STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS

DIVISION OF TAXATION

ADMINISTRATIVE HEARING

FINAL DECISION AND ORDER

#2014-11

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DEPARTMENT OF REVENUE
DIVISION OF TAXATION
ONE CAPITOL HILL
PROVIDENCE, RHODE ISLAND 02908

IN THE MATTER OF:	:	
	:	**Case No.: 19-T-0022**
Taxpayers.	:	

DECISION

I. INTRODUCTION

The above-entitled matter came before the undersigned as the result of a Notice of Hearing and Appointment of Hearing Officer dated November 29, 2013 and issued to the above-captioned taxpayers (collectively "Taxpayer" and individually "Taxpayer Corporation" and "Taxpayer RO (for responsible officer))[1] by the Division of Taxation ("Division") in response to a request for hearing. A hearing was held on March 27, 2014. The Division and Taxpayer were represented by counsel. The parties rested on the record.

II. JURISDICTION

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.*, R.I. Gen. Laws § 44-19-1 *et seq.*, *Division of Taxation*

[1] The initial notice of hearing issued on November 29, 2013 only referred to a hearing on the sales tax assessment issued against the Taxpayer Corporation. At hearing, it was agreed by the parties that the hearing request included a request for hearing regarding the sales tax assessment against the Taxpayer Corporation as well as the assessment for same against the Responsible Officer for the Taxpayer Corporation. Thus, the hearing was for assessment for the Taxpayer Corporation and for the assessment agains (Taxpayer RO) as the Responsible Officer. At hearing, it was agreed that the Division would issue a notice of hearing for the Responsible Officer which would be considered to amend the initial notice of hearing. The notice of hearing for Taxpayer RO was issued on March 31, 2014 but relates back to the initial notice of hearing issued on November 29, 2013 and amends said notice to include the notice of hearing for the assessment for Taxpayer Corporation and Taxpayer RO.

Administrative Hearing Procedures, *Regulation AHP 97-01*, and the *Division of Legal Services Regulation 1 Rules of Procedure for Administrative Hearings*.

III. ISSUE

Whether the Taxpayer Corporation and/or Taxpayer RO owes the sales tax assessment issued by the Division.

IV. MATERIAL FACTS AND TESTIMONY

Senior Revenue Agent, testified on behalf of the Division. He testified that the Taxpayer Corporation was a liquor store with its principal place of business in Rhode Island. He testified that he audited the Taxpayer Corporation for the period of January, 2007 to October, 2011 when the business was sold. He testified that he determined that the Taxpayer Corporation owed sales tax trust funds. He testified that he based his determination on comparing the Taxpayer Corporation's 1120 Rhode Island corporate tax returns with its monthly sales tax returns. He testified that the Taxpayer Corporation's records were very poor since there were no register tapes or invoices to review. He testified that the only bank records available for the Taxpayer Corporation were from 2010 but using those bank records he confirmed that the Taxpayer Corporation's 1120 was accurate. He testified that he compared the gross sales tax to the corporate tax returns and adjusted the sales tax figures. He testified that he gave credit for any documented sales tax exemptions and he was told the business did not sell exempt items like food.[2] He testified that a fraud penalty was assessed for gross underreporting.

On cross-examination, testified that the 2010 bank records were the only available bank records so those records were the only ones with which he could compare the Taxpayer's filings. He testified that there no register tapes or invoices to show whether the Taxpayer Corporation collected taxes. He testified as to his calculations. For example, he testified that he

[2] R.I. Gen. Laws § 3-7-3 strictly limits what a liquor store can sell other than liquor.

took the amount of the tax remitted by the Taxpayer Corporation in 2007 and multiplied that figure to determine the Taxpayer Corporation's gross based on the tax collected He testified that he compared the gross with the 1120 filing amount for that year which was for over but he reduced that figure by what the sales tax would be and by any proof of exempt sales. He then took that figure (the 1120 figure minus sales tax minus exempt) and determined the difference between that figure and the gross. He testified that he used that figure to determine the monthly figure (difference was total, per month) and using the monthly figure determined the tax owed for that year. He testified that the differences increased for each year of the audit. See Division's Exhibits Five (5) (audit workpapers); Six (6) (summary of differences); and Seven (7) (interest calculation worksheet). He testified that he deducted any exemptions for which he had an exemption certificate and there was no evidence that sales tax was collected for the differences.

The parties agreed that the president of Taxpayer Corporation (in other words, the Taxpayer RO) would be the responsible officer for any taxes assessed (if assessed).

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 Statutes and Regulations

Pursuant to R.I. Gen. Laws § 44-18-18, Rhode Island imposes a sales tax of 7% upon sales at retail. 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 § 44-19-10, taxes that are due and payable by taxpayers that hold permits to make sales at retail are to be paid every month. Pursuant to R.I. Gen. Laws § 44-19-35,[3] sales taxes collected by any retailer from purchasers constitute a trust fund for the state until paid to the tax administrator.

R.I. Gen. Laws § 44-19-27[4] requires retailers to keep records of taxes collected and such records shall be open for inspection by the Division. The Division's *Sales and Use Tax*

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[3] R.I. Gen. Laws § 44-19-35 states in part as follows:

> Tax collection as property held in trust for the state. – All taxes collected by any retailer from purchasers in accordance with the provisions of chapter 18 of this title, and all taxes collected by any retailer from purchasers under color of those provisions, constitutes a trust fund for the state until paid to the tax administrator. That trust is enforceable against:
>
> (1) The retailer;
>
> (2) Any officer, agent, servant, or employee of any corporate retailer responsible for either the collection or payment, or both, of the tax.

[4] 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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> (b) Every person required to collect tax shall keep records of every sale or occupancy and of all amounts paid, charged, or due and of the tax payable, in forms the tax administrator may by regulation require. The records shall include a true copy of each sales slip, invoice, receipt, statement, or memorandum upon which § 44-19-8 requires that the tax be stated separately.

Regulation SU 89-91 ("SU 89-91")[5] [6] further details what records retailers must keep and that such records must be maintained so that the Division may conduct audits and the failure to keep such records is evidence of negligence or intent to evade tax. R.I. Gen. Laws § 44-19-27.1[7] authorizes the Division to examine taxpayers' records in order to determine the correctness of tax

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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

[5] *Division's Regulation* SU 89-91 entitled Records states in part as follows:

Each retailer as defined in the act shall keep adequate and complete records of his or her business in this state showing:

1. The gross receipts from the sales of tangible personal property including both taxable and nontaxable items and any services that are part of a sale.
2. All deductions allowed by law and claimed in filing returns.
3. Total purchase price of all tangible personal property purchased for resale and the total purchase price of all such property purchased for use or consumption in this state.

These records must include the normal books of account ordinarily maintained by the average prudent business person engaged in the activity in question, together with all bills, receipts, invoices, cash register tapes, magnetic tapes, hard or "floppy" discs or other media, or other documents of original entry supporting the entries in the books of account as well as all schedules or working papers used in connection with the preparation of tax returns.

Failure to maintain such records will be considered evidence of negligence or intent to evade the tax, and will result in the imposition of appropriate penalties.

Records based on any of the above media must be maintained for state Tax Division audits for a period of at least three years unless the destruction or other disposal of the same shall be authorized by the Tax Administrator or his/her authorized representative in writing.

[6] R.I. Gen. Laws § 44-19-33 specifically states that the Tax 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.

[7] 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.

filed or the amount of tax imposed. The burden is on a taxpayer to demonstrate that tax is not owed. See R.I. Gen. Laws § 44-18-25.[8]

The Parties agreed that the owner of Taxpayer Corporation, the Taxpayer RO, was a Responsible Officer pursuant to R.I. Gen. Laws § 44-19-35.

C. Arguments

The Division argued that the auditor had to fill in the gaps for the Taxpayer's missing records and the Division gave credit when it was shown something was exempt.

The Taxpayer argued that the assumption that the difference between the gross based on the amount remitted in sales tax and the 1120 derived gross represented collected sales tax that had not been remitted was wrong because there was no showing that the Taxpayer collected that sales tax. The Taxpayer argued that the standard for fraud is clear and convincing evidence and there was no showing that the Taxpayer took action not to report sales tax.

D. Whether the Taxpayer Owes Sales Tax

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.

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[8] R.I. Gen. Laws § 44-18-25 states 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 shall contain any information and be in the form that the tax administrator may require.

SU 89-91 details the type of records – such as register tapes, invoices, receipts - that must be maintained and provides for the tax liability if such records are failed to be maintained. The easiest way for a taxpayer to overcome the presumption of taxability is to keep the statutory and regulatory required records. Prior Division administrative decisions have addressed similar matters where there were few or no records and have found that the lack of records is evidence that tax is owed.[9]

The Taxpayer did not have the requisite records nor have any other type of records demonstrating that the taxes collected were remitted to the Division. R.I. Gen. Laws § 44-19-11[10] permits the Division to compute and determine the amount owed on the basis on any information in the Division's possession. The testimony at hearing was that the Division used what records it could obtain from the Taxpayer to determine that there were differences in the gross based on the amount of sales tax remitted and the 1120 gross so that the sales tax was collected that was not remitted to the Division. The Taxpayer had the burden to show otherwise but did not. A presumption of taxability cannot be overcome by argument, inference and/or

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[9] 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 but 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. 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 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).

[10] R.I. Gen. Laws § 44-19-11 provides as follows:

> Deficiency determinations – Interest. – If the tax administrator is not satisfied with the return or returns or the amount of tax paid to the tax administrator by any person, the administrator may compute and determine the amount required to be paid upon the basis of the facts contained in the return or returns or upon the basis of any information in his or her possession or that may come into his or her possession. One or more deficiency determinations may be made of the amount due 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 day (15th) after the close of the month for which the amount, or any portion of it, should have been paid until the date of payment.

testimony[11] without some kind of back up documentary materials for each specific sale. To find otherwise would render the recordkeeping statute and presumption of taxability statute as well as the regulation meaningless.

It is the Taxpayer's statutory and regulatory obligation to maintain all appropriate records. Based on the records produced, pursuant to R.I. Gen. Laws § 44-19-11, the Division made an estimate of the tax owed by the Taxpayer based on the available records. There has been no showing by the Taxpayer that the methodology used by the Division was improper or incorrect. See *Administrative Decision* 2010-08 (10/4/10). Rather the Taxpayer argued there was no showing that tax was not collected. However, the evidence was that there were differences between the Taxpayer Corporation's 1120 derived gross and the total sales amount based on tax remitted. The Taxpayer had no records (no invoices, no register tapes) to overcome the presumption of taxability of those differences. See Division's Exhibits Five (5), Six (6), and Seven (7).

Therefore, the Division properly assessed the Taxpayer Corporation the trust fund sales tax that it owed. See Division's Exhibit Eight (8) (Notice of Deficiency).

E. Responsible Officer

The Taxpayer RO did not dispute that he was a Responsible Officer and as such is liable for any tax assessments against the Taxpayer Corporation. Pursuant to R.I. Gen. Laws § 44-19-35, the Taxpayer RO is liable for the sales tax assessment set forth in the Notice of Deficiency. See Division's Exhibit Eight (8).

F. Interest and Penalty

Pursuant to R.I. Gen. Laws § 44-19-11, the Division properly imposed interest on the trust fund assessment. See Division's Exhibit Seven (7) (interest calculation).

[11] The Taxpayer did not present any testimony in this matter.

In addition, the Division imposed a 50% penalty on the said deficiency pursuant to R.I. Gen. Laws § 44-19-12.[12] The statute provides for a 10% penalty for negligently not paying tax but provides a 50% penalty for fraud or intent to evade the provisions of this chapter. Allegations of fraud by the Division have a burden of proof of "clear and convincing proof" (rather than a preponderance of the evidence).[13] The Taxpayer Corporation was a retailer who collected sales tax and remitted some sales tax to the Division. It clearly knew it had legal responsibility to remit collected sales tax to the Division. It failed to maintain statutory and regulatory records of sales made at retail. The failure to maintain such records under SU 89-91 is "considered evidence of negligence or intent to evade the tax." Here, there were absolutely no sales records maintained. The sales records were not incomplete but rather there was a complete absence of register tapes and invoices (etc.) to show what sales tax was collected. In light of the absence of all sales records, the Taxpayer Corporation was intending to evade the payment of tax. In light of the absence of all sales records, the Taxpayer Corporation fraudulently did not remit the tax it collected. The Division properly imposed the 50% penalty on the basis of fraud **or** the intent to evade payment of tax. Such a penalty is not discretionary because the statute provides that the penalty "is" to be added rather than "may be added." See *Brier Mfg. Co. v. Norberg*, 377 A.2d 345 (R.I. 1977).[14]

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[12] R.I. Gen. Laws § 44-19-12 states as follows:

> Pecuniary penalties for deficiencies. – If any part of the deficiency for which a deficiency determination is made is due to negligence or intentional disregard of the provisions of this chapter and chapter 18 of this title, a penalty of ten percent (10%) of the amount of the determination is added to it. If any part of the deficiency for which a deficiency determination is made is due to fraud or an intent to evade the provisions of this chapter or chapter 18 of this title, a penalty of fifty percent (50%) of the amount of the determination is added to it.

[13] See R.I. Gen. Laws § 8-8-28. Though this statute only provides for a clear and convincing standard for fraud and not for an intent to evade taxes.

[14] R.I. Gen. Laws § 44-19-13 extends the time allowed to issue a notice of deficiency in cases of fraud or intent to evade payment of tax.

VI. FINDINGS OF FACT

1. On or about November 29, 2013, the Division issued a Notice of Hearing and Appointment of Hearing Officer to the Taxpayer Corporation. Said Notice was amended to include the Taxpayer RO by notice issued on March 31, 2014.

2. A hearing was held on March 27, 2014 with the parties resting on the record.

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 Corporation was unable to overcome the presumption of taxability and is liable for the sales tax assessment.

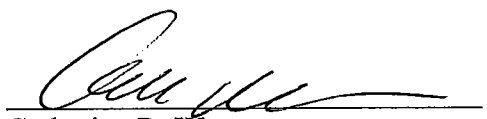
3. The Taxpayer RO is liable for the sales tax deficiency issued to the Taxpayer Corporation.

VIII. RECOMMENDATION

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

As set forth above, the Taxpayer Corporation did not overcome the presumption of taxability contained in R.I. Gen. Laws § 44-18-25 so owes the tax, interest, and penalty 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.* As the Taxpayer Corporation owes said assessment (tax, interest, penalty), the Taxpayer RO is also liable for said deficiency. See Division's Exhibit Eight (8).

Date: May 6, 2014



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:

__X__ ADOPT
_____ REJECT
_____ MODIFY

Date: May 15, 2014

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 15th day of May, 2014 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