Cite as 6 WTD 317 (1988)

BEFORE THE DIRECTOR
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Correction of Assessments of	)	F I N A L D E T E R M I N A T I O N
	)	Nos. 87-192A
	)	85-125A
	)	
. . .	)	Registration No. . . .
	)	
	)	
	)	
and	)	
	)	
. . .	)	Registration No. . . .

[1] **RULE 211 AND RCW 82.04.050:** RETAIL LEASES -- RENTAL CONSIDERATION --AMOUNTS PAID FROM PROFITS -- CLOSE CORPORATIONS. Amounts actually paid by one closely held corporation to another for the use of construction equipment, whether paid as periodic rents reserved or from contract profits at the end of the contract, constitutes sales taxable rental income.

[2] **MISCELLANEOUS:** ESTOPPEL -- PRIOR AUDIT OVERSIGHT. The Department may not be estopped to collect taxes which are legally and properly due, simply because such taxes were not assessed for collection in previous audits of the same taxpayer.

[3] **RCW 60.28.050:** PUBLIC WORKS CONTRACT CLEARANCES -- RELEASE OF RETAINAGE --- DISCRETIONARY CERTIFICATION OF TAX PAYMENT. The Department's issuance of a contract clearance under RCW 60.28.050 does not unqualifiedly certify that all taxes have been paid which may be due under the contract, but only that the Department, in its discretion, is satisfied that other means of tax collection are available.

[4] **RULE 171 AND RCW 82.04.190:** PUBLIC ROAD CONSTRUCTION -- USE TAX ON ROAD MATERIALS -- DEFAULTING SUBCONTRACTOR. A prime road construction contractor who undertakes a public road installation contract of a defaulting road subcontractor is itself the installing party who is liable for use tax upon materials installed in performance of the subcontract.

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: . . .
. . .

HEARING CONDUCTED BY DIRECTOR'S DESIGNEES:
Garry G. Fujita, Assistant Director
Edward L. Faker, Sr. Administrative Law Judge

DATE AND PLACE OF HEARING: December 16, 1987; Olympia, Washington

NATURE OF ACTION:

Appeals by separate but related business entities with respect to tax liability arising from the same leasing arrangements. Separate and individual Determinations are jointly appealed by permission of the Department.

FACTS AND ISSUES:

The facts and historical background of these cases are fully reported in Determinations Nos. 85-125 and 87-192. They are not repeated here. These Determinations are fully incorporated herein by this reference.

There are four issues for our reconsideration.

1) Are amounts paid from contract profits, to compensate for the use of construction equipment by the contractor, subject to retail sales tax as lease payments where there is no written lease or rents reserved and the owner entity and the user entity (the contractor) are closely related?

2) Is the Department estopped to assert tax liability after an audit investigation when it has failed to assert such liability through previous audits of precisely similar business transactions by the same taxpayer?

3) Does the issuance of a public works contract clearance pursuant to RCW 60.28.050 prohibit the Department from subsequently asserting additional tax liability in connection with the contract?

4) Does the use tax properly apply to the value of materials provided by a public road construction subcontractor who defaults on the installation work, leaving it to be performed by the prime road contractor?

TAXPAYER'S EXCEPTIONS:

Neither the taxpayers' petitions to the Director nor the oral testimony at the hearing raised any new or different arguments which have not been fully considered in the previously issued Determinations. Apparently the taxpayers simply disagree with the findings and conclusions of these Determinations and seek our review.

The taxpayer, . . . , reargues that the Department should be estopped from asserting retail sales tax liability in respect to claimed equipment rentals between the closely held companies because no such tax was ever assessed in previous audits of these taxpayers, even though previous auditors examined precisely the same kinds of arrangements.

This taxpayer also reargues that the Department executed contract clearances and released contract reserve payments under the provisions of RCW 60.28.050, unqualifiedly stating that all taxes due on the contracts under the law had been paid in full. The Department may not now assess additional taxes in connection with these same contracts for allegedly unreported sales tax on equipment rentals.

The taxpayer, . . . , the lessee entity, argues that the joint venture made up of . . . Construction Co., and Mr. . . . was abandoned by Mr. . . . , leaving the Construction Company to perform the contracts using its own equipment. It argues that the finding in Determination No.85-125 was that this entity could not lease property from itself and that the assessment should be abated for periods after November 19, 1982 when the joint venture folded.

DISCUSSION:

We have thoroughly reviewed the findings and conclusions of the prior Determinations in view of the taxpayers' reinforced arguments and we find that they fully and properly represent the position of the Department under the law. We hereby confirm the results of these Determinations.

[1] Amounts actually paid for the use of construction equipment, whether paid as periodic rents reserved or from contract profits at the end of the contract period, constitute sales taxable rental income. As properly explained in the Determinations, the facts of these cases fully satisfy the statutory definitions of "sale at retail", "person", and the statutory conditions under which a seller (lessor) must collect retail sales tax from its buyer (lessee). RCW 82.08.050 further provides that the tax may be pursued for collection by the Department jointly against the seller and the buyer.

[2] The Department may not be estopped to collect taxes which are legally and properly due, simply because such taxes were not assessed for collection in previous audits of the same taxpayer. See the cases cited in the prior Determinations.

[3] Contract clearances issued pursuant to RCW 60.28.050 do not provide that all taxes due on the contract have been paid. Neither does the statutory law contemplate such a conclusion. The statute in question provides in pertinent part as follows:

> Upon final acceptance of a contract, the ... officer charged with the duty of disbursing or authorizing the disbursement or payment of such contracts shall forthwith notify the department of revenue... Such officer shall not make any payment from the retained percentage..., until he has received from the department of revenue a certificate that all taxes, increases and penalties due from the contractor, and all taxes due and to become due with respect to such contract have been paid in full or that they are, in the department's opinion, readily collectible without recourse to the state's

lien on the retained percentage. (Emphasis supplied.)

The emphasized provision above makes it abundantly clear that it is in the discretion of the Department to issue the contract clearance and thus to release the retainage if the Department feels that the state's position is protected and that any taxes remaining unpaid may be recovered without recourse to the lien protection. Contrary to the taxpayer's argument, the act of issuing the contract clearance does not obviate all further tax liability. It is completely immaterial whether the clearance is qualified or unqualified. The Department has no authority or discretion to excuse taxes which are legally due, whether by contract clearances or any other means. The taxpayer has referenced no authority for any other conclusion.

[4] Under the provisions of RCW 82.04.190 and WAC 458-20-171, contractors who construct public roads are themselves the consumers of all tangible personal property installed or applied to the contract work. There is no probative evidence in this case that the taxpayer acted in any capacity other than an installing public road contractor with respect to the railings provided by . . . Metals, Inc. Neither is there any evidence going to establish that the taxpayer purchased the railings from . . . Metals outright and paid sales tax at the source. Under the statute and rule the person who applies the tangible property to the contract is the party who is liable for payment of the use tax if sales tax has not been paid. If a prime road construction contractor undertakes the installation work of a defaulting subcontractor, there is no provision at law which excuses the tax liability attendant to tangible personal property applied to the contract.

Upon review of both Determinations No. 85-125 and 87-192, it is appropriate that retail sales tax assessed upon equipment rentals for all periods after November 19, 1982, and all interest assessed upon all such equipment rental deficiencies should be deleted from the respective tax assessments. Such were the rulings of those Determinations which are not disturbed here.

DECISION AND DISPOSITION:

The taxpayers' petitions are denied. Tax Assessment Nos. . . . and . . . will be adjusted to comport with the findings and conclusions of the original Determinations. They will be due for payment in full on the due dates to be shown thereon.

Payment of the retail sales tax assessed under either assessment regarding equipment rentals will satisfy the same tax liability assessed under the other assessment.

DATED this 12th day of August 1988.