

Taxpayer during the administrative hearing that provided a breakout of charges invoiced to its customer.

ISSUE

Whether the Department's Assessment, as adjusted, in this matter is correct under Arkansas law. Yes.

FINDINGS OF FACT/CONTENTIONS OF THE PARTIES

The Department's Representative provided the following summary of relevant facts in her Answers to Information Request:

████████████████████ (the Taxpayer) is a ██████████ based flooring installation contractor that specializes in commercial products. *See* Assessment Comments, attached as Exhibit 1. During the course of another assessment, the Department Auditor received copies of invoices and contracts documenting Taxpayer acting as a sub-contractor in Arkansas. *Id.* The Auditor sent letters to the Taxpayer, accompanied by nexus questionnaires. *See* May 4, 2015, Letter, attached as Exhibit 2; and June 5, 2015, Letter attached as Exhibit 3. ██████████, Vice-President of Sales and Marketing for the Taxpayer, called the Auditor and confirmed that the Taxpayer worked on one job in ██████████ remodeling a retail space. *See* Exhibit 1. The Auditor did not receive the requested completed nexus questionnaire and the Taxpayer did not respond to a letter from the Auditor requesting more information about Taxpayer's work in Arkansas. *See* July 23, 2015, Letter, attached as Exhibit 4. The Auditor completed the assessment using the invoices and contracts from the original separate assessment. *See* Agreement Between Contractor and Subcontractor (Flooring), attached as Exhibit 5; Agreement Between Contractor and Subcontractor (Painting), attached as Exhibit 6; Agreement between Contractor and Subcontractor (Finish Carpentry/Demolition), attached as Exhibit 7; and invoices, attached as Exhibit 8.

On October 7, 2015, the Auditor sent the Taxpayer a Summary of Findings which concluded that the Taxpayer owed ██████████ in tax, ██████████ in penalty, and ██████████ in interest. *See* Summary of Findings, attached as Exhibit 9. The next day a Proposed Assessment was sent to the Taxpayer which included a protest form and directions. *See* Notice of Proposed Assessment, attached as Exhibit 10. The Taxpayer timely filed the protest form and stated that "The General Contractor is responsible for this fee," *See* Protest Form, attached as Exhibit 11.

The Auditor testified: (1) The Taxpayer is located in [REDACTED]; (2) the Taxpayer explained that its employees were only present on a single job in Arkansas as a subcontractor for a short period of time; (3) the Taxpayer did not provide a written response to the Department's Nexus Questionnaire; (4) the Department utilized contract copies for descriptions of the services provided and invoices to determine the gross proceeds received by the Taxpayer; (5) those documents were provided by the general contractor; (6) taxable flooring services were provided by the Taxpayer with other services; (7) the invoices to the contractor provided non-itemized costs and did not separate charges for particular services; (8) if service costs for taxable and nontaxable services are combined in one charge on an invoice than the entire billed amount is taxable; (9) absent reliable evidence from the time of the transaction that separates the charges between taxable and nontaxable services, the entire proceeds for all services are taxable; (10) the invoices were deemed more representative of the service costs than the amounts provided in the separate contracts because the contract amounts for the job are prospective and necessarily conclusive of the charges; (11) the failure to file penalty was applied because the Taxpayer did not cooperate during the audit and the taxes were clearly due on the services provided; and (12) if the Taxpayer can provide reliable records to support a breakout of the charges, the Department would be willing to do an adjustment to the audit.

The Taxpayer's Representative testified: (1) the general contractor provided all materials and the amounts billed for the job only represented labor charges; (2) he has a small business which cannot afford to pay this tax bill; (3) he did not make any money on the job; (4) he is willing to enter a payment plan but cannot afford penalty and interest;

(5) he was unaware of his tax reporting duties and thought the general contractor was responsible for any tax payments; (6) the Flooring, Concrete or Ceramic Contract is vinyl composite tile, carpet, and ceramic tile installation; (7) the Painting Contract is just painting services; (8) the Finish Carpentry/Demolition is for installation of shelving and removal and replacement of ceiling tiles, representing ██████ of the total contract; (9) the contract amounts were paid in draws; (10) a ██████ cost was added to hang signs not included in the original contracts; (11) the costs provided in the individual contracts are based on a breakdown provided in the proposal²; (12) he provided the proposal before the contracts were entered; and (13) some finish materials, such as trim pieces like Johsonite Cove Base, Armstrong VCT, and sluter strip, were provided by the Taxpayer to complete the contracts.

As stated above, the Department was able to separate charges for taxable and nontaxable services and agreed to remove the proceeds that were not related to the taxable flooring services. Consequently, this decision is limited to a discussion of the taxation of the flooring services. The Department's Representative argued that the installation of flooring in an existing building is generally taxable and the Taxpayer is responsible for any sales taxes that should have been collected on its sales of flooring services. The Taxpayer's Representative argued that the general contractor was responsible for the collection of any sales taxes that should have been paid. After a general discussion of the burdens of proof in tax proceedings, the relevant legal issue shall be addressed.

² This document was received and discussed during the administrative hearing. Adjustments, discussed previously, were agreed to by the Department based on this documentation.

CONCLUSIONS OF LAW

Ark. Code Ann. § 26-18-313(c) (Supp. 2015) provides, in pertinent part, as follows:

The burden of proof applied to matters of fact and evidence, whether placed on the taxpayer or the state in controversies regarding the application of a state tax law shall be by preponderance of the evidence.

A preponderance of the evidence means the greater weight of the evidence. *Chandler v. Baker*, 16 Ark. App. 253, 700 S.W.2d 378 (1985). In *Edmisten v. Bull Shoals Landing*, 2014 Ark. 89, at 12-13, 432 S.W.3d 25, 33, the Arkansas Supreme Court explained:

A preponderance of the evidence is “not necessarily established by the greater number of witnesses testifying to a fact but by evidence that has the most convincing force; superior evidentiary weight that, though not sufficient to free the mind wholly from all reasonable doubt, is still sufficient to incline a fair and impartial mind to one side of the issue rather than the other.

The Department bears the burden of proving that the tax law applies to an item or service sought to be taxed, and a taxpayer bears the burden of proving entitlement to a tax exemption, deduction, or credit. Ark. Code Ann. § 26-18-313(d) (Supp. 2015). Statutes imposing a tax or providing a tax exemption, deduction, or credit must be reasonably and strictly construed in limitation of their application, giving the words their plain and ordinary meaning. Ark. Code Ann. § 26-18-313(a), (b), and (e) (Supp. 2015). If a well-founded doubt exists with respect to the application of a statute imposing a tax or providing a tax exemption, deduction, or credit, the doubt must be resolved against the application of the tax, exemption, deduction, or credit. Ark. Code Ann. § 26-18-313(f)(2) (Supp. 2015).

Arkansas Gross Receipts (sales) Tax generally applies to the entire gross receipts received on all sales of tangible personal property and certain specifically enumerated taxable services. Ark. Code Ann. § 26-52-301 (Repl. 2014). Flooring services are specifically listed as taxable services. Ark. Code Ann. § 26-52-301(3)(B)(i) (Repl. 2014). An exemption is provided for flooring installation services performed in newly constructed or substantially modified buildings or structures. Arkansas Gross Receipts Tax Rule GR-9.17(C)(2). No evidence was presented that the contract at issue involved a newly constructed or substantially modified building.

Sellers of services subject to Arkansas sales tax are liable for any taxes that should be collected and remitted on their provided services. Ark. Code Ann. § 26-52-508 (Repl. 2014). Ark. Code Ann. § 26-52-307 (Repl. 2014) provides as follows when discussing the sales to contractors:

(a)(1) Sales of services and tangible personal property, including materials, supplies, and equipment, made to contractors who use them in the performance of any contract are declared to be sales to consumers or users and not sales for resale.

(2) Subsequent transfers of title or possession of the property used in the performance of a contract by contractors are not subject to the tax imposed by this chapter.

(b) Provided that, if the performance of a contract or any portion thereof by a contractor constitutes the performance of a taxable service under the terms of § 26-52-301(3), then the entire gross proceeds or gross receipts derived from the performance of the taxable services, including the sale or transfer of title or possession of any materials or supplies used or consumed in performing the taxable services shall be subject to the tax imposed by this chapter.

(c) Contractors shall be entitled to receive a gross receipts tax credit, tax offset, or refund for any gross receipts tax or use tax paid on materials or supplies used or consumed by them which become a part of real estate in performing taxable services. [Emphasis supplied.]

A “contract” is defined as “any agreement or undertaking to construct, manage or supervise the construction, erection, alteration or repair of any building or other improvement or structure affixed to real estate, including any of their component parts. The term contract shall not include a contract to produce tangible personal property.” Arkansas Gross Receipts Tax Rule GR-21(A)(2). A contractor is defined as “any person who contracts or undertakes to construct, manage or supervise the construction, erection, alteration or repair of any building or other improvement or structure affixed to real estate, including any of their component parts.” Arkansas Gross Receipts Tax Rule GR-21(A)(3).

Here, the evidence demonstrates that the Taxpayer performed services for a contractor operating under a contract and those services were utilized by the contractor in completion of a contract to remodel a building or section of a building to be occupied in [REDACTED], Arkansas. Consequently, if the services performed by the Taxpayer are taxable, those services cannot be sold to the general contractor exempt as sales for resale. Flooring services are taxable and represent [REDACTED] of the contract price according to the documentation provided from the Taxpayer; consequently, the assessment of those proceeds is sustained.

A failure to file penalty was assessed against the tax liability. Ark. Code Ann. § 26-18-208(1) (Repl. 2012) provides as follows:

In the case of a taxpayer's failure to file any return required by any state tax law on or before the date prescribed determined with regard to any extension of time for filing the return, unless it is shown that the failure is due to reasonable cause and not to willful neglect, there shall be added to the amount required to be shown as tax on the return five percent (5%) of the amount of the tax if the failure is not more than one (1) month, with an additional five percent (5%) for each additional month or fraction of a month during which the failure continues, not to exceed thirty-five percent (35%) in the aggregate

Further, lack of knowledge of publicly available statutes and rules cannot be recognized as a defense to their enforcement. 29 Am. Jur. 2d Evidence 290; see also *Edward v. US*, 334 F.2d 360 (1964) and *Jellico Coal Min. Co. v. Commonwealth*, 96 Ky. 373, 29 S.W. 26 (Ky. App. 1895). The U.S. Supreme Court has explained the reason for this legal principle as follows:

The whole course of the jurisprudence, criminal as well as civil, of the common law, points to a different conclusion. It is a common maxim, familiar to all minds, that ignorance of the law will not excuse any person, either civilly or criminally; and it results from the extreme difficulty of ascertaining what is, bonâ fide, the interpretation of the party; and the extreme danger of allowing such excuses to be set up for illegal acts, to the detriment of the public.

Barlow v. US, 32 U.S. 404, 411 (1833). The Arkansas Supreme Court has also provided that the maxim that lack of knowledge of the law is no defense applies in equal force “to acts committed or omitted in violation of the criminal or civil laws of the land.” *State v. Simmons*, 1 Ark. 265, 266 (1839). Consequently, the lack of knowledge of the legal requirements cannot be considered in the analysis regarding alleged violations.

Here, the Taxpayer was obligated to file and remit Arkansas sales tax on its charges for flooring services, the general contractor could not purchase those services exempt as sales for resale, and the Taxpayer’s lack of knowledge of these requirements cannot be recognized as a defense to the imposition of a penalty. Consequently, the penalty assessed (after adjustment to the audit to remove the non-flooring proceeds) is sustained.

Interest was properly assessed upon tax deficiencies for the use of the State’s tax dollars. *See* Ark. Code Ann. § 26-18-508 (Repl. 2012).

DECISION AND ORDER

The assessment, after the adjustments agreed to by the Department, is sustained in full. The file is to be returned to the appropriate section of the Department for further proceedings in accordance with this Administrative Decision and applicable law. Pursuant to Ark. Code Ann. § 26-18-405 (Supp. 2015), unless the Taxpayer requests in writing within twenty (20) days of the mailing of this decision that the Commissioner of Revenues revise the decision of the Administrative Law Judge, this decision shall be effective and become the action of the agency. The revision request may be mailed to the Assistant Commissioner of Revenues, P.O. Box 1272, Rm. 2440, Little Rock, Arkansas 72203. The Commissioner of Revenues, within twenty (20) days of the mailing of this Administrative Decision, may revise the decision regardless of whether the Taxpayer has requested a revision.

The Taxpayer may seek relief from the final decision of the Administrative Law Judge or the Commissioner of Revenues on a final assessment by following the procedure set forth in Ark. Code Ann. § 26-18-406 (Supp. 2015).

OFFICE OF HEARINGS & APPEALS



TODD EVANS
ADMINISTRATIVE LAW JUDGE

DATED: August 9, 2016