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

In the Matter of the Petition for Correction of Assessment of	D E T E R M I N A T I O N
	No. 88-372
. . .	Registration No. . . .
	Tax Assessment No. . . .
	Tax Warrant No. . . .

[1] **RULE 228**: RCW 82.32.090 -- PENALTIES -- LATE PAYMENT -- WARRANT -- INADVERTENCE. If a taxpayer fails to pay taxes by the due date, there shall be assessed a penalty, unless the delay was caused by circumstance beyond the taxpayer's control. Claimed ignorance of tax laws is not such a circumstance.

[2] **MISCELLANEOUS**: PARTNERSHIP -- TAX LIABILITY -- GENERAL PARTNER. Obligations incurred by the managing partner in furtherance of partnership activities fastens liability upon all partners, known or unknown, even though, as between the partners, the managing partner is responsible. Dygert v. Hansen, 31 Wash.2d 858 (1948), cited.

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 HEARING: July 22, 1988

NATURE OF ACTION:

Petition regarding the imposition of use tax and penalties on the value of a construction project on which no sales tax had been paid.

FACTS:

Burroughs, A.L.J. -- As a result of an audit covering the period from May 1, 1986 to March 31, 1988 the taxpayer was assessed a total of $ . . . on . . . , which amount included interest and penalties. A post-audit adjustment was issued on . . . assessing $ . . . in use tax, $ . . . in interest, and $ . . . in late payment penalties, and $ . . . in warrant penalties, for a total of $ . . . . Tax warrant number . . . was issued on that date.

The [first] Project. The taxpayer, a Washington corporation, was the general partner of a limited partnership which developed a 108 unit apartment project - " . . . " - in . . . , Washington. The limited partnership, as owner-developer of the project, entered into a construction contract on September 23, 1986 with [A] , another Washington Corporation controlled by essentially the same person which controlled the taxpayer here at issue. [A] was to serve as prime contractor on the project. Total cost of the project was to be $2,515,000. Payment of retail sales tax was not addressed in the contract.

On the very same day, [A] ("the prime contractor") entered into a subcontract agreement with the [B] ("the subcontractor") for the actual construction of the project. Although the subcontractor's proposal had originally been to build the complex for $2,515,000 "plus sales tax," the actual subcontract price was $2,539,000. The prime contractor issued a resale certificate to the subcontractor on September 23, 1986 - the same day the two contracts were signed.

Records available to the auditor - which included the construction contracts, purchase invoices, and check registers of the taxpayer, prime contractor, and subcontractor - indicate that $2,549,096 was actually paid to the subcontractor in construction costs on the project - which amounts were paid by the taxpayer's general partner directly to the subcontractor. The subcontractor did not charge or collect retail sales taxes since it had been issued a resale certificate on the project.

The prime contractor, for the construction periods at issue, submitted tax returns reporting "no taxes due." Thus, neither retail sales taxes nor business and occupation taxes were reported or remitted by that entity for its participation in the project.

In the course of the audit, the taxpayer declined to supply the auditor with progress billings received from the prime contractor during the course of construction. Thus, the auditor was unable to determine whether any retail sales taxes had actually been paid by the taxpayer to the prime contractor. Records available to the auditor, in fact, reflected payments made directly by the developer (of which the taxpayer was general partner) to the subcontractor, thereby bypassing the prime contractor entirely. The taxpayer has reported to the audit staff that the prime contractor has essentially no bank account or any other assets.

The audit staff concluded that the only function served by the prime contractor in the course of the [first] project was its issuance of a resale certificate to the subcontractor to avoid payment of retail sales tax. Although the prime contractor will be assessed retail sales tax on the project, it is unlikely that collection is possible since that entity has no assets. Use tax has thus been assessed against both the limited partnership and the taxpayer, as general partner.

The [second] Project. The taxpayer was originally assessed use tax and penalties on the [second] development in . . . . The Department has since determined, however, that another entity owned and developed that project.

The [third] and [fourth] Projects. The [third] and [fourth] apartment projects were both developed by the same set of participants. The developer was a general partnership consisting of the taxpayer and an individual named [C]. The contractor was [D], a corporation wholly-owned by [C]. No retail sales tax or use tax has been reported on either of these projects. A receiver has been appointed by the court for both projects in order that a partnership accounting can be made, construction progress evaluated, construction completed, the units rented, and the projects sold.

TAXPAYER'S EXCEPTIONS:

In its Petition for Correction of Assessment dated June 23, 1988, the taxpayer objected to the assessment, claiming

(1) that it paid sales tax on its own purchases, and does not owe the service/other activity taxes,

(2) that it had nothing to do with the ownership or development of the [second] project, and finally

(3) that it does not owe any taxes for the [third] or [fourth] Apartment projects, since both projects were owned by partnerships, and the work was being done by [C], who is a part owner in each project who has paid most, if not all, of the sales tax due for those two projects.

Since its petition was submitted, however, the taxpayer has reconsidered its position and admitted liability for the taxes assessed regarding the [first] project and has entered into a partial payment agreement with the Department for payment of that assessment amount. The taxpayer, however, protests the five percent warrant penalty and the ten percent late payment penalty, contending that the individuals actually controlling the taxpayer -having come from California - did not fully understand the nature of Washington's tax obligations and should not thus be penalized.

As to ["second project"], because the Department determined that the taxpayer did not in fact have any interest in that project, the assessed amount pertaining to that project was deleted from the original assessment in the post-audit adjustment.

The amounts due on the [fourth] project were paid by the receiver when that project was sold. The amount received from this project has been treated as a payment and has been deleted from the outstanding amount on the warrant. At the hearing the taxpayer expressed the opinion that the amount assessed on this project was in excess of that which should have been due and owing. It was stated that the receiver would furnish receipts to support that claim. No such receipts have been provided to date to either this office or the auditor.

As to the [third] project, the taxpayer at the hearing did not deny that use tax might be due, but argued that the situation was such that the taxpayer should not be liable. The taxpayer's representative explained that, although the prime contractor was originally to be [A] and the subcontractor for the actual construction was to be the [B], the taxpayer's partner refused to recognize either of these contracts and established his own wholly-owned corporation - [D] - as the sole contractor. Copies of the contract with [D] have not been provided to the Department; information regarding amounts received on the contract as of March 31, 1988 have been obtained from the court-appointed receiver.

The taxpayer emphasized that in the course of these events its partner in the project - [C], through his corporation [D] - has kept all the books, records, and bank accounts, and denied he was a partner at all on the [third] project. The taxpayer thus alleges that it completely lost control of the records on these two projects, and should not be liable for taxes due.

DISCUSSION:

[First project] penalties. As to the ten percent late payment and warrant penalties, Washington's Revenue Act in RCW 82.32.090 provides as follows:

> If payment of any tax due is not received by the department of revenue by the due date, there shall be assessed a penalty of five percent of the amount of the tax; and if the tax is not received within thirty days after the due date, there shall be assessed a total penalty of ten percent of the amount of the tax; and if the tax is not received within sixty days after the due date, there shall be assessed a total penalty of twenty percent of the amount of the tax. . . .
> If a warrant be issued by the department of revenue for the collection of taxes, increases, and penalties, there shall be added thereto a penalty of five percent of the amount of the tax . . . .

As an administrative agency, the Department does not have discretion to change the law. The only authority to cancel penalties or interest is found in RCW 82.32.105. That statute allows the Department to waive or cancel interest or penalties if the failure of a taxpayer to pay any tax on the due date was the result of circumstances beyond the control of the taxpayer. The statute also requires the Department to prescribe rules for the waiver or cancellation of interest and penalties.

[1] The administrative rule which implements the above law is found in WAC 458-20-228 (Rule 228, . . .). Rule 228 lists the situations which are clearly stated as the only circumstances under which a cancellation of penalties and/or interest will be considered by the Department. None of the situations apply in the present case. Claimed ignorance of the tax laws of this state is clearly no a circumstance warranting the cancellation of penalties.

We further think it highly unlikely that the taxpayer's representatives were at any time unaware of how Washington tax liability applies in the construction of a development such as [the first project], since it appears that the entities and contractual relationships had been carefully, thoughtfully, and deliberately structured to avoid any such liability and leave the Department with entities with essentially no assets from whom to collect if ever discovered.

We particularly note that a resale certificate was promptly issued to the unrelated subcontractor, leaving that entity free from any responsibility for collection or ultimate payment; that the prime contractor - owned by out-of-state shareholders - was a mere shell with virtually no assets or bank accounts.

It further appears that the taxpayer entered into the partial payment agreement only because of the difficulty in receiving financing for other projects it just happened to have pending. Had the fifty percent evasion penalty been assessed, it would likely have been upheld.

The penalties assessed on this project are upheld and the taxpayer's petition denied.

["The third"] Project. As to the taxpayer's argument that it should not be liable for taxes due because the other partner in the general partnership took over control without permission, we must disagree.

RCW 25.04.150 provides that in a general partnership,

> All partners are liable:
> (1) Jointly and severally for everything chargeable to the partnership under RCW 25.04.130 and 25.04.140; and
> (2) Jointly for all other debts and obligations of the partnership ...

[2] Further, obligations incurred by the managing partner in furtherance of partnership activities fastens liability upon all partners, known or unknown, even though, as between the partners, the managing partner is responsible. Dygert v. Hansen, 31 Wash.2d 858 (1948).

Here, the construction of the apartment complex was in furtherance of the partnership activities, even though, as between the partners, [C] apparently took control of the

building project. The partnership has been assessed. The taxpayer, as a general partner, is thus jointly liable for the partnership's unpaid taxes and penalties on the enterprise.

DECISION AND DISPOSITION:

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

DATED this 27th day of September 1988.