . . in that amount was issued on November 13, 1986.

At issue is the assessment of retailing and retail sales tax on the contract amount (materials, labor, and overhead) received by the taxpayer as part of the . . . Joint Venture. The taxpayer and . . . (trust) formed the joint venture in December of 1982. The purpose of the joint venture was the construction for resale and resale of a residence.

The agreement provided that the joint adventurers' duties were as follows:

8. a. Duties of [taxpayer]: [taxpayer] shall perform the following in furtherance of the joint venture:

(1) Provide a design for the residence to be constructed. TRUST to review and approve preliminary design prior to construction drawings;

(2) Provide TRUST with building specifications, cost estimate and a fixed dollar amount for overhead, and an estimate for time to construct;

(3) Construct the residence;

(4) Manage the design, construction and marketing of the residence;

(5) Charge overhead at the rate of 2 1/4% of the gross sale price of the residence.

b. Duties of TRUST: TRUST shall perform the following in furtherance of the joint venture:

(1) Provide the building lot;

(2) Provide the necessary financing to construct the residence. Said funds shall be disbursed to [taxpayer] on a monthly basis upon request of [taxpayer] according to reimbursable costs incurred during the prior period as defined in the construction contract. The TRUST shall make checks for [the taxpayer's] labor and overhead payable to [taxpayer]. All other checks shall be payable jointly to [taxpayer] and the subcontractor or supplier. The TRUST shall employ, at its option and expense, a progress inspector to approve monthly drawings. In the event a dispute arises as to the amount of draw to which [taxpayer] is entitled, said dispute shall be resolved by arbitration as hereinafter provided;

(3) Manage the joint venture as provided in Paragraph 15 of this Agreement.

The trust contributed the management of the joint venture and the construction financing for the residence. The title to the property was to remain in the Trust, and upon sale, the conveyance document was to be executed by the Trust as legal title owner, subject to the taxpayer's interest as defined in the agreement.

The net profit/loss was to be the net proceeds of sale reduced by the following which were to be paid in full in the order in which they appear:

- (1) Unreimbursed construction costs owing to the taxpayer;
- (2) Reimbursed construction costs advanced by the Trust;
- (3) Operating expenses, including legal expenses, accounting fees, and advertising costs;
- (4) Lot costs--\$100,000 to the Trust as reimbursement for the unimproved real property upon which the residence was constructed; and
- (5) Financing costs. All monies advanced to the Trust pursuant to the above paragraph 8.b.(2) was to bear interest from the date of disbursement until the date of termination of the venture.

In January of 1982, the Trust quit-claimed an undivided one-half interest in the property to the taxpayer. The deed states the transfer "was for and in consideration of security purposes only." A memorandum of the joint venture agreement was also recorded in January of 1983.

The joint venture treated the construction as speculative. The auditor concluded that the terms of the joint venture agreement indicated the taxpayer was subject to tax as a prime contractor. This conclusion was based primarily on the following:

- 1) the taxpayer was not the owner of the land, and
- 2) the taxpayer was guaranteed payment for its construction activity.

The taxpayer protests the assessment on grounds there was no "customer" until the home was completed and sold to the third party. The taxpayer contends he is being taxed double as if it were both a custom and a spec sale.

Also at issue is deferred sales/use tax assessed on materials and consumable supplies used by the taxpayer in speculative building on which the vendors did not charge sales tax. The taxpayer contends that as a buyer it was not his obligation to collect the sales tax. The taxpayer's position is that the state should collect the \$. . . owing from the sellers.

Finally, the taxpayer seeks a credit of \$. . . sales tax that the company alleges was paid to a subcontractor but not included in the audit.

DISCUSSION:

[1] The term "sale at retail" includes the charge made for the construction of new buildings for consumers. RCW 82.04.050. WAC 458-20-170 (Rule 170) is the administrative regulation dealing with the taxation of the construction of new buildings, including homes. As used in Rule 170, the term "prime contractor" includes a person who constructs new buildings for consumers. The term "speculative builder" means a person who constructs buildings for sale or rental (lease) upon real estate owned by the builder.

Prime contractors are taxable upon the gross contract price under the "retailing" B&O tax classification. Prime contractors also are required to collect from consumers the retail sales tax measured by the full or gross contract price.

Speculative builders, on the other hand, must pay sales tax or use tax upon all materials purchased by them, and on all charges made by their subcontractors. No B&O tax is due on the sale or lease of a "speculative" building.

Rule 170 states the attributes of ownership of real estate for purposes of determining whether one is building upon real estate owned by him, i.e., a speculative builder. The attributes of ownership include:

- (1) The intentions of the parties in the transaction under which the land was acquired;
- (2) the person who paid for the land;
- (3) the person who paid for improvements to the land;
- (4) the manner in which all parties, including financiers, dealt with the land.

In this case, the land was owned by the trust alone. The trust was to be paid for the land from the net proceeds of sale, after payment of all construction costs and operating expenses. The fact that the trust deeded a one-half interest in the property to the taxpayer for security purposes did not make the taxpayer an "owner" of the property. ETB 275.08.170,

[2] The taxpayer contends that the joint venture was the builder and seller of the home. The tax consequences applicable to joint ventures are proper when:

- (1) The joint venture was specifically formed to perform the contract work,
- (2) The formation of the joint venture occurred before any of the work required by the contract had been undertaken,

(3) The contract work was in fact performed by the joint venture,

(4) The funds were handled as a joint venture rather than as separate funds of any party to the joint venture agreement, and

(5) There was a contribution of money, property and/or labor so that any profit or loss incurred by the joint venture was proportionately shared by all joint venturers. 2 WTD 411 (1987).

Applying those factors, we agree with the auditor's conclusion that the construction and sale were not done by the joint venture as a speculative builder. The trust alone owned the property and provided the funds for the construction. Furthermore, the profit or loss was not shared by the joint venturers. Instead, the agreement provided for guaranteed payments to be made to the taxpayer by the trust. The construction payments had priority over operating expenses, lot cost and financing costs and were secured by an interest in the land owned by the trust. These factors support the auditor's conclusion that the retail sale occurred between the taxpayer and the trust, the owner of the land and the person that provided the necessary financing to construct the residence.

Accordingly, we affirm the assessment of retailing B&O and retail sales tax upon the gross contract price.¹

[3] During the audit period, the taxpayer also did some construction as a speculative builder. Speculative builders must

¹ Even if we were to find that the joint venture constructed the home, the venture was not a "speculative builder." Rule 170 clearly states that:

Persons, including corporations, partnerships, sole proprietorships, and joint ventures, among others who perform construction upon land owned by their corporate officers, shareholders, partners, owners, co-venturers, etc., are constructing upon land owned by others and are taxable as sellers under this rule, not as "speculative builders."

Because the taxpayer treated the construction project as speculative building done by the joint venture, the company paid retail sales tax on most materials purchased and charges made by subcontractors. The auditor gave the taxpayer a credit for sales tax paid.

pay sales tax upon all materials purchased by them and all charges made by their subcontractors. The auditor assessed use tax or deferred sales tax on the invoices which showed the vendors did not charge sales tax. A copy of WAC 458-20-178, the administrative rule dealing with the use tax, was provided to the taxpayer.

The taxpayer does not dispute the amount of the tax, but contends that the state should collect the amount owing from the sellers. As a buyer, the taxpayer contends it was not its obligation to collect the sales tax.

RCW 82.08.050 is the statutory provision which provides for the payment of the retail sales tax. The tax is to be paid by the buyer to the seller. Where the tax has not been paid, the Department has discretion to proceed directly against the buyer for collection of the tax. A penalty of 10 percent may be added in addition to the interest and penalties set forth in Chapter 82.32 RCW.

As Rule 170 states, the use tax supplements the retail sales tax by imposing a tax of like amount upon the use within this state as a consumer of tangible personal property on which the retail sales tax was not paid. A speculative builder is the "consumer." Accordingly, the assessment of deferred sales tax or use tax in Schedule III is affirmed.

If the taxpayer has evidence of retail sales tax that was paid, but for which the company was not given a credit in the audit, that evidence should be provided to the auditor. If the invoice separately states the sales tax from the selling price, the taxpayer shall receive a credit for the amount paid.

DECISION AND DISPOSITION:

The taxpayer's petition is denied, except the taxpayer shall receive credit for sales tax paid as provided herein.

DATED this 20th day of April 1988.