

JURISDICTION: OKLAHOMA TAX COMMISSION
CITE: 2006-03-21-02
ID: P-99-297
DATE: MARCH 21, 2006
DISPOSITION: DENIED
TAX TYPE: SALES/USE
APPEAL: NONE TAKEN

FINDINGS OF FACT AND CONCLUSIONS OF LAW

COMPANY and PRESIDENT, as President/CEO, SENIOR V.P., as Sr. Vice President/CFO, and VICE-PRESIDENT, as Vice President/General Counsel/Secretary, and as Individuals (hereinafter "Protestant" or "COMPANY") is represented by ATTORNEY 1, ATTORNEY 2 and ATTORNEY 3, Attorneys at Law, XYZ LAW FIRM. The Audit Division (hereinafter "Division") is represented by OTC ATTORNEY, First Deputy General Counsel, General Counsel's Office of the Oklahoma Tax Commission. A hearing was held in this matter, and upon submission of additional documents, the case was submitted for decision.

FINDINGS OF FACT

1. COMPANY is a Minnesota corporation authorized to do business in the State of Oklahoma.
2. PRESIDENT, SENIOR V.P. and VICE-PRESIDENT ("Officers") were officers of COMPANY during the audit period, May 1, 1992, through April 30, 1997.
3. COMPANY did not hold a sales tax permit, nor file sales or use tax returns during the audit period.
4. Pursuant to the competitive bidding laws of the State of Oklahoma, COMPANY contracted with the BIG CITY PUBLIC TRUST ("TRUST"), a public trust created under the laws of the State of Oklahoma, to operate and maintain the various wastewater treatment and sludge disposal facilities owned by the BIG CITY, Oklahoma, a municipal corporation, and leased to TRUST. The contracted services included sludge disposal services for the various wastewater treatment and sludge disposal facilities. The contract between COMPANY and TRUST was initially entered into December 29, 1987, and has been amended and restated from time to time, including the audit period.
5. During the audit period, COMPANY made purchases of tangible personal property for use in carrying out its duties and responsibilities under the contract. COMPANY made claims with and provided certification to numerous vendors that the purchases were exempt from sales or use tax.
6. A field audit of the books and records of COMPANY was conducted by the Division.

7. AUDITOR, auditor for the Tax Commission, testified that the auditors made no attempt to examine the records of vendors doing business with COMPANY. Only the records of Protestant have been examined. According to the testimony of AUDITOR, documentation that COMPANY had claimed exemption with some vendors was contained in the file upon audit assignment and that he also found in the COMPANY files that it was claiming exemption with some of its vendors.

8. CPA, Certified Public Accountant, indicated that COMPANY had engaged him to review the original and amended assessment report prepared by the Tax Commission. Upon review of the various transactions listed on the proposed assessment CPA stated that he found a limited number of invoices that were stamped to the effect that the purchase was being made pursuant to a public bid contract. On cross-examination, CPA indicated that in his review of Protestant's books and records, he noted invoices that were marked as exempt by the vendor but did not inquire of the vendor the reason this action was taken.

9. EMPLOYEE, an employee of COMPANY, SUBURB Water Project, since 1992, who was employed with the City of SUBURB prior to that time; testified as to the basis of his belief that the Tax Commission, in 1994, changed their position concerning the appointing of a purchasing agent by a public trust and passing through its sales tax exemption. He stated that in every instance during his tenure, a resolution was passed by the city authorizing COMPANY, as well as other contractors, to purchase materials and supplies tax exempt. During his twenty years of experience with the City of SUBURB, and later experience with COMPANY, EMPLOYEE testified that to his knowledge contractors did not pay sales or use tax on purchases made on behalf of the City or the Trust. If sales tax was itemized on any invoice from contractors, it was his testimony that the item was always marked off, because they paid no tax. He was unaware of any instance in which a contractor sought reimbursement of the tax. In his opinion, there seemed to be a change in position taken by the Tax Commission, in 1994, when he became aware of some enforcement changes.

10. Testimony was received from MANAGER, who is employed as an assistant city manager by the City of BIG CITY and as general manager of the TRUST. He stated that from commencement of his employment with the City, in August 1987, through July 1994, the City of BIG CITY and the Trust took the position that purchases made by contractors on behalf of the City or the Trust were tax exempt. Beginning in 1992, MANAGER testified that discussions were had with representatives of the Tax Commission and the City and the Trust. At these, meetings, MANAGER testified that the Tax Commission questioned the trust's ability to pass through a sales tax exemption to a contractor. MANAGER explained that it was not an issue that contractors for the city were tax exempt; it was always an issue regarding trusts. In 1993, the TRUST added contract language indicating that should sales taxes be determined to be due and owing, the Trust would pay them. In July 1994, according to MANAGER'S testimony, notice was received from the Oklahoma Tax Commission that they could no longer assign agents to make tax exempt purchases, but that any third party purchaser would be taxed. He saw the letter as a departure from the earlier position taken by the Tax Commission. MANAGER testified that prior to July 1994, no contractor ever sought reimbursement of sales taxes paid; after July 1994, the Trust changed its procedures and COMPANY was the only contractor to seek reimbursement of the taxes.

11. EMPLOYEE 2, an employee since 1994 of SUCCESSOR (formerly COMPANY) responsible for invoices, accounts payable and payroll, testified that in 1997 or 1998, she was directed to send letters to their vendors stating that COMPANY wa exempt. She added that she did not send this type of exemption letter to their vendors in 1994, 1995 or 1996: EMPLOYEE 2 stated that COMPANY began to seek reimbursement in November 1993 from BIG CITY for sales tax paid.

12. SUPERVISOR, auditor/supervisor with the Account Maintenance Division, testified that he wrote up an audit lead for the Audit Division concerning COMPANY after reviewing books and records of numerous taxpayers in which documents reflected that COMPANY was claiming exemption from the taxes

13. By letter dated September 24, 1999, the Division proposed to assess COMPANY and the Officers additional sales tax, interest and penalty, as follows:

Tax	\$215,043.55
Interest through 09/30/99	139,139.32
Delinquency Penalty	<u>21,504.48</u>
Total	\$375,687.35

14. By letter dated September 24, 1999, the Division proposed to assess COMPANY additional use tax, interest and penalty, as follows:

Tax	\$194,938.11
Interest through 09/30/99	127,281.95
<u>Delinquency Penalty</u>	<u>19,493.91</u>
Total	\$341,713.97

15. By letter dated October 22, 1999, COMPANY and the Officers filed a timely protest to the sales tax and use tax assessments.

16. Following the issuance of the proposed assessments and protest thereof, revisions were made to the proposed assessments. A *Notice of Final sales and Use Tax Adjustments* was filed by the Division on February 1, 2001. Protestant by letter dated January 29, 2001, indicated its agreement that the figures reflected in the Notice are those at issue in this Protest.

17. Pursuant to the *Notice*, the revised proposed assessment of sales tax, interest and penalty is as follows:

Tax	\$ 94,453.41
Interest through 01/31/01	85,081.02
<u>Delinquency penalty</u>	<u>9,445.28</u>
Total	\$188,979.71

18. Pursuant to the *Notice*, the revised proposed assessment of use tax, interest and penalty is as follows:

Tax	\$166,049.59
Interest through 12/31/00	145,808.98
Penalty	<u>16,604.96</u>
Total	\$328,463.53

ISSUES

I. Whether the Division properly assessed sales tax against Protestant pursuant to 68 O.S. § 1361.

II. Whether the Tax Commission is precluded from assessing sales tax against Protestant based on a statute of limitations, pursuant to 68 O.S. § 223.

III. Whether Protestant has sustained its burden of proving its purchases fall within the exemption claimed from sales tax and use tax, pursuant to 68 O.S. §§ 1356(10) and 1404(4), respectively.

IV. Whether the Tax Commission has reversed a long-standing interpretation of the Oklahoma Sales Tax Code without the approval or authorization of the Oklahoma Legislature.

CONTENTIONS

Protestant contends that the proposed sales tax assessment against it is invalid under Oklahoma law, asserting that the vendors were the parties responsible for the collection and payment of sales tax, not Protestant, and that the requirements to shift that responsibility from the vendors to the consumer were not met. Protestant further contends that the assessment is outside the three-year statute of limitations because Protestant was not required to collect and remit sales tax with respect to the transactions, but that the responsibility remained with the various vendors.

Additionally, Protestant contends that the Tax Commission has erred in its interpretation of Title 68 O.S. § 1356 with respect to the sales tax exemptions granted to governmental entities and their agents and contractors and 68 O.S. § 1404 with respect to certain exemptions from the levy of use tax. Finally, Protestant contends that the Tax Commission has made a change of a long-standing interpretation of the Sales Tax Code without intervention by the Oklahoma Legislature.

The Division contends that Protestant improperly presented certification of exemption to its vendors, and therefore the Division has the authority to issue the sales tax assessment pursuant to 68 O.S. § 1361(A). Further, the Division contends that Protestant ignores the clear and unambiguous language of 68 O.S. § 223 and did not file a sales or use tax return for any month in the audit period. Accordingly, the three-year period prescribed in Section 223 has not begun to run and the sales and use tax assessments are timely.

Additionally, the Division contends that no exemption from sales and use tax exists for the purchases by Protestant as contractor to a public trust, and thus those transactions are subject to the tax assessed. Finally, the Division contends that Tax Commission rules since 1986 have consistently stated that the purchases by agents of public trusts are not exempt from sales tax.

CONCLUSIONS OF LAW

1. The Oklahoma Tax Commission has jurisdiction of this protest. 68 O.S. 1991, § 207.

2. Sales tax is paid by the consumer or user to the vendor who, as trustee for the state, must collect and remit the tax to the state. 68 O.S. 1991, § 1361(A). Every person required to collect the tax is personally liable for the tax. *Id.* The State is to pursue collection of the tax from the liable person. *Id.*

3. A “consumer” or “user” for sales tax purposes in Oklahoma is “a person to whom a taxable sale of tangible personal property is made or to whom a taxable service is furnished.” 68 O.S. 1991, § 1352(C).

4. Upon a finding that certain circumstances exist, the Tax Commission is authorized to pursue the collection of the sales taxes from the consumer. The statutory provision authorizing such collection reads:

However, if the Oklahoma Tax Commission finds that a consumer or user improperly presented a sales tax permit or other certification or used the property purchased exempt from tax in a manner that would not have qualified for exemption, the purchaser shall be liable for the remittance of the tax, interest and penalty due thereon and the Tax Commission shall pursue collection thereof from the purchaser in any manner in which sales tax may be collected from a vendor. Upon such determination, the vendor shall be relieved of any liability for any sales tax imposed by the provisions of this section upon such vendor with respect to such sale.

68 O.S. Supp. 1996, §1361(A).

5. In support of its contention that the requirement to shift the responsibility for the payment of sales tax from the vendors to Protestant has not been met, Protestant cites *Oklahoma Administrative Code 710:65-7-6* and Commission Order No. 97-05-22-008. Both the administrative code provision and the Commission Order interpret the vendor good faith statute at 68 O.S. § 1361.1. There is not a vendor good faith requirement contained in Section 1361 of Title 68 as argued by Protestant and therefore those citations of authority are inapplicable to this issue.

6. Here; the facts show that Protestant presented certification to purchase items exempt from sales tax from its vendors. Further the facts show that Protestant was the consumer/user of

the items purchased in fulfillment of contracts with the public trust to operate and maintain wastewater treatment and sludge disposal facilities and that the purchase of same was subject to the sales tax levy. Accordingly, the Tax Commission has properly assessed Protestant for the sales tax as a consumer and properly pursued collection of the tax from Protestant.

7. In regard to whether the proposed assessments were barred by the statute of limitations, Protestant contends that the exception to the three-year limitation period is not applicable because it was not required to collect and remit sales tax with respect to the transactions; that the responsibility remained with the various vendors; that the Commission auditor made no contact with any vendor in this case; and that the three-year statute of limitation should apply. Section 223 of Title 68 is the governing statute of limitations and the pertinent part reads as follows:

§ 223. Limitation of time for assessment of taxes--Extension agreements--False or fraudulent or failure to file report or return

(a) No assessment of any tax levied under the provisions of any state tax law except as provided in the following paragraphs of this Section, shall be made after the expiration of three (3) years from the date the *return* was required to be filed or the date the return was filed, whichever period expires the later, and no proceedings by tax warrant or in Court without the previous assessment for the collection of such tax shall be begun after the expiration of such period.

* * *

(c) In the case of either a false or a fraudulent report or return, or failure to file a report or return, as required under any state tax law, the Tax Commission is authorized to compute, determine and assess the estimated amount of tax due from any information in its possession, or a proceeding in Court may be begun for the collection of such tax without assessment at any time.

8. Section 1365 of Title 68 addresses the filing of sales tax reports and provides in pertinent part as follows;

(A) The tax levied hereunder shall be due and payable on the first day of each month, except as herein provided, by any person liable to remit or pay any tax due under this article. For the purpose of ascertaining the amount of the tax payable under this article, it shall be the duty of all tax remitters, on or before the 15th day of each month, to deliver to the Tax Commission, upon forms, prescribed and furnished by it, sales tax reports signed under oath, showing the gross receipts or gross proceeds arising from all sales taxable or nontaxable *under* this article during the preceding

calendar month. Such reports shall show such further information as the Tax Commission may require to enable it to compute correctly and collect the tax herein levied.

9. Pursuant to 68 O.S. 1991, § 1352(Q), a “tax remitter is any person required to collect, report, or remit the tax imposed by this article.”

10. Under the circumstances present in this case where the Tax Commission determines that a consumer user improperly presented certification, the purchaser is liable for the remittance of the sales tax, interest and penalty due on the property purchased. In the instant case, upon evidence that Protestant had improperly presented certification, Protestant became liable to remit tax on its purchases, qualified as a tax remitter, and has failed to file sales tax reports as required by statute for any time during the audit period. Therefore, the statute of limitations set forth in Section 223 has not begun to run and the sales tax assessment is timely.

11. An excise tax is levied on the storage, use or consumption of tangible personal property in this state in Section 1402 of Title 68, which provides in pertinent part:

There is hereby levied and there shall be paid by every person storing, using, or otherwise consuming within this state, tangible personal property purchased or brought into this state, an excise tax on the storage, use, or other consumption in this state of such property at the rate of four and one-half percent (4.5%) of the purchase price of such property. ...

12. During the audit period Protestant purchased items of tangible personal property out-of-state and brought those items into this state for use or consumption. Further, Protestant failed to report and remit the applicable use tax as required by Section 1405 of Title 68.¹ Therefore, no portion of the *use tax* assessment is barred by Section 223 of Title 68.

13. The sale of tangible personal property in the State of Oklahoma, unless otherwise exempted by the provisions of the Oklahoma Sales Tax Code², is subject to an excise tax of four and one-half percent (4.5%) of the gross receipts or gross proceeds of the sale. 68 O.S. 1991, §

¹ This provision provides in pertinent part as follows:

The tax levied by this article is due and payable on the first day of each month for the preceding calendar month, and if not paid on or before the 15th day of each month shall thereafter be delinquent. Each taxpayer subject to the provisions of this article shall, on or before the 15th day of every calendar month, file with the Tax Commission on forms to be furnished by the Tax Commission, a return verified by affidavit showing in detail the total purchase price of tangible personal property used by him within the state during the preceding calendar month subject to the tax herein levied and such other information as the Tax commission may require. ...

² 68 O.S. 1991, § 1350 *et seq.*

1354(1)(A).³ Protestant urges the application of Subsection 10 of Section 1356 of the Oklahoma Sales Tax Code to otherwise exempt the transactions at issue.

14. Public trusts created pursuant to 60 O.S. § 176 are exempt from paying sales tax on their purchases. A.G. Opinion 77-106.

15. In Opinion No. 81-098, the Attorney General was asked among other questions whether a tax exempt entity, such as a school, church, county, state or trust authority could appoint, under general agency law, an agent to make purchases on behalf of the entity, and whether such purchases retain their tax exempt status under the statutory exemption granted the entity. The Attorney General answered this question in the negative.

16. As stated in Section 1356(A) of Title 68, purchases made by contractors performing services for government entities are generally subject to sales tax. An exception to the rule was codified in 68 O.S. 1981, § 1356(H), which provided as follows:

There are hereby specifically exempted from the tax levied by this article:

(H) Sale of tangible personal property or services to any county, municipality, public school district, the institutions of the Oklahoma system of higher education and the Grand River Dam Authority, or to any person with whom any of the above named subdivisions or agencies of this state has duly entered into a public contract pursuant to law, necessary for carrying out such public contract. Any person making purchases on behalf of such subdivision or agency of this state shall certify, in writing, on the copy of the invoice or sales ticket to be retained by the vendor that the purchases are made for and on behalf of such public subdivision or agency of this state and set out the name of such public subdivision or agency. Any person who wrongfully or erroneously certifies that purchases are for any of the above-named subdivisions or agencies of this state or who otherwise violates this section shall be guilty of a misdemeanor and upon conviction thereof shall be fined an amount equal to double the amount of sales tax involved or incarcerated for not more than sixty (60) days or both.

³ This section provides:

1. There is hereby levied upon all sales, not otherwise exempted in the Oklahoma Sales Tax Code, Section 1350 et seq. of this title, an excise tax of four and one-half percent (4.5%) of the gross receipts or gross proceeds of each sale of the following: -

(A) Tangible personal property

17. This section was amended in 1985 to include subcontractors to a public contract with one of the enumerated agencies or subdivisions. 68 O.S. Supp. 1985, § 1356.⁴ Rural water districts, the Northeast Oklahoma Public Facilities Authority, and the Oklahoma Municipal Power Authority were added to the list of enumerated agencies and subdivisions during the audit period. However, The BIG CITY TRUST nor public trusts created pursuant to Section 176 of Title 60 have been added.

18. As a general rule, statutes exempting property from taxation are to be applied circumspectly and are to be strictly construed against the allowance of an exemption. *Bert Smith Road Machinery Co. v. Oklahoma Tax Commission*, 563 P.2d 641 (Okla. 1977); *Phillips Petroleum Co. v. Oklahoma Tax Commission*, 542 P.2d 1303 (Okla. 1975). The language of an exemption statute may not be construed so as to give it an effect which is not intended. *Protest of Hyde*, 188 Okl. 413, 110 P.2d 292 (1941). Sales to contractors in connection with the performance of any contract with a public trust are not exempt from sales and use tax.

19. The Tax Commission, pursuant to its authority under 68 O.S. § 203 to enforce and implement the provisions of the state tax laws, by Order No. 86-05-10- 03, adopted Regulation 13-38 which addresses the sales tax exemption afforded certain governmental subdivisions and agencies as follows:

Purchases for, or on behalf of, a city county, public school district, Oklahoma state institution of higher education or the Grand River Dam Authority, pursuant to public contract and upon certification. thereof in writing on the copy of the invoice or sales ticket, are exempt from Oklahoma sales and use tax.

This exemption, shall not apply to equipment purchased by the contractor to be used to aid in the completion of the public contract.

All sales made to public trusts or agents thereof, and paid for with other than public monies, are subject to Oklahoma sales and use tax.

All other sales which are not specifically covered above, made to appointed agents of a governmental entity or public trust, are subject to Oklahoma sales and use tax.

Order No. 86-05-19-03 was properly published in accordance with Section 251 of Title 75 of the Oklahoma Statutes.

⁴ This section was recodified in 1993 as 68 O.S. § 1356(10).

20. On March 10, 1989, the Oklahoma Tax Commission adopted Rule '13:013.05 of the Oklahoma Tax Commission Permanent Rules,⁵ which provides in pertinent part:

Industrial Trust Authorities may purchase materia[exempt from sales tax, but may not appoint an agent to do so. ...

21. The rules and regulations of an administrative agency which implement the provisions of a statute are valid unless the rules and regulations are beyond the scope of the statute, are in conflict with the statute or are unreasonable. *See, Boydston v. State*, 277 P.2d 1,38 (Okla. 1954); *Arkansas Louisiana Gas Co. v. Travis*, 682 P.2d 225 (Okla. 1984); *Rutherford v. United States*, 438 F. Supp. 1287 (D.C. Okla. 1977). As a general rule, it is presumed that administrative rules and regulations are fair and reasonable and that the complaining party has the burden of proving the contrary by competent and convincing evidence. *Stiner v. Califano*, 438 F. Supp. 796 (D.C. Okla. 1977); *State ex rel. Hart v. Parham*, 412 P.2d 142 (Okla. 1966).

22. The contemporaneous construction of a statute by a department of government charged with its execution is entitled to great weight and should not be overturned without cogent reasons. *Peterson v. Oklahoma Tax Commission*, 395 P.2d 388, 391 (Okla. 1964). Where the legislature has convened many times during the period of administrative construction without expressing its disapproval, such silence may be regarded as acquiescence in or approval of the administrative construction. *See, Atlantic Refining Company v. Oklahoma Tax Commission*, 360 P.2d 826 (Okla. 1961).

23. Rules promulgated pursuant to the Administrative Procedures Act⁶ are presumed to be valid until declared otherwise by a district court of this state or the Supreme Court. 75 O.S. 1991, § 306(C). They are valid and binding on the persons they affect and have the force of law. 75 O.S. 1991, § 308.2(C). They also are prima facie evidence of the proper interpretation of the matter to which they refer. *Id.*

24. The Oklahoma courts have addressed the issue of reversal of Tax Commission policy several times. *See, E. C. Branch Trucking Co., et al. v. State of Oklahoma ex rel. Oklahoma Tax Commission*, 714 P.2d 1013 (Okla. 1985); *Mazzio's Corporation v. Oklahoma Tax Commission*, 789 P.2d 632 (Okla. Ct. App. 1989). The general rule is that absent cogent reasons, the Tax Commission may not reverse longstanding policy. In the instant cause Protestant asserted, but did not show, that the Tax Commission had a long-standing policy that purchases made by contractors pursuant to a public contract with a trust authority are exempt from sales and use tax. A reading of the policy restatement letter introduced by Protestant in support of the assertion that it illustrated a change in Commission policy, shows only that the extant statutes and the policy were misinterpreted by contractors and in fact reasserts the liability of contractors except for the narrowly-drawn statutory exceptions. The evidence demonstrates that at least since 1986 the

⁵ Amended, effective June 28, 1991, to provide that, "Trust Authorities organized pursuant to 60 O.S. 176 et seq. may purchase material exempt from sales tax, but may not appoint an agent to do so. ..." Currently codified as 710:65-13-140 of the Oklahoma Administrative Code.

⁶ 75 O.S. Supp. § 250 et. seq., § 301 et seq.

Commission has had a published and properly promulgated policy that, although trust authorities may purchase items exempt from sales and use tax, it may not appoint an agent to do so.

25. The protest should be denied.

DISPOSITION

It is the ORDER of the OKLAHOMA TAX COMMISSION, based upon the specific facts and circumstances of this case, that the sales and use tax protest of COMPANY and PRESIDENT, as President/CEO, SENIOR V.P., as Sr. Vice President/CFO, and VICE-PRESIDENT, as Vice President/General Counsel/Secretary, and as individuals, be denied.

OKLAHOMA TAX COMMISSION

CAVEAT: This decision was NOT deemed precedential by the Commission. This means that the legal conclusions are generally applicable or are limited in time and/or effect. Non-precedential decisions are not considered binding upon the Commission. Thus, similar issues may be determined on a case-by-case basis.