
Opinion of the Tax Commissioner

Date Issued: July 11, 2008

Opinion No: 08-0007

Tax: Commercial Activity

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Subject: Agent

This request for an Opinion of the Tax Commissioner was received on April 10, 2008. The request concerns whether the construction management agreement (“Agreement”) between XXXX (“General Contractor”) and XXXX (“Property Owner”) establishes an “agent” relationship as defined in R.C. 5751.01(P) and O.A.C. 5703-29-13 for purposes of the commercial activity tax (“CAT”).

TAXPAYER STATEMENT OF THE FACTS

Property Owner proposes to construct a new health & technology campus for XXXX. In addition to the main building, several other buildings will be constructed and will be built and coordinated by a developer.

Property Owner proposes to enter into Agreement with General Contractor. Pursuant to Agreement, General Contractor will be responsible for overseeing all aspects of the construction of the facility.

General Contractor’s relationship with Property Owner under Agreement is provided in Article 3 of Agreement and in the general conditions of the contract for construction (“General Conditions”) attached to Agreement. Article 3 of Agreement and General Conditions establishes an anticipated relationship of trust and confidence between General Contractor and Property Owner. Also, Article 2 of General Conditions establishes the extent of control that is retained and exercised by Property Owner in all aspects of the work to be performed. General Contractor will be reimbursed for all “contract sums” as defined in Section 5.1.1 of Agreement and will be entitled to a fee as set forth in section 5.1.2 of Agreement. Under Article 5 of Agreement, Property Owner requires that General Contractor provide a guaranteed maximum price (“GMP”) that includes all costs of work and the agreed fee.

With respect to the financial aspects of Agreement, General Contractor is required to act in the best interests of Property Owner. Under Article 3 of Agreement and General Conditions, General Contractor agrees to use its best efforts “in the most expeditious and economical manner consistent with the best interests” of Property Owner.

There is no provision in Agreement or General Conditions that provides that all subcontracts between General Contractor and any subcontractors contain language that General Contractor is acting as the agent of Property Owner, and not as an agent of the subcontractors. Such language has not been included in any of the subcontracts executed pursuant to Agreement. However, under Section 9.6.2 of General Conditions, with respect to payment of subcontractors, General Contractor acts as a conduit for all payments by Property Owner to the subcontractors as provided within Agreement.

QUESTIONS PRESENTED BY TAXPAYER

1. Whether General Contractor, with respect to the payments received from Property Owner to be passed on to subcontractors, is acting as an “agent” as defined in R.C. 5751.01(P) for purposes of R.C. 5751.01(F)(2)(l) and O.A.C. 5703-29-13?
2. Whether General Contractor may exclude from its gross receipts under R.C. 5751.01(F)(2)(l), payments from Property Owner in excess of the fee that General Contractor is required to pay over to subcontractors pursuant to Agreement?

ANALYSIS

The CAT is levied on gross receipts that are situated to Ohio (*i.e.*, “taxable gross receipts”). R.C. 5751.02. The term “gross receipts” is broadly defined in R.C. 5751.01(F) as “the total amount realized by a person, without deduction for the cost of goods sold or other expenses incurred, that contributes to the production of gross income of the person, including the fair market value of any property and any services received, and any debt transferred or forgiven as consideration.” “Gross receipts” excludes money and other amounts received or acquired by an agent on behalf of another in excess of that agent’s commission, fee, or other remuneration. R.C. 5751.01(F)(2)(l). An “agent” is a person authorized by another person to act on its behalf to undertake a transaction for the other. R.C. 5751.01(P).

The Tax Commissioner issued Information Release CAT 2006-03, Commercial Activity Tax Definition of “Agent” - Issued April 2006; Revised July 2006; Revised October 2006; Revised November 2007; Revised April 2008, and adopted a rule, O.A.C. 5703-29-13, to address that provision. Divisions (C)(2)(b) and (C)(2)(c) of the rule specifically addresses the provision in the context of a construction contract. In division (C)(2)(b), the rule explains that no agency relationship exists because the general contractor is not required to act in the best interests of the owner. However, division (C)(2)(c) provides that an agency relationship will be found where the following factors are present:

- (i) The general contractor is required to act in the owner’s best interest;

- (ii) The general contractor, when bidding out the work, has an agreement in writing with the subcontractors that states that the general contractor is acting as the owner's agent and not as an agent of the subcontractors; and
- (iii) The general contractor acts as a conduit with respect to payments made to the subcontractors under the agreement.

Where those conditions are met, the rule provides that the payments the general contractor receives and pays over to the subcontractors may be excluded from the general contractor's gross receipts. However, the fee that the general contractor retains is included in its calculation of gross receipts.

Best Interest of Property Owner

In this case, Article 3 of Agreement and General Conditions provides that General Contractor has an obligation to act in the best interests of Property Owner. In addition, Property Owner retains authority over cost and related issues. For example, under Article 10 of Agreement, General Contractor must obtain bids from subcontractors and from suppliers of materials or equipment fabricated especially for the project and the Property Owner shall then determine which bids are accepted (Section 10.1 of Agreement). Under Article 7 of Agreement, Property Owner determines the acceptance of bids for the rental charges for temporary facilities, machinery, equipment or hand tools not customarily owned by construction workers that are provided (Section 7.5.2 of Agreement). Also, Property Owner determines if it is appropriate under the circumstances to rent or purchase such machinery or equipment (Section 7.5.2 of Agreement) and, if purchased, such machinery or equipment is Property Owner's property (Section 7.5.1 of Agreement). General Contractor must maintain cost accounting records accessible to Property Owner in such form and detail acceptable to Property Owner (Section 11.1 of Agreement). Moreover, Property Owner must approve all change orders (Section 6.2 of Agreement). Finally, under Section 5.2.1.3 of Agreement, savings in the cost of work must be passed on to Property Owner. Based on the facts provided, it appears that Agreement satisfies the first prong of the test.

Agreement Reflecting Property Owner's Best Interests

No provision in Agreement or General Conditions provides that all subcontracts between General Contractor and any subcontractors contain language that General Contractor is acting as the agent of Property Owner, and not as an agent of the subcontractors. However, the Tax Commissioner will look beyond the wording of the contract to the actual facts and circumstances of the situation to determine whether an agency relationship actually exists. O.A.C. 5703-29-13(B)(2). Taking into consideration the all aspects of Agreement and General Conditions, an inference can be made that General Contractor is acting as the agent of Property Owner, and not as an agent of the subcontractors. Specifically, General Contractor shall not obtain for its own benefit any discounts, rebates or refunds in connection with the work prior to notification of Property Owner so that Property Owner may take advantage of such discount, rebate or refund (Section 9.1 of Agreement). Moreover, the parties' relationship established in Article 3 of

Agreement and General Conditions provides that General Contractor has an obligation to act in the best interests of Property Owner. Thus, the second prong of the test appears to be satisfied.

Conduit for Payments

Finally, Section 9.6.2 of General Conditions provides that General Contractor shall act as a conduit for all payments to the subcontractors. General Contractor shall make all such payments promptly to the subcontractor, upon receipt of payment from the Property Owner. The payments General Contractor receives on behalf of the subcontractors are not paid to General Contractor. Instead, General Contractor is required to pass those payments on promptly to the subcontractors on behalf of Property Owner. The payments are excluded from General Contractor's gross receipts for CAT purposes pursuant to R.C. 5751.01(F)(2)(I).

If the parties conduct their affairs in a manner that is consistent with Agreement and General Conditions, General Contractor appears to qualify as an agent under R.C. 5751.01(P) and O.A.C. 5703-29-13, and the payments it receives to be passed on to subcontractors are excluded from its gross receipts under R.C. 5751.01(F)(2)(I).

ANSWER

With respect to the payments received from Property Owner to be passed on to subcontractors, General Contractor appears to be acting as an "agent" as defined in R.C. 5751.01(P) for purposes of R.C. 5751.01(F)(2)(I) and O.A.C. 5703-27-13. General Contractor may exclude from General Contractor's gross receipts payments from Property Owner that General Contractor is required to pass on to subcontractors pursuant to Agreement. However, pursuant to R.C. 5751.01(F)(2)(I), General Contractor must include in General Contractor's gross receipts any fee General Contractor is entitled to retain.

CLOSING

This Opinion applies only to General Contractor and Property Owner. It may not be transferred or assigned. In addition, the tax consequences stated in this Opinion are subject to change for any of the reasons provided in R.C. 5703.53(C). It is the duty of General Contractor and Property Owner to be aware of such changes pursuant to R.C. 5703.53(E).

Richard A. Levin
Tax Commissioner