

Cite as Det. No. 14-0358, 34 WTD 320 (2015)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

[1] RULE 170; RCW 82.04.051: RETAIL SALE – SERVICES IN RESPECT TO CONSTRUCTION. To qualify as a “service rendered in respect to construction” the service must: (1) be “directly related” to the constructing, and (2) the person who performs the services must be “responsible for the performance” of the constructing. Performance of services “directly related” to construction are not “services in respect to construction” if the taxpayer is “not responsible for the performance” of the construction.

[2] RULE 194; RULE 19402: APPORTIONMENT: Income taxable under the service and other activities B&O tax classification is apportionable using the methodology contained in Rule 194 for the period prior to June 2010 and apportionable using the methodology contained in Rule 19402 for the period beginning June 2010.

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.

Lewis, A.L.J. – Taxpayer operates a consulting service that acts as an owner’s representative during the design and construction process of large commercial projects. Taxpayer requested a ruling affirming that it provided a professional service subject to the service and other activities B&O tax and the income could be apportioned. Taxpayer protested the Department’s ruling that it provided services “in respect to construction” that was not apportionable and subject to either the wholesaling B&O tax or retailing B&O and retail sales tax classifications. We grant Taxpayer’s petition.¹

ISSUES:

1. Does [Taxpayer] provide services “in respect to constructing,” subject to wholesaling business and occupation (“B&O”) tax (RCW 82.04.060) or retailing B&O tax and retail sales

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

tax (RCW 82.04.051 and WAC 458-20-170), or does it provide professional services subject to the service and other activities B&O tax classification (RCW 82.04.290(2))?

2. If the services are subject to service and other activities B&O tax may the income derived from providing the services be apportioned under the provisions of WAC 458-20-194 and WAC 458-20-19402?

FINDINGS OF FACT:

Taxpayer is an owner's representative for construction projects. Taxpayer lives in Washington. Taxpayer travels outside Washington to advise and manage the design and construction process on the owner's behalf. Some of the work is done from Taxpayer's home office located within Washington. About 80% of the work is done at project site, owner's office, or meeting with contractors and various consultants. Services performed include oversight of the entitlement and entire design process, managing the negotiations and/or bidding with contractors and subcontractors, and managing the construction process on the owners' behalf.²

Taxpayer opened an account with the Department during May 2002. Taxpayer began reporting its income under the service and other activities B&O tax classification. On April 8, 2014, Taxpayer's representative requested, via the internet, a ruling as to how Taxpayer should report its income. Specifically, Taxpayer asked if it could apportion its income. The email summarized Taxpayer's business operation and explained that from 2010 to present, Taxpayer did not have any jobs located within Washington.

On April 21, 2014, the Department's TI&E section replied to Taxpayer's internet request. The reply stated:

Income received from providing construction management services which includes being responsible to the owners for the construction is classified as "services rendered in respect to construction" and is subject to the business and occupation (B&O) tax in the same manner at (sic) the construction contract. A person does not have to actually perform construction services to be responsible for the construction. (See RCW 82.04.051)

Generally, the gross contract for the construction projects performed for property owners is subject to the Retailing classification of the B&O tax and sales tax applies to the total charges. However, if the construction contract is performed outside the state, the total

² "The definition of entitlement with regard to land development is the legal method of obtaining approvals for the right to develop property for a particular use. The entitlement process is complicated, time consuming and can be costly, but knowing what you can and can't do with a piece of property is vital to determining the real estate feasibility of your project."

Bart S. Pair, *Property Development – What's an Entitlement and Why Do I Need it to Build?*, Ezine , June 4, 2008....

charges may be deducted from both the Retailing B&O tax and retail sales tax as “Intestate (sic) and Foreign Sales.”

This income is not attributed under the economic nexus apportionment formula.

While under the ruling, no tax would be due for work done by Taxpayer outside Washington for his clients, Taxpayer disagreed with the ruling. On May 14, 2014, Taxpayer filed a petition requesting correction of the written ruling. Taxpayer disagreed that it provided “services rendered in respect to construction,” which required the income be taxed as either the wholesaling or retailing. Rather, Taxpayer maintained that [the] professional services [it provided] were taxable under the service and other activities B&O tax classification and apportionable.

As part of its appeal, Taxpayer provided copies of several contracts to show the types of services it performs. Taxpayer provided a December 2013 proposal for work on a project located within California. Pertinent parts of the contract included:

. . . The proposal is for my role in overseeing the project from the “investor” perspective knowing your development partner is managing the building process along with advising/consulting on other on-going projects in the planning stages.

My Proposed overall role on [project] would be as follows:

- Initial review and get current on the contract documents, review proposed contract, terms and conditions, exhibits, schedule etc.... notes and comments to owner.
- Prepare comments on contract document review and review suggestions/concerns with client and [project owner] during week of Dec. 16th.
- Prepare agenda for contract/project introduction and kick off meeting (Tuesday/Wednesday next week?)
- Run/attend weekly job meetings, with [Taxpayer] taking and distributing detailed project meeting notes. [Taxpayer] will attend job site meetings/visits roughly 3 times per month and call in the other times. These meeting will include reviews of progress, schedule, costs, quality, concerns and other important issues.
- Be the initial point of contact for the [project owner] and builder as it relates to the construction progress, funding and decisions on-going construction.
- Review conditions that arise during construction that might affect long terms concerns with the operation and maintenance of the complex.
- Keep the information flowing between all parties. Bring the design/engineering consultants where necessary to determine best course of action on any problems that might arise.
- Review any/all change orders, use of contingencies and overall monitoring of project costs (construction and soft costs).
- Review on regular basis the Guaranteed Maximum Price Projections and any projected savings. It is assumed if desired that [Taxpayer] will have access to subcontract agreements and scopes of work that were used to establish the GMP.
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- Review at weekly meetings the accuracy of “as built” drawings to ensure they are being kept up on regular basis (reflecting actual buried conditions). Review/approve draw requests from contractor along with consultant billings where applicable. Verify contractor is receiving appropriate releases, wage reports and meeting the invoice/documentation requirements of Keep [development partners] informed of on-going project status, concerns, upcoming milestones, etc.
- During job site visits, inspect installations and review any potential deviations, quality issues or causes for concern.
- Be heavily involved in the close out process and start up process, ensuring all proper paperwork is received, city/Municipality inspections and closeouts for bonds and final occupancy requirements, as built O&M manuals, warranties, subcontractor lists, etc.

[Taxpayer’s] role on “other” projects may include such tasks as : meetings with various tenants, contractors, architects and engineers, city planners/staff, utility companies etc., value engineering and plan review/comments; phasing reviews/comments; helping develop outline specifications and contract document concepts; review/recommendations on contracting options and considerations; pricing and scheduling in conceptual formats;

...

This is a “monthly” retainer type proposal that can be cancelled by either party at any time. Once future projects are established, we can finalize job specific agreements for Owner Representative Services. [Taxpayer] will provide [development partners] with a % breakdown monthly on how the hours break down between the various jobs worked on during a given month.

It is clearly understood the [Taxpayer] carries no liability insurance or contractor licenses as I’m working as the owners’ representative (basically as a 1099 employee of your company). Should any lawsuits arise against [development partners], the project ownership and/or [Taxpayer] as a result of this project, the Ownership team would hold [Taxpayer] harmless and defend me as you would an employee of your company.

The other two proposals contained similar work requirements.

ANALYSIS:

Washington imposes a business and occupation (“B&O tax”) “for the act or privilege of engaging in business” in the State of Washington. RCW 82.04.220. Washington levies a retail sales tax on each retail sale in this state. RCW 82.08.020, .050. The measure of the retailing B&O tax is the gross proceeds of the sales. RCW 82.04.250(1); RCW 82.04.070. The measure of the retail sales tax is the selling price. RCW 82.08.020(2). The selling price includes the total consideration paid or delivered by a buyer to a seller. RCW 82.08. 010(1).

The term “retail sale” is defined in RCW 82.04.050 and includes construction activities. RCW 82.04.050(2)(b) states: “(2) The term “sale at retail” or “retail sale” shall include 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 buildings . . . under, upon, or above real property of or for consumers . . .”

WAC 458-20-170 (“Rule 170”) is the administrative rule that explains tax liability for the constructing or repairing of structures on real property. Rule 170 implements RCW 82.04.050, and states, in pertinent part, that the term “constructing, repairing, decorating or improving of new or existing buildings or other structures” includes: “the sale of or charge made for all service activities rendered in respect to such constructing, repairing, etc., regardless of whether or not such services are otherwise defined as ‘sale’ by RCW 82.04.040 or ‘sales at retail’ by RCW 82.04.050.” Rule 170(1)(e).

RCW 82.04.051 defines the term “services rendered in respect to,” for purposes of RCW 82.04.050, as “those services that are directly related to the constructing . . . of buildings . . . and that are performed by a person who is responsible for the performance of the constructing . . . activity.” RCW 82.04.051(1). Thus, to be considered services rendered in respect to constructing, (1) the services must be “directly related” to the constructing, and (2) the person who performs the services must be “responsible for the performance” of the constructing.

RCW 82.04.051(4) explains that “responsible for the performance” as used in this section mean:

[T]hat 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.

For example, we have held that when the services were necessary for the timely completion of the project, such as advising and coordinating information, but did not entail the direction or management of the actual construction process or actual building activities, the person was not “responsible for the performance of the constructing,” and, therefore, not engaged in retail activity. Det. No. 99-346, 19 WTD 891 (2000); Det. No. 99-011R, 19 WTD 423 (2000); Det. No. 99-152, 19 WTD 643 (2000). In contrast, we have held that when the construction manager’s activities were predominantly performed during the construction phase of the project, and the construction manager supervised and directed the constructing activity, the services fit the definition of a “retail sale.” Det. No. 99-011R, 19 WTD 423 (2000). We have rejected the argument that a taxpayer must be obligated to complete the physical construction itself, rather than merely being responsible for supervision or direction. *Id.* at 432. Services involving supervising or directing construction constitute services in respect to construction. *See, e.g.*, Det. No. 99-001, 18 WTD 420 (1999).

Here, Taxpayer refers to itself as providing “owner’s representative services” functioning as the eyes and ears of the owner. Taxpayer’s concerns are those that an absentee owner would have: is the construction progressing as planned, and are the costs being contained? Taxpayer visits the construction site, prepares reports, and “keeps information flowing between the parties”. Although Taxpayer is involved in the actual construction progress and part of the responsibilities include inspecting the work and approving draw requests, Taxpayer remained the contact person for the owner. To be considered services rendered in respect to constructing, (1) the services must be “directly related” to the constructing, and (2) the person who performs the services must be “responsible for the performance” of the constructing. While Taxpayer may be providing services “directly related” to the construction, we do not find that Taxpayer is “responsible for the performance” of the construction. Accordingly, we conclude Taxpayer is not providing services in respect to construction, at least under the contracts provided. Under the contracts

Taxpayer provided, it appears that Taxpayer is providing a professional service to the owner. The income that Taxpayer receives is taxable under the Department's catch-all B&O tax classification, service and other activities B&O tax.

Income taxable under the service and other activities B&O tax classification is apportionable. Thus, income that Taxpayer receives that is subject to the service and other activities B&O tax classification may be apportioned. For the period prior to June 2010, Taxpayer may apportion its income to Washington using the cost apportionment formula found in WAC 458-20-194 ("Rule 194"). For the period beginning June 2010, Taxpayer is instructed to apportion income using the single factor receipts apportionment formula as described in WAC 458-20-19402 ("Rule 19402").

DECISION AND DISPOSITION:

[We grant Taxpayer's petition.]

Dated this 17th day of November, 2014