Cite as 5 WTD 125 (1988)

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

In the Matter of the Petition For Correction of Assessment of)	D E T E R M I N A T I O N
)	No. 88-39
. . .)	Registration No. . . .
)	Assessment No. . . .
)	

[1] **RULE 170 AND RCW 82.04.050 (2)(b)**: CONSTRUCTION AND SERVICES CONTRACTS -- "IN RESPECT TO" CONSTRUCTION. When a construction and service (feasibility) contract are awarded to the same contractor, the Department looks to a number of factors to determine whether the service contract was "in respect to" construction and taxable as a retail sale.

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: June 5, 1986, Seattle, Washington

NATURE OF ACTION:

Petition for correction of assessment imposing Retailing B&O classification and retail sales tax on development contract.

FACTS AND ISSUES:

Hesselholt, A.L.J. (successor to Chandler, A.L.J.) -- On January 21, 1980, . . . (taxpayer) and . . . , entered into a development agreement. The agreement provided that taxpayer

would perform certain necessary preliminary development work with respect to an addition to the . . . facility, and that . . . would pay taxpayer a maximum of $300,000 if the project did not continue to construction or if . . . determined that the taxpayer was not suitable to be contractor. If the project went ahead, with taxpayer as contractor, taxpayer was entitled to a development fee of 5 percent of the estimated costs of the project (less land acquisition costs). The contract further provided that if taxpayer was selected as contractor, taxpayer would construct the project "pursuant to the terms of a construction contract which [taxpayer] shall enter into with [. . .] using AIA form document A-111, ..." This contract was signed July 17, 1980.

On May 19, 1981, taxpayer submitted an "estimate and budget proposal" for the project. On July 21, 1981, taxpayer and . . . signed a construction contract to build the additions.

Taxpayer's records were audited for the period January 1, 1981 to March 31, 1984. Taxpayer objects to that portion of the assessment imposing retail sales tax on the development contract between taxpayer and . . . and the reclassification of the development fee from the Service business and occupation tax rate to the Retailing B&O rate.

The auditor took the position that the development contract guaranteed taxpayer to be contractor, subject to certain conditions, and thus the services rendered under the development contract were "in respect to" a construction contract, and subject to the Retailing B&O tax classification and the retail sales tax.

Taxpayer argues that the two contracts are completely separate; that . . . was free to chose another contractor and had no legal obligation to choose taxpayer as contractor should it decide to go forward with the project.

DISCUSSION:

RCW 82.04.050(2)(b), defines a retail sale as

> the constructing, repairing, decorating, or improving of new or existing buildings or other structures under, upon, or above real property of or for consumers, including the installing or attaching of any article of tangible personal property therein or thereto, whether or not such personal property becomes a part of the realty by virtue of

> installation, and shall also include the sale of services or charges made for the clearing of land and the moving of earth excepting the mere leveling of land used in commercial farming or agriculture.

WAC 458-20-170 (Rule 170), implements the statute. Rule 170 provides, in part:

> The term "constructing, repairing, decorating or improving of new or existing buildings or other structures," . . . includes the sale of or charge made for all service activities rendered in respect to such constructing, repairing, etc., . . . Hence . . . such service charges such as engineering fees, architectural fees or supervisory fees are within the term when the services are included within a contract for the construction of a building . . . . (Emphasis added.)

The Department looks to the substance of the transaction, not just the form, to determine taxability. In Chicago Bridge, the Department taxed three design contracts as retail sales, even though they were separate in form, because both the design and construction contracts were awarded to the same contractor on the same day. Chicago Bridge & Iron Co. v Dept. of Revenue, 98 Wn.2d 814 (1983).

When a service and construction contract are awarded to the same contractor, the Department will look at several factors to determine whether the services contract was rendered "in respect to" the construction contract:

> (1) Were the service and construction contracts awarded within a short time period?
>
> (2) Were the service and construction contracts performed separately?
>
> > (a) Was the service contract finished before the construction contract was awarded?
> >
> > (b) Were the services performed independently of the construction?
>
> (3) Were the service and construction contracts awarded subject to an open, competitive bidding process?

(4) Was the decision to award the construction contract made independently of the decision to award the service contract?

(5) Was the customer free to choose a different construction contractor or abandon the project?

(6) Is the compensation for the service contract separate from the construction contract?

The determination as to whether the services are rendered "in respect to" construction is essentially a question of fact. In this case, the two contracts were awarded nearly a year apart. The feasibility study was finished when the construction contract was awarded. The contracts were not awarded pursuant to a competitive bidding process, taxpayer's bid was the only one submitted to . . . .

The decision to award taxpayer the construction contract was made after taxpayer's completion of the feasibility study and an attractive price was considered by . . . . One of the members of . . . 's Board of Trustees has submitted a sworn statement to the effect that he believed at all times that . . . was free to select another contractor, and taxpayer was chosen because of its attractive construction estimate. The . . . Administrator has also submitted a sworn statement to the same effect. . . . was also free to abandon the project, had it decided against construction.

Finally, taxpayer's compensation was fixed in the development contract as $300,000 or 5% of construction costs, less land. Taxpayer's fee for the construction contract was 8% of the construction costs. Taxpayer's ability to be paid for the feasibility study was not dependent on or set by the construction contract, but was independent of it.

Here we hold that there are sufficient circumstances to find that the initial services contract was not rendered "in respect to" the construction contract, and not subject to retail sales tax and the Retailing B&O tax classification.

DECISION:

The taxpayer's petition is granted.

DATED this 26th day of February 1988.