

Cite as Det. No. 16-0169, 36 WTD 419 (2017)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS 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. 16-0169
)	
... )	Registration No. . . .
)	

RCW 82.04.051 – “Services rendered in respect to”: A mailbox store franchisor that provides a Build-Out Supervisor and labor for assembling store fixtures and building-out stores (construction), is providing services rendered in respect to construction because the supervision and labor are directly related to the build-out of the stores and the franchisor is responsible for the performance of the build-out of the store.

RCW 82.32.105; WAC 458-20-228 – Circumstances beyond the control - Reasonable basis for tax reporting: A reasonable basis for tax reporting does not constitute a circumstance beyond the control of the taxpayer; therefore, the Department cannot waive a 5% assessment penalty.

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.

Anderson, T.R.O. – A store developer disputes an assessment that stems, in large part, from a finding that the store developer provided “services rendered in respect to” construction when it accepted responsibility for assembling and building-out store fixtures. The store developer asserts that, at most, it assembled light shelving and attached slat walling – both of which activities constitute less than 1% of its services. Petition denied.<sup>1</sup>

ISSUES

1. Whether a store developer provides “services rendered in respect to” improving buildings or other structures, under RCW 82.04.051, when the store developer is responsible for supervising and providing labor to assemble [and attach] retail store fixtures and build-out the store.
2. Whether the 5% assessment penalty can be cancelled, under RCW 82.32.105, on the basis that the store developer had a reasonable basis for its tax reporting and the store developer

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

will implement any necessary changes to ensure it is properly reporting and paying taxes, going forward.

#### FINDINGS OF FACT

[Taxpayer] develops mail box and business centers. Customers pay Taxpayer a fixed amount for store development services . . . . Taxpayer advertises a “Full Turn-Key Package Starting at \$ . . . ” that includes build-out staff . . . . [Build-out includes installing all fixtures, placing equipment, mounting of all signage, stocking supplies and setting up all computer systems.]

The Washington State Department of Revenue’s (the “Department’s”) Audit Division (“Audit”) reviewed Taxpayer’s books and records from January 1, 2011, through June 30, 2014 (the “Audit Period”). On February 24, 2015, Audit issued an assessment against Taxpayer in the amount of \$ . . . , comprised of \$ . . . in retail sales tax, \$ . . . in retailing business and occupation (“B&O”) tax, a credit of \$ . . . for paid wholesaling B&O tax, a credit of \$ . . . for paid service and other activities B&O tax, \$ . . . in interest, and \$ . . . in 5% assessment penalty. Taxpayer appeals this assessment.

During the Audit Period, Taxpayer entered into three contracts for the development and construction of new mail box and business centers in Washington and reported some of the gross amounts received [from these contracts] under the wholesaling, retailing, and service and other activities tax classifications. Audit reviewed these contracts and determined that the contract amounts were attributable to Taxpayer’s store development and construction activities, and further, such activities were “services rendered in respect to” construction (a retail sale). Audit reclassified the [entire] contract amounts to retail and assessed retailing B&O tax and retail sales tax.

Taxpayer disputes Audit’s determination that store development and construction activities were the performance of “services rendered in respect to” construction. Taxpayer asserts that, at most, it assembles minimal light shelving and attaches slat walling to existing walls with a handful of screws, and this assembly and attaching constitutes less than 1% of its services.

As relevant here, Taxpayer provided a sample “Purchase Agreement” for [mail box] store development, designing, and building-out services. The Purchase Agreement lists the following as Taxpayer’s responsibilities:

. . .

6. Provide retail store fixtures in accordance with the approved Fixture Plan and deliver them to the Store address in Section 6. Retail store fixtures shall include laminated & melamine covered counters and work stations, computer work station, customer convenience podium, and copier work station. Slat wall on all [or] most interior perimeter retail walls, various display hooks & brackets are also provided. All fixtures shall be installed in a workman-like manner. The fixture component for the store package may include fixtures intended for future use and, as such, may not be used during the initial build-out of Purchaser’s store. These fixtures are the property of the Purchaser, and may not be returned to the Company for credit.

7. Provide Build-Out Supervisor at job site to direct fixturing and merchandising of the store and supervision of build-out crew.

8. Provide labor to assemble all retail store fixtures and stock all merchandise provided in this Agreement.

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...

Taxpayer also disputes the assessment of the 5% assessment penalty, and asks us to abate the penalty because it had reasonable cause for reporting the way it did. Taxpayer adds that this was its first Washington audit and it intends to implement any necessary changes.

## ANALYSIS

### Tax

Washington imposes a B&O tax “for the act or privilege of engaging in business” in the State of Washington. RCW 82.04.220. The tax is measured by the application of rates against the value of products, gross proceeds of sales, or gross income of the business, as the case may be. *Id.* As relevant here, the retailing B&O tax rate (.00471) is applied to the gross proceeds of sales. RCW 82.04.250(1). In addition, Washington levies a retail sales tax on each retail sale in this state. RCW 82.08.020, .050. The retail sales tax is measured by the selling price. RCW 82.08.020(1). Taxpayer disputes that the sale of mail box and business center development, and construction services constitute retail sales.

“Retail sale” is statutorily defined in RCW 82.04.050, which, in part, states:

(2) 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 following:

...

(b) The constructing, repairing, decorating, or improving of new or existing building or other structures under, upon, or above real property of or for consumers, *including the installation 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 also includes 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; . . .

(Emphasis added.) Applied here, the sale of installation or attachment of mail box and business center fixtures (tangible personal property) to the mail box and business center (real property) is construction/improving a new or existing building or other structure and a retail sale. RCW 82.04.050(2)(b). However, Taxpayer asserts that, in most cases, it does not actually perform the improvements – rather, it hires and supervises a crew to perform the installation or attachment of such fixtures.

In the case of constructing, repairing, decorating, or improving buildings or other structures, “retail sale” is not limited to the sale of the activity, it also includes “services rendered in respect to” [the activity]. RCW 82.04.050(2). “Services rendered in respect to” is statutorily as follows:

(1) As used in RCW 82.04.050, the term “services rendered in respect to” means those services that are *directly related* to the constructing, building, repairing, improving, and decorating of buildings or other structures and that are performed by a person who is *responsible for the performance* of constructing, building, repairing, improving, or decorating activity. The term does not include services such as engineering, architectural, surveying, flagging, accounting, legal, consulting, or administrative services provided to the consumer of, or person responsible for performing, the constructing, building, repairing, improving, or decorating services.

RCW 82.04.051 (emphasis added.) Thus, to be considered “services rendered in respect to” improving buildings or other structures, (1) the services must be “directly related” to the improving of buildings or other structures, and (2) the person who performs the services must be “responsible for the performance” of the improvements.

With respect to the first criterion, RCW 82.04.051 does not define what is meant by the phrase “directly related.” “Words in a statute are given their ordinary and common meaning absent a contrary statutory definition.” *John H. Sellen Constr. Co. v. Department of Rev.*, 87 Wn.2d 878, 882, 558 P.2d 1342 (1976); *see also, e.g.*, Det. No. 04-0106, 23 WTD 344 (2004). . . . WEBSTER’S THIRD NEW INTERNATIONAL DICTIONARY 641, 1916 (1993) defines “directly” as including “purposefully or decidedly” and “relate” as including “to show or establish a logical or causal connection between.” Accordingly, only activities that bear a decided and logical connection to improving buildings or other structures are included within the definition of services rendered in respect to improving buildings or other structures. RCW 82.04.051.<sup>2</sup>

Here, Taxpayer is rendering the service of supervising and providing labor for the build-out of mail box and business centers, which entails installation and attachment of the fixtures (laminated and melamine covered counters and work stations, computer work station, customer convenience podium, copier work station, and slat wall on . . . interior perimeter retail walls with various display hooks and brackets). As discussed above, the build-out is construction or improvement to a building or other structure. Supervision implies providing instruction and direction or purpose; thus, there is a logical connection between supervising the build-out of a mail box and business center and the actual build-out of the mail box and business center, and we conclude that such supervision is directly related to the construction or improvement of a building or other structure. Similarly, because labor actually performs the installation and attachment of fixtures, we conclude that providing labor is directly related to construction or the improvement of a building or other structure. The first criterion is met; Taxpayer was providing services “directly related” to the

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<sup>2</sup> RCW 82.04.051 explains that the term “services rendered in respect to” constructing does not include “accounting, legal, consulting, or administrative services provided to the consumer of, or person responsible for performing, the . . . improving . . . services.” Although the statute does not specifically state the reason these services are excluded from the definition, it appears that these services are excluded because they do not “directly relate” to improving.

construction or improvement of buildings or other structures in supervising and providing labor to perform the build-out mail box and business centers.

With respect to the second criterion, RCW 82.04.051 defines “responsible for performance” as follows:

(4) As used in this section “responsible for the performance” means that the person is obligated to perform the activities, either personally or through a third party. A person who reviews work for a consumer, retailer, or wholesaler but does not supervise or direct the work is not responsible for the performance of the work. A person who is financially obligated for the work, such as a bank, but who does not have control over the work itself is not responsible for the performance of the work.

Here, the Purchase Agreement states that Taxpayer will provide a Build-Out Supervisor to supervise the build-out crew and provide labor to assemble all mail box and business center fixtures. This contract (the Purchase Agreement) explicitly establishes that Taxpayer is responsible for the performance of the build-out – either by performing the work itself or through a third party. Were this contract not enough, we have consistently found that a person is “responsible for performance” when the person is providing direction or management of the construction process or building. *See* Det. No. 99-011R, 19 WTD 423 (2000) (Construction manager’s services of supervising and directing construction constitute a retail sale); *compare* Det. No. 99-346, 19 WTD 891 (2000) (Person not directing or managing the actual construction process or building was not responsible for the performance of constructing). In acting as build-out supervisor, Taxpayer is directing and managing the build-out, [which constitutes] improving buildings or other structures. We conclude that Taxpayer was “responsible for the performance” of the build-out of mail box and business centers. The second criterion is met.

In supervising and providing labor to build-out mail box and business centers, Taxpayer is performing “services rendered with respect to” construction or the improvement of buildings or other structures because Taxpayer is providing services “directly related” to the build-out and “responsible for the performance.” RCW 82.04.051. In the case of “services rendered with respect to” construction or the improvement of buildings or other structures, RCW 82.04.050(2)(b) specifies that such services are a retail sale. . . . Accordingly, we sustain the assessment of retailing B&O tax and retail sales tax on the contract amounts.

### Penalty

RCW 82.32.090(2) provides that the Department shall assess an assessment penalty when it determines that any tax has been substantially underpaid. A tax is “substantially underpaid” when a taxpayer has paid less than 80% of the tax due and the amount of the underpayment is at least \$1,000. RCW 82.32.090(2). Taxpayer paid \$ . . . in tax during the Audit Period, and Audit determined \$ . . . in tax was due during the Audit Period. As Taxpayer paid less than 80% of the tax due ( $\$ . . . / \$ . . . = 32.48\%$  paid) and the amount of the underpayment ( $\$ . . .$ ) exceeds \$1,000, the Department assessed a 5% assessment penalty.

The Department is required to waive the assessment penalty where it finds that the underlying act giving cause to the assessment of the penalty, i.e., substantial underpayment, was due to circumstances beyond the control of the taxpayer. RCW 82.32.105.

“Circumstances beyond the control of the taxpayer” is defined in WAC 458-20-228(9), which states:

The circumstances beyond the control of the taxpayer must actually cause the late payment. Circumstances beyond the control of the taxpayer are generally those which are immediate, unexpected, of in the nature of an emergency. Such circumstances result in the taxpayer not having reasonable time or opportunity to obtain an extension of the due date or otherwise timely file and pay.

WAC 458-20-228(9) goes on to provide a non-exclusive list of circumstances that generally will and will not be considered circumstances beyond the control of the taxpayer. A misunderstanding or lack of knowledge of a tax liability is generally not considered a circumstance beyond the control of the taxpayer. WAC 458-20-228(9)(a)(iii)(B); Det. No. 01-096, 22 WTD 126 (2003) (“Lack of knowledge’ is not a ‘circumstance beyond the control of the taxpayer’ because the law, regulations, and Department publications explaining all tax laws are publicly available . . .”). Accordingly, we sustain the assessment of the 5% assessment penalty.

#### DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 10th day of May 2016.