Cite as Det. No. 14-0088R, 34 WTD 27 (2015)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition for Correction of Assessment of	)	D E T E R M I N A T I O N
	)	
	)	No. 14-0088R
. . .	)	
	)	Registration No. . . .
	)	
	)	

[1] RULE 254; RCW 82.32.070; RECORDKEEPING; RECORDS SUFFICIENT TO SUPPORT ADJUSTMENT. Upon converting from cash to accrual accounting, invoices in accounts receivable become subject to tax. Tax was properly assessed on outstanding invoices in accounts receivable on the date of the conversion and a general assertion that tax was remitted on a number of invoices is insufficient to support adjustment where the taxpayer can not substantiate that tax was actually remitted for the invoices at issue.

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.

Kreger, A.L.J. – A construction company petitions for reconsideration of a determination affirming an assessment of tax for failing to report tax on outstanding invoices when it converted from cash to accrual method of accounting. The Taxpayer asserts tax was remitted on a number of the invoices at issue. Because the Taxpayer has not been able to substantiate tax was remitted on the invoices at issue, we sustain the assessment as issued and deny the Taxpayer's petition.[1]

ISSUE

Under WAC 458-20-254 is the identification of a number of invoices the Taxpayer asserts it reported as taxable income sufficient to establish that tax was remitted and support adjustment to an assessment?

FINDINGS OF FACT

[Taxpayer] is a Washington corporation engaged in the business of providing custom construction services to residential customers. The Department of Revenue (Department) audited the Taxpayer's business activities for the period of September 1, 2007 through December 31, 2007. An assessment for additional retail sales tax was issued at the conclusion of the audit

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

in the amount of $. . . . The Assessment was comprised of $. . . in retail sales tax and $. . . in interest. The Taxpayer timely appealed the assessment asserting tax had in fact been remitted on a number of invoices at issue.

In September 2007, the Taxpayer converted from the cash method of accounting to the accrual method of accounting. The audit review of the Taxpayer's books and records identified payments in the accounts receivable category as of September 2007. The auditor reviewed the total accrued retail sales tax recorded in the Taxpayer's records and assessed tax on outstanding invoices that were accrued as of September 30, 2007. The auditor reviewed and verified that the list of open invoices, identified as taxable upon the conversion to the accrual method, were marked as paid subsequent to the conversion.

On appeal, the Taxpayer produced a number of invoices where it asserts the retail sales tax was previously reported, but did not provide sufficient information to tie the income at issue in a particular invoice to amounts reported on a specific return. At the hearing, the Taxpayer explained some entries into the sales tax account were incorrect and some had been duplicated due to the inclusion of amounts that had not been invoiced yet when entered into the accounting system. The Taxpayer asserted it would be able to provide detail that would specifically establish which tax return the sales tax on the contested invoices had been reported on. The Audit Division agreed if this detail were available it would be sufficient to support an adjustment to the assessment.

Our initial determination affirmed the assessment as issued because, despite providing numerous opportunities and extensions of time, the Taxpayer failed to produce records identifying when tax had been remitted on the contested invoices. On reconsideration, the Taxpayer acknowledges it owes additional tax due to the conversion from cash to accrual accounting, but continues to assert that income from a number of the invoices identified by the Audit Division was included in prior returns. Taxpayer has provided some additional accounting information, which was reviewed by the Audit Division. However, after review of the additional detail, the Audit Division found the accounting detail provided did not establish that the income from the invoices at issue had been included in taxable income reported on prior returns.

ANALYSIS

Taxpayers have an affirmative duty to maintain adequate records and to provide the Department access to those records so that the Department can reasonably ascertain a taxpayer's tax liability. RCW 82.32.070. *See also* WAC 458-20-254 (Rule 254); Det. No. 99-341, 20 WTD 343 (2001). RCW 82.32.070 specifically requires that "[e]very person liable for any fee or tax imposed by chapters 82.04 through 82.27 RCW 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 [or she] may be liable…." . . . .

In September 2007, the Taxpayer switched from a cash accounting methodology where amounts are reported based upon cash receipts to the accrual method of accounting where amounts are reported when the income is accrued. . . . . With the change in accounting methodology, invoices that were recorded in the Taxpayer's accounts receivable records as of September 30, 2007, became taxable at that point in time because the Taxpayer had accrued a right to that income, even though a particular invoice may not have been actually paid as of that date. In conducting the audit review, the auditor itemized the invoices at issue and noted they were subsequently marked paid and accordingly assessed tax on these invoices as the Taxpayer was not able to establish that the retail sales tax itemized, and subsequently collected, on the invoices at issue had been remitted.

On appeal and on reconsideration, the Taxpayer has articulated a number of errors in how sales were recorded in its books and records. These errors indicate the date stamped on a particular invoice may not correspond to the date the revenue was received for that invoice, but rather corresponds to when that invoice was processed for accounting purposes. However, what is lacking are records and detail to support Taxpayer's assertion that income from [the] invoices at issue in the assessment were included in taxable revenue in previous returns. Absent specific detail that indicates income from a particular invoice was included in taxable income for prior periods, we conclude the Audit Division's reliance on the Taxpayer's characterization of this invoice as an account receivable, at the time of conversion, supports characterizing income as taxable at that time.

In this case, the invoices at issue became taxable upon the conversion to accrual accounting. The auditor reviewed the available records, which established that the invoices at issue were subsequently marked paid, indicating the subsequent receipt of the retail sales tax at issue. As the available records indicated, the retail sales tax at issue was actually received after the conversion of accounting method. These amounts would not have ordinarily been reported upon receipt, due to the change in accounting method. The Audit Division has reviewed the additional information provided on reconsideration, but concluded this information does not establish tax was actually remitted on the invoices at issue. Without information that established tax was actually remitted on the invoices at issue prior to the conversion, we conclude the Audit Division properly characterized these amounts as subject to tax upon the conversion to accrual accounting. Due to the absence of detail to support the Taxpayer's assertions, we sustain the assessment as issued.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 23rd day of September, 2014.