Cite as 3 WTD 165 (1987)

BEFORE THE INTERPRETATION AND APPEALS SECTION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

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| In the Matter of the Petition For Correction of Assessment of) | | D E T E R M I N A T I O N |
| | ) | No. 87-173 |
| | ) | |
| . . . | ) | Registration No. . . . |
| | ) | Tax Assessment No. . . . |
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[1] **RULE 17001:** FEDERAL CONTRACTORS -- USE TAX. Contractors for the federal government are liable for use tax on the value of materials supplied to the contractors by the government. Washington v. United States, 75 L. Ed. 2d 264 (1983).

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.

TAXPAYER REPRESENTED BY: . . .

DATE OF HEARING: May 12, 1987

NATURE OF ACTION:

The taxpayer petitioned for correction of a use tax assessment.

FACTS:

Normoyle, A.L.J. -- The taxpayer is a corporation engaged in the carpet installation business. It does not make retail sales, to any significant degree. During the audit period, January 1, 1982, through March 31, 1986, the taxpayer successfully bid on a number of carpet installation jobs for the United States. The work was done at Fort Lewis and McChord. The government supplied the carpeting and pads for each job. The taxpayer would go to a government warehouse, show the bid or other job identification number, was told

which carpet roll to cut from, and then transport the carpet and pad back to the job site for installation. Nothing on the bid form or any other documents in the taxpayer's possession showed the type, cost, or value of the carpeting and pad -- only the quantity. The bid forms indicated that the United States was exempt from sales tax. The taxpayer states that it was unaware that Washington law imposes a use tax in cases such as this (the tax being measured by the value of the carpeting supplied by the government). Consequently, none of its bids incorporated the use tax as part of its cost.

The auditor determined that the reasonable value of the carpeting and pads was $7 per square yard. He then multiplied that value times the amount of yards installed, and assessed use tax on that total.

The taxpayer states that:

1. It does not know what the government paid for the carpeting;

2. The government does not know what was paid for it;

3. This corporation is not a retailer and had no way of estimating the value when making the bid, even if it had known of the use tax liability.[1]

4. Not only could the corporation not value the carpeting at the time of the bid, but cannot do so today either.

ISSUES:

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[1] The corporation was represented at the hearing by its president. At the hearing, he stated that there was no way for the corporation to reasonably estimate the cost or value of the carpeting, because this corporation is an installer, not a retailer. What he forgot to mention was that he not only owns this business but also has an interest in a retail carpet store. We find it difficult to believe that he personally (or an employee of the retail store) could not visually inspect the carpeting and pad, determine its general type and quality, and arrive at a reasonable estimate of the value at the time of installation.

1. Is a contractor for the federal government liable for use tax on the value of materials supplied to the contractor by the government?

2. If so, how is the value of the carpeting to be determined?

DISCUSSION:

We start with historical background, supplied by the United States Supreme Court in Washington v. U.S., 75 L. Ed. 2d 264 (1983):

> Before 1941, (Washington) building contractors were treated as consumers for sales tax purposes. All sales of tangible personal property, such as construction materials, to contractors were subject to the sales tax. The legal incidence of this tax was on the contractor; the tax was collected by suppliers who sold to contractors, and remitted by them to the state.
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> In 1941, Washington changed the sales tax system it applied to contractors by defining the landowner who purchases construction work from the contractor, rather than the contractor, as the "consumer." The legal incidence of the tax was now on the landowner, who paid tax on the full price of the construction project. The net result was that contractors' labor costs and markups were added to the tax base, which had previously included only the cost of tangible personal property sold to contractors.
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> The post-1941 tax system could not, however, be applied to construction for the Federal Government because the Supremacy Clause prohibits states from taxing the United States directly. United States v. New Mexico, 455 U.S. 720 (1982). Thus, when the United States was the landowner, Washington did not collect any tax on the sale either of tangible personal property to the contractor or of the finished building to the Government.
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> In 1975, the Washington Legislature acted to eliminate the complete tax exemption for construction purchased by the United States. It did so by re-imposing the pre-1941 tax on contractors that work for the federal government ("federal contractors"). Thus, Washington now taxes the sale

> of non-federal projects to the landowner, and taxes the sale of materials to federal contractors. The net result is that for federal projects the legal incidence of the tax falls on the contractor rather than the landowner, and the tax is measured by a lesser amount than the tax on non-federal projects because the contractor's labor costs and markup are not included in the tax base.

We now move to a summary of the specific statutes governing tax liability of this taxpayer:

**RCW 82.04.190(6) --** The word "consumer" is defined to include anyone in business who improves real estate of the United States, such as the installation of tangible personal property for the government (here, the carpet and pads).

**RCW 82.12.010(1) --** "Value of the article used" is defined. In pertinent part, the statute reads:

> . . . That in case any such articles of tangible personal property are used in respect to the construction, repairing, decorating, or improving of, and which become or are to become an ingredient or component of, new or existing buildings or other structures under, upon, or above real property of or for the United States . . . including the installing or attaching of any such articles therein or thereto, whether or not such personal property becomes a part of the realty by virtue of installation, then the value of the use of such articles so used shall be determined according to the retail selling price of such articles, or in the absence of such a selling price, as nearly as possible according to the retail selling price at place of use of similar products of like quality and character or, in the absence of either of these selling price measures, such value may be determined upon a cost basis, in any event under such rules and regulations as the department of revenue may prescribe. (Emphasis added.)

**RCW 82.12.020(5) --** The definitions from RCW Chapter 82.04 (thus, including 82.04.190(6), above) are incorporated into RCW Chapter 82.12 (the use tax chapter).

**RCW 82.12.020 --** The use tax is imposed on "consumers" who use tangible personal property. The tax rate is identical to

the retail sales tax and is determined by multiplying that rate times "the value of the article used."

**RCW 82.12.0252 --** The use tax does not apply if the present user or his bailor or donor had already paid sales or use tax. (Such was not the case here, because the federal government is constitutionally exempt from sales or use tax.)

We now address the two specific issues. First, the question is whether or not this taxpayer is subject to the use tax. Under the facts of this case, it is clear that the taxpayer's activities fell within the use tax statutes. Because the use tax on federal contractors has been specifically upheld in Washington v. United States, cited earlier, we conclude that this taxpayer is liable for use tax, based on the value of the materials supplied by the federal government.

With regard to issue no. 2, RCW 82.12.010(1) provides three methods of valuing the carpeting: a. Retail sales price; b. comparable sales; and c. the cost approach. We can first eliminate the cost method as being inapplicable to the facts here.

The taxpayer did not provide the auditor with any information as to the retail sales price paid by the government, nor as to comparable sales. The Department determined the value as best it could, under the comparable sales method. The Department used figures supplied by a Department employee who had been involved in similar tax disputes with other installers of carpeting supplied by the federal government. This employee also discussed this matter with military purchasing personnel, and was given an average per square yard of military carpeting. The figure he arrived at, $7 per square foot, was the best approximation under the circumstances.

The burden of determining, reporting, and paying taxes falls on each taxpayer. That is, Washington's excise taxes are of a self-assessing nature. Each taxpayer is required to maintain records from which the correct tax liability may be determined. If a taxpayer does not pay a tax when due or properly make a return, "the Department shall proceed, in such manner as it deems best, to obtain facts and information on which to base its estimate of the tax" and shall then assess additional taxes found to be due. RCW 82.32.050, .100.

In this case, the estimate of the value per square yard was the result of a reasonable attempt to arrive at the value under the comparable sales method of RCW 82.12.010.

Nonetheless, we believe that the taxpayer should be given an opportunity to refute that valuation. Although not exclusive, we suggest three ways by which the taxpayer may do this:

1. Request the purchasing offices of the federal agencies for whom the work was done to attempt to determine what the government paid for the carpeting supplied to the taxpayer. We are unconvinced that the taxpayer has been diligent in attempting to obtain this information. At the hearing, the taxpayer indicated that the government had refused to reimburse it for the use tax. That does not necessarily mean that the government cannot arrive at the cost of the carpeting supplied to the taxpayer.

2. If the government cannot determine what was paid for this particular carpeting, the taxpayer could request that the government provide an estimate of the cost, based on purchases of comparable carpeting by the government.

3. Failing the above, the taxpayer could have the installed carpeting or a part thereof analyzed by a carpet retailer, who would then provide an estimate of the value at the time of installation, based on the comparable sales method.

Whichever approach is used, the taxpayer will be required to provide written documentation to the auditor within thirty days of the date of this Determination. Any estimate of value arrived at by the taxpayer must be reasonable and based on credible documentation.

The taxpayer raised additional arguments at the hearing which will be briefly discussed. First, it claims a lack of knowledge of the statute imposing use tax on government contractors. Our response is:

1. The taxpayer was also audited in 1970. One of the assessments was for unpaid use tax for items purchased for use of the taxpayer. The owner of the corporation was the same then as now. He cannot claim that the use tax concept was new to him.

2. The law imposing the use tax on government contractors was enacted in 1975. That same year, the Department issued an excise tax bulletin (ETB).

ETBs are published by the Department and are available to anyone who subscribes. In this case, ETB 496.08.170 specifically advised federal contractors of their use tax liability. The taxpayer could have subscribed to this service.

3. Each taxpayer is held to be knowledgeable of tax changes made by legislation. Here, as mentioned above, the statute was enacted in 1975. The saying "ignorance of the law is no excuse," is apt here.

Another argument raised by the taxpayer is that the statute places an unfair burden on federal contractors, because it is difficult, if not impossible, to arrive at the value of the materials supplied by the government. One response is that a person bidding on a government contract should request that the federal agency provide sufficient information on the cost or value of the materials, before the bid is submitted, so that the use tax can be determined and the bid made accordingly.

Another response to this last argument is that this criticism of the tax statute should be addressed to the legislature. The highest court of the land has held that the tax is constitutional. The taxpayer cannot avoid that holding simply by claiming that the tax is unfair and burdensome.

DECISION AND DISPOSITION:

The petition for correction of Tax Assessment No. . . . is denied. However, in accordance with this Determination, the Audit Section will reduce the assessment by the appropriate amount if the taxpayer, by June 27, 1987, provides written documentation of the actual value of the carpeting and pads. If the taxpayer does not provide reasonable and credible proof of value by that date, the assessment will become final in the amount of $ . . . , plus extension interest of $ . . . , for a total due of $ . . . .

DATED this 28th day of May 1987.