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I. INTRODUCTION

This case involves the assessment of retailing business and occupation (“B&O”) tax and retail sales tax on amounts received by Nord Northwest Corporation from constructing condominiums on land owned by two limited liability companies. Nord Northwest Corporation asserts that no retailing B&O tax or retail sales tax is owed on the two construction projects. The Washington State Board of Tax Appeals agreed, concluding that Nord Northwest qualified as a “speculative builder” on the two projects.¹ The Superior Court, in an appeal filed by the Department of Revenue under the Administrative Procedure Act, reversed the Board of Tax Appeals and reinstated the tax assessment. The Superior Court concluded that Nord Northwest Corporation did not qualify as a “speculative builder” because it did not own the real property upon which the condominiums were built. This appeal followed.²

¹ As discussed in detail *infra*, a “speculative builder” does not owe retailing B&O tax, and is not required to charge itself retail sales tax, on the value of construction services it performs on real property it owns.

² Nord Northwest Corporation filed this appeal from the decision of the Superior Court reversing the Board of Tax Appeals’ administrative decision. CP at 64. However, pursuant to General Order 2010-1, the Department of Revenue, as the party that filed the appeal to the Superior Court under the Administrative Procedure Act, is responsible for filing the opening and reply briefs before the Court of Appeals.

II. ASSIGNMENTS OF ERROR AND ISSUES PRESENTED

1. The Board of Tax Appeals erred in concluding that Nord Northwest Corporation qualified as a speculative builder on the two construction projects at issue.

Issue presented: Did the Board of Tax Appeals err in concluding that Nord Northwest Corporation qualified as a speculative builder on the two construction projects at issue where Nord Northwest did not own the real property upon which the construction services were performed?

2. The Board of Tax Appeals erred in applying the “attributes of ownership” set out in WAC 458-20-170(2)(a) when it was undisputed that Nord Northwest Corporation did not own the real property upon which the construction services were performed.

Issue presented: Did the Board of Tax Appeals err in applying the “attributes of ownership” set out in WAC 458-20-170(2)(a) when there was no dispute that Nord Northwest Corporation did not own the real property upon which it performed the construction services?

3. Even if the “attributes of ownership” can properly be applied when, as here, there is no dispute as to who owned the real property, the Board erred in finding of fact no. 7 that “[t]he non-Nord LLC members who contributed cash to the LLCs were loaning money to Nord.” This finding of fact is not supported by evidence that is substantial when viewed in light of the record as a whole. Moreover, the finding is reversible error because it was critical to the Board’s application of the “attributes of ownership” and resulted in other erroneous findings of fact, including the following:

- Finding of fact no. 4: “Nord [Northwest Corporation] determined that it could obtain loans from another source to meet its equity requirements for the two new projects and approached other parties to loan it \$200,000 of the equity needed.” There is no evidence in the record that the “other parties” loaned Nord Northwest Corporation \$200,000.
- Finding of fact no. 8: “Bellingham Condominium LLC and Stanwood Condominium LLC (the LLCs) were created to give the non-Nord LLC members security for their loans to Nord

[Northwest Corporation] by holding title to the properties because this would be a way to both provide the members security for their loans to Nord [Northwest Corporation] and not mix their activities with Nord [Northwest Corporation]’s.” There is no evidence in the record that the “non-Nord LLC members” loaned money to Nord Northwest Corporation or that the LLCs were created to provide the minority LLC members security for “their loans” to Nord Northwest Corporation.

- Finding of fact no. 10: “The LLC documentation clearly demonstrates that Nord [Northwest Corporation] bore the entire risk of loss on the two condominium developments and the responsibility for paying the debt back to the other members of the LLCs.” There is no evidence in the record that the “LLC documentation” demonstrate that Nord Northwest Corporation bore the entire risk of loss, or that Nord Northwest Corporation owed a “debt” to the other LLC members.
- Finding of fact no. 11: “Horizon Bank fully recognized that Bellingham Condominium LLC was set up only to hold title to land to protect the non-Nord members’ loans to Nord [Northwest Corporation] for its 20-percent equity requirement for the construction loans for the Woodland Hill project near Bellingham.” There is no evidence in the record that the minority LLC members loaned money to Nord Northwest Corporation, or that that Horizon Bank “recognized” that Bellingham Condominiums LLC “was set up only to hold title to land to protect the non-Nord members’ loans to Nord” Northwest Corporation.
- Finding of fact no. 12: “Peoples Bank fully recognized the Stanwood Condominium LLC was set up to protect the non-Nord members’ loans to Nord [Northwest Corporation] for its 20-percent equity requirement for the construction loan for . . . the Stanwood condominium development.” There is no evidence in the record that the minority LLC members loaned money to Nord Northwest Corporation, or that Peoples Bank “recognized” that Stanwood Condominiums LLC was “set up to protect the non-Nord members’ loans to Nord” Northwest Corporation.

- Finding of fact no. 13: “Pacific Northwest Bank fully recognized that Bellingham Condominium LLC was set up only to hold title to land to protect the non-Nord members’ loans to Nord [Northwest Corporation] for its 20-percent equity requirement for the construction loan for the Woodland Hill project near Bellingham, and the Stanwood Condominium LLC was set up to protect the non-Nord members’ loans to Nord [Northwest Corporation] for its 20-percent equity requirement for the construction loan for the Stanwood condominium development.” There is no evidence in the record that the minority LLC members loaned money to Nord Northwest Corporation, or that Pacific Northwest Bank “recognized” that the Bellingham Condominiums LLC and Stanwood Condominiums LLC were “set up only to hold title to land to protect the non-Nord members’ loans to Nord” Northwest Corporation.
- Finding of fact no. 20: “The banks making the construction loans and the other members of the LLCs treated the projects as if Nord [Northwest Corporation] was the developer of the projects in all respects, and recognized that the LLCs were just financing vehicles for Nord [Northwest Corporation]’s 20-percent equity requirement to obtain construction loans.” To the extent this finding is intended to imply that the LLCs were created to secure “loans,” there is no evidence in the record that the minority LLC members loaned money to Nord Northwest Corporation.
- Finding of fact no. 28: “The LLCs were holding title as security for the LLCs’ members for their loans to Nord” Northwest Corporation. There is no evidence in the record that the minority LLC members loaned money to Nord Northwest Corporation.

Issue presented: If the “attributes of ownership” are applicable in this case, is there evidence in the agency record that is substantial when viewed in light of the whole record before the court to support the Board of Tax Appeals’ finding that “[t]he non-Nord LLC members who contributed cash to the LLCs were loaning money to Nord” Northwest Corporation?

4. The Board of Tax Appeals erred in refusing to consider WAC 458-20-170(2)(f), which provides that “[p]ersons, including corporations, partnerships, sole proprietorships, and joint ventures, . . .

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 . . . , not as ‘speculative builders.’”

Issue presented: Did the Board of Tax Appeals err in refusing to consider WAC 458-20-170(2)(f) where there was no dispute that Nord Northwest Corporation performed construction services on land owned by affiliated limited liability companies?

5. The Board of Tax Appeals erred by misapplying the common law resulting trust doctrine when it concluded that Nord Northwest Corporation was the beneficial owner of the real property upon which the two condominiums were built even though the undisputed evidence shows that the two limited liability companies acquired the real property with amounts loaned or advanced from Nord Northwest Corporation.

Issue presented: Did the Board of Tax Appeals err by misapplying the common law resulting trust doctrine where the undisputed evidence shows that the two limited liability companies acquired the real property with amounts loaned or advanced from Nord Northwest Corporation?

III. STATEMENT OF THE CASE

A. Nord Northwest Corporation’s Need For Additional Equity To Fund The Condominium Construction Projects Led To The Formation Of Two LLCs.

Nord Northwest Corporation is a licensed construction contractor and is engaged primarily in the construction of single family homes and multi-unit condominiums. Transcript of Proceedings (hereinafter “Tr.”) at 117-18. In late 1998 or early 1999, Nord Northwest Corporation began looking into the feasibility of two construction projects, one to build condominiums in Stanwood, Washington, and the other to build condominiums in Bellingham, Washington. Tr. at 22-23. Because Nord

Northwest Corporation was in the construction phase of another project, the company did not have the means to take on the two new projects without obtaining financing. Tr. at 33-34. Nord Northwest Corporation initially sought financing for the two construction projects at its local bank, but was informed that additional equity financing would be required before the bank would agree to loan money for the proposed construction. Tr. at 23, 32-33.³ Thereafter discussions were held between Richard Nord Sr., sole shareholder and President of Nord Northwest Corporation, Richard Nord, Jr., Vice President of Nord Northwest Corporation, and Ronald Hoelscher, Chief Financial Officer of Nord Northwest Corporation. Tr. at 31-33. As a result of these discussions, it was decided that Nord Northwest Corporation could raise the needed equity by bringing in additional investors. Tr. at 33-35. To accomplish this, two limited liability companies were formed: Stanwood Condominiums LLC and Bellingham Condominiums LLC.

B. Formation Of Stanwood Condominiums LLC.

Stanwood Condominiums LLC was formed on June 7, 1999. Cert. Administrative Record (hereinafter “AR”) at 635. The stated purpose of the LLC was to “own, manage, and/or develop real estate; and to carry on any lawful business or activity.” AR at 639 (Article 3(a)). Stanwood

³ At the Board of Tax Appeals hearing, Grace Pescheck, commercial loan officer with Horizon Bank, explained that a bank normally requires an eighty percent (80%) “loan to value ratio” before it will make a construction loan. Tr. at 166-67.

Condominiums LLC had five members: Nord Northwest Corporation, three married couples, and a trust. AR at 635, 657. Nord Northwest Corporation contributed “services” and received an initial 40% ownership interest. AR at 657. The married couples and the trust each contributed \$37,500 and each received an initial 15% ownership interest. *Id.* Richard Nord, Sr. was named Manager of the LLC. AR at 637.

Shortly after Stanwood Condominiums LLC was formed, the members passed a resolution that provided in part that Nord Northwest Corporation “shall be entitled to, and by this resolution does hereby receive a fully vested sixty percent (60%) ownership interest in Stanwood Condominiums, LLC, in consideration for Nord’s agreement to develop the real property.” AR at 658 (§ 1). The resolution also provided that Nord Northwest Corporation “is hereby authorized and directed to act as prime contractor for said development and receive payment (out of the gross proceeds from the sale of units so constructed) for said services in an amount equal to ten percent (10%) of construction costs as Nord’s profit.” *Id.* (§ 2).

On June 11, 1999, Stanwood Condominiums LLC acquired the real property upon which the proposed condominium project was to be built. AR at 660. Sometime thereafter, Stanwood Condominiums LLC entered into a construction loan agreement with Peoples Bank. AR at 662. The loan

agreement identified Stanwood Condominiums LLC as the “Borrower” and Peoples Bank as the “Lender.” *Id.*

Nord Northwest Corporation was hired by the LLC to perform the construction work on the condominium project. AR at 669. However, when performing the construction, Nord Northwest Corporation treated itself as a speculative builder even though the real property was owned by the LLC. At the Board of Tax Appeals hearing, Richard Nord, Sr., President of Nord Northwest Corporation, explained that he understood the term “speculative construction” to mean “construction that is constructed by a contractor for sale to the general public or to some individual client . . . on a speculative basis.” Tr. at 100. Ronald Hoelscher, Chief Financial Officer of Nord Northwest Corporation, had a similar misunderstanding of the distinction between a speculative builder and a prime contractor. Tr. at 36-37 (Hoelscher testified that he understood a “speculative builder” to “be a contractor who builds strictly on a speculative basis, has no buyer, pre buyer. In other words, it’s not pre sold.”). As a result of this misunderstanding of the law, Nord Northwest Corporation did not pay retailing B&O tax, and did not charge or collect retail sales tax, on the construction services it rendered to Stanwood Condominiums LLC.

C. Formation Of Bellingham Condominiums LLC.

The facts surrounding the construction of the Bellingham condominiums were similar. Nord Northwest Corporation initially conceived the Bellingham condominium project in late 1998 or early 1999. AR at 762 (memo describing the proposed project). Bellingham Condominiums LLC was formed in June 1999. AR at 766. The LLC was made up of six members, including Nord Northwest Corporation. AR at 766, 787. Nord Northwest Corporation contributed “services” and received an initial 30% ownership interest. AR at 787. Four of the other six members contributed \$12,500 each, and each received an initial 12.5% ownership interest. *Id.* The final member, Western Resource Group, Inc., received a 20% interest in exchange for selling land to Nord Northwest Corporation at a reduced price.

At around the same time that Bellingham Condominiums LLC was formed, Nord Northwest Corporation purchased real property in Bellingham from Western Resource Group, Inc. AR at 763 (statutory warranty deed recorded June 16, 1999). On September 27, 1999, Nord Northwest Corporation transferred the real property to Bellingham Condominiums LLC. AR at 796. Bellingham Condominiums LLC and Nord Northwest Corporation both accounted for the transfer of the real property as a sale, with Bellingham Condominiums LLC taking title to the

land in exchange for an account payable to Nord Northwest Corporation.

Tr. at 192-94, 208.

On September 22, 1999, the members of Bellingham Condominiums LLC passed a resolution that provided in part that Nord Northwest Corporation “shall be entitled to, and by this resolution does hereby receive a fully vested sixty percent (60%) ownership/economic interest in Bellingham Condominium, LLC, in consideration for Nord’s agreement to develop the real property” AR at 788 (¶ 1). The resolution also provided that Nord Northwest Corporation “is hereby authorized and directed to act as prime contractor for said development and receive payment (out of the gross proceeds from the sale of units so constructed) for said services in an amount equal to ten percent (10%) of construction costs as Nord’s profit.” *Id.* (¶ 2).

Shortly after Bellingham Condominiums LLC was formed, the LLC negotiated a construction loan with InterWest Bank. AR at 790. In May 2001, Bellingham Condominiums LLC entered into a construction loan agreement with Horizon Bank. AR at 798. Both loan agreements identified Bellingham Condominiums LLC as the borrower and the bank as the lender. AR 790, 798.

As agreed in the LLC resolution, Nord Northwest Corporation performed the construction work on the Bellingham condominium project.

In performing the construction, Nord Northwest Corporation treated itself as a speculative builder even though the real property was owned by the LLC.⁴ As a result, Nord Northwest Corporation did not pay retailing B&O tax, and did not charge or collect retail sales tax, on the construction services it rendered to Bellingham Condominiums LLC.

D. Audit Assessment And Department Of Revenue Determination.

Nord Northwest Corporation was audited by the Department of Revenue (“Department”) in 2003. The audit covered the January 1998 through February 2002 reporting periods, and resulted in a notice of tax assessment dated November 12, 2003. AR at 486. The two primary audit adjustments made to Nord Northwest Corporation’s excise tax returns were to reclassify the Stanwood and Bellingham projects as retail construction. AR at 488-89 (discussing “Schedule 4” of audit report).

Nord Northwest Corporation filed a timely appeal of the tax assessment with the Department’s Appeals Division. On April 30, 2008, the Department issued its Final Executive Level Determination denying Nord Northwest Corporation’s appeal and affirming the tax assessment. AR at 515.

⁴ Both Richard Nord, Sr., President of Nord Northwest Corporation, and Ronald Hoelscher, Chief Financial Officer, misunderstood the distinction between a speculative builder and a prime contractor. Tr. at 100 (testimony of Richard Nord, Sr.); Tr. at 36-37 (testimony of Ronald Hoelscher). Neither one believed that ownership of the real property by Nord Northwest Corporation was required.

E. The Board Of Tax Appeals' Decision.

Nord Northwest Corporation filed a timely appeal with the Board of Tax Appeals. After a formal hearing under the Administrative Procedure Act, the Board issued its decision in favor of Nord Northwest Corporation. AR at 9. The Board concluded that Nord Northwest Corporation was a speculative builder on the Stanwood and Bellingham condominium projects either because Nord Northwest satisfied the “attributes of ownership” set out in WAC 458-20-170(2) or because Nord Northwest Corporation held a beneficial interest in the real property under the resulting trust doctrine. AR at 19-21.

In reaching its decision that Nord Northwest Corporation qualified as a speculative builder, the Board of Tax Appeals concluded that capital contributions made by the minority members of the two LLCs were actually “loans” from those members to Nord Northwest Corporation. AR at 19 (“the non-Nord members of the LLCs were making loans to Nord, and the LLCs were merely a vehicle to provide both a security interest for their loan and to ensure that Nord was completely in charge of the two developments.”). This conclusion—which is not supported by any substantial evidence—was critical to the Board’s analysis. *See* AR at 22-23 (Board refers to “loans” from minority members of LLCs in findings of fact no. 4, 7, 8, 10, 11, 12, 13, and 28).

F. The Superior Court Reverses The Board.

The Department petitioned for judicial review of the final decision of the Board of Tax Appeals. CP at 3. On February 12, 2010, the Thurston County Superior Court, the Honorable Carol Murphy, issued a letter opinion reversing the Board's decision. CP at 55-57. In that letter opinion, the court concluded that Nord Northwest Corporation did not qualify as a speculative builder as a matter of law because the undisputed evidence showed that the corporation "did not own the real estate upon which it constructed the condominiums." CP at 57. Shortly thereafter the court issued an order consistent with its letter opinion. CP at 58-63. Nord Northwest Corporation then filed this appeal. CP 64.

IV. SUMMARY OF ARGUMENT

Construction services are taxable as a retail sale when performed "upon . . . real property of or for consumers." RCW 82.04.050(2)(b). A "consumer" includes "[a]ny person who is an owner, lessee or has the right of possession to or an easement in real property which is being constructed, repaired, decorated, improved, or otherwise altered by a person engaged in business" RCW 82.04.190(4). Together, these two statutes provide that a person performing construction services on real property owned, leased, or possessed by any different person is engaged in retail construction.

Conversely, a person performing construction services on real property it owns is not engaged in an activity meeting the definition of a retail sale. *Rigby v. State*, 49 Wn.2d 707, 306 P.2d 216 (1957). A person performing construction upon real property that it owns is commonly referred to as a “speculative builder.” Because construction services performed by a speculative builder do not qualify as a retail sale, retailing B&O tax and retail sales tax is not owed on the value of those services. The tax advantage for a construction contractor that qualifies as a speculative builder can be significant.

The condominiums at issue in this case were constructed by Nord Northwest Corporation on real property owned by two separate limited liability companies—Stanwood Condominiums LLC and Bellingham Condominiums LLC. Because the limited liability companies were separate entities from Nord Northwest Corporation, the construction services were performed on real property “of or for consumers” and qualify as retail construction under RCW 82.04.050(2)(b). However, the Board of Tax Appeals, in reversing the tax assessment issued by the Department, ignored the plain language of the statute. Instead, the Board held that Nord Northwest Corporation qualified as a “speculative builder” even though Nord Northwest Corporation did not own the real property

upon which the construction was performed. The Board's decision was correctly reversed by the Thurston County Superior Court.

The Board of Tax Appeals made several critical errors. First and foremost, it erred as a matter of law in holding that Nord Northwest Corporation qualified as a speculative builder even though Nord Northwest did not own the real property upon which the construction was performed. The Board of Tax Appeals also erroneously interpreted and applied the "attributes of ownership" set out in WAC 458-20-170(2)(a) and the common law "resulting trust" doctrine. As a result of these errors, the Board expanded the "speculative builder" classification far beyond what the law allows, and permitted Nord Northwest Corporation to obtain a tax advantage that the company simply is not entitled to. For all these reasons, this Court should reverse the Board of Tax Appeals' decision and affirm the judgment of the superior court.

V. ARGUMENT

A. Standard Of Review.

The Administrative Procedure Act (APA) governs judicial review of a formal Board of Tax Appeals decision. RCW 82.03.180. Under the APA, the burden of demonstrating the invalidity of the Board's order is on the Department of Revenue because it asserts that the Board erred. RCW 34.05.570(1)(a). This Court may reverse the Board's order if, among

other reasons, the Board erroneously interpreted or applied the law, the Board made a finding of fact that is not supported by substantial evidence, or the Board's order is arbitrary and capricious. RCW 34.05.570(3).

An appellate court reviews the decision of the administrative agency and "applies the APA standards directly to the administrative record." *Verizon Nw., Inc. v. Employment Sec. Dep't.*, 164 Wn.2d 909, 915, 194 P.3d 255 (2008). The court reviews an agency's legal conclusions under the error of law standard. *Id.* (citing RCW 34.05.570(3)(d)). *See also Cascade Court Limited Partnership v. Noble*, 105 Wn. App. 563, 567, 20 P.3d 997 (2001). Findings of fact, on the other hand, are reviewed under the "substantial evidence" standard. *Wilson v. Employment Sec. Dep't.*, 87 Wn. App. 197, 200-01, 940 P.2d 269 (1997).

B. The Board Of Tax Appeals Erred In Concluding That Nord Northwest Corporation Qualified As A Speculative Builder.

1. There is an important legal distinction between a prime contractor and a speculative builder.

Washington imposes a retail sales tax on each retail sale in this state. RCW 82.08.020. In addition, Washington imposes a gross receipts tax on the gross proceeds derived from the business of making retail sales in this state. RCW 82.04.250(1).

The term "retail sale" is defined in RCW 82.04.050 and includes services rendered in respect to constructing buildings or other structures

upon “real property of or for consumers.” RCW 82.04.050(2)(b). The term “consumer” is defined in RCW 82.04.190 and includes “[a]ny person who is an owner, lessee or has the right of possession to . . . real property which is being constructed, repaired, decorated, improved, or otherwise altered by a person engaged in business.” RCW 82.04.190(4). Together, these provisions dictate that a person performing construction services on real property owned, leased, or possessed by another person is engaged in making retail sales and must pay retailing B&O tax, and must collect and remit retail sales tax, on the gross amount derived from the construction activity. Such a person is commonly referred to as a “prime contractor.” See WAC 458-20-170(1)(a).⁵

By contrast, a person constructing buildings on real property it owns is not engaged in an activity within the definition of a “retail sale.” *Rigby v. State*, 49 Wn.2d 707, 306 P.2d 216 (1957). This is because a builder is not the “consumer” of construction services it provides to itself. *White-Leasure Development Co. v. Dep’t of Revenue*, 2001 WL 1807636 (Wash. Bd. Tax. App. 2001). A person constructing buildings on real property it owns is referred to as a “speculative builder.” See WAC 458-20-170(2)(a).

⁵ A copy of WAC 458-20-170 is attached hereto as Appendix A.

A speculative builder enjoys two important tax advantages over a prime contractor. First, a speculative builder is not required to pay B&O tax on the amount attributed to the construction project even though the value of the real property is increased. This is because a speculative builder does not charge itself for its own construction services, and amounts derived from the sale of real property are exempt from the B&O tax. RCW 82.04.390. In contrast, a person performing construction services on land owned, leased, or possessed by another person engaged in retail construction and is liable for B&O tax on the gross amount received from the consumer.

The second tax advantage relates to the measure of the retail sales tax. A prime contractor is required to collect and remit retail sales tax on the “selling price” paid by the consumer for the construction. RCW 82.08.020(1). *See also* RCW 82.08.010(1) (defining “selling price”); *Klickitat County v. Jenner*, 15 Wn.2d 373, 382, 130 P.2d 880 (1942) (the measure of a retail sale is “the cost to the buyer or consumer, and not the cost to the seller.”). Thus, the measure of the retail sales tax includes the amount charged for construction services performed by the contractor. In contrast, a speculative builder pays retail sales tax only on its purchase of building materials and subcontract labor. When the property is sold (presumably at a price incorporating the costs and labor by the speculative

builder), the speculative builder is not required to collect retail sales tax on the sale of the improved real property, thus avoiding any sales tax for the contractor's labor. *Riley Pleas Inc. v. State*, 88 Wn.2d 933, 934, 568 P.2d 780 (1977).

2. The undisputed evidence shows that Nord Northwest Corporation did not own the real property upon which the condominiums were built.

The distinction between a prime contractor and a speculative builder turns on whether the person doing the construction owns the real property upon which the construction is performed. In the present case, there is no dispute that Nord Northwest Corporation (the contractor) did not own the real property upon which the Stanwood and Bellingham condominiums were built. *See* AR at 660 (statutory warranty deed establishing Stanwood Condominiums LLC's ownership of the Stanwood real property); AR at 796 (quit claim deed establishing Bellingham Condominiums LLC's ownership of the Bellingham real property). In closing argument to the Board of Tax Appeals, Richard Nord Sr.—president of Nord Northwest Corporation—conceded that “we knew we didn't own the property. We admit we don't own the property.” Tr. at 214. The documents relating to the two construction projects also make clear that the LLCs owned the real property throughout the construction and final sale of the condominium units. *See, e.g.*, AR at 712

(Condominium Purchase and Sale Agreement listing Stanwood Condominiums LLC as the seller of unit 501); AR at 855 (Condominium Purchase and Sale Agreement listing Bellingham Condominiums LLC as the seller of unit 101). Furthermore, it is undisputed that the two LLCs are separate legal entities from Nord Northwest Corporation. RCW 25.15.070(2)(c) (“A limited liability company formed under this chapter shall be a separate legal entity . . .”). Therefore, there is simply no doubt that the real property was owned by a person other than Nord Northwest Corporation during the time the condominiums were constructed. These facts establish that both Stanwood Condominiums LLC and Bellingham Condominiums LLC were “consumers” of the construction services performed by Nord Northwest Corporation.

Treating the LLCs as “consumers” of construction services is not only correct as a matter of law, it is also consistent with the course of dealing between Nord Northwest Corporation and the two LLCs. In both construction projects, Nord Northwest entered into a construction service contract with the LLC. AR at 669 (construction service agreement between Stanwood Condominiums LLC and Nord Northwest Corporation).⁶ Both LLCs issued resolutions specifically naming Nord Northwest Corporation as the prime contractor and directing that Nord

⁶ Nord Northwest Corporation was unable to locate the construction services contract it entered into with Bellingham Condominiums LLC.

Northwest “receive payment . . . for said services in an amount equal to ten percent (10%) of construction costs as Nord’s profit.” AR at 658, 788. Consistent with the LLC resolutions, Nord Northwest Corporation billed the LLCs for work performed, including its profit. AR at 812-17 (billing statements listing “Profit @ 10% of total project costs.”). Moreover, Nord Northwest Corporation accounted for the amounts received from the two projects consistent with a “prime contractor.” Tr. at 194-96 (testimony of Department’s auditor that Nord Northwest Corporation billed the LLCs for construction services, including “profit,” which is not typical for a speculative builder). Had Nord Northwest Corporation truly been performing construction services on real property that it owned, it would not have billed itself for its own construction services. Tr. at 196. Moreover, any “profit” would have been realized from selling the improved real property, not from construction services rendered to itself. In short, the manner in which Nord Northwest Corporation treated the construction projects is consistent with a prime contractor performing construction services “upon . . . real property of or for consumers.”

It is immaterial that Nord Northwest Corporation was a majority member of both LLCs or that Mr. Nord was the manager of both LLCs. Washington law specifies that a limited liability company is a separate legal entity from its owners. RCW 25.15.070(2)(c). Moreover, it is well

settled that affiliated business entities, such as a parent and its subsidiary corporations, are treated as separate persons for B&O and retail sales tax purposes. *Simpson Inv. Co. v. Dep't. of Revenue*, 141 Wn.2d 139, 154, 3 P.3d 741 (2000) (citing *Sav-Mor Oil v. Tax Comm'n*, 58 Wn.2d 518, 520-23, 364 P.2d 440 (1961)). For all these reasons, construction performed by a member or manager of these LLCs on real property owned by the LLCs does not qualify as speculative construction.

This Court should conclude that Nord Northwest Corporation performed construction services on real property it did not own, and therefore it cannot qualify as a speculative builder. The Board's final decision to the contrary is incorrect as a matter of law and was correctly reversed by the Superior Court.

C. The Board Of Tax Appeals Erred In Applying The "Attributes Of Ownership" Set Out In WAC 458-20-170(2)(a) When It Was Undisputed That Nord Northwest Corporation Did Not Own The Real Property Upon Which The Construction Services Were Performed.

Nord Northwest Corporation conceded that it did not own the real property upon which the two condominiums were built, and that should end this case. Tr. at 214. Nord Northwest, however, argues that it should be treated as a speculative builder based on its belief that it had sufficient "attributes of ownership" to qualify as a speculative builder under WAC 458-20-170(2)(a). The Board of Tax Appeals accepted this argument. AR

at 19. However, proper application of WAC 458-20-170(2)(a) does not support Nord Northwest Corporation's argument or the Board's ruling.

WAC 458-20-170(2)(a) (hereinafter "Rule 170(2)(a)") provides as follows:

(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 first sentence of Rule 170(2)(a) defines a "speculative builder" as "one who constructs buildings for sale or rental upon real estate owned by him." The second sentence lists four nonexclusive "attributes of ownership."

The purpose of Rule 170(2)(a) is not to create an exception to the "ownership" requirement. Rather, the Rule is designed to ensure that any claim of ownership of real property is genuine. In other words, the "attributes of ownership" establish that a formal transfer of title to real property may not be enough to show ownership of that property where the substance of the transaction indicates that the property was transferred for some other purpose. This becomes evident when Rule 170(2)(a) is read in context with Rule 170(2)(b), which provides:

(b) Where an owner of real estate sells it to a builder who constructs, repairs, decorates, or improves new or existing buildings or other structures thereon, and the builder thereafter resells the improved property back to the owner, the builder will not be considered a speculative builder. In such a case that portion of the resale attributable to the construction, repairs, decorations, or improvements by the builder, shall not be considered a sale of real estate and shall be fully subject to retailing business and occupation tax and retail sales tax. It is intended by this provision to prevent the avoidance of tax liability on construction labor and services by utilizing the mechanism of real property transfers.

WAC 458-20-170(2)(b) (emphasis added).

Rule 170(2)(a) and (b) recognize and reflect Washington property law. Under Washington law, a transfer of title to real property does not always establish ownership of that property. Instead, “a deed that contains or is accompanied by an agreement that it shall be canceled or the land reconveyed upon payment of a debt is a mortgage.” *Bank of Am. v. Prestance Corp.*, 160 Wn.2d 560, 562 n.1, 160 P.3d 17 (2007) (quoting 18 William B. Stoebuck & John W. Weaver, *Wash. Practice: Real Estate: Transactions* § 20.2 (2d ed. 2004)). *See also Gossett v. Farmers Ins. Co. of Wash.*, 133 Wn.2d 954, 966, 948 P.2d 1264 (1997) (if a “deed is conveyed with the intent of the parties being to create a debtor-creditor relationship, then the deed may be declared to create an equitable mortgage.”). As a result, when a construction contractor has taken title to real property prior to starting construction on that land, it is important to

look beyond the face of the deed to determine whether the contractor actually received ownership of the property or merely a security interest.

Because a deed might not convey ownership, the Department looks to certain “attributes of ownership” to determine whether the person with title to the real property is truly the owner. The Department first articulated its position in former Excise Tax Bulletin 275. AR 569. That Excise Tax Bulletin, issued in September 1966, explained that “[d]eeds, though absolute on their face, may be mortgages, depending upon the surrounding circumstances.” *Id.* As a result, a landowner who deeds a lot to a construction contractor for the purpose of securing financing for the construction project remains the owner of the real property. The construction contractor in this scenario holds only a mortgage interest.

The “attributes of ownership” should be applied in a manner that is consistent with Rule 170(2)(b) and with Washington property law. Neither the language nor the purpose of Rule 170(2)(a) creates an exception to the requirement that the builder must be the bona fide owner of the real property to qualify as a speculative builder. *See Coast Pacific Trading, Inc. v. Department of Revenue*, 105 Wn.2d 912, 917, 719 P.2d 541 (1986) (Department cannot use administrative rules to expand tax immunity beyond the exemptions provided by statute or required by the state and federal constitutions). Rather, the factors listed in Rule 170(2)(a)

are relevant only insofar as they help distinguish actual ownership from a mortgage or similar security interest.

In this case, it is undisputed that Nord Northwest Corporation did not own the real property upon which the two condominium projects were built. Tr. at 214. Because ownership was not in dispute, Rule 170(2)(a) was not implicated. Consequently, the Board erred by applying the attributes of ownership set out in Rule 170(2)(a). Nord Northwest Corporation was not the owner of the real property at issue, and Rule 170(2)(a) does not change that fact.

D. If The “Attributes Of Ownership” Were Applicable, There Is No Evidence In The Agency Record To Support The Board Of Tax Appeals’ Finding That “The Non-Nord LLC Members Who Contributed Cash To The LLCs Were Loaning Money To Nord” Northwest Corporation.

Even if the attributes of ownership were relevant, the Board of Tax Appeals misapplied the rule. The Board’s primary error was to conclude that amounts contributed by the minority members of the two LLCs were not capital contributions as reflected on the face of the limited liability agreements, but loans from those minority members to Nord Northwest Corporation. *See* AR 19 (“the non-Nord members of the LLCs were making loans to Nord . . .”). *See also*, AR 22 (finding of fact no. 7, stating that “[t]he non-Nord LLC members who contributed cash to the LLCs were loaning money to Nord to meet Nord’s 20-percent equity

requirement for the construction loans.”). As a direct result of this erroneous finding, the Board of Tax Appeals went on to hold that Nord Northwest Corporation met the four non-exclusive attributes of ownership listed in Rule 170(2)(a). According to the Board:

Nord correctly applies the non-exclusive attributes of ownership criteria in Rule 170 at face value:

- Clearly, the intention of the non-Nord members of the LLCs were that the LLCs were created to take title to the land upon which the condominium projects would be built as security for their loans, while ensuring that Nord continued to have all responsibilities for the development of the condominium projects.

....

- Clearly, all the parties, in particular the parties who contributed cash to the LLCs and the banks that recognized that the LLC members were loaning money to Nord to meet Nord’s 20-percent equity requirement for the construction loans, regarded the LLCs as holding title to the land only for the purpose of securing the loans made by non-Nord LLC members as to its equity requirement to obtain construction financing.

AR at 19 (footnotes omitted) (emphasis added).

There is no evidence in the record to support the Board’s finding that the initial capital contributions made by the minority members of Stanwood Condominiums LLC and Bellingham Condominiums LLC were actually loans to Nord Northwest Corporation. Nord Northwest Corporation did not even argue that the initial contributions into the LLCs

were loans. *See* AR at 172-187 (opening brief of Nord Northwest Corporation containing no argument that capital contributions were loans); AR at 66-75 (reply brief of Nord Northwest Corporation containing no argument that capital contributions were loans); Tr. at 214-24 (in closing argument on behalf of Nord Northwest Corporation, Richard Nord, Sr. did not argue that capital contributions were loans). The Board came up with the “loan” theory on its own.

The fact that there were no loans by the minority LLC members to Nord Northwest Corporation is clear from the record. First, it must be noted that there is no promissory note or similar loan document contained in the agency record whereby the minority members are purporting to loan money to Nord Northwest Corporation. If the minority members were loaning money to Nord Northwest Corporation, they did so without any of the normal formalities associated with making a loan.

Moreover, the LLC agreements clearly do not support the Board’s finding. The limited liability company agreement for Stanwood Condominiums LLC specifically provides that “[e]ach Member shall contribute such amount as is set forth in attached Schedule 1 as such Member’s share of the Members’ Initial Capital Contribution.” AR at 642 (¶ 8.1) (emphasis added). The schedule attached to the agreement provides that each of the minority members is making an initial capital

contribution of \$37,500. AR at 657. The federal partnership tax returns filed by Stanwood Condominiums LLC also confirm that the amounts contributed by the minority members were capital contributions, not loans. AR at 724 (listing capital contributions of minority members totaling \$150,000). In short, the objective evidence relating to Stanwood Condominiums LLC clearly shows that the amounts contributed by the minority members were capital contributions, not loans to Nord Northwest Corporation.

The LLC agreement for Bellingham Condominiums LLC is similar. It specifically provides that “[e]ach Member shall contribute such amount as is set forth in attached Schedule 1 as such Member’s share of the Members’ Initial Capital Contribution.” AR 772 (¶ 8.1). The schedule attached to the agreement specifies the amount of each members “Initial Capital Contribution.” AR 787. Again, the objective evidence clearly shows that the amounts contributed by the members of the LLC were capital contributions, not loans.

A capital contribution is a payment or donation of money, property, or services to a business for the purpose of commencing or carrying on the business, and is generally made by an owner or member in exchange for equity in the business. 68 C.J.S. *Partnership* § 126 (2009); 18 C.J.S. *Corporations* § 174 (2007). It is beyond dispute that a capital

contribution is not a loan. *Saviano v. Westport Amusements, Inc.*, 144 Wn. App. 72, 81, 180 P.3d 874 (2008). *See generally* 68 C.J.S. *Partnership* § 126 (2009) (“A contribution to the capital of a partnership by a member does not constitute a loan to his or her copartner.”) (Footnote omitted). Thus, the Board of Tax Appeals could not have relied on the documents contained in the agency record as support for its finding that the contributions of the minority LLC members were actually loans to Nord Northwest Corporation. The documents contained in the agency record clearly refute the Board’s finding.

In addition, the testimony presented at the hearing does not support the Board’s finding that the capital contributions of the minority members were actually loans to Nord Northwest Corporation. The only minority member of either LLC to testify at the hearing was Ronald Hoelscher. Mr. Hoelscher and his wife, Virginia, were minority members of both Stanwood Condominiums LLC and Bellingham Condominiums LLC. *See* AR at 657 (listing members of Stanwood Condominiums LLC, including Ronald and Virginia); AR at 787 (listing members of Bellingham Condominiums LLC, including Mr. and Mrs. Hoelscher). Mr. Hoelscher also was the Chief Financial Officer of Nord Northwest Corporation during the periods at issue. Tr. at 22.

During direct testimony, Mr. Hoelscher explained that while Nord Northwest Corporation and Richard Nord, Sr. were in control of the LLCs and made all decisions relating to the business operations of the LLCs, the minority members were equity investors in those LLCs. Tr. at 27. More specifically, Mr. Hoelscher provided the following testimony relating to the formation of the two LLCs:

The investors would provide \$200,000 in equity in the form of cash and then Nord Northwest would provide the balance of the equity required. I think in this particular project it's -- that there was approximately \$350,000 of money-covered equity needed to secure the financing. For providing the equity investors would receive a percentage of the profits. So we were trying to, uh, separate this project, uh, and we did it using this LLC, but it was only to secure the equity funding and to provide the equity holders a participation in the overall project as it was finished.

Id. (emphasis added). Mr. Hoelscher provided similar testimony during cross-examination. Tr. at 32 (“[O]n the other side of the equation you got to provide the investor some protection and -- and some way of showing how they are going to be -- their equity is going to get paid back or they are going to get a return on their equity.”); Tr. at 35 (“[I]f we wanted to secure the financing, we had to come up with some additional equity, ‘we’ being Nord Northwest.”); Tr. at 46 (“[T]he only thing that I can recall about [the creation of the Stanwood Condominium LLC resolution] was providing each party some amount of protection, the investors some

protection as to their equity”). At no point did Mr. Hoelscher testify that the contributions made by the minority members were intended to be loans to Nord Northwest Corporation. Instead, he consistently referred to the contributions as “equity” and the minority members as “investors.”

Richard Nord, Sr. also testified that the purpose of the LLCs was to bring in additional equity investors to meet the loan-to-value requirements of the banks. Tr. at 119, 128. As succinctly explained by Mr. Nord:

We had investors that wanted to invest in this project but didn’t want to have liability beyond the amount of their investment. We needed the investors in order to start construction, because the banks weren’t interested in releasing funds unless we had some additional funding.

Tr. at 128. Mike Cunningham, another witness for Nord Northwest Corporation, testified that raising additional equity capital is a legitimate business reason for forming a limited liability company. Tr. at 74.

The testimony of the witnesses during the hearing is consistent with the documents provided to the Board of Tax Appeals. The two LLCs were formed to obtain additional equity funding so that the construction projects could get started. The minority LLC members contributed cash to the LLCs in exchange for their equity interest in those LLCs. The capital contributions of the minority members were not loans to Nord Northwest

Corporation, and the Board's findings of fact to the contrary are not supported by any evidence.⁷

Finding of fact number 7 is not supported by substantial evidence when viewed in light of the record as a whole. RCW 34.05.570(3)(e). Moreover, since this erroneous finding was central to the Board's analysis of the "attributes of ownership," this error establishes that the Board "erroneously . . . applied the law." RCW 34.05.570(3)(d). As a result, the Court should reject the Board's conclusion that Nord Northwest Corporation met the "attributes of ownership" under Rule 170(2)(a).

E. The Board Of Tax Appeals Erred In Refusing To Consider Rule 170(2)(f).

In its final decision, the Board of Tax Appeals concluded that "[i]n light of WAC 458-20-170(2)(a), WAC 458-20-170(f) does not apply to the facts of this case." AR at 24 (conclusion of law no. 7). The rule the Board refused to consider or apply, Rule 170(2)(f), states:

(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-ventures, etc., are contracting upon land owned by others and are taxable as sellers under this rule, not as "speculative builders."

WAC 458-20-170(2)(f).

⁷ As noted above at page 12, the Board's "loan" theory was critical in its analysis of the "attributes of ownership." The Board specifically referred to these "loans" from the minority LLC members in findings of fact number 7, 8, 10, 11, 12, 13, and 28, and implicitly relied on these "loans" as support for findings of fact number 4 and 20.

In this case, Nord Northwest Corporation was a member of two limited liability companies and performed construction services upon real property owned by those LLCs. Under Rule 170(2)(f), Nord Northwest Corporation is considered a separate person from the LLCs even though Nord Northwest held an ownership interest in both LLCs. The rule is consistent with Washington law, which treats an owner of a business entity as a separate person from the entity itself. *See* RCW 25.15.070(2)(c) (limited liability company is a separate legal entity from its owners); *Simpson Inv. Co. v. Dep't. of Revenue*, 141 Wn.2d 139, 154, 3 P.3d 741 (2000) (“It is well settled that a parent and subsidiary are for legal purposes generally treated as separate entities.”). In short, Rule 170(2)(f) sets out the well-established legal principle that a business entity is a distinct, separate “person” from its owners.

The Board of Tax Appeals did not explain why it held that subsection (2)(f) of Rule 170 did not apply in this case. *See* AR 19 (Board begins its “Analysis” with the subheading “Nord is within Rule 170(2)(a), and not within Rule 170(2)(f),” but provides no explanation supporting its conclusion.). Regardless of the Board’s unstated reasoning, subsection (2)(f) of Rule 170 is on point and is not trumped or countermanded by subsection (2)(a). Moreover, it is well-established that an administrative rule such as Rule 170 should be read and construed as a whole, not

piecemeal. *Cannon v. Dep't of Licensing*, 147 Wn.2d 41, 57, 50 P.3d 627 (2002). For the Board to conclude, without explanation, that Rule 170(2)(a) applied in this case and therefore Rule 170(2)(f) did not is an erroneous interpretation and application of the Rule and of well-established rules of construction.

Finally, Rule 170(2)(f), when coupled with the undisputed fact that the real property at issue was owned by the two LLCs, clearly contradicts the Board's conclusion that Nord Northwest Corporation qualified as a speculative builder. The Board's refusal to consider Rule 170(2)(f) and to recognize that Nord Northwest Corporation was a separate and distinct "person" from the two LLCs is an error of law requiring reversal of the Board's decision. RCW 34.05.570(3)(d).

F. The Board Of Tax Appeals Erred By Misapplying The Common Law Resulting Trust Doctrine.

The Board of Tax Appeals also ruled that Nord Northwest Corporation was a speculative builder because, according to the Board, the corporation held the beneficial ownership interest in both the Stanwood real property and the Bellingham real property under the common law "resulting trust" doctrine. AR at 20-21. The Board's conclusion is not supported by the evidence and misapplies the law pertaining to resulting trusts and speculative builders.

1. The undisputed facts in the agency record refute the Board's conclusion that Nord Northwest Corporation proved the existence of a resulting trust.

Generally stated, a trust is “[a] fiduciary relationship regarding property and charging the person with title to the property with equitable duties to deal with it for another’s benefit.” Black’s Law Dictionary 1546 (8th ed. 2004). In certain situations where no express trust has been created, a court utilizing its equitable powers may impose a “resulting trust.” See *Manning v. Mount St. Michael’s Seminary*, 78 Wn.2d 542, 545, 477 P.2d 635 (1970) (listing situations where a resulting trust may arise). An essential element of a resulting trust “is that there be an intent that the beneficial interest in property not go with the legal title.” *Engel v. Breske*, 37 Wn. App. 526, 529, 681 P.2d 263 (1984). The party attempting to impose a resulting trust has the burden of proving its existence by clear, cogent, and convincing evidence. *Id.* at 530 (citing *In re Estate of Spandoni*, 71 Wn.2d 820, 823, 430 P.2d 965 (1967)). “This burden is not met if the evidence points to some other hypothesis or does not unmistakably point to the existence of the claimed trust.” *Id.* at 530-31. Evidence is clear, cogent, and convincing if it shows that the ultimate fact in issue is highly probable. *In re Estate of Watlack*, 88 Wn. App. 603, 610, 945 P.2d 1154 (1997).

One circumstance where a resulting trust may arise is “[w]here property is purchased and the purchase price is paid by one person and at his direction the vendor transfers the property to another person.” *Manning*, 78 Wn.2d at 545 (citing Restatement (Second) of Trusts, §§ 440-460 (1959)). Thus, where property is purchased by one person but titled in the name of another, the person with legal title is presumed to hold it in trust subject to the equitable ownership of the purchaser, absent evidence of contrary intent. *In re Estate of Spandoni*, 71 Wn.2d 820, 822, 430 P.2d 965 (1967).

However, a resulting trust is not created where the “transfer of property is made to one person and the purchase price is advanced by another as a loan to the transferee.” Restatement (Second) of Trusts, § 441 comment c (1959). *See also* Restatement (Second) of Trusts, § 445 (1959) (“Where a transfer of property is made to one person and the purchase price is advanced by another as a loan to the transferee, no resulting trust arises.”); *Thompson v. Hunstad*, 53 Wn.2d 87, 89, 330 P.2d 1007 (1958) (“where the purchase price is advanced by one person as a loan to another, no resulting trust arises.”). “For a resulting trust to exist, the would-be beneficiary must have paid the purchase money as his or her own, and not as a loan to the title holder.” 76 AM. JUR. 2D *Trusts* § 157 (2005).

To establish a resulting trust, Nord Northwest Corporation was required to prove by clear, cogent, and convincing evidence that it paid for the Stanwood and Bellingham properties outright and directed that title be transferred to the LLCs without any right to future repayment. Nord has not met that burden. Rather, the undisputed evidence shows that the two LLCs acquired the real property with money advanced by Nord Northwest Corporation as a loan. Tr. at 192-94, 208. As expressly held by the Washington Supreme Court in *Thompson v. Hunstad*, no resulting trust arises where—as here—the purchase price is advanced as a loan by another. *Thompson*, 53 Wn.2d at 89.

The Board’s imposition of a resulting trust when the agency record clearly shows that Nord Northwest Corporation advance the purchase price of the properties as a loan to the LLCs is incorrect as a matter of law and should be reversed. RCW 34.05.570(3).

2. Regardless of whether a resulting trust existed, Nord Northwest Corporation was performing construction services upon real property “of or for a consumer” and cannot qualify as a speculative builder.

RCW 82.04.050(2)(b) provides that the term “‘retail sale’ shall include . . . [t]he constructing, repairing, decorating, or improving of new or existing buildings or other structures under, upon or above real property of or for consumers” Pursuant to this statute, construction services

are normally taxable as a retail sale. The tax advantage enjoyed by a speculative builder is an exception to the general rule. Nord Northwest Corporation is trying to fit within this exception.

In determining whether construction services are retail sales, it is important to recognize that a “consumer” includes “[a]ny person who is an owner, lessee or has the right of possession to or an easement in real property which is being constructed, repaired, decorated, improved, or otherwise altered by a person engaged in business.” RCW 82.04.190(4). The Legislature did not limit the definition of “consumer” only to a person holding fee simple ownership in real property. For example, a person holding a leasehold or other possessory interest in real property also qualifies as a “consumer” of construction services. Otherwise, a lessee that hired a contractor to repair or improve its leased property would not be a “consumer” of the construction services.

Under a resulting trust, where ownership is divided into its legal interest and its beneficial interest, the person holding the legal interest in the real property retains the right of possession, albeit in trust for the beneficial owner. *See* Restatement (Second) of Trusts, § 2 comment f (1959) (describing the distinction between legal interest and equitable interest). The person holding the legal interest in real property—with the

corresponding right of possession—is a “consumer” under the plain language of RCW 82.04.190(4).

Not only did the LLCs have the right of possession of the real property during the construction of the condominiums, but they clearly exercised that right by transferring the finished condominium units to buyers. *See* AR at 712-17 (example “Condominium Purchase and Sale Agreements” listing Stanwood Condominiums LLC as the seller of the condominium units); AR at 718 (example statutory warranty deed listing Stanwood Condominiums LLC as “Grantor”); AR at 855-61 (example “Condominium Purchase and Sale Agreements” listing Bellingham Condominiums LLC as the seller of the condominium units); AR at 862 (example statutory warranty deed listing Bellingham Condominiums LLC as “Grantor”). Selling the finished condominium units is certainly an act of possession. Thus, even if the LLCs were selling the finished condominium units as “trustees” of resulting trusts,⁸ they most certainly had “the right of possession to . . . real property which is being constructed, repaired, decorated, improved, or otherwise altered by a

⁸ There is no evidence in the agency record to suggest that the LLCs were selling the condominium units as “trustees” of a resulting trust, or that the condominium buyers received anything other than fee simple interest in the units. The Board of Tax Appeals does not address whether its imposition of a resulting trust has clouded title to the condominium units that were sold by the LLCs.

person engaged in business.” Therefore, they were consumers of the construction services performed by Nord Northwest Corporation.

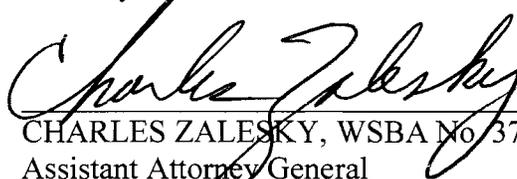
Because Nord Northwest was performing construction services on real property “of or for consumers,” it does not qualify as a speculative builder. This is so even if the two LLCs held only a possessory interest—as opposed to a fee simple interest—in the real property under the common law resulting trust doctrine. Consequently, the Board of Tax Appeals misapplied the law in concluding that Nord Northwest was a speculative builder under the common law resulting trust doctrine. The Board’s erroneous ruling should be reversed.

VI. CONCLUSION

Nord Northwest Corporation did not qualify as a speculative builder with respect to the two constructions projects at issue. The Board of Tax Appeals' decision to the contrary is incorrect as a matter of law and is not supported by the evidence. Accordingly, this Court should reverse the decision of the Board of Tax Appeals.

RESPECTFULLY SUBMITTED this 17th day of September, 2010.

ROBERT M. MCKENNA
Attorney General



CHARLES ZALESKY, WSBA No 37777
Assistant Attorney General
Attorneys for Appellant

WAC 458-20-170

Constructing and repairing of new or existing buildings or other structures upon real property.

(1) **Definitions.** As used herein:

(a) The term "prime contractor" means a person engaged in the business of performing for consumers, the constructing, repairing, decorating or improving of new or existing buildings or other structures under, upon or above real property, either for the entire work or for a specific portion thereof. The term includes persons who rent or lease equipment to property owners for use in respect to constructing, repairing, etc., buildings or structures upon such property, when the equipment is operated by the lessor.

(b) The word "subcontractor" means a person engaged in the business of performing a similar service for persons other than consumers, either for the entire work or for a specific portion thereof. The term includes persons who rent or lease equipment to prime contractors or subcontractors for use in respect to constructing, repairing, etc., when such equipment is operated by the lessor. When equipment or other tangible personal property is rented without an operator to contractors, subcontractors or others, the transaction is a sale at retail (see RCW 82.04.040 and 82.04.050).

(c) The terms "prime contractor" and "subcontractor" include persons performing labor and services in respect to the moving of earth or clearing of land, cleaning, fumigating, razing, or moving of existing buildings or structures even though such services may not be done in connection with a contract involving the constructing, repairing, or altering of a new or existing building or structure. The terms also include persons constructing streets, roads, highways, etc., owned by the state of Washington.

(d) The term "buildings or other structures" means everything artificially built up or composed of parts joined together in some definite manner and attached to real property. It includes not only buildings in the general and ordinary sense, but also tanks, fences, conduits, culverts, railroad tracks, tunnels, overhead and underground transmission systems, monuments, retaining walls, piling and privately owned bridges, trestles, parking lots, and pavements for foot or vehicular traffic, etc.

(e) The term "constructing, repairing, decorating or improving of new or existing buildings or other structures," in addition to its ordinary meaning, includes: The installing or attaching of any article of tangible personal property in or to real property, whether or not such personal property becomes a part of the realty by virtue of installation; the clearing of land and the moving of earth; and the construction of streets, roads, highways, etc., owned by the state of Washington. The term 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. Hence, for example, such service charges as engineering fees, architectural fees or supervisory fees are within the term when the services are included within a contract for the construction of a building or structure. The fact that the charge for such services may be shown separately in bid, contract or specifications does not establish the charge as a separate item in computing tax liability.

(2) **Speculative builders.**

(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.

(b) Where an owner of real estate sells it to a builder who constructs, repairs, decorates, or improves new or existing buildings or other structures thereon, and the builder thereafter resells the improved property back to the owner, the builder will not be considered a speculative builder. In such a case that portion of the resale attributable to the construction, repairs, decorations, or improvements by the builder, shall not be considered a sale of real estate and shall be fully subject to retailing business and occupation tax and retail sales tax. It is intended by this provision to prevent the avoidance of tax liability on construction labor and services by utilizing the mechanism of real property transfers. (RCW 82.04.050 (2)(c).)

(c) Amounts derived from the sale of real estate are exempt from the business and occupation tax. (RCW 82.04.390.) Consequently, the proceeds of sales by legitimate speculative builders of completed buildings are not subject to such tax. Neither does the sales tax apply to such sales, since such a sale involves no charge made for construction for a consumer, but the price paid is for the sale of real estate.

(d) However, when a speculative builder sells or contracts to sell property upon which he is presently constructing a building, all construction done subsequent to the date of such sale or contract constitutes a retail sale and that portion of the sales price allocable to construction done after the agreement shall be taxed accordingly. Consequently, the builder must pay business and occupation tax under the retailing classification on that part of the sales price attributable to construction done subsequent to the agreement, and shall also collect sales tax from the buyer on such allocable part of the sales price.

(e) Speculative builders must pay sales tax upon all materials purchased by them and on all charges made by their subcontractors. Deductions for such tax paid with respect to materials used or charges made for that part of the construction

APPENDIX A

done after the contract to sell the building should be claimed by the speculative builder on his tax returns in accordance with WAC 458-20-102, under the subheading PURCHASES FOR DUAL PURPOSES.

(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."

(3) Business and occupation tax.

(a) Prime contractors are taxable under the retailing classification, and subcontractors under the wholesaling classification upon the gross contract price.

(b) Where no gross contract price is stated in any contract or agreement between the builder and the property owner, then the measure of business and occupation tax is the total amount of construction costs, including any charges for licenses, fees, permits, etc., required for the construction and paid by the builder.

(4) Retail sales tax.

(a) Prime contractors are required to collect from consumers the retail sales tax measured by the full contract price. Where no gross contract price is stated, the measure of sales tax is the total amount of construction costs including any charges for licenses, fees, permits, etc., required for construction and paid by the builder.

(b) The retail sales tax does not apply to charges made for janitorial services nor for the mere leveling of land used in commercial farming or agriculture. The tax does apply, however, in respect to contracts for cleaning septic tanks or the exterior walls of buildings, as well as to earth moving, land clearing and the razing or moving of structures, whether or not such services are performed as incidents of a contract to construct, repair, decorate, or improve buildings or structures.

(c) Sales to prime contractors and subcontractors of materials such as concrete, tie rods, lumber, finish hardware, etc., which become part of the structure being built or improved are sales for resale and are not subject to the retail sales tax. Sales of form lumber to such contractors are sales for resale provided that such lumber is used or to be used first by such persons for the molding of concrete in a single contract, project or job and the form lumber is thereafter incorporated into the product of that same contract project or job as an ingredient or component thereof. Sales of form lumber not so incorporated as an ingredient or component are sales at retail.

(d) The retail sales tax applies upon sales and rentals to prime contractors and subcontractors of tools, machinery and equipment, and consumable supplies, such as hand and machine tools, cranes, air compressors, bulldozers, lubricating oil, sandpaper and form lumber which are primarily for use by the contractor rather than for resale as a component part of the finished structure.

(e) The retail sales tax applies upon sales to speculative builders of all tangible personal property, including building materials, tools, equipment and consumable supplies and upon sales of labor, services and materials to speculative builders by independent contractors.

(5) Use tax.

The use tax applies generally to the use by prime contractors and subcontractors of tools, machinery, equipment and consumable supplies acquired by them primarily for their own use and upon which the retail sales tax has not been paid. This includes equipment and supplies purchased in a foreign state for use or consumption in performing contracts in this state. The use tax applies generally to the use by speculative builders of all tangible personal property, including building materials, purchased or acquired by them without payment of the retail sales tax (see also WAC 458-20-178).

[Statutory Authority: RCW 82.32.300, 87-19-007 (Order ET 87-5), § 458-20-170, filed 9/8/87; 83-07-033 (Order ET 83-16), § 458-20-170, filed 3/15/83; Order ET 71-1, § 458-20-170, filed 7/22/71; Order ET 70-3, § 458-20-170 (Rule 170), filed 5/29/70, effective 7/1/70.]

-FILED
COURT OF APPEALS
DIVISION II

10 SEP 20 AM 9:02

NO. 40601-2-II STATE OF WASHINGTON

COURT OF APPEALS FOR ~~DIVISION II~~
STATE OF WASHINGTON DEPUTY

STATE OF WASHINGTON
DEPARTMENT OF REVENUE,

Appellant,

v.

NORD NORTHWEST
CORPORATION,

Respondents.

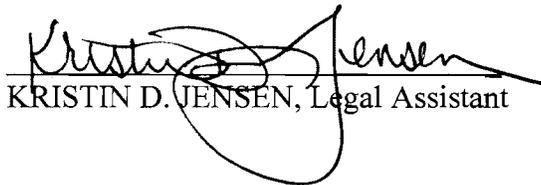
CERTIFICATE OF
SERVICE

I certify that on September 17, 2010, I served a true and correct copy of the Brief of Appellant, via U.S. Mail, postage prepaid, through Consolidated Mail Services, on the following:

Martin D. Meyer, Esq.
U.S. Bank Building, Suite 12
402 South Capital Way
Olympia, WA 98501

I certify under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED this 17th day of September, 2010, at Tumwater, WA.


KRISTIN D. JENSEN, Legal Assistant

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