

## DECISION OF MUNICIPAL TAX HEARING OFFICER

Decision Date: February 22, 2007

Decision: MTHO #332

Taxpayer: *Taxpayer ABC*

Tax Collector: City of Mesa

Hearing Date: None

### DISCUSSION

#### Introduction

On October 20, 2006, *Taxpayer ABC* (“Taxpayer”) filed a protest of a tax assessment made by the City of Mesa (“City”). After review, the City concluded on November 3, 2006, that the protest was timely and in the proper form. On November 7, 2006, the Municipal Tax Hearing Officer (“Hearing Officer”) classified the matter as a redetermination and ordered the City to file a response to the protest on or before December 22, 2006. On December 18, 2006, the City filed a response. On December 22, 2006, the Hearing Officer ordered the Taxpayer to file any reply on or before January 22, 2007. On January 19, 2007, Taxpayer filed a reply. On January 24, 2007, the Hearing Officer indicated the record was closed and a written decision would be issued on or before March 12, 2007.

#### City Position

The City performed an audit of the Taxpayer for the period April 1, 1998 through March 31 2004. As a result of the audit, the City assessed Taxpayer for additional taxes in the amount of \$36,832.40, penalties of \$2,207.32, and interest up through August 31, 2006 in the amount of \$17,619.60. According to the City, Taxpayer manufactures scented candles and miscellaneous items that are provided to distributors and retailers in the State and out-of-State. The City indicated Taxpayer established a website in January 2001 for retail sales and obtained a City license to report the sales. The City noted that prior to January 2001, Taxpayer considered the sales to be exempt resale orders and did not have a license. According to the City, Taxpayer was located at *Address ABC* in the City when the audit was initiated. Subsequently, Taxpayer moved into a new office building in the City of Chandler in May 2004. The City assessed tax on the sales to two of Taxpayer’s customers, *Customer 1* and *Customer 2* which Taxpayer had claimed as exempt sales. The City noted that City Code Section 5-10-360 (“Section 360”) provides that all exemptions are conditional upon adequate proof and documentation being provided by the taxpayer. According to the City, Regulations 5-10-350.1(d)(1) (“Regulation 350.1 and 5-10-360.1 (“Regulation 360.1”) require that a taxpayer must provide evidence sufficient to persuade a reasonably prudent businessman that the items are being acquired for resale in the ordinary course of business.

While Taxpayer had claimed that *Customer 1* had provided a sales tax exemption certificate, the City asserted that no copy was provided to the City. The City indicated that no City tax license has ever been issued to *Customer 1*. The City also noted that the transaction privilege license tax number provided for the sales to *Customer 1* was for another company, *Office Furniture Store*. Based on the City's review, no City tax was paid on the sale of the candles by Taxpayer, *Customer 1*, or *Office Furniture Store*. The City could find no mention of tax treatment in the distributor agreement between Taxpayer and *Customer 1*. As a result, the City argued they had no basis to hold *Customer 1* responsible for claiming an invalid exemption.

The City noted that Taxpayer had provided an exemption for *Customer 2* as part of its protest. After review of the certificates, the City agreed the sales to *Customer 2* were exempt from the City tax. As a result, the City recommended a reduction in tax of \$10.31 as related to the sales to *Customer 2*.

### **Taxpayer Position**

Taxpayer protested the City's assessment on sales to *Customer 1* and *Customer 2*. Taxpayer indicated they made sales to *Customer 1* from 1998 to 2004. According to Taxpayer, they entered into an agreement with *Customer 1* in 1997 whereby *Customer 1* would become an independent distributor of Taxpayer products. Taxpayer asserted that *Customer 1* provided a sales tax exemption certificate with a transaction privilege tax ("TPT") license number of 07-457965. Taxpayer noted that during the audit, the City informed Taxpayer the TPT license number was for an office furniture business located at the same address as *Customer 1*. Taxpayer also noted that *Customer 1* and the office furniture business had the same ownership. Taxpayer concluded it was fair to assume that *Customer 1* intended to account for its resale of products under the office furniture business TPT number. Taxpayer asserted it was not Taxpayer's responsibility to verify the authenticity of the TPT number. According to Taxpayer, it was always Taxpayer's practice to obtain sales tax exemption certificates. As a result, Taxpayer was confident that a certificate was obtained from *Customer 1* in 1977. However, Taxpayer indicated they could not produce a certificate for *Customer 1* because of Taxpayer's lack of understanding that any certificates had to be retained after the customer relationship had terminated and because of Taxpayer's misplacement of certificates after the three office moves during the audit period.

Taxpayer also requested any sales to *Customer 2* be considered as exempt. In support of the request, Taxpayer provided a copy of an exemption certificate for *Customer 2* with its protest.

### **ANALYSIS**

There was no dispute that Taxpayer owed additional City taxes. The only dispute was

whether or not sales to *Customer 1* and *Customer 2* were exempt sales. The burden of proof pursuant to Section 360 was on Taxpayer to demonstrate the claimed exemptions were proper. Clearly, Taxpayer met its burden of proof for *Customer 2* by providing a completed exemption certificate. While Taxpayer claimed to have an exemption certificate for *Customer 1*, Taxpayer was unable to locate the certificate in order to provide a copy to the City. While we agree with Taxpayer that it may not be their responsibility to verify the authenticity of a TPT number, it is Taxpayer's responsibility to maintain a copy of such a certificate in order to provide "reasonable evidence" that the purchaser of the product was claiming a sale for resale. If Taxpayer had a completed written document signed by *Customer 1* that claimed the sales were exempt, we would allow the claim. At this point, it would appear there is a dispute between Taxpayer and *Customer 1* on whether an exemption claim was actually made. The City should not be required to resolve that dispute. Accordingly, Taxpayer's protest of the disallowed *Customer 1* sales is denied.

### **FINDINGS OF FACT**

1. On October 20, 2006, Taxpayer filed a protest of a tax assessment made by the City.
2. After review, the City concluded on November 3, 2006, that the protest was timely and in the proper form.
3. On November 7, 2006, the Hearing Officer classified this matter as a redetermination and ordered the City to file any response on or before December 22, 2006.
4. On December 18, 2006, the City filed a response to the protest.
5. On December 22, 2006, the Hearing Officer ordered Taxpayer to file a reply on or before January 22, 2007.
6. On January 19, 2007, Taxpayer filed a reply.
7. On January 24, 2007, the Hearing Officer indicated the record was closed and a written decision would be issued on or before March 12, 2007.
8. The City performed an audit of Taxpayer for the period April 1, 1998 through March 31, 2004.
9. The City assessed Taxpayer for additional taxes due of \$36,832.40 and interest up through August 2006 in the amount of \$17,619.60.
10. Taxpayer manufactures scented candles and miscellaneous items that are provided to distributors and retailers in the State and out-of-State.

11. Taxpayer established a website in January 2001 for retail sales and obtained a City tax license to report the sales.
12. Prior to January 2001, Taxpayer considered the sales to be exempt resale orders and did not have a license.
13. In May 2004, Taxpayer moved into a new office building in the City of Chandler.
14. The City assessed tax on the sales by Taxpayer to *Customer 1* and *Customer 2*, which Taxpayer had claimed as exempt sales.
15. No City tax license has ever been issued to *Customer 1*.
16. The TPT number provided for *Customer 1* was for *Office Furniture Store*.
17. No City tax was paid on the sale of the candles by Taxpayer, *Customer 1*, or *Office Furniture Store*.
18. There was no mention of tax treatment in the distribution agreement between Taxpayer and *Customer 1*.
19. As part of its protest, Taxpayer provided an exemption certificate for *Customer 2*.
20. Taxpayer made sales to *Customer 1* from 1998 to 2004.
21. *Customer 1* and *Office Furniture Store* had the same business address and the same ownership.
22. Taxpayer was unable to provide an exemption certificate for *Customer 1*.

### CONCLUSIONS OF LAW

1. Pursuant to ARS Section 42-6056, the Municipal Tax Hearing Officer is to hear all reviews of petitions for hearing or redetermination under the Model City Tax Code.
2. Taxpayer owed additional taxes for the audit period.
3. The burden of proof was on Taxpayer pursuant to Section 360 and Regulations 350.1 and 360.1 to provide adequate proof and documentation to demonstrate sales were exempt from City tax.
4. Taxpayer met its burden of proof for *Customer 2* by providing a completed exemption certificate as part of its protest.

5. Taxpayer did not meet its burden of proof for its claimed exemption for sales to *Customer 1*.
6. Taxpayer's protest for sales to *Customer 2* should be granted and its protest for sales to *Customer 1* should be denied.

### **ORDER**

It is therefore ordered that the October 20, 2006 protest by *Taxpayer ABC* of a tax assessment made by the City of Mesa is hereby denied, in part, and granted, in part, consistent with the Discussion, Findings, and Conclusions, herein.

It is further ordered that the City of Mesa shall revise its assessment by exempting all sales to *Customer 2*.

It is further ordered that this Decision is effective immediately.

Jerry Rudibaugh  
Municipal Tax Hearing Officer