

Cite as Det. No. 14-0281, 34 WTD 056 (2015)

BEFORE THE APPEALS DIVISION  
DEPARTMENT OF REVENUE  
STATE OF WASHINGTON

In the Matter of the Petition for ) D E T E R M I N A T I O N  
Correction of Assessment of )  
                                    )  
                                    No. 14-0281  
                                   ...  
                                    )  
                                    Registration No. . . .  
                                    )

[1] RULE 254; RCW 82.32.070: RECORDS - SUBSTANTIATION - BEST EVIDENCE. Rule 254(3) requires taxpayers to prepare and preserve original source documents or such other records as may be necessary to substantiate gross receipts. Where a taxpayer did not provide requested business records to substantiate construction income, county construction permit information was reasonably relied upon to establish value of construction projects at issue.

[2] RULE 100; RCW 82.32.160: APPEAL PROCESS – IMPACT OF BANKRUPTCY FILING. The Department's appeal process is not an administrative or judicial proceedings stayed by 11 U.S.C.A. § 362(a), but rather is the final step in the issuance of a notice of tax deficiency authorized by 11 U.S.C.A. § 362(b)(9). Therefore, the taxpayer's filing of a Chapter 7 Bankruptcy petition does not stay the appeal process or stay the issuance of a determination.

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.

Kreger, A.L.J. – A business objects to the assessment of tax for custom construction activities asserting the company was a non-operating corporation and did not engage in business. As the Taxpayer has not provided any records or information to contest the audit, we sustain the assessment as issued.<sup>1</sup>

#### ISSUES

1. Did a Taxpayer meet its obligation to maintain suitable records to establish tax liability under RCW 82.32.070 and WAC 458-20-254 when it failed to respond to requests from the Audit Division for business records?
2. Pursuant to RCW 82.32.070 and .100, did the Department of Revenue properly base an estimate of construction income, relying on County Department of Assessments Parcel Data

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

and Contractor Permit detail, when the Taxpayer repeatedly failed to provide additional information?

3. Does the filing of a bankruptcy petition stay the appeals process initiated by the Taxpayer?

#### FINDINGS OF FACT

[Taxpayer] is a Washington corporation. The North American Industry Classification System (NAICS) code listed for the Taxpayer's business account indicated contracting activities focused on painting and wall covering services. However, county records indicated the Taxpayer was also engaged in the business of custom construction of residential homes.

In early 2013, the Audit Division (Audit) of the Department of Revenue (Department) contacted the Taxpayer to schedule an audit of the Taxpayer's business. In a phone call, between the auditor and the president of the Taxpayer, on March 30, 2013, the president stated he had sent the letter informing him of the audit to his accountant and was not sure what records needed to be produced. The president requested the auditor send him another copy of the letter notifying the business of the pending audit detailing the records to be provided, which the auditor sent. The president also requested additional time to consult with his accountant prior to the scheduling audit. The auditor agreed to call back in a week to schedule a time for the audit.

Over the next two months, the auditor continued to call the Taxpayer and attempt to schedule the audit. After subsequent phone calls where the president of the Taxpayer stated he was still working on getting the records together and requesting additional time to schedule the audit, the auditor informed the Taxpayer if the audit was not scheduled by June 5, 2013, the auditor would proceed with an estimated audit based on the information available.

On June 13, 2013, the auditor again spoke with the Taxpayer and informed him based on failure to schedule an appointment for the audit or provide any records an . . . audit based on the contractor permit values filed with the county would be used to estimate the [tax liability]. The estimated audit detail was provided to the Taxpayer; however, the Taxpayer failed to produce any records or additional information, schedule a time for a direct audit, or schedule a time to discuss the estimate of tax liability.

On July 2, 2013, the Department issued an assessment, Document No. 20140051, in the amount of \$ . . . , to the Taxpayer for additional retail sales tax and retailing Business and Occupations (B&O) tax due on unreported construction income.<sup>2</sup> The assessment was based on the review of county tax records for the sales of six residential properties in . . . Washington where the president of the Taxpayer or the Taxpayer was listed as the seller, and for which the Taxpayer was identified as the contractor on the construction permits. Audit noted, based on the Parcel Data in the . . . County Department of Assessments, the Taxpayer did not own the property upon which the building occurred.

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<sup>2</sup> The assessment was comprised of \$ . . . in retail sales tax, \$ . . . in retailing B&O tax, \$ . . . in interest, and a 5% assessment penalty of \$ . . .

The Taxpayer appealed the assessment generally alleging the business was a non-operating corporation that did not receive or generate any income. The appeal petition indicated the Taxpayer was gathering supporting documentation that would be provided; however, no additional records or information was produced.

A hearing on the appeal was scheduled for February 6, 2014.<sup>3</sup>

On February 5, 2014, the Taxpayer's bankruptcy attorney sent copies of a petition filing for Chapter 7 Bankruptcy, and asserted the filing of this petition should stay the appeal process. The ALJ contacted the bankruptcy attorney and left a message for the Taxpayer indicating because the appeal process is the last step in the assessment becoming final, it is considered part of the assessment process by the Department and accordingly is not stayed by the bankruptcy filing. The bankruptcy attorney was provided with a contact in the Attorney General's office, who works on bankruptcy matters for the Department, if he wished to discuss the matter further.

Messages were subsequently left for both the Taxpayer and the bankruptcy attorney requesting they contact the ALJ to reschedule the hearing and if the hearing was not rescheduled, the ALJ would proceed to resolve the case based on the materials available. Two additional phone calls were made to the Taxpayer on February 26, 2014 and March 31, 2014; however, the Taxpayer did not respond to these calls. The hearing was never rescheduled and no additional materials were provided.

## ANALYSIS

RCW 82.32.070 provides:

- (1) Every person liable for any fee or tax imposed by chapters 82.04 through 82.27 RCW shall keep and preserve, for a period of five years, suitable records as may be necessary to determine the amount of any tax for which he may be liable, which records shall include copies of all federal income tax and state tax returns and reports made by him. All his books, records, and invoices shall be open for examination at any time by the department of revenue.

*See also* WAC 458-20-254 (Rule 254); Det. No. 99-341, 20 WTD 343 (2001).

In this case, when contacted by the Department and [asked to produce] business records for Audit, the Taxpayer evaded scheduling an appointment for the audit and did not [produce] any of the requested business records. Audit then informed the Taxpayer it would proceed to estimate the tax liability based on the information in its possession. The authority to generate such an estimate is provided by RCW 82.32.100, which provides:

- (1) If any person fails or refuses to make any return or to make available for examination the records required by this chapter, the department shall proceed, in such manner as it may deem best, to obtain facts and information on which to base its estimate of the tax;

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<sup>3</sup> The letter setting the hearing also informed the Taxpayer in the event he failed to appear for the hearing the appeal may be decided without a hearing.

and to this end the department may examine the records of any such person as provided in RCW 82.32.110.

Washington imposes the B&O tax on the privilege of engaging in business in this state. Depending on the nature of the business activity being conducted, the tax is levied upon the value of products, the gross proceeds of sales, or the gross income of the business. RCW 82.04.220.

WAC 458-20-170 (Rule 170) is the Department's administrative rule implementing the statutes regarding construction activities, RCW 82.04.040, RCW 82.04.050, RCW 82.08.020, RCW 82.08.130, and RCW 82.12.020. Prime contractors are taxable upon the gross contract price under the retailing B&O tax classification and are required to collect from consumers the retail sales tax measured by the full or gross contract price. RCW 82.04.050(2)(b); Rule 170(3)(2). Prime contractors are also required to collect from consumers the retail sales tax measured by the full or gross contract price. See RCW 82.08.020. Speculative Builders in contrast construct buildings for sales or rental upon real estate they own.<sup>4</sup> Rule 170(2).

Contractor permit detail in . . . County identified the Taxpayer as the contractor for the construction of six residential properties in . . . , Washington. The construction permits for these properties were obtained between March of 2010 and February of 2013. Because the parcel information for the property upon which the houses were built did not identify the Taxpayer as the owner of the property on which the construction occurred, the records did not indicate a basis to consider the construction work as speculative building. Because the Taxpayer did not provide Audit with record or detail, the value of the construction detailed on the construction permit was used as the total contract price for the construction at issue. We conclude [that,] because of Taxpayer's failure to provide the requested detail on the construction activities at issue, Audit reasonably relied upon the price information in the construction permits to provide an estimate of the total contract price subject to retail sales tax and retailing B&O tax under the authority provided by RCW 82.32.100(1) for developing estimates.

We find no facts that would establish Audit abused its discretion in generating the estimate at issue. An abuse of discretion occurs when a decision rests on untenable grounds or is manifestly unreasonable. *Mayer v. Sto Indus., Inc.*, 156 Wn.2d 677, 684, 132 P.3d 115 (2006). Ample opportunity was provided to the Taxpayer to produce the requested business records and no detail was provided; so, Audit reasonably relied upon the contract price information detailed in the construction permits for the residences to estimate the taxable contract price for the construction services at issue.

We note it is the taxpayer who bears the burden of proof when contesting a tax assessment. RCW 82.32.160; .180; *Budget Rent-A-Car of Washington-Oregon, Inc. v. Dep't of Revenue*, 81 Wn.2d 171, 500 P.2d 764 (1972). The taxpayer must prove that a tax assessment should be modified or cancelled. *Group Health Co-op v. Tax Comm'n*, 72 Wn.2d 422, 433 P.2d 201 (1967). In this case, the Taxpayer has provided neither information nor any substantive argument

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<sup>4</sup> Speculative builders pay sales tax or use tax upon all materials purchased by them, and on all charges made by their subcontractors, but do not pay B&O tax on the sale or lease of the building they have constructed. Rule 170(2).

that established a basis for contesting the assessment. Accordingly, we affirm the assessment as issued.

The next question is whether the Taxpayer's filing of a Chapter 7 Bankruptcy petition provides a basis to stay the appeal at issue or preclude issuance of this determination. We conclude it does not. 11 U.S.C.A. § 362(b) details activities that are not stayed by the filing of the bankruptcy petition. 11 U.S.C.A. § 362(b)(9) authorizes the audit, issuance of a notice of tax deficiency, and the making of an assessment for any tax and issuance of a notice and demand for payment of such an assessment. 11 U.S.C.A. § 362(b)(9)(A)-(D).

The appeal process provides for the review of assessments under the authority of RCW 82.32.160. WAC 458-20-100 (Rule 100) is the administrative regulation addressing the appeal process. The appeal process provides a review of the assessment issued to the Taxpayer and the opportunity for the Taxpayer to detail a basis for the assessment to be adjusted. As detailed in Rule 100(d), the determination will notify the taxpayer in writing of the decision. In this case, the question is whether the Taxpayer has established a valid basis to adjust the assessment at issue. The determination, therefore, is the last step in the issuance of the assessment at issue rather than a separate administrative action. Having appealed the assessment at issue, the Taxpayer contested that assessment and this determination reviews that assessment and finalizes it. Accordingly, this appeals process does not fit within the administrative or judicial proceedings stayed by 11 U.S.C.A. § 362(a), but rather is the final step in the issuance of a notice of tax deficiency authorized by 11 U.S.C.A. § 362(b)(9).

#### DECISION AND DISPOSITION

Taxpayer's petition is denied.

Dated this 4th day of September, 2014.