

Cite as Det. No. 16-0408, 36 WTD 490 (2017)

BEFORE THE ADMINISTRATIVE REVIEW AND HEARINGS 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. 16-0408
)	
...)	Registration No. . . .
)	

[1] RULE 254; RCW 82.32.100: RETAIL SALES TAX – RETAILING B&O TAX – RECORDKEEPING – REASONABLE ESTIMATES. Where a taxpayer’s records of sales did not match records maintained by the department of licensing, the Department had authority to estimate the taxpayer’s gross sales of the business, and it was reasonable for the Department to rely on the department of licensing records in estimating such sales.

[2] RULE 228; RCW 82.32.090(7): EVASION PENALTY – INTENT TO EVADE. Where a taxpayer produced records indicating that it had collected more retail sales tax than it actually remitted satisfied the Department’s burden of proving that the taxpayer had willfully failed to remit retail sales tax it had collected from customers.

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.

Yonker, T.R.O. – A seller of used cars (Taxpayer) protests an estimated tax assessment that included an evasion penalty. Taxpayer maintains that the basis for the estimate used by the Department was flawed, and that the apparent underreporting of tax liability was not the result of an intent to evade. We deny Taxpayer’s petition.¹

ISSUES

1. Did the Department properly estimate the amount of Taxpayer’s vehicle sales under RCW 82.32.100(1), where Taxpayer’s records were incomplete and were not consistent with Department of Licensing records?
2. Did the Department properly assess an evasion penalty under RCW 82.32.090(7) and WAC 458-20-228?

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

FINDINGS OF FACT

. . . (Taxpayer) operates a used car dealership with reported locations in [Washington].² In 2014, the Department's Audit Division commenced a review of Taxpayer's books and records for the time period of January 1, 2011, through September 30, 2014 (audit period).

During the course of its review, the Audit Division found inconsistencies in Taxpayer's records. Specifically, Department of Licensing (DOL) records, which the Audit Division had independently obtained, indicated that Taxpayer had sold 1,523 vehicles during the audit period whereas the Audit Division's initial review of Taxpayer's "sales jackets" indicated that Taxpayer had sold significantly fewer vehicles during the audit period. Taxpayer supplemented the record on three occasions during the Audit Division's review, ultimately providing records indicating Taxpayer sold 1,392 vehicles – 131 vehicles fewer than what DOL records indicated.

During the Audit Division's review, Taxpayer attributed the discrepancy in sales to two circumstances. First, Taxpayer stated it had leased space at its facility to five other independent sellers, all of which had access to Taxpayer's records and office space, and those other sellers may have used Taxpayer's dealer number when reporting their vehicle sales to DOL.³ Taxpayer provided no evidence that any other business had actually used Taxpayer's dealer number. Second, Taxpayer represented that its office was burglarized sometime during the audit period and that some of its sales jackets and other records were stolen.

On February 11, 2016, while the Audit Division's review was still pending, Taxpayer also produced a document entitled ". . . Close Out Report" (Report), which Taxpayer represented detailed all of its vehicle sales during the entire audit period. The Report indicated that Taxpayer collected a total of \$. . . in retail sales tax, compared to \$. . . in retail sales tax that Taxpayer actually remitted to the Department during the audit period.⁴

The Audit Division ultimately used the DOL records as the basis of its estimate for Taxpayer's total vehicle sales during the audit period. Where Taxpayer had sales jackets or other records that included the actual sale price, the Audit Division used the documented price. For the 131 vehicle sales for which Taxpayer had no sales records, the Audit Division relied on Kelley Blue Book published vehicle values to estimate the sale prices.⁵

As a result of the Audit Division's review, on June 29, 2016, the Department issued a tax assessment for a total of \$. . . , which included \$. . . in retail sales tax, \$. . . in motor vehicle tax, \$. . . in retailing business and occupation (B&O) tax, \$. . . in service and other activities B&O

² Taxpayer represented that its . . . location only existed for about a year. Currently . . . is the only location Taxpayer maintains.

³ Taxpayer identified the five sellers as follows: . . . Taxpayer provided a copy of a lease between it and . . . that commenced on December 1, 2014, which is after the end of the audit period.

⁴ We note that Taxpayer claimed various deductions that would have reduced the amount of retail sales tax Taxpayer remitted to the Department; however, when factoring in the deductions Taxpayer claimed during the audit period, the Report indicated that \$. . . in retail sales tax was not remitted to the Department.

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tax, a \$. . . evasion penalty, a \$. . . five-percent assessment penalty, and \$. . . in interest.⁶ Taxpayer subsequently sought review of the entire tax assessment.

ANALYSIS

1. Retailing B&O Tax and Retail Sales Tax

Taxpayer does not dispute that the gross proceeds of its vehicle sales during the audit were subject to retailing B&O tax. Nor does Taxpayer dispute that it was required to collect retail sales tax on such vehicle sales, and remit such retail sales tax to the Department. Instead, Taxpayer disputes the Audit Division's estimate of Taxpayer's gross proceeds from vehicle sales during the audit period.

RCW 82.32.070 requires taxpayers to maintain suitable records as may be necessary to determine the amount of any tax for which they may be liable. WAC 485-20-254 (Rule 254), which is the administrative rule regarding recordkeeping, states in pertinent 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 for 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.

...

- (c) The records kept, preserved, and presented must include the normal records maintained by an ordinary prudent business person. Such records may include general ledgers, sales journals, cash receipts journals, bank statements, check registers, and purchase journals, together with all bills, invoices, cash register tapes, and other records or documents of original entry supporting the books of account entries. The records must include all federal and state tax returns and reports and

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all schedules, work papers, instructions, and other data used in the preparation of the tax reports or returns.

When complete records are not made available to the Department, it is authorized to “proceed, in such manner as it may deem best, to obtain facts and information on which to base” an estimated tax liability. RCW 82.32.100(1). Here, the number of Taxpayer’s actual vehicle sales during the audit period is unclear because Taxpayer’s sales records did not match DOL records. Taxpayer concedes that it is unable to produce sales jackets, or equivalent records, for all of its vehicle sales. As such, in the absence of complete records, the Audit Division was authorized to estimate Taxpayer’s gross proceeds of sales under RCW 82.32.100(1).

The only limitation to the Department’s authority to estimate tax liability under RCW 82.32.100(1) is that the method used must be “reasonable.” Det. No. 15-0104, 34 WTD 434 (2015). We conclude that it was reasonable for the Audit Division to rely on DOL records to determine the number of vehicle sales Taxpayer made during the audit period. RCW 46.70.083 requires all vehicle dealers to report “the number of vehicle sales transacted” each year to renew its vehicle dealer license. *See also* WAC 308-66-165. Thus, it is reasonable to presume that Taxpayer would have accurately reported the number of vehicles it sold to DOL.

Taxpayer speculated that it was possible other sellers with access to Taxpayer’s office space may have used Taxpayer’s dealer number when reporting their own vehicle sales to DOL. Presumably, if this were true, Taxpayer’s total vehicle sales according to DOL would be inflated. Yet, Taxpayer concedes that it has no evidence that other sellers used its dealer number. We conclude it was reasonable to derive the total number of Taxpayer’s vehicle sales from DOL records.

We likewise conclude that the Audit Division’s reliance on Kelley Blue Book value to estimate the selling price for the 131 sales for which Taxpayer did not have sale records was reasonable. We have previously held that book-value publications are an appropriate basis for determining retail sales tax liability where a taxpayer fails to maintain or produce complete records. *See* Det. No. 89-471, 8 WTD 251 (1989) (upholding an estimate based on National Automobile Dealers Association (NADA) blue book values). While Taxpayer argues that Taxpayer historically sold its vehicles at prices, on average, below the Kelley Blue Book values, we conclude that, even if true, that fact does not render the Audit Division’s reliance on the values listed in Kelley Blue Book “unreasonable.” As such, we conclude that reliance on the Kelley Blue Book values alone for estimating the selling price of the 131 vehicles for which there are no sales jackets was reasonable under the Department’s broad authority to estimate tax liability pursuant to RCW 82.32.100(1).

2. Evasion Penalty

RCW 82.32.090(7) requires that “[i]f the department finds that all or any part of the deficiency resulted from an intent to evade the tax payable hereunder, a further penalty of fifty percent of the additional tax found to be due **must** be added.” (Emphasis added).

WAC 458-20-228 (Rule 228), the Department’s administrative rule addressing penalties, provides the following additional guidance regarding the evasion penalty:

The evasion penalty is imposed when a taxpayer knows a tax liability is due but attempts to escape detection or payment of the tax liability through deceit, fraud, or other intentional wrongdoing. An intent to evade does not exist where a deficiency is the result of an honest mistake, miscommunication, or the lack of knowledge regarding proper accounting methods. **The department has the burden of showing the existence of an intent to evade a tax liability through clear, cogent and convincing evidence.**

Rule 228(5)(f) (emphasis added). Therefore, imposition of the evasion penalty requires the Department to prove the following two elements by clear, cogent, and convincing evidence that is both objective and creditable: (1) the existence of a tax liability which the taxpayer knows is due; and (2) an attempt by the taxpayer to escape taxation through deceit, fraud, or other intentional wrongdoing. Det. No. 99-141, 19 WTD 638 (2000); *see also* Det. 94-007, 14 WTD 174 (1995); Det. 90-314, 10 WTD 111 (1990).

Clear, cogent, and convincing evidence has been described as evidence convincing the trier of fact that the issue is “highly probable,” or, put differently, the evidence must be “positive and unequivocal.” 19 WTD 638 (citing *Colonial Imports, Inc. v. Carton Northwest, Inc.*, 121 Wn.2d 726, 853 P.2d 913 (1993)). Mere suspicion of an intent to evade is not enough to meet this burden. Det. 04-0098, 23 WTD 331 (2004). Instead, there must be proof of a deliberate attempt on the part of the taxpayer to evade a tax liability. *Id.* However, Rule 228(5)(f)(ii)(B) states that “[t]he willful failure of a seller to remit retail sales taxes collected from customers to the department” will generally be “considered to establish an intent to evade a tax liability.”

Here, the Report, produced by Taxpayer, indicated that Taxpayer collected a total of \$. . . in retail sales tax during the audit period. Yet, Taxpayer only remitted \$. . . to the Department during that same period. Even taking into consideration the deductions Taxpayer originally claimed that were later disallowed, Taxpayer still failed to remit \$. . . , according to the Report. The fact that Taxpayer collected retail sales tax demonstrates its knowledge that the tax was due. Further, the Report demonstrates that Taxpayer knew it was not remitting all retail sales tax due to the Department. Thus, Taxpayer’s intent to evade its tax liability is proven under Rule 228(5)(f)(ii)(B). The Department has, therefore, met its burden of showing the elements of evasion.

Once the Department has clearly demonstrated the existence of each of the elements of evasion, a burden of production is imposed on the taxpayer to come forward with evidence of honest mistake, ignorance of the law, negligence, or some other fact which tends to rebut the Department’s evidence. 23 WTD 331. Mere subjective and self-serving statements by the taxpayer regarding intent, without more, are insufficient to meet this burden of production. *Id.* Taxpayer argued that many of its sales jackets were stolen during a burglary of its office, leading to Taxpayer underreporting its income on its excise tax returns, and failing to remit all retail sales tax it collected on its vehicle sales during the audit period. Yet, even if some of the sales jackets were stolen . . . the Report still contained enough information to put Taxpayer on notice that it had collected significantly more retail sales tax during the audit period than it remitted to the Department.

Accordingly, we find by clear, cogent, and convincing evidence that the Taxpayer knew it had a Washington State tax obligation and through intentional wrongdoing acted with the specific purpose to avoid paying this obligation. We conclude that the Audit Division properly assessed the evasion penalty.

DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 29th day of December 2016.