COURT OF APPEALS
DIVISION II
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STATE OF WASHINGTON
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No. 40601-2-II

COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON

STATE OF WASHINGTON DEPARTMENT OF REVENUE,

Appellant,

v.

NORD NORTHWEST CORPORATION,

Respondent.

BRIEF OF RESPONDENT

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I. BACKGROUND

This case stems from the construction of 2 condominium projects by Nord Northwest Corporation (NNC) in 1998 and 1999. One was 30 unit project located in Bellingham WA and one was a 55 unit project located in Stanwood, WA. Tr. At 22.

In 2002, Peg Power, a revenue auditor with the Department of Revenue audited NNC's two projects from January, 1998 through February of 2002. Tr. at 186. As a result of her audit, she concluded that NNC was not a "speculative builder" as that term is defined at WAC 458-20-170(2) and levied an assessment in the amount of $352,270.00 in unpaid B&O taxes that NNC should have paid as a "custom builder." AR 486-514.

NNC initiated a petition for review which was held October 26, 2004 before ALJ Randolph E. Okimoto who issued his decision on September 2005 denying NNC's petition. AR 515-525. NNC initiated a request for executive level reconsideration which was denied April 30, 2008. AR 529-

545.

NNC appealed to the Board of Tax Appeals (BTA). A hearing was held December 16, 2008 in which testimony was taken from witnesses, NNC submitted 23 Exhibits (AR 252-413) into evidence and the Department of Revenue submitted 38 Exhibits (AR 481-883) into evidence. Tr. at 2. The BTA issued its opinion in favor of NNC on March 5, 2009. AR 9-26.

The Department of Revenue then filed a Petition for Review in Thurston County Superior Court. CP 10-54. Following a review of the administrative record and oral argument to the Court, the Honorable Carol Murphy issued a letter opinion reversing the Board of Tax Appeals by concluding that NNC did not own the properties in question and that the "attributes of ownership" analysis under WAC 458-20-170(2)(a) did not apply. CP 55-57. Subsequently, an Order Reversing Agency Decision was entered March 26, 2010 from which this appeal was taken. CP 64-70.

II. STANDARD OF REVIEW

The burden of demonstrating the invalidity of agency action is on the party asserting invalidity. RCW 34.05.570(1)(a). When reviewing an administrative decision, the appellate court stands in the same position as the superior court and applies the appropriate standard of review directly to the administrative record. Wilson v. Employment Sec. Dept., 87 Wn. App. 197, 200, 940 P.2d 269 (1997).

As to factual issues, relief from the agency order can only be granted if the order is not supported by substantial evidence when viewed in the light of the whole record before the court. Hamel v. Employment Sec. Dept., 93 Wn. App. 140, 144, 966 P.2d 1282 (1998) *citing* RCW 34.05.570(3)(e). "Substantial evidence is 'evidence in sufficient quantum to persuade a fair-minded person of the truth of the declared premises.'" Hamel at p.144 *citing* Heinmiller v. Department of Health, 127 Wn.2d 595, 607, 903 P.2d 433, 909 P.2d 1294 (1995)

As to errors of law, the appellate court may substitute its judgment for the administrative agency; however substantial weight is accorded to the agency's interpretation of a statute or rule promulgated by that agency. Verizon NW., Inc. v. Employment Sec., 164 Wn.2d 909, 915, 194 P.3d 255 (2008). RCW 34.05.570(3)(d).

III. ISSUE PRESENTED

WHETHER OR NOT THE RECORD IS SUPPORTED BY SUBSTANTIAL EVIDENCE THAT NORD NORTHWEST CORPORATION WAS A "SPECULATIVE BUILDER" AS THAT TERM IS DEFINED AT WAC 458-20-170-(2)(A) DURING THE CONSTRUCTION OF THE BELLINGHAM AND STANWOOD CONDOMINIUM PROJECTS.

IV. ARGUMENT

After a thorough review of the evidence heard and the exhibits submitted, the Board of Tax Appeals issued an exhaustive FINAL DECISION concluding Nord Northwest

was a "speculative builder" and the land in question was owned by Nord Northwest as the beneficiary of a resulting trust. AR 9-26. Furthermore, the BTA found each of Nord's witnesses very credible at Finding of Fact No. 29. AR 24. At the BTA, NNC proved with "clear, cogent, and convincing evidence" that NNC held all the non-exclusive attributes of ownership in both projects. Conclusion of Law No. 8. AR 25.

The Washington Administrative Code defines the term "speculative builder" as follows:

> 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. WAC 458-20-170(2)(a).

The Department of Revenue wants this court to interpret the facts of this case as if the second sentence of this WAC did

not exist. In fact, that's where the Superior Court's analysis began and ended after concluding Nord Northwest Corporation did not own or have bare legal title to the land. CP 55-70.

In 2002, the Department of Revenue issued a 60 page Construction Tax Guide. AR 570-630. The very first sentence of the guide states that it was "created to assist people engaged in construction activities to better understand the Washington State taxes that apply to their businesses." AR 571. At page 21 of the guide there is a section devoted to speculative building. AR 590. "Speculative builders construct residential or commercial building on land they own (or on real estate for which they are a lessee, or have the right of possession). AR 590.

In reference to Land Ownership, the guide states:

> The owner of real property is generally the holder of the recorded title. However, it is possible for a person to hold title to real property which he/she does not own. Therefore, attributes of ownership, other than mere title to the property, may determine the tax application. AR 590.

The guide then sets forth the four criteria of WAC-458-20-

170 identified as the "attributes of ownership" followed by the following sentence: "The attributes of ownership establish who has the rights and liabilities of a property owner." AR 590

A review of the record reveals there is no question that Nord Northwest Corporation exercised all attributes of ownership as it related to both properties.

1) The intentions of the parties in the transaction under which the land was acquired.

Respondent Nord Northwest Corporation (NNC) was a general contracting firm operated principally by Richard G. Nord, Sr. Tr. At 93. In 1998, NNC sought financing to fund two construction projects, a 55 unit condominium project in Stanwood, WA and a 55 unit project in Bellingham that would be built and marketed to potential buyers. Tr. At 22-23.

After seeking financing from a bank, NNC learned that NNC could not obtain financing because NNC did not have a minimum required equity interest in the two properties. Tr. At

120. Nonetheless, NNC could see a market for the 2 projects and wanted to proceed. Tr. At 23.

NNC needed additional equity funding in order to secure loans from banks to proceed with construction of the projects. Tr at 120-128. Ron Hoelscher, NNC's Chief Financial Officer and CPA, devised a plan whereby investors could be provided security for their loans and not mix their activities with other activities of NNC. Tr at 21-55. "So we felt that the LLC's were just a financing vehicle to get the equity required so that we could get financing from the lending institutions." Tr at 24.

There were never any meetings of the LLC's, ever. Tr at 25. NNC was the sole decision maker and never lost control of the property. Tr. at 25. Ron Hoelscher was also one of the investors in both LLC's. Tr at 25. There was no way NNC was going to give up control of the property. Tr at 37-38.

There is no question that at the outset of these projects, NNC and Ron Hoelscher were aware of the existence of WAC 458-20-170 and the importance of owning the land, or in the

alternative, have the attributes of ownership in order to qualify as a "speculative builder." Tr. At 93-96.

Bellingham Property.

Initially, this property was purchased by Nord Northwest Corporation and later Quit Claimed by NNC to the Bellingham Condominiums, LLC AR 340-343. It is interesting to note here that NNC paid no excise tax on this transfer as it was a "mere change in identity" under the then WAC 458-61-375 for such exceptions. AR 343. Tr. At 109.

Stanwood Property.

Initially, this property was also purchased by Nord Northwest Corporation on 2/8/99. AR 332. However, when the sale closed, at the direction of NNC, title was conveyed to the Stanwood Condominiums LLC on 6/7/99. AR 336 Tr. at 95.

2) The person who paid for the land.

It is undisputed that NNC paid for the land in both projects. AR 332. AR 340-341. Tr. at 95.

3) The person who paid for improvements to the land.

Clearly it was NNC that provided the impetus for the banks to finance these projects. AR 401, 403 & 405. Tr. at 166-168. "The primary guarantee and strength of our loan was NNC. Horizon Bank would not have made this loan had they not been convinced that NNC had the majority rights and control to develop this project" AR 401. "Peoples Bank looked to Nord Northwest and its president, Richard G. Nord, Sr. to oversee the land, land development, construction and ultimate sale of this project to the general public and would not have made loans to Stanwood Condominiums, LLC were it not for the project experience and the guaranties of Nord Northwest and Richard G. Nord, Sr." AR 403

Pacific Northwest Bank loaned money on both projects solely on the strength of NNC with the stated purpose for NNC to build and sell speculative condominiums with the understanding that NNC "controlled and was responsible for the land as if they were the title holders...." AR 405

The investors in the LLCs provided the initial capital investment in order for NNC to obtain the financing from the

banks. Tr. at 129-131. NNC received two lines of loans; one from the bank and one from the investors. Tr. at 131. The LLCs were a financing vehicle in order for NNC to qualify for the bank loan. Tr. at 24.

The "investors" were only exposed to the extent of the money each provided. Tr. at 32 & 127-128. NNC bore the risk of loss on these projects and in fact, NNC bore an $18,766 loss on the Bellingham project. Tr. at 70 AR 394. The Bellingham investors were paid back their initial capital contributions plus 10% interest. Tr. at 71. AR 394. All of the assets and liabilities of the LLCs were included in NNC's consolidated financial statements. AR 392-395.

4. The manner in which all parties, including financiers, dealt with the land.

The record is overwhelming that it was NNC that controlled every aspect of these projects including the land and that was all the parties' intent at the outset. As previously stated above, the banks viewed NNC as being in complete control of the entire

projects, including the land. AR 401, 403 & 405.

NNC believed it retained complete control of the land and would not have transferred title to the land if it felt if it were giving up control. Tr. at 37-38. NNC paid the insurance and was the named insured on both projects. AR 390.

NNC marketed the property to the public for sale. Tr. at 24, 126, & 146. NNC found the properties, arranged for financing, arranged for the equity in order to secure the financing, designed the projects, built the projects, marketed the projects and finished them. Tr. at 24.

NNC provided the warranties for the projects. Tr. at 146-147. NNC even provided warranties that exceeded the time required by law. Tr. at 147. AR 883.

The LLC's were set up for NNC to retain control of the land and the project in general. AR 279-328. The members of the LLC never met, never held meetings never made decisions and had no input on the projects. Tr. at 25, 27, & 129. NNC was building condominiums for NNC that were going to be offered to the

general public. Tr. at 28.

It would constitute a double taxation against NNC for this assessment to stand. The Washington State excise tax was paid on the full market value of each unit as it was sold to the public.

V. RESULTING TRUST

There was absolutely no intent by NNC that either LLC would take beneficial interest in the ownership of the land when the properties were transferred into the LLC's Tr. P.23-25, 37, and 93-97. NNC retained 60 percent interest in the LLC's and thus retained control of the land. AR 301-302 & 327-328

A resulting trust arises where a person makes or causes to be made a disposition of property under circumstances which raise an inference that he does not intend that the person taking or holding the property should have the beneficial interest therein, unless the inference is rebutted or the beneficial interest is otherwise effectively disposed of. See Manning v. Mount St. Michaels, 78 Wn.2d 542, 544 477 P.2d 635 (1970). There was no way these properties would have ever been transferred to the LLC's had NNC

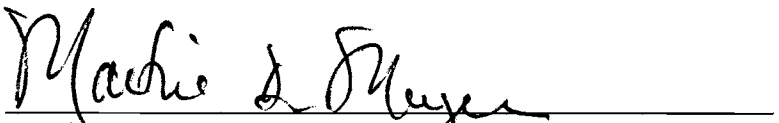
not retained control of every aspect of the projects in question.

VI. CONCLUSION

The evidence is overwhelming in this case that it was NNC that exercised all the attributes of ownership with respect to both the Stanwood and Bellingham properties. In light of the record as a whole and all the remaining unchallenged findings and conclusions, the BTA did not err in concluding NNC was a "speculative" builder as that term has been defined and interpreted by the Department of Revenue as applied to the two projects that gave rise to this case.

NNC respectfully submits that this Court should affirm in all respects, the Final Decision of the BTA issued March 5, 2009 herein.

RESPECTFULLY SUMITTED this 3rd day of December, 2010.



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COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON

STATE OF WASHINGTON DEPARTMENT OF REVENUE, Appellant, vs. NORD NORTHWEST CORPORATION, Respondent..	**DECLARATION OF SERVICE**

Martin D. Meyer, upon oath, deposes and says: I am the attorney for Nord Northwest Corporation, Respondent herein. On December 3, 2010 I personally served a copy of Respondent's Brief and this Declaration of Service to Charles Zalesky, Attorney for Appellant by delivering a copy to his office at 7141 Cleanwater Lane SW, Tumwater WA and that I filed the original of the same in the Clerk's Office of the Court of Appeals, Division II, 950 Broadway, Suite 300, Tacoma, WA on December 3, 2010.

I declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct. Signed at Olympia, WA this 3rd day of December, 2010

Martin D. Meyer

Martin D. Meyer