

Cite as Det. No. 12-0349, 33 WTD 45 (2014)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of)	<u>D E T E R M I N A T I O N</u>
Assessment of)	
)	No. 12-0349
...)	
)	Registration No. . . .
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[1] RULE 102 and 102A; RCW 82.04.470, RCW 82.08.020: RETAIL SALES TAX – BURDEN OF PROVING WHOLESALE SALES. Where the seller failed to meet its burden of proving that sales were at wholesale, Audit was justified in assessing retail sales tax and retailing B&O tax.

[2] RULE 254; RCW 82.32.070, RCW 82.32.100: RECORDS – MEASURE OF SALES – BANK DEPOSITS. Where the seller failed to provide original source documents or records showing that the measure of sales as determined by bank deposits was incorrect, Audit was justified in using bank deposits to determine the measure of taxes.

[3] RULE 254; RCW 82.08.0273, RCW 82.32.070: RETAIL SALES TAX – NONRESIDENT EXEMPTION – RECORDS. Taxpayers must maintain records required under RCW 82.08.0273 for each nontaxable sale to nonresidents to qualify for that statutory exemption¹.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

Margolis, A.L.J. – An operator of a wrecking yard that sells cars and car parts (Taxpayer) protests the assessment of retail sales tax and business and occupation (B&O) tax on grounds that the measure of taxes and allocation between retail and wholesale sales should be based on its general ledger rather than bank deposits and documentation of wholesale sales. Taxpayer also

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

argues that certain sales are deductible from retail sales because they were made to qualified nonresidents. We deny the petition.²

ISSUES

1. Whether, under RCW 82.32.070 and WAC 458-20-254, the records support an adjustment to the measure and classification of Taxpayer's activities.³
2. Has Taxpayer shown, under RCW 82.08.0273, that some of its sales are exempt from retail sales tax as sales to nonresidents?

FINDINGS OF FACT

Taxpayer operates an auto wrecking yard in . . . Washington, and sells parts and materials harvested from cars. The Department of Revenue's (Department's) Audit Division (Audit) performed a compliance audit for the period January 1, 2007, through September 30, 2010, to determine whether Taxpayer's business activities and transactions were properly reported on excise tax returns. On October 5, 2011, Audit assessed Taxpayer \$. . . , consisting of \$. . . in retail sales tax, \$. . . in retailing B&O tax, \$. . . in credit for wholesaling B&O tax, \$. . . in interest, and \$. . . in a 5% assessment penalty.

Audit used a random sample to verify that wholesale sales were correctly reported during the audit period. Audit discovered that some of Taxpayer's sales should have been reported as retail sales because Taxpayer could not document that they were wholesale sales. Audit determined a percentage error based on sales that were not documented as wholesale sales in the sample, applied that percentage to total net wholesale sales reported, reclassified those sales from wholesaling to retailing, and assessed retail sales tax on those sales.

Audit also compared total bank deposits, adjusted to reflect cash register pay outs, retail sales tax remitted, and transfers from a line of credit, with total amounts of gross income reported to the Department, and determined that Taxpayer had underreported its sales.⁴ Audit allocated the difference between wholesale and retail sales based on the percentage of wholesale and retail sales reported, as adjusted by reclassified sales, and assessed retail sales tax and B&O tax accordingly.

Taxpayer also took deductions for sales of tangible personal property to nonresidents for use outside Washington. Audit used a random sample to verify that these deductions were correctly reported during the audit period. Audit found that the records of each sale only included

² Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

³ At the hearing, Taxpayer suggested that he may qualify for a deduction for tax paid at source as he might have paid retail sales tax when he acquired cars. We asked taxpayer to provide supporting documentation, which is required under RCW 82.08.130, but none was provided. Thus, we will not address this issue.

⁴ Taxpayer's adjusted bank deposits totaled Taxpayer reported \$. . . , comprised of \$. . . in wholesale sales and \$. . . in retail sales.

identification numbers, and sometimes names, which is insufficient to establish that the sales were made to nonresidents. Thus, Audit disallowed all of these deductions.

Taxpayer appeals the assessment, asserting that Audit should have accepted the amounts of wholesale and retail sales from its accrual basis books, including its general ledger, rather than reclassifying some of its sales as retail sales and determining the measure of tax from bank deposits. Taxpayer provides a document titled “Comparison of General Ledger Recorded Sales to Washington Excise Tax Reports” that lists wholesale and retail sales for the audit period, and amounts reported on excise tax returns.⁵ According to this document, in 2007, Taxpayer underreported \$. . . in wholesale sales and over-reported \$. . . in retail sales; in 2008, Taxpayer over-reported \$. . . in wholesale sales and under-reported \$. . . in retail sales; in 2009, Taxpayer over-reported \$. . . in wholesale sales and under-reported . . . in retail sales; and, in 2010, Taxpayer under-reported \$. . . in wholesale sales and \$. . . in retail sales. Total sales per this document are \$. . . , which is \$. . . more than what Taxpayer had reported on excise tax returns and \$. . . less than adjusted bank deposits. Taxpayer’s breakdown between retail and wholesale sales is unsubstantiated.

Taxpayer asserts that most unreported sales were wholesale sales to car crushers that crush cars and sell the metal to recyclers. However, Taxpayer provided no records to establish the measure of these sales, explaining that it did not create invoices and had discarded records.

Taxpayer also asserts that Audit erred in denying deductions for sales to Oregon residents, and explained that when Taxpayer makes sales to Oregon residents, the clerk examines the resident’s drivers’ license, noting the name, address, and expiration date, writes the drivers’ license number on the invoice, and requires the purchaser to sign the invoice. Taxpayer provided 2 sample invoices. Under “Tax Code,” the invoices list “ODL” followed by a 7 digit number, and include signatures on a line designated “Received by.”

ANALYSIS

[1] Washington law imposes retail sales tax on every retail sale in this state. RCW 82.08.020. The definition of “retail sale” excludes “purchases for the purpose of resale as tangible personal property in the regular course of business without intervening use by such person.” RCW 82.04.050(1)(a)(i). Washington also imposes a B&O tax on various tax classifications, including making retail sales under RCW 82.04.250 and wholesale sales under RCW 82.04.270. A “wholesale sale” is defined as “any sale, which is not a sale at retail.” RCW 82.04.060(1).

RCW 82.04.470(1) explains:

⁵ The document is not accurate. For example, it shows that total wholesale sales per excise tax returns for 2008 were \$. . . , but Department records show that Taxpayer reported \$. . . . The \$. . . difference is because Taxpayer’s document states that in October 2008, Taxpayer reported \$[X]. in wholesaling B&O tax, and the Department’s records show that Taxpayer reported \$.[Z] We reviewed an image of the October 2008 return signed by . . . Taxpayer’s President, on November 24, 2008. It lists gross wholesale sales of \$[X].

The burden of proving that a sale is a wholesale sale rather than a retail sale is on the seller. A seller may meet its burden of proving a sale is a wholesale sale rather than a retail sale by taking from the buyer, at the time of sale or within a reasonable time after the sale as provided by rule of the department, a copy of a reseller permit issued to the buyer by the department under RCW 82.32.780 or 82.32.783.

The Washington Legislature amended this statute during the audit period. The current version applies retroactively to January 1, 2010. Laws 2010 c 112 § 7; see note following RCW 82.32.780. The language of RCW 82.04.470(1) in effect prior to January 1, 2010 is similar to the current language. It also placed the burden of proving that the sale is wholesale on the seller. More importantly, RCW 82.04.470(1) allows the seller to meet this burden by providing either a copy of a reseller permit issued to the buyer for periods for periods after January 1, 2010, or a resale certificate for periods prior to that date. *See also* WAC 458-20-102 and 102A.

In this matter, Audit assessed retail sales tax and retailing B&O tax on sales that it could not verify were wholesale sales with resale certificates or reseller permits. The only documentation Taxpayer provides to show that this was incorrect is an inaccurate and unsubstantiated document comparing general ledger figures to amounts reported on excise tax returns. We find this document insufficient to show that Audit's classification of sales was incorrect, and thus sustain the classification.

[2] RCW 82.32.070(1) explains that taxpayers "shall keep and preserve, for a period of five years, suitable records as may be necessary to determine the amount of any tax for which he may be liable" Washington law also imposes the responsibilities on taxpayers to "[k]eep accurate and complete business records" and "[e]nsure the accuracy of the information entered on their tax returns." RCW 82.32A.030(3), (5).

WAC 458-20-254 (Rule 254) implements RCW 82.32.070, and states as follows (in part):

(3) Recordkeeping requirements – General.

(a) Every taxpayer liable for a tax or fee imposed by the laws of the state of Washington for which the department of revenue has primary or secondary administrative responsibility... must keep complete and adequate records from which the department may determine any tax liability for such taxpayer.

(b) It is the duty of each taxpayer to prepare and preserve all records in a systematic manner conforming to accepted accounting methods and procedures. Such records are to be kept, preserved, and presented upon request of the department or its authorized representatives which will demonstrate:

(i) The amounts of gross receipts and sales from all sources, however derived, including barter or exchange transactions, whether or not such receipts or sales are taxable. **These amounts must be supported by original source documents or records including but**

not limited to all purchase invoices, sales invoices, contracts, and such other records as may be necessary to substantiate gross receipts and sales

(Emphasis added.) If any person fails or refuses to make records available for examination, RCW 82.32.100 authorizes the Department to proceed, “in such manner as it may deem best, to obtain facts and information on which to base its estimate of the tax.” Once the Department obtains the facts and information, the Department “shall proceed to determine and assess against such person the tax and any applicable penalties or interest due.” RCW 82.32.100.

In this matter, Taxpayer asserts that its books, rather than bank account deposits, should determine the measure of sales subject to tax. Because sales must be supported by original source documents or records, and Taxpayer has provided no original source documents or records showing that the measure of sales as determined by bank deposits is incorrect, we sustain the measure as determined by Audit.

[3] Taxpayer also challenges Audit’s denial of its claimed exemptions for sales to non residents. RCW 82.08.0273 provides an exemption from the retail sales tax for:

[S]ales to nonresidents of this state of tangible personal property, digital goods, and digital codes, when:

- (a) The property is for use outside this state;
- (b) The purchaser is a bona fide resident of a province or territory of Canada or a state, territory, or possession of the United States, other than the state of Washington; and
- (i) Such state, possession, territory, or province does not impose, or have imposed on its behalf, a generally applicable retail sales tax, use tax, value added tax, gross receipts tax on retailing activities, or similar generally applicable tax, of three percent or more

RCW 82.08.0273(1).

At issue in this case is whether Taxpayer collected sufficient documentation to show that some of its sales were to nonresidents of Washington. RCW 82.08.0273(4)(a) explains, in pertinent part:

If the vendor chooses to make a sale to a nonresident without collecting the sales tax, the vendor must examine the purchaser's proof of nonresidence, determine whether the proof is acceptable under subsection (3)(b) of this section, and maintain records for each nontaxable sale which shall show the type of proof accepted, including any identification numbers where appropriate, and the expiration date, if any.

RCW 82.08.0273(3)(b) provides what documentation an out of state purchaser must provide to prove the person’s nonresident status. Basically, the purchaser would need to provide an

identification card from his/her jurisdiction, such as an out of state driver's license, which shows the person's out-of-state address, along with a photograph of the person.

Therefore, to properly document sales to nonresidents, Taxpayer must examine the purchaser's out-of-state identification to determine if it is acceptable and maintain records that show: (1) the type of proof of out-of-state residency accepted, (2) the identification number of that proof, and (3) its expiration date. Taxpayer must maintain such records "for each nontaxable sale." RCW 82.08.0273(4)(a).

In this case, Taxpayer did not maintain records that showed expiration dates. Taxpayer asserts that the expiration date requirement is permissive, and disallowance is too high a penalty. However, the statute requires taxpayers to maintain records that show the purchaser's out of state residence, along with any identification numbers *and expiration dates*. RCW 82.08.0273(6)(a) explains that "[a]ny vendor who makes sales without collecting the tax and who fails to maintain records of sales to nonresidents *as provided in this section* is personally liable for the amount of tax due." (Italics added.) Because Taxpayer failed to keep such records, it is personally liable for the retail sales tax. We do not have the authority to allow the exemption when the records required for the exemption are not maintained. Det. No. 04-0102, 23 WTD 340 (2004).

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 4th day of December 2012.