Cite as Det. No. 01-028, 20 WTD 514 (2001)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Refund of	)	D E T E R M I N A T I O N
	)	
	)	No. 01-028
	)	
. . .	)	Registration No. . . .
	)	FY. . ./Audit No. . . .
	)	Docket No. . . .
	)	
	)	

RULE 170: JOINT VENTURE – TAX LIABILITY OF EACH PARTY TO JOINT VENTURE. Members of a joint venture engaged in speculative construction are jointly and separately liable for payment of retail sales tax on obligations of the joint venture, and the fact that one member managed the project and ordered materials and subcontract work in that member's name does not relieve the other members of liability for unpaid sales tax on the materials and subcontracts when the managing member incurred the third-party expenses in the capacity of a partner.

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:

Joint venturers in the construction and sale of a residence request refund of amounts the Department seized from their bank account in partial satisfaction of a warrant for unpaid retail sales tax on construction invoices, contending other members of the joint venture should be held solely liable for the unpaid taxes.[1]

[1] Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

FACTS:

Prusia, A.L.J. -- The taxpayer, . . ., is a joint venture tax account set up by the Department of Revenue ("Department") in 1999. During an audit of [Electric Co.], a sole proprietorship of [Mr. B. and Mrs. B.,] the Department saw records relating to the construction and sale of a house by [Mr. B.] and his wife and another couple, [Mr. F.] and wife. The Department's Audit Division set up the joint venture account for the purpose of auditing business activities jointly engaged in by the two couples. The Department's Audit Division examined books and records of the [Bs] and [Fs] for the period July 1, 1995, through July 31, 1996. The audit examination found the couples had jointly purchased real property on which a single-family residence was built during 1995-96, had jointly borrowed money to build the residence, and had divided the proceeds upon sale of the property in 1996. The audit examination found retail sales tax had not been paid on some purchases of construction materials and contractor services. On November 19, 1999, the Audit Division issued an assessment against the joint venture for use tax in the amount of $. . ., plus $. . . interest.

No one appealed the assessment, and no one paid the assessment by the due date stated in the assessment notice. In May 2000, the Department filed a warrant against the taxpayer in the amount of the assessment plus a late payment penalty, a warrant penalty, and additional interest. The face value of the warrant was $. . . . The Department subsequently seized $. . . from a bank account belonging to the [Bs], and $. . . from a bank account belonging to the [Fs], which satisfied the warrant and subsequently-accrued interest and fees.

The [Bs] petitioned for refund of the $. . . seized from their account. They contend the Department should hold the [Fs] solely responsible for the uncollected retail sales tax, and should pursue collection only against the [Fs].

The petition states that [Mr. F.] handled all financial matters of the joint venture, including payment of taxes. It states:

> This was a house built by [Fs] Const. We [presumably referencing the [Bs]] had nothing to do with any of the billing – receiving any draws – or making any payments to anyone.
>
> . . .
>
> All draws from the bank were put into [Fs] Const. Account, which [Mr. F.] would not let us be on his account, he wanted full control of all money coming in & going out. We had no part of it because he didn't want us to. All bills are and were billed to [Fs] Const. not to us. [Mr. F.] therefore was to have paid all bills & quarterly taxes, which we were not a part of, because he wanted all control.
>
> If you go through [auditor's] audit you will see that all money's were put into his account. All bills were paid by him. All bills are made out to him, not us.
>
> . . .

> Please reconsider this situation & return our money & take it from [Mr. F.] as he made all this possible – not us. We just assumed he knew what he was doing as he kept telling us that he has quick books & its never wrong!

At hearing, [Mr. B.] added the following: The [Bs] and [Fs] were neighbors. Both were involved in the construction trades. They decided to buy a neighboring acreage together, build a house, and split the proceeds. Each couple put up half the purchase price of the land. The two couples jointly obtained a construction loan. [Fs] Construction performed some of the work, [Mr. B.] performed some of the work, and some work was subcontracted. [Mr. B.'s] initial understanding was that he and Mr. [F] together would buy materials and subcontract out work, would both sign any checks, and would jointly split the profit on the sale.

However, after they obtained the construction loan, Mr. [F.] insisted on being in full control of all loan money coming in and going out. Mr. [F.] opened a bank account for the project that was in his name alone, into which the bank deposited construction draws. Materials and subcontract work were ordered in the name of [Fs] Construction, none in the name of the [Bs]. Mr. [Fs] alone prepared and submitted the construction draws to the bank. The [Bs] did not even see the invoices until after the Department's audit. At the time of closing on the sale of the house, $. . . was owed the bank on the construction loan. The settlement papers showed the amount due the sellers, after deducting the loan amount and settlement costs, was $. . . . At that time, Mr. [F.] indicated there still were unpaid materials, contracts, and taxes. Mr. [F.] calculated the amount of those to be $. . ., a part of which was owed to [Mr. B.] for work and materials incorporated into the construction. The parties discussed various figures presented by Mr. [F.], and finally agreed that the split of the net proceeds at closing would be $. . . to Mr. [F.], and $. . . to [Mr. B.] [Mr. B.] agreed to those figures only after Mr. [F.] agreed to be responsible for all outstanding construction costs and taxes. The company that handled the closing issued checks in those amounts to the [Fs] and the [Bs] at closing.

Mr. B. argues the Department should look only to Mr. [F.] for payment of the tax, and should refund the amount it seized from the [Bs]' account, for the following reasons. 1) The [Bs] are not liable for the unpaid sales tax, because they did not purchase any of the materials or construction services. All the invoices are in the name of [Fs] Construction only. If the invoices were not paid, the sellers could not go after the [Bs], so how can the Department hold the [Bs] liable for the tax due on the invoices? 2) Mr. [F.] received money to cover unpaid taxes at closing, which was in addition to his half of the net proceeds. Since Mr. [F.] received the money to pay the taxes, the Department should go after him if he failed to pay the taxes. 3) Mr. [F.] agreed to be responsible for all unpaid construction costs and taxes, and that alone is reason enough for the Department to look only to him for payment. 4) After he was audited, [Mr. B.] finally was able to see the construction invoices and other records, and discovered that Mr. [F.] had taken a number of draws to pay himself, his wife, and his children out of the construction loan. [Mr. B.] suspects the draws were excessive, and that Mr. [F.] "padded" the draws by an amount that would more than cover the taxes the Audit Division found due.

ISSUE:

Were the [Bs] jointly and severally liable for unpaid retail sales tax on the construction project?

DISCUSSION:

All sales of tangible personal property to consumers in the state of Washington, including successive retail sales of the same property, are subject to retail sales tax, unless there is a specific exemption. RCW 82.08.020 and 82.04.050. In general, the use tax applies upon the use within Washington of any tangible personal property the sale or acquisition of which has not been subjected to the Washington retail sales tax. It supplements the retail sales tax by imposing a tax of like amount. WAC 458-20-178 (Rule 178); RCW 82.12.020; RCW 82.12.0252.

The term "sale at retail" or "retail sale" includes the sale of or charge made for tangible personal property consumed and/or for labor and services rendered in respect to the constructing, repairing, decorating, or improving of new or existing buildings on real property of or for consumers. RCW 82.04.050(2)(b).

WAC 458-20-170 (Rule 170) is the administrative rule dealing with the taxation of the construction of buildings, including homes. Rule 170 explains that a "speculative builder," defined as "one who constructs buildings for sale or rental upon real estate owned by him," is the consumer of materials the builder purchases, and the consumer of all charges made by the builder's subcontractors, for excise tax purposes. Speculative builders must pay sales tax upon all materials purchased by them and on all charges made by their subcontractors. Speculative builders do not owe business and occupation (B&O) tax on the sale of the constructed building, but rather owe real estate excise tax (REET) upon sale. A "prime contractor" is a person engaged in the business of performing construction for consumers. Prime contractors are required to collect from consumers (i.e., from the speculative builder in speculative construction), the retail sales tax measured by the prime contractor's full contract price. Prime contractors owe B&O tax on their gross contract price, under the retailing B&O classification. Prime contractors do not owe retail sales tax on their purchases of materials and subcontractor charges for which they give resale certificates, because these sales are sales for resale not subject to the retail sales tax.

The Audit Division characterized the arrangement between the [Bs] and the [Fs] as a "joint venture" that engaged in speculative construction. It set up the assessment on the basis that the invoices on which retail sales tax was not paid were construction expenses of the joint venture, i.e., of the speculative builder. We believe the Audit Division's characterization of the arrangement and treatment of the invoices was correct.

A joint venture is a separately-taxable "person" for Washington tax purposes. RCW 82.04.030. Title 82 RCW does not define "joint venture." Therefore, we look to its common and ordinary meaning. "Joint adventure" is defined as "any association of persons to carry out a single business enterprise for profit, for which purpose they combine their property, money, effects, skill, and knowledge . . ." Black's Law Dictionary 837 (6th ed. 1990). Similarly, a "joint venture" is defined as:

> A legal entity in the nature of a partnership engaged in the joint undertaking of a particular transaction for mutual profit. [Citation omitted]. An association of persons or companies jointly undertaking some commercial enterprise; generally all contribute assets and share risks. It requires a community of interest in the performance of the subject matter, a right to direct and govern the policy in connection therewith, and duty, which may be altered by agreement, to share both in profit and losses. [Citation omitted].

Id. At 839. There is no requirement that the joint venture agreement be in writing if the facts indicate the parties acted as a joint venture in performing the contract. Det. No. 87-93, 2 WTD 411 (1987); Det. No. 99-176, 19 WTD 456 (2000).

A joint venture is in the nature of a partnership, and the right, duties, and liabilities of the venturers are generally tested by the same rule applicable to partners. *Barrington v. Murry*, 35 Wn.2d 744, 752, 215 P.2d 433 (1950). All partners are jointly and severally liable for everything chargeable to the partnership. RCW 25.04.150. Similarly, joint venturers are each liable for everything chargeable to the joint venture.

We find there was a joint venture between the [Fs] and the [Bs]. The [Fs] and the [Bs] combined their property, money, and skills to carry out a single business enterprise for profit. The enterprise was the speculative construction of a residence. They shared the risks of the venture. They divided the net proceeds after deducting an amount to cover unpaid costs. Apparently, only Mr. [Fs] handled the finances, but the [Bs] agreed to that arrangement. Since joint venturers are jointly and severally liable for everything chargeable to the joint venture, [Mr.] and [Mrs. B.] were jointly and severally liable for any unpaid retail sales tax obligation of the joint venture.

The [Bs]' first reason for refund -- that the invoices represent obligations of [Fs] Construction only -- raises a question whether the invoices on which sales tax was not paid represent obligations of the joint venture or obligations of [Fs] Construction. A joint venture may hire one or more prime contractors that in turn purchase materials and subcontract parts of the construction. When one of the joint venturers is a construction contractor, there may be a question whether it obtained materials and subcontractor services as a prime contractor, or obtained them in the capacity of a partner. *See* Det. No. 90-74, 9 WTD 143 (1990); Det. No. 87-254, 3 WTD 431 (1987); Det. No. 86-296, 2 WTD 19 (1986); Excise Tax Advisory (ETA) 73.08.106; Rule 170(f).

The facts presented are consistent with the Audit Division's resolution of this question. [Fs] Construction treated the transactions with third parties as purchases by the joint venture rather than purchases by itself as a prime contractor. It did not give the sellers resale certificates, which would have been appropriate had it considered itself a prime contractor. Rather, it followed a pattern of paying retail sales tax on the purchases, out of the joint venture's loan funds. The facts are similar to those in Det. No. 90-74, *supra*, in which a general contractor was found to be acting on behalf of a joint venture, of which it was a member, when it incurred and paid third-party expenses.

The alternative interpretation -- that [Fs] Construction was a prime contractor that procured the materials and construction services on its own behalf rather than as a partner -- would not benefit the [Bs]. It would merely shift the transaction on which retail sales tax was owed, from the sales by the materials suppliers and subcontractors, to the transaction between [Fs] (as prime contractor) and the joint venture (as consumer). The joint venture would owe retail sales tax on [Fs] Construction's full contract price. Thus, the alternative interpretation would not change the answer to the question whether the [Bs] are liable for unpaid sales tax. It would only change the transaction on which they are liable. At any rate, as discussed above, the alternative interpretation does not fit the facts of this case.

The other reasons the [Bs] assert for relieving them of liability and refunding the amount seized are not relevant on the question of their liability for uncollected retail sales tax. The Department was not a party to any agreement that may have existed between the [Fs] and the [Bs]. If the [Bs] were injured by the breach of an agreement between the couples, that is a private matter between the couples.

In sum, we find there was a joint venture of the [Fs] and the [Bs], the joint venture engaged in speculative construction, the joint venture incurred sales tax liability on the sales that are the subject of the assessment, sales tax was not paid as determined in the audit assessment, and the [Bs] were jointly and severally liable for the unpaid sales taxes. Accordingly, the petition for refund must be denied.

DECISION AND DISPOSITION:

The petition for refund of [Mr.] and [Mrs.B.] is denied.

Dated this 26th day of February, 2001.