

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

In the Matter of the Petition For Correction of	)	<u>D E T E R M I N A T I O N</u>
Assessment of	)	
	)	No. 97-115
	)	
...	)	Registration No. . . .
	)	YR . . . /Audit No. . . .
	)	

- [1] RULE 217; RCW 60.28.040: SALES TAX -- TRUST FUND ACCOUNTABILITY ASSESSMENT -- PUBLIC WORKS CONTRACT -- RETAINAGE -- APPLICATION OF. Retainage paid the Department from a public works contract must first be applied to tax, interest, and penalty liability arising directly out of the project for which it was withheld before it may be used for other state tax arrearages.
- [2] RULE 217; RCW 82.32.145 SALES TAX -- TRUST FUND ACCOUNTABILITY ASSESSMENT -- PENALTIES AND INTEREST. A trust fund accountability assessment may include penalties and interest that accrue on the tax debt of a defunct corporation.

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:

Protest of personal liability sales tax assessment against the former officer of a defunct corporation.<sup>1</sup>

FACTS:

Dressel, A.L.J. – (Taxpayer) is the former president of . . . , a now defunct home building contractor that did business under Registration No. . . . . The taxpayer was assessed \$ . . . . under the trust fund accountability statute when the Compliance Division (Compliance) of the

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

Department of Revenue (Department) could not collect a \$ . . . tax debt from the above-mentioned corporation. The taxpayer appeals.

In its petition for correction, the taxpayer raised a single issue, regarding the personal liability imposed by Compliance. He alleged that a portion of the trust fund accountability assessment was based on sales tax owed on consumable items purchased by the corporation, as opposed to sales tax that was collected from customers but not remitted to the state.

At the hearing of this matter, though, the taxpayer's attorney acknowledged that Compliance had reduced the original trust fund accountability assessment so that it did reflect only sales tax collected but not remitted. At the same time, the taxpayer entered two new objections to the assessment. His corporation had previously done some construction work on a state project. Pursuant to law, that state agency withheld certain monies as "retainage". When Compliance became aware of this, it requested payment from the agency to be applied to the corporation's tax liability. As a result, Compliance was paid \$ . . . , which it applied to penalties and interest related to the taxpayer's overall liability to the Department. The taxpayer objects to this allocation and contends that Compliance may apply funds from that retainage only to debts related to the particular project for which the retainage was established.

The second objection raised relates to delinquent payment penalties imposed against the corporation. Such penalties, as well as interest, were added to the corporation's tax liability when it became overdue. The taxpayer claims that such penalties that accrued before the corporation was dissolved cannot be included in the trust fund accountability assessment made against him.

#### ISSUES:

1. Is the Department limited to applying the retainage on a public works construction project to the tax liability arising out of that particular project?
2. In asserting trust fund accountability against a corporate officer, may the Department include in that liability delinquent payment penalties that accrue before the corporation becomes defunct?

#### DISCUSSION:

Compliance applied the \$ . . . in retainage to warrant number . . . . This tax warrant, in addition to the tax bills for August and September, 1994, included approximately \$ . . . in taxes, interest, and penalties from 1990-1992. Altogether, this warrant included more than \$ . . . in interest and penalties. Citing WAC 458-20-228 (Rule 228), Compliance applied the \$ . . . to interest and penalties only. The retainage payment, therefore, did not reduce the amount of actual tax owed for August and September, 1994.<sup>2</sup>

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<sup>2</sup> See November 14, 1995 letter from District Compliance Manager . . . to the taxpayer's attorney, . . .

The authority for retainage in a public works contract is found in Chapter 60.28 RCW. RCW 60.28.040 lists the priority of liens against that retainage. The statute reads, in part:

The amount of all taxes, increases and penalties due or to become due under Title 82 RCW, from a contractor or the contractor's successors or assignees with respect to a public improvement contract wherein the contract price is twenty thousand dollars or more shall be a lien prior to all other liens upon the amount of the retained percentage withheld by the disbursing officer under such contract . . . The amount of all other taxes, increases and penalties due and owing from the contractor shall be a lien upon the balance of such retained percentage remaining in the possession of the disbursing officer after all other statutory lien claims have been paid.

[1] We interpret the cited language to mean that all state excise tax-related amounts due on a public works project must be paid first before retainage can be paid out for any other purpose, including state tax debts unrelated to the particular project for which the retainage is held. That was not done in this case.

The taxpayer objects to the trust fund accountability assessment<sup>3</sup> in that, he says, it does not give him credit for the \$ . . . in retainage that was paid the Department. The Department, on the other hand, maintains that it acted properly in applying the funds to penalties and interest as described above. As we will explain below, both parties are partially correct.

After being issued initially for \$ . . . , which included part of the 1990 through 1992 [Corporate] tax liability, the trust fund accountability assessment was pared down to \$ . . . . This was based on the taxpayer's objection to Compliance that the larger figure included sales taxes other than those collected by the taxpayer but not remitted to the state.<sup>4</sup> The [reduced] figure reflects sales tax amounts taken from the taxpayer's August and September, 1994 tax returns, that were filed but not paid. The taxpayer has supplied a breakdown of the income amounts which comprise the figures reported on the August and September, 1994 tax returns. It reflects that of \$ . . . in total income for the two months, \$ . . . was from the public works project done for the Washington State Patrol (WSP).<sup>5</sup> Thus, 29.1% of the income for that period was from the WSP project; 70.9% of the income was from other sources. Using a rate of 8%, the sales tax due on \$ . . . is \$ . . . . Therefore, of the \$ . . . in sales tax liability reflected on the amended trust fund accountability assessment, [only] \$ . . . is attributable to the WSP project.

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<sup>3</sup> Trust fund accountability assessments are authorized by RCW 82.32.145 against former corporate officials in certain situations when sales tax has been collected from customers but not turned over to the Department of Revenue.

<sup>4</sup> See previously-referenced November 14, 1995 letter from . . .

<sup>5</sup> Not all of the income from the state patrol project was reported by the taxpayer. A *Notice of Completion of Public Works Contract*, dated. . . , shows the amount of the contract at \$ . . . , plus \$ . . . in "additions".

The Department determined that the total in sales tax, penalties, and interest owed on the WSP project was \$ . . .;<sup>6</sup> \$ . . . was paid out of the retainage. As stated previously, that amount, in its entirety, should have been applied to the WSP project. If one does that and credits the \$ . . . against the [total sales tax, penalties, and interest owed on the project] \$ . . ., a difference of \$ . . . is derived. As indicated earlier, though, the trust fund accountability assessment includes \$ . . . in sales tax related to the WSP project. Thus, we see that the referenced assessment is \$ . . . higher than it should be, if the retainage had been properly allocated.

We, therefore, grant the taxpayer's petition on the first issue. While the taxpayer did, effectively, get some credit for the retainage, it did not receive as much as it should have. The Compliance Division will amend the trust fund accountability assessment to reduce it by \$ . . .<sup>7</sup>

Resolution of the second issue is much easier than the first. The taxpayer argues that a trust fund accountability assessment may not include delinquent payment penalties that accrue before the corporation becomes defunct. RCW 82.32.145, however, states, in part:

**Termination, dissolution, or abandonment of corporate or limited liability business-- Personal liability of person in control of collected sales tax funds.** (1) Upon termination, dissolution, or abandonment of a corporate or limited liability company business, any officer, member, manager, or other person having control or supervision of retail sales tax funds collected and held in trust under RCW 82.08.050, or who is charged with the responsibility for the filing of returns or the payment of retail sales tax funds collected and held in trust under RCW 82.08.050, *shall be personally liable for any unpaid taxes and interest and penalties on those taxes*, if such officer or other person willfully fails to pay or to cause to be paid any taxes due from the corporation pursuant to chapter 82.08 RCW. For the purposes of this section, any retail sales taxes that have been paid but not collected shall be deductible from the retail sales taxes collected but not paid. (Italics ours.)

[2] As stated in the statute, the liability of the corporate officer extends to interest and penalties, as well as to taxes. On the second issue the taxpayer's petition is denied.

#### DECISION AND DISPOSITION:

The taxpayer's petition is granted in part and denied in part.

DATED this 30th day of May 1997.

<sup>6</sup> Per a "Certificate" from Department of Revenue to Washington State Patrol, dated June 15, 1995. This is the document by which the Department requested payment out of the retainage for the amounts it was owed on the WSP project.

<sup>7</sup> Relative to the exact amount by which the trust fund accountability assessment will be reduced, see the "Decision and Disposition" portion of this Determination.