STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS

DIVISION OF TAXATION

ADMINISTRATIVE HEARING

FINAL DECISION AND ORDER

#2016-23

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

IN THE MATTER OF:	:	**15-T-0099**
	:	**sales tax**
Taxpayer.	:	

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 September 23, 2015 and issued to the above-captioned taxpayer ("Taxpayer") by the Division of Taxation ("Division") in response to a request for hearing. A hearing was held on September 23, 2016. The Division was 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 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 owes the sales tax assessment issued by the Division.

IV. MATERIAL FACTS AND TESTIMONY

("Auditor"), Revenue Agent I, testified on behalf of the Division. She testified that she conducted a sales audit of the Taxpayer, a gas station convenience store, which covered April 1, 2011 through March 31, 2014. She testified that for the audit, the Taxpayer provided her with its general ledger, bank statements, purchase invoices, and Federal tax returns. See Division's Exhibits F (general ledger for 2011, 2012, 2013); G (Taxpayer's 1120 returns for 2011, 2012, 2013), and H (all purchase invoices reviewed in audit and summary of bank statements). She testified that the Taxpayer did not have any original sales records. She testified that she performed her audit on the best available evidence. She testified that for some months, the Taxpayer overpaid its sale tax, but for most months, the Taxpayer underpaid its sale tax. See Division's Exhibit B (Taxpayer's sales tax filings). She testified that the Taxpayer's certified public accountant ("CPA") signed the work papers receipt. See Division's Exhibit L. See also Division's Exhibit E (statute of limitations waiver).

The Auditor testified that she reviewed the purchase invoices which included invoices for tobacco, gas, and items for the store to sell, e.g. soda, snacks. She testified that some purchases were made by check and she could trace those payments in the general ledger and bank statements. She testified that some invoices were paid in cash and those cash payments could not be traced to the general ledger and bank statements. She testified that for each month she listed the bank deposits but gave credit for any bank transfers for each month and added the cash purchases for each month to obtain a total revenue for the month. She testified that from the total revenue, she subtracted gasoline purchases, lottery sales, and lottery commissions to determine the net sales. She testified that based on the

industry standard, she used a taxable measure of sales of 86.5%. She testified that percentage represents the percentage of sales made by the Taxpayer that would have been subject to sales tax. She testified that she applied the taxable measure to the net sales and came up with an amount that represented taxable sales and then determined what 7% of that amount which represented the sales tax. She testified that she credited any sales tax paid for each month, but that overall the Taxpayer owed sales tax. She testified that a Notice of Deficiency was issued on March 16, 2015 representing the amount of tax owed as well as a penalty and interest. See Division's Exhibits I (audit report); J (Schedule 1 of audit report showing calculations of net sales and applying taxable measure); M (Notice of Deficiency); and K (interest calculation as of the Notice of Deficiency).

The owner's son testified on behalf of the Taxpayer. He testified that he spoke to the CPA[1] regarding this audit. He testified that she explained to him that the Division's numbers were wrong and that the Taxpayer paid its sale tax. On cross-examination, he testified that there were no paper rolls for the cash register as they were thrown out. He testified that the CPA was told orally what to remit for sales tax. He testified that the Taxpayer did not keep the register receipts nor the daily reports of sales made.

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

[1] This CPA was the CPA who handled the audit for the Taxpayer and interacted with the Auditor on behalf of the Taxpayer during the audit. See Division's Exhibit D (power of attorney for CPA for audit).

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).

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. R.I. Gen. Laws § 44-18-25 presumes that all gross receipts are subject to sales 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, or prewritten computer software delivered electronically or by load and leave, or services as defined in § 44-18-7.3, are subject to the use tax, and that all tangible personal property, or prewritten computer software delivered electronically or by load and leave, or services as defined in § 44-18-7.3, 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.[2]

[2] This is the current version of this statute which was amended in 2011 and 2012 during the audit period for this matter. Neither amendments were relevant to the issue in this matter. The 2011 amendment inserted the provision about pre-written code. The 2011 amendment also inserted a provision regarding scenic tours which was then deleted by the 2012 amendment. The 2012 amendment also added the provision regarding R.I. Gen. Laws § 44-18-7.3. See See P.L. 2011, ch. 151, art. 19, § 24; and P.L. 2012, ch. 241, art. 21, § 3.

R.I. Gen. Laws § 44-19-27[3] requires every person storing or using tangible personal property in this State to keep books, records, receipts, etc. R.I. Gen. Laws § 44-19-27.1[4] 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 *Sales and Use Tax Regulation* SU 13-91 *Records Requirements* ("SU 13-91") delineates the type of records required to be kept. Rule 5 and Rule 6 of SU 13-91 state in part as follows:

> Rule 5 Records
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> (a) Each retailer as defined in RIGL §44-18-15 shall keep adequate and complete records of the business entity showing:
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> 1. The gross receipts from the sales of tangible personal property and services, including both taxable and nontaxable items and any services necessary to complete a sale.
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> 2. All deductions allowed by law and claimed in filing returns.

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[3] 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.

[4] 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.

3. Total purchase price of all tangible personal property or services purchased for resale and the total purchase price of all such property or services purchased for use or consumption in this state.

(b) These records, but not limited to, shall 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, all data collected or stored by means of electronic or magnetic 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.

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Rule 6 Requirement for Record Retention

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(b) 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 as provided by statute.[5]

C. Whether the Taxpayer Owes the Assessed 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. The burden of proof for the Taxpayer is the preponderance of the evidence. See R.I. Gen. Laws § 8-8-28 and *DeBlois v. Clark*, 764 A.2d 727 (R.I. 2003).

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[5] SU 13-91 was amended during the audit period. Prior to SU 13-91 which became effective on May 1, 2013, the Division had *Sales and Use Tax Regulation* SU 11-91 *Records Requirements* which replaced the Division's *Sales and Use Tax Regulation* SU 89-91 *Records Requirements* on December 1, 2011. Rule 5 of the 2011 amended regulation added the provision regarding scenic tours which was then deleted in the 2013 regulation due to the statutory amendment discussed in footnote two (2). Consistent with the statutory requirements, the three (3) versions of this regulation in effect during the audit period all require the keeping of bills, receipts, invoices, cash register tapes, and documents of original entry supporting the entries in the books of account. All versions include the provision in Rule 6 that the failure to maintain such records will be considered evidence of negligence or intent to evade tax and will result in the imposition of appropriate penalties as provided by statute.

While the Taxpayer argued that the Division's assessment was too high, the Taxpayer had no documentary evidence of the actual sales it made (as those records were not kept) so that the Division had to rely on what records were produced. The Auditor testified as to how she calculated the sales tax owed by the Taxpayer based on the available records. The Taxpayer did not offer any testimony or evidence that the Auditor's methodology was incorrect or that another method could have been used instead.

As stated above, by statute, a taxpayer is liable for sales and by statute, a taxpayer must keep certain records. The Division has promulgated regulations[6] that detail the type of records that must be maintained and the tax liability if such records are failed to be maintained. When a taxpayer cannot produce records demonstrating its sales and/or taxes collected, the Division will use the available evidence to make an assessment as provided for in R.I. Gen. Laws § 44-19-11 and R.I. Gen. Laws § 44-19-14.[7] Such audits where there

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[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] The Taxpayer remitted sales tax for some months, but not others.

R.I. Gen. Laws § 44-19-11 states 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.

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

were few or no records have been the subject of prior administrative decisions which have found that assessments are to be made on the available evidence.[8]

In this matter, the Taxpayer did not have the requisite records nor any other type of records, invoices, receipts, or back-up materials demonstrating what sales tax had been collected and/or charged. A taxpayer must overcome the presumption of taxability to the satisfaction of the Tax Administrator. A presumption of taxability cannot be overcome by inference and testimony without some kind of back up documentary materials for each specific payment.[9] 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.[10]

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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.

[8] 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. 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 concluded that "[o]nly scrupulous recordkeeping could verify the claims of nontaxability." (p. 4 of decision).

[9] 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.

[10] The matter initially came for hearing on November 16, 2015 and was continued at the request of the Taxpayer. The Taxpayer had time during the audit (see Division's Exhibit I (field report)) and during the hearing to produce any more records about sales made, but did not. At hearing, the Taxpayer's owner's son testified that those type of records had been thrown out.

Based on the records produced, pursuant to R.I. Gen. Laws § 44-19-11 and R.I. Gen. Laws § 44-19-14, 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).

D. Interest and Penalties

The Division properly imposed interest on the assessment pursuant to R.I. Gen. Laws § 44-19-11 and R.I. Gen. Laws § 44-19-14. The Division properly imposed a penalty on the assessment pursuant to R.I. Gen. Laws § 44-19-12[11] which 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 September 23, 2015, the Division issued a Notice of Hearing and Appointment of Hearing Officer to the Taxpayer.

2. A hearing was held on September 23, 2016 with the parties resting on the record.

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

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[11] 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.

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 contained in R.I. Gen. Laws § 44-18-25.

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 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.* See Division's Exhibits K and M.

Date: 10/7/16

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: 10/12/16

Neena S. Savage
Acting 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 13th day of October, 2016 a copy of the above Decision and Notice of Appellate Rights were sent by first class mail to the Taxpayer's address on file with the Division and by hand delivery to Ann Marie Maccarone, Esquire, Department of Revenue, One Capitol Hill, Providence, RI 02908.

Gail Bilasco