

Cite as 9 WTD 143 (1990)

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. 90-74
	)	
. . .	)	Registration No. . . .
	)	. . ./Audit No. . . .
	)	

[1] **RULE 170:** RETAILING B&O TAX -- RETAIL SALES TAX/USE TAX -- CONSTRUCTION -- ACTING AS A PARTNER OR PRIME CONTRACTOR. When taxpayer supervises construction, etc., on a project owned by a partnership of which it is a member, it is acting as a partner when it receives no compensation for its efforts other than its partner share of the profits. Where the taxpayer receives an amount for its efforts otherwise, it is subject to tax as would be any other independent provider of materials or services. Accords: 87-254, 3 WTD 431 (1987); ETB 73.

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 TELEPHONE CONFERENCE: . . .

NATURE OF ACTION:

Taxpayer protests the assessment of use tax on labor and business and occupation tax on amounts it received for the construction of retirement homes.

FACTS AND ISSUES:

Hesselholt, A.L.J. -- Taxpayer is a general contractor with its principal place of business [out of state]. Taxpayer works as a contractor, and also participates in various real estate ventures. The Department of Revenue (Department) audited the books and records of the taxpayer for the period . . . through . . . , and issued an assessment. The entire balance remains due. Taxpayer protests all of the retailing B&O tax assessed on three projects, as well as some of the use tax assessed on the projects. The three projects are the . . . ([A]), the . . . ([B]), and the . . . ([C]).

The taxpayer, in conjunction with other people, formed three partnerships to build the three projects. These same people have been affiliated in various other partnerships over the years. The partnerships build . . . in various states. Taxpayer is always a general partner and usually the largest general partner.

The three projects here at issue were constructed with proceeds from loans granted to the partnerships. These loans were secured by real property owned by the partnerships. Taxpayer drew down funds on the loans, and used the funds to pay partnership construction expenses. Taxpayer states that the funds were also used to reimburse partners for advances made to purchase the land or pay other expenses, and any remaining funds were paid to the partnership's accounts. Taxpayer claims that it had no right to the loan draws other than as partner for the reimbursement of costs incurred on behalf of the partnerships.

Taxpayer states that it was not entitled to and did not receive a fee for the construction activities. It did not receive a builder's fee for the construction, and except for the [C] project, no construction contracts existed. The construction contract for that project existed only because the lender required it, and taxpayer states that it provided that the builder's profit was zero. Taxpayer states that it did not give resale certificates to suppliers and subcontractors, and that the partnership acted as a speculative builder and taxpayer was simply acting as a partner in the partnership. The partnerships are continuing to operate the retirement homes that were constructed.

The Audit Division believed that the taxpayer was acting as a prime contractor, and was therefore subject to tax on the all of the amounts it received from the loans. The Audit Division included copies of forms titled "Contractor's application for

payment" on the various projects that taxpayer submitted to the lending institutions. Some forms show taxpayer signing as "contractor," without noting that it was signing as general partner. Another form shows taxpayer signing on the line "contractor or borrower" with its name, but again without the notation that it was signed as general partner. One of the payment requests shows a series of payments going to taxpayer, for amounts designated as "reimburse fee", excavation, labor, insurance, and travel. The [C] project form shows \$ . . . as the "builder's overhead" in a total contract of \$ . . . . Taxpayer has submitted a breakdown of amounts it was paid for labor expenses on the projects. It also rented some equipment to the partnerships.

Taxpayer has submitted copies of the partnership agreements, promissory notes [and] construction loan agreements for all three projects. All documentation submitted by taxpayer supports its claims. The partnership agreements make no provision for any payment or distribution of profits to any partner except according to their ownership percentages. Taxpayer has not provided a copy of the construction contract on the [C] project.

#### DISCUSSION:

RCW 82.04.050 defines a "retail sale" in relevant part, as follows:

. . . 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 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. .

(Emphasis added.)

The statute is implemented by WAC 458-20-170 (Rule 170). Rule 170 defines a prime contractor as a "person engaged in the business of performing for consumers contracts for the construction. . . ." Prime contractors must collect the retail sales tax on the full contract price. A speculative builder, as defined in the Rule, is one who performs construction on land owned by it. A speculative builder is not liable for sales tax on the full contract price but must pay sales tax on

all tangible personal property, as well as all labor and services purchased from an independent contractor. The rule further provides that

(a) As used herein the term "speculative builder" means one who constructs buildings for sale or rental upon real estate owned by him. The attributes of ownership of real estate for purposes of this rule include but are not limited to the following: (i) The intentions of the parties in the transaction under which the land was acquired; (ii) the person who paid for the land; (iii) the person who paid for improvements to the land; (iv) the manner in which all parties, including financiers, dealt with the land. The terms "sells" or "contracts to sell" include any agreement whereby an immediate right to possession or title to the property vests in the purchaser.

\* \* \*

(f) 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."

[1] In this case, the Audit Division believed that taxpayer was acting as a prime contractor for the partnerships. For the most part, we believe that such a conclusion is in error. The taxpayer was supervising and managing, in the capacity of a partner, construction activities upon land owned by the partnership of which it was a member. To the extent that the taxpayer was not receiving consideration for its efforts, the taxpayer was acting as a partner in the partnership, and had no right to any payment as anything but as a partner.

The Department has recognized the general principle of partnership law that each partner acts for the benefit of the partnership and on its behalf. ETB 73.08.106 discussed the liability of partners for sales tax on equipment furnished to the partnership by one of the partners. The ETB stated that the payments would be taxable if they were "absolute" and payable in any event, regardless of whether or not the venture had adequate profits to meet the payments. Thus, partners are considered as third party service providers to the partnership of which they are a member when the obligation of the

partnership to pay for such services is "absolute" or fixed, and exists independently of any right to profit or gain. Where a partner has no right to any payment unless some profit or gain exists, the payment is not absolute and therefore not subject to tax.

In this case, taxpayer received amounts for its services that were shown on the construction draws, such as the builder's overhead in the [C] project, the costs in the [B] project, and the labor it provided. Taxpayer is subject to retailing B&O tax, and these amounts are subject to retail sales or use tax, as would be any other provider of materials or services, if taxpayer has a right to payment of those amounts that exists independently of its right to share in the profits. In the partnership agreement for the [C] project, the partners have the right to cash distributions in the same proportions as their ownership interest in the partnership. Profits and losses are to be shared the same way. Expenses are to be paid by the partnership for all costs incurred in running the partnership, and partners are to be reimbursed for the expenses they incur in so running the partnership. Taxpayer's own expenses, for such things as labor and overhead, are no different than any other expenses incurred by the partnership. Amounts paid to suppliers or providers are fully taxable by the suppliers or providers. We see no difference in taxpayer's position when it receives payment for its services.

Here, when taxpayer receives money from the partnership, by way of the construction draw, that is not in proportion to its ownership interest, for services it has performed, it is acting as a third-party service provider and taxable on that income.

Under these circumstances, when taxpayer is paying third-party providers for services rendered to the partnership, the taxpayer is acting as a partner and not as a prime contractor, and the money is not attributable to it. When it is itself receiving payment for services it has provided, it is acting in the same capacity as any other service provider and is taxable on that income. Here, where it provided labor or equipment, it is taxable as any other contractor to a spec builder would be; that is, the amounts are subject to retailing B&O tax and retail sales tax. The amount that it receives as its partnership share of the profits, that is not received for services performed, is not taxable income, as it is a partnership distribution.

DECISION AND DISPOSITION:

The taxpayer's petition is granted in part and denied in part. The file shall be referred to the Audit Division for adjustments in accordance with this opinion.

DATED this 21st day of February 1990.