

REDACTED DECISION – DK# 15-102 CU-W

BY: A.M. “FENWAY” POLLACK, CHIEF ADMINISTRATIVE LAW JUDGE  
SUBMITTED FOR DECISION ON SEPTEMBER 30, 2019  
ISSUED ON DECEMBER 12, 2019

FILED

REC'D FEB 27 P 3:26  
OFFICE WEST VIRGINIA  
SECRETARY OF STATE

**BEFORE THE WEST VIRGINIA OFFICE OF TAX APPEALS  
FINAL DECISION**

On February 9, 2015, the Auditing Division of the West Virginia State Tax Department (the “Tax Commissioner” or “Respondent”) issued an Audit Notice of Assessment against the Petitioner (hereinafter “Petitioner”). This assessment was issued pursuant to the authority of the State Tax Commissioner, granted to him by the provisions of Chapter 11, Article 10 *et seq.*, of the West Virginia Code. The assessment was for combined sales and use tax for the period January 1, 2010, through December 31, 2014, for tax in the amount of \$ \_\_\_\_\_, and interest in the amount of \$ \_\_\_\_\_, for a total assessed tax liability of \$ \_\_\_\_\_.

Thereafter, on March 27, 2015, the Petitioner timely filed with this Tribunal, the West Virginia Office of Tax Appeals, a petition for reassessment. *See* W. Va. Code Ann. §§ 11-10A-8(1); 11-10A-9 (West 2010).

Subsequently, notice of a hearing on the petition was sent to the Petitioner, and, in accordance with the provisions of West Virginia Code Section 11-10A-10, a hearing was held on July 16, 2018, after which the parties filed two rounds of legal briefs. The matter became ripe for decision at the conclusion of the briefing schedule.

**FINDINGS OF FACT**

1. The Petitioner is a West Virginia S Corporation, in the business of new home construction. The Corporation was formed in 1994, and its principal place of business is in a city in West Virginia.

2. In January of 2015 the West Virginia Tax Department undertook an audit of the Petitioner's books and records. Tr. P104 at 8-10.

3. During the audit the auditors discovered various problems with the Petitioner's books and records. The first problem was that the Petitioner did not keep copies of all of the contracts it had with its customers to build their homes. Next was the fact that the Petitioner did not keep copies of the receipts/invoices for the home building materials it purchased. Finally, for the five years of the audit period, the Petitioner had not filed West Virginia sales and use tax returns.<sup>1</sup>

4. The auditors did have certain records from the Petitioner, namely some federal tax returns, general ledgers for tax years 2010-2012 and some check registers. Tr. P94 at 12-14 & Tr. P99 at 22-23.

5. The general ledgers showed many, if not all of the vendors used by the Petitioner to buy building materials. The ledgers also showed the income received by the Petitioner during the years in question.

6. Some of the income amounts in the ledgers were so small as to raise a red flag with the auditors. Tr. P93 at 19-22.

7. These deficiencies in the Petitioner's record keeping caused the auditors to make two audit determinations. First, they determined that five percent (5%) of the Petitioner's work was not capital improvements, due to the small dollar income entries in the ledgers. Next, they determined that no sales tax was paid on any material purchases where the Petitioner could not provide an invoice.

---

<sup>1</sup> Traditionally this Tribunal provides citation to the transcript for its findings of fact. In this matter, the facts in paragraph 3 were discussed at length by all three witnesses, the Petitioner's accountant, its representative, and the Tax Commissioner's only witness. There is no dispute among the parties regarding the relevant facts.

8. These two audit determinations are what led to the assessment in this matter.

### **DISCUSSION**

As is typical with so many cases before this Tribunal, neither party disputes the relevant facts. The Petitioner's record keeping was not sufficient for the Tax Commissioner to conduct a detailed audit. The issue in this matter is the propriety of how the Tax Commissioner conducted the audit. The Petitioner argues that there is no evidence that it performed work other than new home building, and that there is no evidence that it failed to pay sales and use tax on its purchases of building materials.

The basic law of this case is not in dispute. If the Petitioner is performing a service it generally must collect sales tax, however, there is an exemption if the service is contracting. *See* W. Va. Code Ann. § 11-15-8a (West). Conversely, sales tax needed to be paid on all of the materials purchased. *See* W. Va. Code Ann. § 11-15-8a and § 11-15A-2(a) (West). The requirement for Taxpayers to keep records accurate enough to allow the Tax Commissioner to properly determine sales and use tax liability is also clear and not in dispute. *See* W. Va. Code R. § 110-15-14 (1993). Finally, the Tax Commissioner's ability to conduct a sample and projection audit, such as was done in this case is also clear. *See* W. Va. Code R. § 110-15-14b (1993). However, none of these statutory or regulatory provisions answer the question before this Tribunal, namely, was it proper for the Tax Commissioner to make the determinations he made regarding the Petitioner's business. Specifically, does the Petitioner's poor record keeping allow the auditors to conclude that some of its business was not contracting, and that sales tax was not paid on certain material purchases?

The assessment in this matter is the result of two separate conclusions from the audit. First, the auditors determined that because the Petitioner's general ledger showed numerous small

income amounts, that it was possible that the Petitioner was doing non-exempt service work, such as home repairs. Next, the auditors determined that if the Petitioner could not provide invoices/receipts for material purchases, then use tax was not paid on those purchases, and they assessed use tax. At hearing and in post hearing briefs, the Petitioner argues that it only performed new home construction, and that “common sense” dictates that if it paid use and sales tax on all the purchases where invoices were provided, then it paid tax on all its purchases.

We are unpersuaded by the Petitioner’s arguments. In a hearing before the West Virginia Office of Tax Appeals on a petition for reassessment, the burden of proof is upon the Petitioner to show that any assessment of tax against it is erroneous, unlawful, void or otherwise invalid. *See* W. Va. Code Ann. § 11-10A-10(e) (West). In this matter, we cannot rule for the Petitioner, based solely upon its reiteration of the same arguments it made to the auditors. The Petitioner told the auditors that it only performed new home construction and that it paid tax on all material purchases. Due to the lack of sufficient records, the auditors were unconvinced. Now, before this Tribunal, the Petitioner argues the same points as during the audit, essentially saying “I know I kept bad records, but take my word for it.” The problem with that argument is that it ignores West Virginia law. Lots of Taxpayers keep bad records, and when that happens, according to Section 110-15-14b of Series 15, Title 110 of the West Virginia Code of State Rules, the Tax Commissioner’s auditors can rely on a sample of the Taxpayer’s records. Therefore, for the Petitioner to argue “take my word for it” and expect that to suffice is not contemplated under West Virginia law.

Therefore, we rule that the issue before this Tribunal is, has the Tax Commissioner committed an error of law, been arbitrary and capricious, or is he clearly wrong in issuing the assessment. Or put another way, was it correct for the auditors, in conducting that audit, for them

to attribute some of the Petitioner's business to repair work and to determine that not all sales and use taxes were paid?

The Petitioner has not met its burden of showing error on the Tax Commissioner's part. In post-hearing briefs, the Petitioner has provided this Tribunal with no statutory, regulatory or case law authority standing for the proposition that the audit was incorrect as a matter of law, clearly wrong, or arbitrary and capricious. More troublesome to the Petitioner's position is the testimony offered at hearing. The Petitioner presented two witnesses, a corporate representative and its accountant. Neither witness offered any explanation for the small income amounts contained in the general ledger. To be fair, the corporate representative did testify that during new home construction the lenders would often dole out the payments at specified intervals, such as when the foundation was completed, or the walls were up. However, this general testimony does not specifically explain general ledger entries showing cash payments in the hundreds of dollars. Therefore, we keep circling back to the only issue in this matter, namely, when confronted with a three hundred dollar (\$300) income notation in the ledger, what is the proper course of action for an auditor, to take the Petitioner at its word, or to attribute the income to service work?

Most problematic for the Petitioner is the testimony of its accountant. When asked the question above, regarding the propriety of the auditors' actions, he testified that what the auditors had done was proper.

JUDGE POLLACK: So isn't it normal practice, procedure, whatever term you want to use, for the auditors in a situation like that to say, well, hey, you don't have all the paperwork you need to have, so we're going to extrapolate a certain amount of tax information because you can't prove that you paid it. I mean, we've got --- in other words, we've got your list of vendors here. Sherman Paints, Joe's Tire, Bill's Block. But you don't have invoices from all of them. So we have to assess you. Isn't that correct procedure?

MR. A: If the state says so, yeah. Yeah.

JUDGE POLLACK: Well, no. But what I mean is, I'm asking you as an accountant. In other words, he doesn't have all the invoices. As a matter of fact, apparently, we're going to hear from the Tax Department's witness in a while. But presumably, judging from the list Ms. Breece was reading from, there are whole vendors where there's no invoices from them at all.

MR. A: That is correct.

JUDGE POLLACK: So as an accountant, would you say that it's proper for an auditor in that situation to say, we need to --- you know, you don't have good enough records. We have to assess you because you can't prove what you need to prove. Is that legitimate?

MR. A: It is legitimate. . . .

Tr. P78 at 1-18.

In summation, we understand the Petitioner's position, that it properly collected and paid tax regarding its contracting work and its purchases for the same. However, it has not met its burden of showing that the Tax Commissioner committed an error when his auditors did not take the Petitioner at its word on these topics. On the contrary, the Petitioner's own witness testified that what the auditors did was proper.

### CONCLUSIONS OF LAW

1. It is the duty of the Tax Commissioner to see that the laws concerning the assessment and collection of all taxes and levies are faithfully enforced. *See* W. Va. Code Ann. § 11-1-2 (West 2010).
2. "The Tax Commissioner shall collect the taxes, additions to tax, penalties and interest imposed by this article or any of the other articles of this chapter to which this article is applicable." W. Va. Code Ann. § 11-10-11(a) (West 2010).
3. Article Fifteen of the West Virginia Tax Code imposes a general consumer's sales and service tax, for the privilege of selling tangible personal property or custom software and for

the privilege of furnishing certain selected services, and it is the duty of the vendor to collect the same. *See* W. Va. Code Ann. § 11-15-1 and § 11-15-3 (West 2010).

4. The provisions of this article shall not apply to contracting services. However, purchases by a contractor of tangible personal property or taxable services for use or consumption in the providing of a contracting service shall be taxable beginning the first day of March, one thousand nine hundred eighty-nine, except as otherwise provided in this article. W. Va. Code Ann. § 11-15-8a(a) (West)

5. An excise tax is hereby levied and imposed on the use in this state of tangible personal property, custom software or taxable services, to be collected and paid as provided in this article or article fifteen-b of this chapter, at the rate of six percent of the purchase price of the property or taxable services, except as otherwise provided in this article.” W. Va. Code Ann. §11-15A-2(a) (West 2010).

6. **Keeping and Preserving Records.** - Each person shall keep complete and accurate records of taxable sales and of charges, together with a record of the tax collected thereon, and shall keep all invoices, bills of lading and such other pertinent documents in such form as the Tax Commissioner may require. W. Va. Code R. § 110-15-14.1.1. (1993).

7. Every person doing business in the State of West Virginia or storing, using, or otherwise consuming tangible personal property purchased from a vendor, and every lessor and lessee of tangible personal property used in this State shall keep complete and accurate records as are necessary for the Tax Commissioner to determine the liability of each vendor or vendee for consumer sales and use tax purposes. W. Va. Code R. § 110-15-14a.1 (1993).

8. The Tax Commissioner may use a detailed auditing procedure or a sample and projection auditing method to determine tax liability. W. Va. Code R. § 110-15-14b.2 (1993).

9. A sample and projection auditing method is appropriate if: the taxpayer's records are inadequate or insufficient, so that a competent audit for the period in question is not otherwise possible. W. Va. Code R. § 110-15-14b.3.2 (1993).

10. In a hearing before the West Virginia Office of Tax Appeals on a petition for reassessment, the burden of proof is upon the Petitioner to show that any assessment of tax against it is erroneous, unlawful, void or otherwise invalid. *See* W. Va. Code Ann. § 11-10A-10(e) (West 2010); W. Va. Code. R. §§ 121-1-63.1 and 69.2 (2003).

11. The Petitioner in this matter has not met its burden of showing that the combined sales and use tax assessment against it was erroneous as discussed above.

#### **DISPOSITION**

**WHEREFORE**, it is the final decision of the West Virginia Office of Tax Appeals that: the combined sales and use tax assessment issued against Petitioner on February 9, 2015, for a total assessed tax liability of \$\_\_\_\_\_ is hereby **AFFIRMED**.

Interest continues to accrue on these unpaid taxes until fully paid. W. Va. Code Ann. § 11-10-17(a) 2010).

#### **WEST VIRGINIA OFFICE OF TAX APPEALS**

By: \_\_\_\_\_  
A. M. "Fenway" Pollack  
Chief Administrative Law Judge

\_\_\_\_\_  
Date Entered