JURISDICTION: OKLAHOMA TAX COMMISSION
CITE: 2006-04-20-02
ID: P-04-178-H
DATE: APRIL 20, 2006
DISPOSITION: SUSTAINED IN PART/DENIED IN PART
TAX TYPE: USE TAX
APPEAL: NONE TAKEN

FINDINGS OF FACT AND CONCLUSIONS OF LAW

DENTIST d/b/a PRIVATE PRACTICE ("Protestant") appears through attorney, ATTORNEY. The Field Audit Section, Audit Division ("Division"), Oklahoma Tax Commission appears through OTC ATTORNEY, Assistant General Counsel, and OTC ATTORNEY 2, Senior Deputy Counsel, Office of General Counsel, Oklahoma Tax Commission.

On December 23, 2004, the Division forwarded the audit file to the Office of Administrative Law Judges for further proceedings consistent with the Uniform Tax Procedure Code[1] and the Rules of Practice and Procedure Before the Oklahoma Tax Commission.[2] An open hearing[3] was held on May 10, 2005, at approximately 9:45 a.m. The Protestant called one witness, DENTIST d/b/a PRIVATE PRACTICE, who testified regarding the records of the Protestant. The Protestant's Exhibits One (1) and Two (2) were identified, offered, and admitted into evidence. The Division called one witness, AUDITOR, Field Auditor, Field Audit Section, Audit Division, Oklahoma Tax Commission, who testified regarding the records of the Division. The Division's Exhibits A through L were identified, offered, and admitted into evidence. Upon conclusion of the hearing, the record was closed and the case was submitted for decision on May 10, 2005.

FINDINGS OF FACT

Upon review of the file and records, including the record of the proceedings, the exhibits received into evidence, and the position letters, the undersigned finds:

1. The Protestant operates a dental practice as a sole proprietor and holder of a Use Tax Permit.[4]

2. The Division conducted a use tax audit on the Protestant for the period beginning March 1, 2001, and ending August 31, 2003 ("Audit Period").

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[1] OKLA. STAT. ANN. tit. 68, § 201 et seq. (West 2001).

[2] OKLA. ADMIN. CODE §§ 710:1-5-20 through 710:1-5-47 (2004).

[3] The Protestant waived his right to a confidential hearing as provided by the provisions of OKLA. STAT. ANN. tit. 68, § 205 (West 2001).

[4] *See* Division's Exhibits A and B.

3. On September 24, 2004, the Protestant was notified by facsimile of the Division's intent to conduct a use tax audit. The facsimile consisted of the Facsimile Cover Sheet, Taxpayer's Power of Attorney Form, Records Request Forms (401.1 and 401.2), Audit Methodology Agreement, and copies of the Division's Random Number Generator Screens.[5]

4. On September 24, 2003, the Protestant filled out and signed the Taxpayer's Power of Attorney Form ("POA"), designating LAW FIRM as the Protestant's Attorneys-In-Fact. The Protestant sent the POA to the Division by facsimile on September 24, 2003. No other forms or documents were sent with the facsimile or otherwise received by the Division.[6]

5. The Division conducted the use tax audit on the basis of a sample audit (projection audit) sent to the Protestant by facsimile on September 24, 2003.[7] The Audit Methodology Agreement was never signed and returned to the Division by the Protestant or his Attorneys-in-Fact.

6. On or about October 7, 2003, the Division requested additional information from the Protestant and provided the Protestant a copy of the "Error Rate Calculation Spreadsheet."[8]

7. On April 9, 2004, the Division issued a proposed use tax assessment[9] against the Protestant, with interest calculated through May 25, 2004, as follows:

Tax	$2,606.08
Interest	745.47
Penalty	260.64
Total	$3,612.19

8. On March 30, 2004, a timely filed protest letter was received from ATTORNEY. The basis of the protest was that items included in the proposed assessment consisted of services (labor) from (out-of-state) dental labs and included two (2) exempt drugs. The protest letter also requested the authorization to use sample records as the basis of the audit.[10]

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[5] Division's Exhibit L. AUDITOR testified that the Division originally intended to conduct a five (5) year audit of the period beginning September 1, 1998, and ending August 31, 2003, but the audit period changed to a three (3) year audit upon learning that the Protestant was the holder of a Use Tax Permit. AUDITOR further testified that the five (5) year packet was standard for the use tax audits being conducted on dentists. The three (3) year audit sample months used from the Original Audit Methodology Agreement were June 2001 and April 2002. *See also* the last page of Exhibit L, the confirmation that the facsimile was received by the Protestant on September 24, 2003, at 11:23 a.m.

[6] Division's Exhibit K.

[7] *See* Note 5. *See also* Division's Exhibits D and F.

[8] Division's Exhibit E.

[9] Division's Exhibit G.

[10] Division's Exhibit I. ATTORNEY'S concern with the sample audit was "the taxpayer's business fluxuates [sic] drastically from time to time during the years involved such as April of 2002 and June of 2003."

9. On April 1, 2004, the Division responded to ATTORNEY'S letter of March 30, 2004. The Division advised that the invoices used for the sample months consisted of tangible personal property which was subject to use tax. The Division gave the Protestant three (3) more audit options if the error rate for the two (2) randomly selected months was two high. No response was received from the Protestant or his Attorneys-In-Fact.[11]

10. Based upon information provided by the Protestant, the two (2) drugs at issue were removed from the original audit work papers.[12]

11. On October 20, 2004, the Division issued revised audit work papers and a revised use tax assessment against the Protestant, with interest calculated through January 14, 2005, as follows:

Tax	$1,941.75
Interest	741.51
Penalty	194.21
Total	$2,877.47

12. The items under protest (porcelain crowns, sleep appliances, and ERA Housings/Trays for Partial Plates) were made from impressions of patients' teeth taken in the Protestant's office and sent to out-of-state dental labs to be made.[13]

13. None of the invoices examined by the Division reflect that the Protestant was purchasing labor only. The invoices do not reflect that the Protestant was charged use tax or sales tax by the out-of-state dental labs.[14]

CONCLUSIONS OF LAW

1. The Oklahoma Tax Commission is vested with jurisdiction over the parties and subject matter of this proceeding.[15]

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[11] Division's Exhibit J. The three (3) audit options were described in detail by the Division. In abbreviated form, the audit options consisted of the Protestant selecting two (2) additional sample months, the Division conducting a detail audit, or conducting the audit based upon fees/production/sales. The response listed five (5) ways the Division could be contacted to discuss the response.

[12] Division's Exhibit C.

[13] *See* Protestant's Exhibits One (1) and Two (2). The Protestant also described the processes through testimony.

[14] *See* Division's Exhibit F. AUDITOR testified that in his examination of the invoices the out-of-state dental labs were charging for the tangible personal property and that none of the invoices reflected that use tax or sales tax was being charged and collected by the out-of-state dental labs. Exhibit F does not include all the invoices used as the "basis" of the sample audit.

[15] OKLA. STAT. ANN. tit. 68, § 221(D) (West 2001).

2. Sales taxes and use taxes were meant to be complementary and supplementary, but not overlapping.[16] While the sales tax and the use tax codes are complementary and supplementary to one another, they are neither identical nor coterminous.[17]

3. Use tax is an excise tax which the State of Oklahoma is authorized to exact, in connection with sales tax, for the primary purpose of raising revenue for state purposes, and is designed to prevent consumers from escaping sales tax by going outside the state and purchasing property and bringing it into the State of Oklahoma for use or consumption.[18]

4. The Oklahoma Use Tax Code imposes tax solely on tangible personal property purchased outside the State of Oklahoma and brought into the State of Oklahoma. Neither intangible personal property nor services fall within the scope of the Oklahoma Use Tax Code.[19]

5. A tax of four and one-half percent (4.5%) is imposed and shall be paid by every person "storing, using, or otherwise consuming within this state, tangible personal property purchased or brought into this state. . . ."[20] An additional tax may be levied by a county levying a county sales tax or a municipality levying a municipal sales tax, at a rate that equals the county or municipal sales tax of such county or municipality.[21]

6. The provisions of the Oklahoma Use Tax Code[22] shall not apply to the use of tangible personal property[23] specifically exempted from taxation under the Oklahoma Sales Tax Code.[24]

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[16] *Phillips. v. Oklahoma Tax Commission*, 1978 OK 34, 577 P.2d 1278.

[17] *Globe Life and Accident Insurance Company v. Oklahoma Tax Commission*, 1996 OK 39, 913 P.2d 1322.

[18] *Southeastern, Inc. v. Oklahoma Tax Commission*, 1960 OK 97, 351 P.2d 739.

[19] *Globe Life and Accident Insurance Company v. Oklahoma Tax Commission*, 1996 OK 39, 913 P.2d 1322.

[20] *See* OKLA. STAT. ANN. tit. 68, § 1401 (West 2001) and OKLA. STAT. ANN. tit. 68, § 1402 (West 2001). *See also* OKLA. ADMIN. CODE § 710:65-21-2 (2004), OKLA. ADMIN. CODE § 710:65-21-3 (2004) and OKLA. ADMIN. CODE § 710:65-21-4 (2004).

[21] OKLA. STAT. ANN. tit. 68, § 1411 (West 2001). *See also* OKLA. ADMIN. CODE § 710:65-1-3 (2004).

[22] OKLA. STAT. ANN. tit. 68, § 1401 et seq. (West 2001).

[23] OKLA. STAT. ANN. tit. 68, § 1352(23) (West 2001), in pertinent part states:

> "Tangible personal property" means personal property that can be seen, weighed, measured, felt, or touched or that is in any other manner perceptible to the senses.

See also OKLA. ADMIN. CODE § 710:65-1-2 (2004).

[24] *See* OKLA. STAT. ANN. tit. 68, § 1350 et seq. (West 2001) for the Oklahoma Sales Tax Code. OKLA. STAT. ANN. tit. 68, § 1404(4) (West 2001).

7. Rules promulgated pursuant to the Administrative Procedures Act,[25] are presumed to be valid until declared otherwise by a district court of this state or the Supreme Court.[26] The rules are valid and binding on the persons they affect, have the force of law, and are prima facie evidence of the proper interpretation of the matter to which they refer.[27]

8. In all proceedings before the Tax Commission, the taxpayer has the burden of proof.[28] A proposed assessment is presumed correct and the taxpayer bears the burden of showing that it is incorrect and in what respect.[29]

9. The Division has the authority to conduct a use tax audit using a sample audit.[30] The Protestant has not cited any authority that the sample audit method is incorrect and in what respect. The Protestant was given three (3) other audit options if the sample months selected by the Division were unacceptable. No response was received by the Protestant.

10. Dentists primarily render services and incidentally use tangible personal property in connection therewith. The gross receipts of dentists derived from these sources are not subject to the sales tax.[31]

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[25] OKLA. STAT. ANN. tit. 75, § 250 et seq. (West 2001).

[26] OKLA. STAT. ANN. tit. 75, § 306(C) (West 2001).

[27] OKLA. STAT. ANN. tit. 75, § 308.2(C) (West 2001).

[28] OKLA. ADMIN. CODE § 710:1-5-47 (2004):

> In all administrative proceedings, unless otherwise provided by law, the burden of proof shall be upon the protestant to show in what respect the action or proposed action of the Tax Commission is incorrect. If, upon hearing, the protestant fails to prove a prima facie case, the Administrative Law Judge may recommend that the Commission deny the protest solely upon the grounds of failure to prove sufficient facts which would entitle the protestant to the requested relief.

OKLA. ADMIN. CODE § 710:1-5-77(b) (2004), provides in pertinent part:

> . . . "preponderance of the evidence" means the evidence which is of greater weight or more convincing than the evidence which is offered in opposition to it; evidence which as a whole shows that the fact sought to be proved is more probable than not.

[29] *See Enterprise Management Consultants, Inc. v. State ex rel Oklahoma Tax Com'n*, 1988 OK 91, 768 P.2d 359.

[30] OKLA. ADMIN. CODE § 710:65-5-2 (2004):

> An auditor for the Commission may suggest a sample sales/use tax audit rather than a detailed audit. The auditor shall select the periods to sample and apply the results to all the periods of the audit. The auditor shall prepare forms to be signed by the taxpayer stating they agree with the periods and method chosen for the sample.

See OKLA. STAT. ANN. tit. 68, § 206 (West 2001).

[31] OKLA. ADMIN. CODE § 710:65-19-71(a) (2004).

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11. Dental laboratories that purchase tangible personal property to produce plates, bridge-work, artificial teeth, prosthetic devices[32] and the like must pay tax when the material is purchased and must not charge tax to the dentist when the finished product is transferred to the dentist."[33]

12. The items included in the revised audit work papers, such as porcelain crowns (Belle Glass/Vectris and Empress F C) and ERA Housings/Trays for Partial Plates, are tangible personal property, but exempt from the imposition of use tax. These items meet the criteria of OKLA. ADMIN. CODE 710:65-19-71(c).

13. The items included in the revised audit work papers described as sleep appliances are tangible personal property, but are subject to the imposition of use tax. Sleep appliances do not qualify as prosthetic devices as defined by Oklahoma Statutes and the Oklahoma Administrative Code.[34] Sleep appliances do not replace a missing part of the body. The products are used by the Protestant's patients to alleviate snoring and the clinching/bruxing (grinding) of the teeth at night during sleep.

14. Items which are purchased by dentists, but which are used incidentally in the rendition of professional or laboratory services, are subject to use tax and the dentist must pay use tax when the item is purchased.[35]

15. The remaining items described in the revised audit work papers are incidental in the rendition of professional or laboratory services and are subject to the imposition of use tax.[36]

The Protestant asserts that the invoices from out-of-state dental labs included in the revised audit work papers are not charges for products but charges for labor only. The Protestant's position is tenuous at best. Impressions are taken from the teeth of the Protestant's patients. The impressions are sent to out-of-state dental labs. The out-of-state dental labs produce porcelain crowns, sleep appliances, and ERA Housings/Trays for Partial Plates. The items can be seen, weighed, measured, felt, or touched. All of these products are clearly tangible personal property.

The Division's position is equally tenuous. The Division states that these same items are not finished products, but materials to be used by the Protestant in his practice. The Division

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[32] "Prosthetic device" means a device which replaces a missing part of the human body, and includes any supplies physically connected to the device. This is the definition of prosthetic device during the Audit Period. *See* OKLA. STAT. ANN. tit. 68, § 1357(20) (West Supp. 2003) and OKLA. ADMIN. CODE § 710:65-13-171 (2003).

[33] OKLA. ADMIN. CODE § 710:65-19-71(c) (2003).

[34] *See* Note 32.

[35] OKLA. ADMIN. CODE § 710:65-19-71(d) (2003).

[36] *See* OKLA. ADMIN. CODE § 710:65-19-71(d) (2003).

does not cite any authority to support its position. When the Protestant receives these items from the out-of-state dental labs they are finished products. All that remains for the Protestant in his practice as a dentist is the installation and/or fitting of the products for his patients.

DISPOSITION

It is the ORDER of the OKLAHOMA TAX COMMISSION based upon the specific facts and circumstances of this case, that the protest should be sustained in part and denied in part.

The protest is sustained as to those items described in the revised audit work papers as porcelain crowns (Belle Glass/Vectris and Empress F C) and ERA Housing/Trays for Partial Plates. These items should be removed from the revised audit work papers and the use tax assessment recalculated.

The protest is denied as to the items described in the revised audit work papers as sleep appliances, along with the remaining items used by the Division as the basis of the sample audit, which are incidental in the rendition of the Protestant's practice.

It is further ORDERED that the amount at issue, as finally determined by the Division after the adjustments, be fixed as the Protestant's deficiency due and owing, including interest accrued and accruing.

ADDENDUM TO
FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

The *Findings, Conclusions and Recommendations* issued on June 8, 2005, in the above styled and numbered cause, comes on for consideration of recommendations as to the amount of the deficiency, which should be confirmed by an order the Oklahoma Tax Commission.

The Division, as directed by the *Findings, Conclusions and Recommendations,* revised the proposed use tax assessment and provided notice of the revisions to the Protestant. The Protestant has not challenged the revisions proposed by the Division.

Upon consideration of the *Findings, Conclusions and Recommendations* and the revisions to the proposed use tax assessment, the undersigned finds that the following findings should be added to and incorporated in the *Findings, Conclusions and Recommendations* issued on June 8, 2005, as follows:

1. On January 13, 2006, the Division filed a Notice of Use Tax Adjustment submitting work papers for the revised use tax assessment.

2. The proposed use tax assessment was revised as follows:

Use Tax	$1,514.41
Interest @ 15% through 03/15/06	845.09
30 Day Delinquent Penalty @ 10%	151.49

Total	$2,510.99

3. The revisions comply with the recommendations set forth in the *Findings, Conclusions and Recommendations* issued on June 8, 2005.

4. The Protestant was provided notice of the revisions.

5. The Protestant did not file a response to the revisions.

The undersigned further finds that the following recommendation should be added to and incorporated in the *Findings, Conclusions and Recommendations*:

> It is further ORDERED that the revised use tax, inclusive of accrued interest, should be fixed as the amount due and owing.

THEREFORE, the *Findings, Conclusions and Recommendations* issued on June 8, 2005, are amended to include and incorporate the above and foregoing findings of fact and recommendation.

SECOND ADDENDUM TO
FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

The *Findings, Conclusions and Recommendations* issued on June 8, 2005, in the above styled and numbered cause, comes on for consideration of recommendations as to the amount of the deficiency, which should be confirmed by an order the Oklahoma Tax Commission.

1. The Division, as directed by the *Findings, Conclusions and Recommendations,* revised the proposed use tax assessment by excluding porcelain crowns (Belle Glass/Vectris and Empress F C) and ERA Housing/Trays for Partial Plates.

2. On January 13, 2006, the Division filed a *"Notice of Use Tax Adjustment"* as follows, to-wit:

Use Tax:	$1,514.41
Interest@ 15% through 03/15/06:	845.09
30 Day Delinquent Penalty@ 10%	151.49
Total	$2,510.99

3. On January 30, 2006, the undersigned issued an *Addendum to Findings, Conclusions and Recommendations* reflecting the revisions.

4. On February 2, 2006, Commission Order No. 2006-02-02-02 was adopted incorporating the June 8, 2005, *Findings, Conclusions and Recommendations* and the January 30, 2006, *Addendum to Findings, Conclusions and Recommendations*.

5. On February 9, 2006, the Protestant filed a *Motion for Reconsideration* as to the first two (2) items (Alliance Dental) on the Division's revised audit work papers filed on January 16, 2006.

6. On February 14, 2006, the parties were notified by letter that the Division could file a response to the *Motion for Reconsideration of the Addendum* on or before February 24, 2006, at which time the motion would be submitted for ruling.[1]

7. On February 16, 2006, Commission Order No. 2006-02-16-03 *vacated* Commission Order No. 2006-02-02-02 as being entered prematurely.

8. On February 22, 2006, the Division filed a Memorandum advising that the first two (2) items on the revised audit work papers (Alliance Dental) would be removed.

9. On February 23, 2006, the Division filed a *"Notice of Use Tax Adjustment"* as follows, to-wit:

Use Tax:	$1,124.04
Interest @ 15% through 03/031/06:	633.45
30 Day Delinquent Penalty @ 10%:	112.41
Total	$1,869.90

10. On March 3, 2006, the parties were advised that the Protestant could file a response to the Division's *"Notice of Use Tax Adjustment"* on or before March 10, 2006, at which time the motion would be submitted for ruling.[2]

11. On March 3, 2006, the Protestant filed a *"Protest"* to the Division's *"Notice of Use Tax Adjustment"* filed February 23, 2006, due to the inclusion of two (2) items from "DENTAL LAB."[3]

12. On March 8, 2006, the parties were advised that the Division could file a response to the *"Protest"* on or before March 17, 2006.

13. On March 9, 2006, the Division filed its Response to the *"Protest"* to the inclusion of two (2) items from DENTAL LAB.[4]

14. On March 16, 2006, the undersigned issued an *Order Denying "Protest" to Notice of Use Tax Adjustment Filed February 23, 2006*.

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[1] OKLA. ADMIN. CODE § 710:1-5-40.

[2] *See* Note 1.

[3] The protest indicated that the inclusion of these two items was contrary to the *Findings, Conclusions and Recommendations* issued on June 8, 2005.

[4] The Division referred to paragraph 13 of the Conclusions of Law, which found that "sleep appliances are tangible personal property subject to the imposition of use tax."

Upon consideration of the *Findings, Conclusions and Recommendations* and the revisions to the proposed use tax assessment, the undersigned finds that the following findings should be added to and incorporated in the *Findings, Conclusions and Recommendations* issued on June 8, 2005, as follows:

6. On February 23, 2006, the Division filed a *"Notice of Use Tax Adjustment"* submitting audit work papers for the revised use tax assessment.

7. The proposed use tax assessment was revised as follows:

Use Tax	$1,124.04
Interest @ 15% through 03/31/06	633.45
30 Day Delinquent Penalty @ 10%	112.41
Total	$1,869.90

The undersigned further finds that the following recommendation should be added to and incorporated in the *Findings, Conclusions and Recommendations*:

> It is further recommended that the revised use tax, inclusive of accrued interest, should be fixed as the amount due and owing.

THEREFORE, the *Findings, Conclusions and Recommendations* issued on June 8, 2005, are amended to include and incorporate the above and foregoing findings of fact and recommendation.

OKLAHOMA TAX COMMISSION