

Jerry Rudibaugh
Municipal Tax Hearing Officer

DECISION OF MUNICIPAL TAX HEARING OFFICER

Decision Date: October 2, 2003

Decision: MTHO #79

Tax Collector: City of Phoenix

Hearing Date: March 24, 2003

DISCUSSION

Introduction

On October 21, 2002, *Taxpayer* ("Taxpayer") filed a protest of a tax assessment made by the City of Phoenix ("City"). After review, the City concluded on October 24, 2002, that the protest was timely but not in the proper form. On November 4, 2002, the Municipal Tax Hearing Officer ("Hearing Officer") granted the Taxpayer an extension until December 19, 2002 to correct the form of the protest. On December 3, 2002, the Taxpayer corrected the form of the protest. On December 9, 2002, the Hearing Officer ordered the City to file a response to the protest on or before January 23, 2003. On January 17, 2003, the City filed a response to the protest. On January 23, 2003, the Hearing Officer ordered the Taxpayer to file any reply on or before February 13, 2003. A Notice of Tax Hearing ("Notice") was issued setting the matter for a March 10, 2003 hearing. On February 6, 2003, the Taxpayer requested the hearing be rescheduled. On February 11, 2003, the Hearing Officer granted the Taxpayer's request to reschedule the hearing. On February 10, 2003, a Notice was issued rescheduling the hearing for March 24, 2003. The Taxpayer and the City both appeared and presented evidence at the March 24, 2003 hearing. On March 28, 2003, the Hearing Officer ordered the City to provide their comments/recommendations to the additional documentation provided by the Taxpayer at the hearing. The Taxpayer was to file any reply on or before June 2, 2003. On May 14, 2003, the Taxpayer requested an extension to provide more information to the City. On May 16, 2003, the Hearing Officer granted the Taxpayer's request and extended the response date of the City to June 18, 2003 and the Taxpayer's reply until July 2, 2003. On June 18, 2003, the City requested an extension for their response. On June 21, 2003, the Hearing Officer granted the City an extension until July 25, 2003 and the Taxpayer an extension until August 8, 2003. On July 17, 2003, the City filed a response to the Taxpayer's additional documentation. On August 7, 2003 the Taxpayer filed a reply. On August 21, 2003, the Hearing Officer closed the record and indicated a written decision would be issued on or before October 6, 2003. On September 4, 2003, the Taxpayer filed a letter inquiring about the appeal process.

The Taxpayer was in the business of leasing or renting steel storage containers and manufacturing storage containers. The City conducted an audit for the period January 1997 through June 2000 and assessed additional taxes of \$29,066.60. In addition, the city assessed a penalty in the amount of \$2,906.66 for failure to timely pay taxes and interest up through August of 2002 in the amount of \$11,723.44.

City Position

The Taxpayer failed to maintain or provide records to support their claim that revenues were exempt from tax or that tax was paid on the purchases. According to the City, every effort was made during the audit to obtain documentation that non-taxed revenues were exempt from tax. The City asserts that City Code Section 14-350 (“Section 350”) requires that taxpayers keep and preserve adequate records to determine the amount of tax for which they are liable. Further, City Code Section 14-360(a) (“Section 360(a)”) states “all deductions, exclusions, exemptions, and credits provided in this Chapter are conditional upon adequate proof and documentation of such as may be required either by this Chapter or Regulation”. The City reviewed and provided the following comments to documentation provided by the Taxpayer prior to the hearing:

1. A claimed exemption for Indian Tribe (“*Tribe*”) would be allowed if the Taxpayer provides documentation to show that the order and delivery of the product occurred on the reservation;
2. A claimed exemption for *ABC* Contractors (“*ABC*”) was disallowed because it was not apparent that the *ABC* sells raw materials that are incorporated into construction contracting;
3. A claimed exemption for *DEF* Equipment (“*DEF*”) was disallowed because *DEF* is not in the business of selling fire equipment;
4. A prime contractor’s certificate from *GHI* Services (“*GHI*”) was disallowed because it does not include any information about the sub-contractor or project information;
5. An exemption certificate for *JKL* (“*JKL*”) does not indicate why a transaction would be exempt;
6. The Taxpayer provided sufficient documentation to demonstrate that *MNO Hospital* (“*MNO*”) was a qualifying exempt hospital;
7. A claimed exemption for *PQR* Corporation (“*PQR*”) was disallowed because *PQR* does not sell mining supplies; and,
8. A claimed exemption for *STU* (“*STU*”) was disallowed because *STU* does not sell mining supplies.

Subsequent to the hearing the Taxpayer provided additional documentation to demonstrate certain sales were exempt and that some transactions were non-taxable. After review, the City recommended adjustments to the original assessment. The City re-calculated the error rate for rental of tangible personal property to be 0.3647 percent and the error rate for retail sales to be 5.2170 percent. As a result, the privilege license tax was revised from \$18,326.43 to \$11,856.85.

Subsequent to the hearing, the Taxpayer also provided documentation for some of the fixed assets for 1998, 1999, and 2000. After review, the City concluded that the Taxpayer built many of their fixed assets and they had documents to show how much was for materials. The Taxpayer was able to show that some of the materials were taxed upon purchase and thus not subject to use tax. As a result, the City recommended the assessment be adjusted for these items. While the Taxpayer provided invoices for aluminum purchased from *XYZ* Aluminum (“*XYZ*”) on which tax was paid, the City rejected the documentation because the aluminum could not be identified to the twelve-foot PV series trailers in 1999.

The City utilized the amount of materials and parts for all fixed assets from 1998, 1999, and 2000, excluding the twelve foot PV series trailers for 1999, to determine the amount subject to use tax. As a result, the City concluded that the percentage subject to use was 55.1919 percent. The City recommended that percentage be applied to 1997 when no documentation was available and to the twelve-foot PV series trailers from 1999 when documentation could not be identified to the trailers. Utilizing the 55.1919 percent, the City recommended the use tax assessment be revised from \$17,889.43 to \$9,907.22. Because the revised tax due was now less than ten percent of the total tax paid for the audit period, the City recommended the penalty of \$2,906.66 be waived.

Taxpayer Position

The Taxpayer protested the tax assessment made by the City and asserted the total amount of taxes, penalties and interest due should be no more than \$7,000.00. According to the Taxpayer, many of the sales picked up by the City in the audit were sales that were exempt from the City tax. The Taxpayer provided additional resale certificates to the City in order to demonstrate the sales were exempt. Subsequent to the hearing, the City received the Taxpayer's additional documentation resulting in revisions to the City's tax assessment. In its August 7, 2003 letter, the Taxpayer indicated they were in agreement with the City's revised assessment for exempt sales.

The Taxpayer also protested the City's assessment of use tax in the amount of \$17,889.46. According to the Taxpayer, the majority of the assessment was on twelve-foot PV trailers built by the Taxpayer. The Taxpayer asserted they have already paid taxes on the materials used to make the trailers. According to the Taxpayer, the trailers are primarily made from aluminum and the Taxpayer pays taxes on all the aluminum they purchase. Further, the Taxpayer asserted they provided the City with a bill of materials that proves what the trailers are made of.

ANALYSIS

During the audit period, the Taxpayer had underreported rental income from tangible personal property pursuant to City Code Section 14-450 ("Section 450") and underreported retail sale revenues pursuant to City Code Section 14-460 ("Section 460"). While the Taxpayer had claimed that some of the revenues were exempt from tax, the Taxpayer failed to provide sufficient documentation to support their claim pursuant to Section 360(a). As a result, the City's initial assessment was proper. At the hearing, the Taxpayer provided additional documentation in support of its claimed exemptions. It was proper for the City to revise the error rate to reflect the new documentation provided by the Taxpayer. Accordingly, we approve the City's revised privilege license tax of \$11,856.85.

Similarly, the Taxpayer also had unreported use tax purchases during the audit period. The majority of the use tax was on twelve-foot PV trailers built by the Taxpayer. While the Taxpayer claimed they had already paid taxes on the materials used to make the trailers, no documentation was provided during the audit process to support the Taxpayer's claim. As a result, the City's original assessment was proper. At the hearing and subsequent to the hearing, the Taxpayer provided additional documentation to support its claim. It was proper for the City to review the

additional documentation and revise the use tax. It was also reasonable for the City to utilize the same percentage subject to use tax for 1997, when no documentation was available, as was calculated for 1998, 1999, and 2000. The only issue remaining was whether or not the City did not allow sufficient credit for the aluminum used to build the twelve-foot PV series trailers. While the method utilized by the City appears to be reasonable, we are concerned whether that provides a sufficient credit for the taxes paid on the aluminum utilized in building the trailers. It is the Hearing Officer's understanding that the aluminum was purchased to be used in building the trailers and tax was paid on the aluminum purchase. It is further the Hearing Officer's understanding that while each aluminum purchase may not be identifiable to a specific trailer, the purchase as a whole was utilized in building the twelve-foot PV series trailers. Based on the above, we shall order the City to recalculate the use tax assessment after allowing the Taxpayer credit for the taxes paid on the aluminum. Lastly, we find the City's recommended waiver of the penalty to be appropriate since the revised tax due was now less than ten percent of the total tax.

FINDINGS OF FACT

1. On October 21, 2002, the Taxpayer filed a protest of a tax assessment made by the City.
2. After review, the City concluded on October 24, 2002 that the protest was timely but not in the proper form.
3. On November 4, 2002, the Hearing Officer granted the Taxpayer an extension until December 19, 2002 to correct the form of the protest.
4. On December 3, 2002, the Taxpayer corrected the form of the protest.
5. On December 9, 2002, the Hearing Officer ordered the City to file a response to the protest on or before January 23, 2003.
6. On January 17, 2003, the City filed a response to the protest.
7. On January 23, 2003, the Hearing Officer ordered the Taxpayer to file any reply on or before February 13, 2003.
8. A Notice was issued setting the matter for a March 10, 2003 hearing.
9. On February 6, 2003, the Taxpayer requested the hearing be rescheduled.
10. On February 11, 2003, the Hearing Officer granted the Taxpayer's request to reschedule the hearing.
11. On February 10, 2003, a Notice was issued rescheduling the hearing for March 24, 2003.
12. The Taxpayer and the City both appeared and presented evidence at the March 24, 2003 hearing.

13. On March 28, 2003, the Hearing Officer ordered the City to provide their comments/recommendations to the additional documentation provided by the Taxpayer at the hearing.
14. The Taxpayer was to file any reply on or before June 2, 2003.
15. On May 14, 2003, the Taxpayer requested an extension to provide more information to the City.
16. On May 16, 2003, the Hearing Officer granted the Taxpayer's request and extended the response date of the City to June 18, 2003 and the Taxpayer's reply until July 2, 2003.
17. On June 18, 2003; the City requested an extension for their response.
18. On June 21, 2003, the Hearing Officer granted the City an extension until July 25, 2003 and the Taxpayer an extension until August 8, 2003.
19. On July 17, 2003, the City filed a response to the Taxpayer's additional documentation.
20. On August 7, 2003, the Taxpayer filed a reply.
21. On August 21, 2003, the Hearing Officer closed the record and indicated a written decision would be issued on or before October 6, 2003.
22. On September 4, 2003, the Taxpayer filed a letter inquiring about the appeal process.
23. The Taxpayer was in the business of leasing or renting steel storage containers and manufacturing storage containers.
24. The City conducted an audit for the period January 1997 through June 2000 and assessed additional taxes of \$29,066.66.
25. In addition, the City assessed a penalty in the amount of \$2,906.66 for failure to timely pay taxes and interest up through August of 2002 in the amount of \$11,723.44.
26. The Taxpayer failed to provide records during the audit to support their claim that revenues were exempt from tax or that tax was paid on the purchases.
27. Subsequent to the hearing, the Taxpayer provided additional documentation to demonstrate certain sales were exempt and that some transactions were non-taxable.
28. After review of the additional documentation, the City recommended adjustments to the original assessment.

29. The City recalculated the error rate for rental of tangible personal property to be 0.3647 percent and the error rate for retail sales to be 5.2170 percent.
30. As a result of the error rate change, the City revised the privilege license tax from \$18,326.43 to \$11,856.85.
31. Subsequent to the hearing, the Taxpayer also provided documentation for some of the fixed assets for 1998, 1999, and 2000.
32. After review, the City concluded that the Taxpayer built many of their fixed assets and the Taxpayer had documents to show how much was for materials.
33. The Taxpayer was able to show that some of the materials were taxed upon purchase and thus not subject to the use tax.
34. Based on the additional documentation, the City recommended the assessment be adjusted.
35. The Taxpayer provided invoices for aluminum purchased from *XYZ* on which tax was paid.
36. The City rejected the *XYZ* documentation because the aluminum could not be identified to the twelve-foot PV series trailer for 1999, to determine the amount subject to use tax.
37. The City concluded the percentage subject to use tax was 55.1919 percent.
38. The City applied the 55.1919 percent to 1997 when, no documentation was available.
39. The City also applied the 55.1919 percent to the twelve-foot PV series trailers for 1999 when documentation could not be identified to the trailers.
40. Utilizing the 55.1919 percent, the City recommended the use tax assessment be revised from \$17,889.43 to \$9,907.22.
41. Because the revised tax due was less than ten percent of the total tax paid for the audit period, the City recommended the penalty of \$2,906.66 be waived.
42. The twelve-foot PV series trailers are primarily made from aluminum and the Taxpayer paid taxes on all of the aluminum purchased.
43. The Taxpayer provided the City with a bill of materials that proves what the trailers are made of.

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. The Taxpayer had underreported rental income from tangible personal property pursuant to Section 450 and underreported retail sale revenues pursuant to Section 460.
3. Section 350 requires that taxpayers keep and preserve adequate records to determine the amount of tax for which they are liable.
4. Section 360(a) provides that all exemptions and credits are conditional upon adequate proof and documentation.
5. During the audit process, the Taxpayer failed to provide sufficient documentation to support claimed exemptions.
6. At the hearing, the Taxpayer provided additional documentation in support of its claimed exemptions.
7. It was proper for the City to review the additional documentation and revise the error rate to reflect the new documentation provided by the Taxpayer.
8. During the audit process, the Taxpayer failed to provide sufficient documentation to support its claim that it had already paid taxes on the materials used to build assets subject to the use tax.
9. At the hearing and subsequent to the hearing, the Taxpayer provided documentation to demonstrate it paid taxes on materials for some fixed assets for 1998, 1999, and 2000.
10. It was proper for the City to review the additional documentation and revise the use tax to reflect the new documentation provided by the Taxpayer.
11. The Taxpayer has not received sufficient credit for taxes paid on aluminum utilized to build the twelve-foot PV series trailers.
12. The City's recommended waiver of the penalty is appropriate since the revised tax due was now less than ten percent of the total tax.
13. The Taxpayer's protest should be granted to the extent that it is consistent with the Discussion herein.

ORDER

It is therefore ordered that the October 21, 2002 protest of *Taxpayer* of a tax assessment by the City of Phoenix is granted to the extent that it is consistent with the Discussion herein.

It is further ordered that the City of Phoenix shall revise the assessment of *Taxpayer* consistent with the conclusions in the City's July 17, 2003 letter subject to the revision for the taxes paid on the aluminum as discussed herein.

It is further ordered that this Decision is effective immediately.

Jerry Rudibaugh
Municipal Tax Hearing Officer