

Cite as Det. No. 16-0263, 36 WTD 114 (2017)

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. 16-0263
))	
. . .)	Registration No. . . .
))	

RCW 82.32.050(4): STATUTORY PERIOD FOR ENFORCING TAX OBLIGATIONS. RCW 82.32.050(4) is a non-claim statute because it limits when the Department of Revenue (Department) may enforce taxpayer's tax obligations. The Department may only enforce tax obligations for periods no earlier than four years after the close of the current tax year, unless an exception in RCW 82.32.050(4) applies. If such an exception does apply, there is no limit to how far back the Department may enforce tax obligations.

RCW 82.08.130; RCW 82.08.020: RETAIL SALES TAX – TAX PAID AT SOURCE DEDUCTION. In order for a Taxpayer to establish it is entitled to the tax paid at source deduction, the Taxpayer must establish that it actually paid retail sales tax through records.

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.

Fisher, T.R.O. (Successor to Pree, T.R.O.) – A contractor engaged in construction petitions for the correction of assessment, contending the Department is barred by statute from assessing taxes for certain prior tax periods and, for the open tax periods, Taxpayer's tax liability should be offset by a tax paid at source deduction. Taxpayer's petition is denied.¹

ISSUES

1. Is the [Department] barred by the limitations for assessing tax for the tax periods 2006, 2007, 2008, 2009, and 2010 under RCW 82.32.050(4)?
2. Has Taxpayer provided records sufficient to substantiate additional tax paid at source deductions under RCW 82.08.130(2)?

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

FINDINGS OF FACT

[Taxpayer] is an [out-of-state] limited liability company, which is registered to do business in Washington with its principal place of business [out-of-state]. Taxpayer performed construction services on houses owned by a speculative builder in Washington. Taxpayer prepared purchase orders for the speculative builder, which included charges for retail sales tax. The speculative builder paid Taxpayer the totals on the purchase orders. Taxpayer did not remit sales tax to the [Department].

Taxpayer filed returns for Quarters 1 and 2 of 2006, and Quarter 1 of 2007. On each return, Taxpayer marked that Taxpayer did no business in Washington. Taxpayer did not file any returns for Quarters 3 and 4 of 2006; Quarters 2, 3, and 4 of 2007; 2008; 2009; 2010; 2011; 2012; or 2013.

. . . On November 1, 2013, the Department's Audit Division ("Audit") sent an initial contact letter to Taxpayer. Taxpayer assembled its records and met with the auditor on January 14, 2014. The auditor reviewed Taxpayer's QuickBooks records for the period from January 1, 2006, through December 31, 2013. Taxpayer's purchase orders showed that Taxpayer charged the speculative builder sales tax on home construction in Washington. Taxpayer's QuickBooks also had purchase orders prepared by Taxpayer to the speculative builder, which added, "WASHINGTON TAX" to Taxpayer's subcontractors' prices for Washington jobs.

Audit requested that Taxpayer provide copies of its subcontractor invoices. Taxpayer did not have invoices from the subcontractors, but instead had purchase orders showing an amount billed by each subcontractor to Taxpayer for various jobs; the amounts billed by the subcontractors did not separately state retail sales tax, nor did the purchase orders state that the price listed by the subcontractor included retail sales tax. Taxpayer created invoices to correspond with the full amount charged by the subcontractor and billed those invoices to the speculative builder. However, when creating invoices for the speculative builder, instead of adding retail sales tax to the amount Taxpayer paid to its subcontractors, Taxpayer would factor retail sales out of the subcontractors' prices so that the total amount charged to the speculative builder would match the amount Taxpayer was charged by the subcontractor.

On June 5, 2015, the Department issued two assessments against Taxpayer:

1. Document No. . . . assessed \$. . . in retail sales tax for the period from January 1, 2006, through December 31, 2008. A 5% assessment penalty of \$. . . and a \$. . . delinquent penalty were added, plus \$. . . in interest.² Document No. . . . totaled \$. . .
2. Document No. . . . assessed \$. . . in retail sales tax, plus \$. . . in business and occupation (B&O) tax, offset by a \$. . . small business tax credit for the period from January 1, 2009, through September 30, 2013. A 5% assessment penalty of \$. . . and a \$. . . delinquent penalty were added, plus \$. . . in interest.³ Document No. . . . totaled \$. . . due.

² The Audit Division waived interest for the period February 1, 2014, through April 30, 2015.

³ The Audit Division waived interest for the period February 1, 2014, through April 30, 2015.

Taxpayer appealed both assessments. Taxpayer asserts that the Department could not assess retail sales tax on early years of the audit period because the Department had not found that Taxpayer (1) misrepresented a material fact, (2) agreed to extend the statutory period for assessments, or (3) was unregistered to do business in Washington. Taxpayer also contends the Department could not assess retail sales tax based upon Taxpayer's purchase orders issued to the builder without allowing a tax paid at source credit for the sales tax shown on Taxpayer's purchase orders for the services provided by its subcontractors, and the materials provided by its vendors.

Taxpayer explains that it primarily worked for the same speculative builder, who paid Taxpayer to install drywall in the houses it built. According to Taxpayer, there were no written contracts or invoices between the speculative builder and Taxpayer. Rather, the speculative builder generated an electronic purchase order, which it transmitted to Taxpayer electronically, to pay Taxpayer a specified amount for drywall at each house. The purchase orders added Washington sales tax to arrive at the amount due, which the builder paid upon completion of the work. Taxpayer acknowledges that the total paid included sales tax, which was deposited into Taxpayer's bank account.⁴ Taxpayer did not remit the retail sales tax it collected to the Department.

Taxpayer paid the subcontractors to attach, tape, and texture the drywall for each house. The subcontractors did not invoice Taxpayer for each job it performed, but instead combined many jobs together in single purchase orders. The price for each job does not include separately stated retail sales tax.

Taxpayer also claims that it generated purchase orders to its subcontractors showing the tax paid for each order. According to Taxpayer, its accountant advised it to discard its records after three years. Therefore, Taxpayer did not keep its older invoices. However, Taxpayer did retain its electronic purchase orders. The electronic purchase orders between Taxpayer and its subcontractors do not contain separately stated charges for retail sales tax.

After Taxpayer received notice of the audit, it scheduled a meeting with the auditor and made its electronic purchase orders available. The Department allowed the taxpayer a tax paid at source credit for the sales taxes it paid at sources verified with the vendors' invoices in 2013, but not for sales taxes prior to 2013 due to a lack of documentation. Taxpayer did not provide additional records showing retail sales tax paid on its vendor purchases prior to 2013.

Taxpayer also submitted a public records request, and received several documents related to the audit of Taxpayer. One document is titled "Transcript Request." The Transcript Request states that on January 20, 2012, a "Current Audit Assignment" was generated for 2008 through 2011. Taxpayer asserts that this means the Department discovered, or should have discovered, the taxes allegedly owed by Taxpayer by the end of 2012, which would trigger the limitations period for assessments under RCW 82.32.050(4). Taxpayer asserts that because the assessment was not issued until 2015, the assessment can only cover the four years prior to 2015.

⁴ Taxpayer asserts in its petition that because Taxpayer did not issue an actual sales invoice to the speculative builder, there was no opportunity to collect retail sales tax by Taxpayer. Because Taxpayer admits it collected and did not remit retail sales tax, and because Taxpayer's records contain purchase records from Taxpayer to the speculative builder that separately state retail sales tax, this argument is without merit. *See* Hearing Notes / Memorandum, Exhibit B (purchase order from Taxpayer to speculative builder separately stating retail sales tax).

ANALYSIS

Statutory Period for Assessments

Taxpayer argues the Department may not assess retail sales taxes for periods prior to 2011.

RCW 82.32.050(4) limits the time the Department may issue an assessment of tax to enforce tax obligations:

No assessment or correction of an assessment for additional taxes, penalties, or interest due may be made by the department more than four years after the close of the tax year, except (a) against a taxpayer who has not registered as required by this chapter, (b) upon a showing of fraud or misrepresentation of a material fact by the taxpayer, or (c) where a taxpayer has executed a written waiver of such limitation.

The Department issued two assessments against Taxpayer for tax periods 2006 through 2013 in 2015. Thus, because part of the assessments were issued more than four years after the close of 2015 tax year (i.e., the 2006, 2007, 2008, 2009, and 2010 tax periods), an exception to the statutory period for assessment must apply for the Department to impose tax during the earlier years at issue.

There is no limitation for the period in which an assessment or a correction of assessment can be made upon a showing of misrepresentation of a material fact. RCW 82.32.050(4); *see also* WAC 458-20-230(4). The Department has the burden to show a material misrepresentation by clear, cogent, and convincing evidence. Det. No. 98-039, 19 WTD 101, 105 (2000). Clear, cogent, convincing evidence is that which convinces the trier of fact that the issue is "highly probable," or, stated another way, the evidence must be "positive and unequivocal." *Colonial Imports, Inc. v. Carlton Northwest, Inc.*, 121 Wn.2d 726, 853 P.2d 913 (1993).

Here, not only did Taxpayer collect retail sales tax that it did not remit to the Department, Taxpayer represented to the Department it was not engaged in any activity subject to tax in Washington during the audit period through its tax returns.⁵ This was not true. Taxpayer knew it owed Washington taxes as evidenced by its purchase orders and QuickBooks documentation showing that it collected retail sales tax. Taxpayer also admitted it collected retail sales tax. Taxpayer never sent that money to the Department. This misrepresentation was material as it enabled Taxpayer to avoid its duty to pay Washington the retail sales tax Taxpayer held in trust for Washington. Taxpayer's admission that it collected and failed to remit retail sales tax, along with the purchase orders and QuickBooks showing Taxpayer collected retail sales tax, satisfies the clear, cogent, and convincing evidentiary standard.

Moreover, with respect to retail sales tax collected by a seller upon retail sales and not remitted to the Department, WAC 458-20-230(6) provides:

Retail sales tax which is collected by a seller must be remitted to the department of revenue. These amounts are deemed to be held in trust by the seller until paid to the department.

⁵ Taxpayer had an affirmative duty to file accurate returns and ensure the accuracy of the information entered on its tax returns. RCW 82.32A.030(4)-(5).

The statute of limitations does not apply to retail sales tax which was collected and not remitted to the department.

(Emphasis added); *see also* WAC 458-20-230(2)(d) (sales tax collected by a seller and not remitted to the Department is grounds to extend the statutory period for assessments). In Det. No. 98-039, 19 WTD 101 (2000), we explained that this exception to the normal four-year time limit is a specific application of the fraud and misrepresentation provisions. It arises out of fraud or misrepresentation that is inferred from the unexcused failure of a fiduciary holding trust funds to pay over such funds to the state. *Id.*; *see also* RCW 82.08.050(2) (sales tax collected by a seller are held in trust by the seller on behalf of the state until paid to the Department). In *Kitsap-Mason Dairymen's Ass'n v. Wash. Tax Comm'n*, 77 Wn.2d 812, 817, 467 P.2d 312 (1970), the Washington Supreme Court explained the unique nature of the retail sales tax scheme: “[i]nherent in RCW 82.08 is the fact that taxes collected in the name of the state are not property of the seller. . . . The integrity of the entire taxing system demands that funds collected as taxes be remitted to the state.”

Accordingly, because Taxpayer collected retail sales tax and failed to remit such tax to the Department, and because Taxpayer misrepresented a material fact when it stated it was not conducting any business in Washington while it was in fact collecting retail sales tax, the time limitation in RCW 82.32.050(4) does not apply.

Taxpayer argues that the Department should have discovered Taxpayer's breach of duty on January 20, 2012, the day the “Current Audit Assignment” was generated, or sometime before. Put another way, Taxpayer argues that RCW 82.32.050(4) is a statute of limitations, and that without any equitable tolling of the statute, the Department is barred from assessing these taxes. It is the Department's position that RCW 82.32.050(4) is a nonclaim statute rather than a statute of limitations.

A statute of limitations limits when a party may seek a remedy; conversely, a nonclaim statute limits the time in which a party must enforce a right or enforce an obligation. *Bellevue School Dist. No. 405 v. Brazier Const. Co.*, 100 Wn.2d 776, 784, 675 P.2d 232 (1984) (citing *Lane v. Dept. of Labor & Indus.*, 21 Wn.2d 420, 425-6, 151 P.2d 440 (1944)). Nonclaim statutes impose a condition precedent to the enforcement of a right of action, and thus compliance with the statute is a condition precedent to prosecution of a claim. 51 Am. Jur. 2d Limitation of Actions § 23.

The Department is authorized to collect taxes by statute. *See generally* Title 82 RCW. Once four years elapse after the close of a tax year, RCW 82.32.050(4) prevents the Department from enforcing a taxpayer's obligations to pay taxes for that tax year unless an exception applies. Compliance with the four-year time limit in RCW 82.32.050(4), i.e., issuing an assessment before four years following the close of a tax year, is a condition precedent to enforcing tax obligations, so RCW 82.32.050(4) is a nonclaim statute. *See Guy F. Atkinson v. State*, 66 Wn.2d 570, 572, 403 P.2d 880 (1965) (“ . . . strictly speaking the question presented is one of nonclaim, rather than one of statute of limitations. . . . we are concerned with a statute which designates the time allowed for the taking of a step which is a prerequisite to bringing an action. . . .”). Accordingly, when the Department discovered or should have discovered Taxpayer's failure to remit the retail sales taxes it collected is irrelevant because Taxpayer misrepresented that it was not doing any business

in Washington when in fact it was collecting and keeping retail sales tax belonging to the state, thus falling into an exception in the nonclaim statute.⁶

Because Taxpayer collected retail sales tax, which it failed to remit to the Department, the exceptions in the nonclaim statute apply. RCW 82.32.050(4); WAC 458-20-230(4).

Tax Paid at Source Deduction

RCW 82.08.020 imposes a tax on each retail sale in this state. The retail sales tax is imposed on the buyer, but is normally collected and remitted to the Department by the seller. RCW 82.08.050(1)-(2).

RCW 82.08.050(9) generally requires retail sales tax to be separately stated on any instrument of sale and states:

[T]he tax required by this chapter to be collected by the seller must be stated separately from the selling price in any sales invoice or other instrument of sale. . . . Except as otherwise provided in this subsection, for purposes of determining the tax due from the buyer to the seller and from the seller to the department it must be conclusively presumed that the selling price quoted in any price list, sales document, contract or other agreement between the parties does not include the tax imposed by this chapter. But if the seller advertises the price as including the tax or that the seller is paying the tax, the advertised price may not be considered the selling price.

(Emphasis added).

Thus, under RCW 82.08.050(9), if a seller does not advertise its price as including the retail sales tax or that the seller is paying the retail sales tax, and the seller does not separately state the retail sales tax in its invoices to its customers, there is a conclusive presumption that the selling price quoted in the price list does not include the retail sales tax.

There are a number of deductions from retail sales tax, one of which is the tax paid at source deduction. Taxpayer maintains that it is entitled to an additional tax paid at source deduction, above and beyond the tax paid at source deduction allowed by the Audit Division. This deduction is found in RCW 82.08.130:

A buyer who pays a tax on all purchases and subsequently resells property or services at retail, without intervening use by the buyer, must collect the tax from the purchaser as otherwise provided by law and is entitled to a deduction on the buyer's tax return equal to the cost to the buyer of the property or service resold upon which retail sales tax has been

⁶ On its face, RCW 82.32.050(4) contains no reference to whether or not the Department should have "discovered" the tax liability. If the Department discovers tax liability for a tax period more than four years in the past, the Department cannot enforce those obligations unless an exception contained in RCW 82.32.050(4) applies, even if it was practically impossible for the Department to discover the tax liability. Accordingly, Taxpayer's arguments regarding when the Department should have discovered the tax liability are irrelevant to the analysis of whether or not the Department may assess taxes for prior tax periods.

paid. The deduction is allowed only if the taxpayer keeps and preserves records that include the names of the persons from whom the property or services were purchased, the date of the purchase, the type of property or services, the amount of the purchase, and the tax that was paid.

RCW 82.08.130(2) (emphasis added).

Businesses subject to excise tax or obligated to collect and remit retail sales tax must keep, for five years, records necessary to determine the amount of any tax for which it may be liable. RCW 82.32.070(1). These records must show that the retail sales tax was actually paid. RCW 82.32.130(2).

Taxpayer seeks tax paid at source deductions for the work performed by its subcontractors and the materials Taxpayer purchased from vendors.

The purchase orders from the subcontractors for work performed do not separately state retail sales tax. The purchase orders constitute an “other agreement between the parties” within the meaning of RCW 82.08.050(9), so there is a conclusive presumption the amounts in the purchase orders do not include retail sales tax. Taxpayer has not provided any proof it paid the retail sales tax on the work provided by the subcontractors, and therefore is ineligible for a tax paid at source deduction. RCW 82.08.130(2).

Similarly, Taxpayer has not provided documentation showing it paid retail sales tax on purchases of materials from vendors prior to 2013.⁷ Accordingly, Taxpayer is also not eligible for a tax paid at source deduction for purchases of materials from vendors.

DECISION AND DISPOSITION

Taxpayer’s petition is denied.

Dated this 24th day of August 2016.

⁷ Audit allowed tax paid at source deductions for transactions in 2013 for which Taxpayer was able to provide documentation showing it paid retail sales tax; such transactions are not at issue in this administrative review.