

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS

DIVISION OF TAXATION

ADMINISTRATIVE HEARING

FINAL DECISION AND ORDER

#2013-01



### III. ISSUE

Whether the Taxpayer owes the various sales tax assessments issued by the Division.

### IV. MATERIAL FACTS AND TESTIMONY

Senior Revenue Agent, testified on behalf of the Division. She testified that she works in field audit and conducted a sales and use audit of the Taxpayer for the period of April 1, 2001 to March 31, 2007. She testified that the Taxpayer incorporated in 1992 and its principal place of business was in Rumford, Rhode Island. She testified that she reviewed purchasing invoices and fixed assets with the depreciation schedule. She testified there were no back-up records for the assets and the records were incomplete. She testified that there was no statute of limitations waiver and no agreement for the test period because the Taxpayer was a non-filer of sales and use tax so that the six (6) year time period applied to the Taxpayer.

testified that she found different liabilities for each Taxpayer entity: 1) Taxpayer – for assets and supply and expenses; 2) Taxpayer II – for assets and supply and expenses; 3) Taxpayer III – for assets and supply and expenses; 4) Taxpayer VI – for supply and expenses; 5) Taxpayer VII – for supply and expenses; and 6) Taxpayer IX – for supply and expenses. See Division's Exhibit Eight (8). She testified that she assessed all assets and supply and expenses purchases when no tax was paid. She testified that she usually performs an actual review of assets but was not provided with all depreciation schedules for the entire audit period so she had to estimate from the Federal return and extrapolate over the audit period. She testified that when there was no proof of tax paid for supply and expenses, she assessed based on purchase invoices. She testified that she

did not review assets for all entities since the last three (3) entities did not have depreciation schedules.

testified that Notices of Deficiency were issued on February 11, 2009 for the six (6) entities with revisions made to the assessments based on invoices that the Taxpayer provided after the initial Notice of Hearing was issued so that some deficiencies were revised as of October 4, 2012. See Division's Exhibits 11 (initial Notices of Deficiency) and 13 (10/4/12 revised workpapers).

The owner ("Owner") of these six (6) consolidated entities designated as the Taxpayer testified on the Taxpayer's behalf. She testified that her businesses did not sell any goods for which she was required to collect sales tax. She testified that all the Division's assessments were for her purchase of goods. She testified that she purchased goods for her businesses in Rhode Island and in Massachusetts and also made internet purchases. She testified that on some of her internet purchases, she did not pay sales tax. She testified that she tried to gather as many invoices as she could after the audit. She testified that she tried to get the Division to contact the businesses from which she purchased items to verify that she paid sales tax. She testified that she also sent a letter to all her vendors asking for them to provide her with copies of her invoices and she was able to receive some receipts from the vendors. See Taxpayer's Exhibits 1B and 1C (letter to vendor). She testified that in her business, she relied on other people for her recordkeeping and she realized that the recordkeeping was not very good. She testified she never intentionally did not pay sales tax and never represented that she was a sales tax exempt entity.

The Owner testified that for some purchases where she did not have actual receipts, she owed an additional 2%<sup>2</sup> since large chain stores like \_\_\_\_\_ or \_\_\_\_\_ always charge sales tax and she was not sure if the purchases were in Rhode Island or Massachusetts. See Taxpayer's Exhibit One (1). She testified that for purchases that she bought online or at a conference where she did not have invoices, she owed 7% sales tax. She testified that she has receipts for some internet purchases like \_\_\_\_\_ e but not all of them; however, based on the receipts she has, she testified that it shows she paid sales tax on all those receipts. She testified that the checks made to cash could be payments for field trips or loans between the entities and she would have been reimbursed. She testified that some invoices were for contracting work and she always bought her own materials from the \_\_\_\_\_ so she only paid the contractors for their services so does not owe sales tax on those invoices. She testified that \_\_\_\_\_ provided professional services so she does not owe tax on those services but was assessed for those payments. See Taxpayer's Exhibit One (1). She testified that the \$ \_\_\_\_\_ cash entry (10/22/01) for Taxpayer was for \_\_\_\_\_ and provided a copy of the check (check is for cash with notation for \_\_\_\_\_ ). She testified that the \$ \_\_\_\_\_ cash entry for 9/27/02 matches a certified check deposited into the expense account for Taxpayer and the \$ \_\_\_\_\_ cash entry (9/27/02) matches a certified check to Taxpayer II and was a loan to Taxpayer II. See Taxpayer's Exhibit Two (2) (copies of checks testified to).

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<sup>2</sup> The difference between Massachusetts sale tax and Rhode Island sales tax.

## V. DISCUSSION

### A. Legislative Intent

The Rhode Island Supreme Court has consistently held that it effectuates legislative intent by examining a statute in its entirety and giving words their plain and ordinary meaning. *In re Falstaff Brewing Corp.*, 637 A.2d 1047 (R.I. 1994). If a statute is clear and unambiguous, “the Court must interpret the statute literally and must give the words of the statute their plain and ordinary meanings.” *Oliveira v. Lombardi*, 794 A.2d 453 (R.I. 2002) (citation omitted). The Supreme Court has also established that it will not interpret legislative enactments in a manner that renders them nugatory or that would produce an unreasonable result. See *Defenders of Animals v. Dept. of Environmental Management*, 553 A.2d 541 (R.I. 1989) (citation omitted). In cases where a statute may contain ambiguous language, the Court has consistently held that the legislative intent must be considered. *Providence Journal Co. v. Rodgers*, 711 A.2d 1131 (R.I. 1998). The statutory provisions must be examined in their entirety and the meaning most consistent with the policies and purposes of the legislature must be effectuated. *Id.*

### B. Relevant Statute and Regulation

Pursuant to R.I. Gen. Laws § 44-18-18, Rhode Island imposes a sales tax of 7% on gross receipts of a retailer. Pursuant to R.I. Gen. Laws § 44-18-19, the retailer is responsible for the collection of sales tax. Pursuant to R.I. Gen. Laws § 44-18-20, a use tax is imposed on the storage, use or consumption of tangible personal property. As explained in *Dart Industries, Inc. v. Clark*, 696 A.2d 306, 309 (R.I.1997), “[t]he use tax . . . is a complement to Rhode Island's sales tax . . . The sales tax applies to ‘sales at

retail in this state.’ (citation omitted). The use tax, in contradistinction, is imposed on ‘the storage, use, or other consumption in this state of tangible personal property.’”

R.I. Gen. Laws § 44-18-25 presumes that all gross receipts are subject to sales tax and all use of tangible personal property is subject to use tax and that the burden of proving otherwise falls on the taxpayer. Said statute is as follows:

Presumption that sale is for storage, use, or consumption —Resale certificate. — It is presumed that all gross receipts are subject to the sales tax, and that the use of all tangible personal property is subject to the use tax, and that all tangible personal property sold or in processing or intended for delivery or delivered in this state is sold or delivered for storage, use, or other consumption in this state, until the contrary is established to the satisfaction of the tax administrator. The burden of proving the contrary is upon the person who makes the sale and the purchaser, unless the person who makes the sale takes from the purchaser a certificate to the effect that the purchase was for resale. The certificate relieves the person making the sale from the burden of proof only if taken in good faith from a person who is engaged in the business of making sales at retail and who holds a permit as provided in section § 44-19-2 and 44-19-3 and who, at the time of the making the purchase, intends to sell what is so purchased in the regular course of business or is unable to ascertain at the time of purchase whether what is purchased will be sold or will be used for some other purpose. The certificate shall contain any information and be in the form that the tax administrator may require.<sup>3</sup>

R.I. Gen. Laws § 44-19-27<sup>4</sup> requires every person storing or using tangible personal property in this State to keep books, records, receipts, etc. R.I. Gen. Laws § 44-

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<sup>3</sup> This is the version that was in effect during the audit period. It was amended effective January 1, 2007. See PL 2006, ch. 246, Art. 30 § 9. It also has been amended subsequently as well.

<sup>4</sup> R.I. Gen. Laws § 44-19-27 states in part as follows:

Records required – Users – Collectors of taxes – Promoters – Inspection and preservation of records. – (a) Every person storing, using, or consuming in this state tangible personal property purchased, leased, or rented from a retailer, or from a person other than a retailer in any transaction involving a taxable casual sale, shall keep books, records, receipts, invoices, and other pertinent papers in the form the tax administrator may require. Those books, records, receipts, invoices, and other papers shall at all reasonable times be open to the inspection of the tax administrator and his or her agents.

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(d) The records shall be available for inspection and examination at any time upon demand by the tax administrator or his or her authorized agent or employee and preserved for a period of three (3) years, except that the tax administrator may consent to their destruction within that period or may require that they be kept longer.

19-27.1<sup>5</sup> authorizes the Division to examine taxpayers' records in order to determine the correctness of any tax return filed or the amount of any tax imposed.

The Division's Regulation SU 95-114 *Use Tax – Payment of by Purchasers* ("SU 95-114")<sup>6</sup> states that purchasers shall be liable for the payment of tax "unless receipts are obtained from the sellers." Said regulation states as follows:

Purchasers of tangible personal property, the storage, use, or other consumption of which is subject to the use tax, must pay the tax:

**Business Purchases:**

- (1) to the person from whom such property is purchased if such person holds a seller's permit, or a certificate of authority to collect tax, under the Sales and Use Tax Act,
- (2) directly to the Tax Administrator if the person from whom the tangible personal property is purchased does not hold such a permit or certificate.

**Individual Consumer Purchases:**

Individual consumers may pay the tax when filing their personal income tax return by entering the amount of use tax due on the appropriate line on RI Form 1040.

Purchasers should not pay the tax to a person who does not hold a seller's permit or a certificate of authority to collect tax. Purchasers will be liable for payment of the tax to the Tax Administrator unless receipts are obtained from sellers holding a retailer's permit or a certificate of authority to collect tax.

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<sup>5</sup> R.I. Gen. Laws § 44-19-27.1 states as follows:

Examination of taxpayer's records – Witnesses. – The tax administrator and his or her agents for the purpose of ascertaining the correctness of any return, report, or other statement required to be filed under chapters 18 or 19 of this title or by the tax administrator under those chapters, or for the purpose of determining the amount of any tax imposed under the provisions of those chapters, may examine any books, papers, records, or memoranda bearing upon the matters required to be included in the return, report, or other statement, and may require the attendance of the person executing the return, report, or other statement, or of any officer or employee of any taxpayer, or the attendance of any other person, and may examine the person under oath respecting any matter which the tax administrator or his or her agent deems pertinent or material in determining the liability of any person to a tax imposed under the provisions of chapters 18 or 19 of this title.

<sup>6</sup> This regulation was effective from January 1, 1995 to December 1, 2011 so was effective during the audit period.

The Division's Regulation SU 87-90 *Receipts for Use Tax Paid to Retailers* ("SU 87-90") sets forth the requirements of what must be included in receipts issued by retailers and given to purchasers. Said regulation also requires that purchasers will be liable for payment of tax to the State "unless they obtain and retain for inspection receipts as herein provided." Said regulation provides as follows:

Each retailer required or authorized to collect use tax from purchasers must give a receipt to each purchaser for the amount of tax collected. The receipt need not be in any particular form but must show the following:

- (1) The name and place of business of the retailer.
- (2) The serial number of the retailer's permit to engage in business as a seller or the serial number of the retailer's certificate of authority to collect use tax.
- (3) The name and address of the purchaser.
- (4) A description identifying the property sold to the purchaser.
- (5) The date on which the property was sold.
- (6) The sale price of the property.
- (7) The amount of tax collected by the retailer from the purchaser.

A sales invoice containing the data required above, together with evidence of payment of such sales invoice, will constitute a receipt.

Purchasers will be liable for payment of the tax to the state unless they obtain and retain for inspection receipts as herein provided.

### **C. Arguments**

The Taxpayer argued that it does not have invoices for all its payments but has invoices from some of the same vendors used by the Taxpayer that show those vendors collected sales tax so based on those invoices, it should be concluded that sales tax was collected by those same vendors even when the Taxpayer does not have invoices for its purchases. The Taxpayer also argued that some invoices were for professional services so no tax was owed. The Taxpayer argued that some of the items assessed were for credit card purchases or some of the invoices were for loans among the various entities so not

all invoices were for purchases. The Taxpayer admitted it owed 2% tax on some items purchased in Massachusetts.

The Division argued that there are no invoices supporting the payment of sales tax so the conclusion must be that sales tax was not paid. The Division argued that credit cards and other invoices were listed on the asset depreciation schedule so were taxed as assets and without the back up records those items have to be assessed. The Division argued that it is the obligation of the Taxpayer to maintain records.

**D. Whether the Taxpayer Owes the Assessed Tax**

In this matter, the Taxpayer has belatedly<sup>7</sup> tried to gather the records for the purchases and assets. The Owner testified that she relied on the wrong people for recordkeeping and understands that the businesses' recordkeeping was not good.

Pursuant to R.I. Gen. Laws § 44-18-25, the burden of proof is on the Taxpayer rather than the Division since the statute provides for a statutory presumption that all items purchased or sold are subject to tax unless the "contrary" is established by a taxpayer to the satisfaction of the Tax Administrator. The purpose of this hearing was to provide the Taxpayer with an opportunity to rebut the presumption of taxability. The burden of proof for the Taxpayer is the preponderance of the evidence.<sup>8</sup>

As stated above, by statute, a taxpayer is liable for sales or use tax and by statute, a taxpayer must keep certain records. The Division has promulgated regulations that detail the type of records that must be maintained and the tax liability if such records are failed to be maintained. R.I. Gen. Laws § 44-19-33 specifically states that the Tax

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<sup>7</sup> testified that the Taxpayer was uncooperative during the audit and the Division had to issue a summons to obtain records. See Division's Exhibit Six (6). She also testified that she did not have a closing conference with the Taxpayer because of the unresponsiveness.

<sup>8</sup> See R.I. Gen. Laws § 8-8-28 and *DeBlois v. Clark*, 764 A.2d 727 (R.I. 2003).

Administrator may prescribe regulations that are not inconsistent with the law and are reasonably designed to carry out the intent and purposes of the law and are *prima facie* evidence of the proper interpretation of statutes. SU 87-90 states that “[p]urchasers will be liable for payment of the tax to the state (sic) unless they obtain and retain for inspection receipts as herein provided.” SU 95-114 states that “[p]urchasers will be liable for payment of the tax . . . unless receipts are obtained from sellers.”

The easiest way for a taxpayer to overcome the presumption of taxability is to keep the statutory and regulatory required records.<sup>9</sup> Audits like this matter where there were few or no records have been the subject of prior administrative decisions. In a 2003 Division administrative decision (2003 WL 23105231), an audit found *ex tax* purchases by a taxpayer of supplies and expenses. The auditor reviewed that taxpayer’s depreciation schedules and purchase invoices. There were no records of any sales or use tax paid on the purchase invoices or of any tax paid and based on that information, the conclusion was that tax was owed. In a 1995 Division administrative decision (1990 WL 668667),<sup>10</sup> that taxpayer had no record of tax paid on a purchase and was given time to rebut presumption of taxability but was unable to provide information to the contrary so was found liable for the tax.

A 1994 Division administrative decision (1994 WL 143289) found that that taxpayer was able to apply some invoices showing when taxes were paid so that the assessment was reduced but when that taxpayer could not show such information, the

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<sup>9</sup> *Correia v. Norberg*, 391 A.2d 94 (R.I. 1978) found that there was no statutory or regulatory requirements regarding the type of evidence needed to establish out-of-state delivery so the Court accepted oral testimony regarding delivery. However, the Division has promulgated regulations requiring certain documentary proof of payment of tax by purchasers and that the lack thereof results in owing said tax.

<sup>10</sup> The decision was issued by the Division of Taxation on June 20, 1995; though, Westlaw assigned it a 1990 date in its citation.

assessment was not reduced. The decision found that the ability to overcome the taxability presumption with invoice records was a reason it is “so important to retain all the invoices (both sales and purchases) representing expenses of a business (bills paid) or the income of a business.” The decision concluded that “[o]nly scrupulous recordkeeping could verify the claims of nontaxability.” (p. 4 of decision).

In this matter, the Taxpayer did not have the requisite records nor have any other type of records, invoices, receipts, or back-up materials demonstrating the payments were what the Owner testified they were.<sup>11</sup> A prior Division administrative decision has found that since the law is clear in requiring specific records to be kept, it cannot be the intent to require a hearing officer to accept just the bare testimony of a taxpayer’s business dealings. See 1990 WL 204412. A taxpayer must overcome the presumption of taxability to the satisfaction of the Tax Administrator. The required records would overcome the presumption as some other type of records might (e.g. sellers’ records, receipts, etc.).

The Taxpayer argues that an inference should be made based on invoices that tax was paid on certain items as the sellers usually collected tax based on the sellers’ other invoices. However, the Taxpayer is unable to provide any records linked to the specific assessed sales. The Taxpayer also argues that some items were loans or checks for services. The Taxpayer did not have any documentary evidence of checks being for loans or payment for field trips as testified to. The Taxpayer provided evidence regarding Rhode Island registered companies and Rhode Island companies providing services and argued that inferences should be made that those companies charged tax

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<sup>11</sup> See *M&A Distributors, Inc. v. Division of Taxation*, CA 74-1142 (3/1/76) 1976 WL 181963 (unreported Superior Court decision). This case discusses how a seller who takes from the purchaser a resale certificate is relieved of the burden of taxability and that the presumption of taxability can be rebutted with the prescribed evidence (in this case a resale certificate) or the seller must show to the satisfaction of the Tax Administrator that the receipts are attributable to an exempt category.

when necessary but not when they only provided services. However, the Taxpayer had no documentary evidence demonstrating that the claimed payments were only for services and not for goods (e.g. for contractor). The Taxpayer did not present either the required records or other types of records that could substantiate the Owner's testimony needed to overcome the presumption of taxability.

A presumption of taxability cannot be overcome by inference and testimony without some kind of back up documentary materials for each specific payment. To find otherwise would render the recordkeeping statute and presumption of taxability statute as well as the regulations meaningless.

It is the Taxpayer's statutory and regulatory obligation to maintain all appropriate records. The Division gave the Taxpayer an opportunity to produce additional records. Based on the records produced, pursuant to R.I. Gen. Laws § 44-19-14,<sup>12</sup> the Division made an estimate of the tax owed by the Taxpayer. There has been no showing by the Taxpayer that the methodology used by the Division was improper or incorrect. See 2010 WL 3948095 (Division administrative decision). Finally, as no return was filed by

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<sup>12</sup> R.I. Gen. Laws § 44-19-14 states as follows:

Determination without return – Interest and penalties. – If any person fails to make a return, the tax administrator shall make an estimate of the amount of the gross receipts of the person or, as the case may be, of the amount of the total sales price of tangible personal property sold or purchased by the person, the storage, use, or other consumption of which in this state is subject to the use tax. The estimate shall be made for the month or months in respect to which the person failed to make a return and is based upon any information, which is in the tax administrator's possession or may come into his or her possession. Upon the basis of this estimate, the tax administrator computes and determines the amount required to be paid to the state, adding to the sum arrived at a penalty equal to ten percent (10%) of that amount. One or more determinations may be made for one or for more than one month. The amount of the determination, exclusive of penalties, bears interest at the annual rate provided by § 44-1-7 from the fifteenth (15th) day after the close of the month for which the amount or any portion of the amount should have been paid until the date of payment. If the failure of any person to file a return is due to fraud or an intent to evade the provisions of this chapter and chapter 18 of this title, a penalty of fifty percent (50%) of the amount required to be paid by the person, exclusive of penalties, is added to the amount in addition to the ten percent (10%) penalty provided in this section. After making his or her determination, the tax administrator shall mail a written notice of the estimate, determination, and penalty.

the Taxpayer, pursuant to R.I. Gen. Laws § 44-19-13<sup>13</sup> and Regulation SU 87-115 *Use Tax Statute of Limitation*,<sup>14</sup> the Division properly made an assessment covering six (6) years.<sup>15</sup>

#### **F. Interest and Penalties**

The Division properly imposed interest and penalties on the assessments pursuant to R.I. Gen. Laws § 44-19-14 which provides for interest and penalties for deficiencies where no returns were filed. See Division's Exhibits Ten (10) (interest calculation) and 13 (revised workpapers). This statute provides that if a taxpayer does not pay a tax because of negligence (e.g. poor records) or does not pay, a 10% penalty is imposed. See *Brier Mfg. Co. v. Norberg*, 377 A.2d 345 (R.I. 1977).

### **VI. FINDINGS OF FACT**

1. On or about August 5, 2009, the Division issued a Notice of Hearing and Appointment of Hearing Officer to the Taxpayer.
2. A hearing was held on December 14, 2012 and January 31, 2013 with the parties resting on the record.

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<sup>13</sup> R.I. Gen. Laws § 44-19-13 states as follows:

Notice of determination. — The tax administrator shall give to the retailer or to the person storing, using, or consuming the tangible personal property a written notice of his or her determination. Except in the case of fraud, intent to evade the provisions of this article, failure to make a return, or claim for additional amount pursuant to §§ 44-19-16 – 44-19-19, every notice of a deficiency determination shall be mailed within three (3) years after the fifteenth (15th) day of the calendar month following the month for which the amount is proposed to be determined or within three (3) years after the return is filed, whichever period expires later, unless a longer period is agreed upon by the tax administrator and the taxpayer.

<sup>14</sup> Said regulation provides in part as follows:

Use Tax — Statute of Limitations

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Where a taxpayer or retailer who is required to file a return under the provisions of the sales and use tax law fails to do so, the statute of limitations is inoperative against the State and an assessment covering a period of six (6) years may be made.

<sup>15</sup> See also *Couture v. Norberg*, 338 A.2d 538 (R.I. 1975).

3. The facts contained in Sections IV and V are reincorporated by reference herein.

**VII. CONCLUSIONS OF LAW**

Based on the testimony and facts presented:

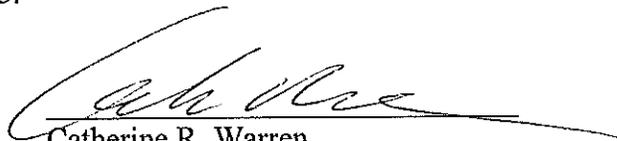
1. The Division has jurisdiction over this matter pursuant to R.I. Gen. Laws § 44-1-1 *et seq.*, R.I. Gen. Laws § 44-18-1 *et seq.*, and R.I. Gen. Laws § 44-19-1 *et seq.*
2. The Taxpayer was unable to overcome the presumption of taxability.

**VIII. RECOMMENDATION**

Based on the above analysis, the Hearing Officer recommends as follows:

As set forth above, the Taxpayer did not overcome the presumption of taxability contained in R.I. Gen. Laws § 44-18-25 so owes the tax, interest, and penalties assessed by the Division pursuant to R.I. Gen. Laws § 44-1-1 *et seq.* and R.I. Gen. Laws § 44-19-1 *et seq.* See Division's Exhibits 11 and 13.

Date: March 14, 2013

  
Catherine R. Warren  
Hearing Officer

**ORDER**

I have read the Hearing Officer's Decision and Recommendation in this matter, and I hereby take the following action with regard to the Decision and Recommendation:

ADOPT  
 REJECT  
 MODIFY

Date: March 27, 2013

  
David Sullivan  
Tax Administrator

**NOTICE OF APPELLATE RIGHTS**

**THIS DECISION CONSTITUTES A FINAL ORDER OF THE DIVISION. THIS ORDER MAY BE APPEALED TO THE SIXTH DIVISION DISTRICT COURT PURSUANT TO THE FOLLOWING WHICH STATES AS FOLLOWS:**

**R.I. Gen. Laws § 44-19-18 Appeals**

Appeals from administrative orders or decisions made pursuant to any provisions of this chapter are to the sixth (6th) division district court pursuant to chapter 8 of title 8. The taxpayer's right to appeal under this chapter is expressly made conditional upon prepayment of all taxes, interest, and penalties, unless the taxpayer moves for and is granted an exemption from the prepayment requirement pursuant to § 8-8-26.

**CERTIFICATION**

I hereby certify that on the 27th day of March, 2013 a copy of the above Decision and Notice of Appellate Rights were sent by first class mail to the Taxpayer's attorney's address on file with the Division and by hand delivery to Linda Riordan, Esquire, Department of Revenue, One Capitol Hill, Providence, RI 02908.

*Gail Belasco*