

Cite as 5 WTD 205 (1988)

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. 88-156
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. . . )	Registration No. . . .
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- [1] **RULE 170:** SPECULATIVE BUILDERS -- RETAIL SALES TAX -- INDEPENDENT CONTRACTOR -- LABOR. Speculative builders must pay retail sales tax to independent contractors performing labor and services on speculative construction projects.
- [2] **RULE 105:** EMPLOYEE -- INDEPENDENT CONTRACTOR. Claim of employee status with respect to son performing labor and services on speculative building project rejected. No evidence of employee status, such as payroll records or tax withholding.
- [3] **RULE 170:** SPECULATIVE BUILDER -- INDEPENDENT CONTRACTOR -- LABOR AND SERVICES. Person performing labor and services on speculative building projects held to be an independent contractor and sales tax due on the charges therefore. The fact that the independent contractor was the builder's son found to be irrelevant since billings and payments to this individual were treated like any other independent contractor performing work on the projects.

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 protested the assessment of retail sales tax on amounts claimed as "draws" which were paid to the taxpayer's son. The Department classified the payments as amounts paid to an independent contractor for construction services on speculative building projects.

#### FACTS AND ISSUES:

Mastrodonato, A.L.J. -- The taxpayer engages in several real estate related activities, namely: real estate sales, including land, commercial, and residential property, and custom and speculative home building. The taxpayer was audited by the Department of Revenue for the period from November 22, 1985, through June 30, 1987. As a result of this audit, the Department issued Tax Assessment No. . . . on September 24, 1987, in the amount of \$ . . . . The taxpayer made a partial payment of \$ . . . on October 22, 1987. The balance of the assessment (\$ . . . ), plus extension interest, remains unpaid.

The sole issue for our consideration concerns the taxes assessed in Schedule VII of the audit report. Under Schedule VII, the Department assessed retail sales tax on payments made, in the total amount of \$ . . . , to Mr. [A]. Mr. [A] is the son of Mr. [B], owner of [taxpayer I] and its affiliated company, [taxpayer II].

Mr. [A] performed construction labor and/or services for the taxpayer on some speculative building projects. He was found by the auditor not to be an employee of the company. Instead, Mr. [A] billed the taxpayer for work he performed in the same manner as any other contractor on the project. The payments made to Mr. [A] were also recorded on the taxpayer's business records as an independent contractor labor expense. Consequently, the Department applied the sales tax to these charges pursuant to WAC 458-20-170.

In a letter dated October 20, 1987, the taxpayer protested this classification and application of tax. This Determination is in response to the taxpayer's protest.

The taxpayer claims that the amounts paid to Mr. [A] were "draws" for company expenses and normal living costs. In addition, the taxpayer alleged that Mr. [A] was a partner in the company, and, as a partner, he had a duty to account for his time and accomplishments. The taxpayer contends that although the amounts paid to Mr. [A] appeared to be treated similar to the way independent contractor labor was paid, the

taxpayer argued that Mr. [A] was nevertheless a part of [taxpayer II] and these were merely draws against the business.

Consequently, the taxpayer contends that the Department has erred in assessing tax in this instance.

#### DISCUSSION:

[1] WAC 458-20-170 (Rule 170) is the administrative rule dealing with the taxation of the construction of new buildings, including custom and speculative homes. The rule provides, in pertinent part, as follows:

##### (2) SPECULATIVE BUILDERS.

(a) As used herein the term "speculative builder" means one who constructs buildings for sale or rental upon real estate owned by him. . .

(e) Speculative builders must pay sales tax upon all materials purchased by them and on all charges made by their subcontractors. . . .

##### (4) RETAIL SALES TAX.

(e) . . . [T]he retail sales tax applies upon sales to speculative builders of all tangible personal property, including building materials, tools, equipment and consumable supplies and upon sales of labor, services and materials to speculative builders by independent contractors. (Emphasis supplied.)

Thus, as used in Rule 170, the term "speculative builder" means a person who constructs buildings for sale or rental (lease) upon real estate owned by the builder. Speculative builders must pay sales tax upon all materials purchased by them, and upon sales of labor and services made by independent contractors. Thus, if an independent contractor performs labor and/or services for a speculative builder, the sales or use tax applies to those charges.

In this case, Mr. [A] performed labor and services for the taxpayer on several speculative building projects. Mr. [A]'s

charges, and the payments made to him, were subject to retail sales tax under the express provisions of Rule 170, quoted above.

[2] The taxpayer argued that Mr. [A] was "a part of [taxpayer II]." However, the auditor reports that Mr. [A] was not an employee of the taxpayer. The taxpayer does not have payroll records showing Mr. [A] as an employee. Moreover, the taxpayer did not withhold any payroll taxes from the payments made to Mr. [A]. Therefore, there is no evidence that Mr. [A] was an employee of the taxpayer company. (See following paragraph.)

For example, under the Department's administrative rule, WAC 458-20-105 (Rule 105), a person is an "employee" for state tax purposes if that person's (1) entire compensation is fixed at a certain rate per day, week, or month, payable in all events, or if that person (2) has no direct interest in the income or profits (or losses) of the business other than a wage, (3) has no liability for the expenses of maintaining the office or place of business, for other overhead, or for the compensation of employees, (4) has no liability for indebtedness incurred in conducting the business, and (5) whose conduct is supervised or controlled by another. Using these general guidelines, it is clear that Mr. [A] was not an employee of the taxpayer.

The taxpayer also contended that Mr. [A] was a partner in the business. However, the taxpayer has not produced any documentary proof that Mr. [A] was, indeed, a partner in the business, nor that he shared in the profits or losses of the company.

Furthermore, if it was true that Mr. [A] was an employee or partner in the business, he was not treated as such in the taxpayer's business records. The auditor also reports that the taxpayer maintained a draw account. This account was used to pay the principals in the business, namely Mr. [B] and his wife, Mrs. [B]. However, Mr. [A] was not paid through this account but, instead, he was paid through the job cost ledger where all other contractor labor costs were recorded.

[3] In summary, it is uncontroverted that Mr. [A] performed construction activities for the taxpayer. Although Mr. [A] is closely related to the owners of the taxpayer company, he billed the company for work performed in the same manner as any other independent contractor or supplier. Furthermore, Mr. [A]'s charges were recorded in the taxpayer's business

records as an independent contractor labor expense. Thus, Mr. [A] acted, and was treated in the taxpayer's records of account, like any other independent contractor. As such, the taxpayer was liable for taxes on Mr. [A]'s construction related labor and services in accordance with the guidelines of Rule 170. This required the payment of sales or use tax on the total amount billed and charged by Mr. [A].

In conclusion, the taxpayer has presented no evidence which would controvert or contradict the auditor's findings. Furthermore, the taxpayer's arguments are unsupported by the evidence presented by the Department's auditor. In short, there is nothing in evidence which implies that Mr. [A] did anything other than perform labor and services as an independent contractor, notwithstanding his close personal and family relationship to the owners of the taxpayer business.

#### DECISION AND DISPOSITION:

The taxpayer's petition for correction of assessment is hereby denied.

DATED this 16th day of March 1988.