JURISDICTION:	OKLAHOMA TAX COMMISSION DECISION
CITE:	2008-09-09-03 / NON-PRECEDENTIAL
ID:	P-07-075-K
DATE:	SEPTEMBER 9, 2008
DISPOSITION:	DENIED
TAX TYPE:	SALES
APPEAL:	PENDING OK S.CT. 106,380

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Protestant, PROTESTANT is represented by ATTORNEY, Attorney at Law. The Compliance Division of the Oklahoma Tax Commission (hereinafter "Division") is represented by OTC ATTORNEY, Assistant General Counsel, Office of the General Counsel, Oklahoma Tax Commission.

STATEMENT OF THE CASE

A cost mark-up depletion audit of Protestant's inventory available for sale for the periods inclusive of January, 2004 through December, 2005 was conducted by the Division. As a result of the audit, the Division by letter dated August 24, 2006 proposed the assessment of additional sales tax, interest and penalty against Protestant for the audit period. Protestant timely filed a written protest to the proposed assessment.

On May 4, 2007, the file was referred to the Office of the Administrative Law Judges ("ALJ's Office") for further proceedings consistent with the Uniform Tax Procedure Code[1] and the Rules of Practice and Procedure before the Oklahoma Tax Commission[2]. The case was docketed as Case No. P-07-075-K and assigned to ALJ, Administrative Law Judge.[3]

A pre-hearing conference was scheduled for June 21, 2007, by *Prehearing Conference Notice* issued May 23, 2007.[4] For good cause shown the conference was rescheduled for August 1, 2007.[5] The conference was held as rescheduled. Pursuant to the conference, the Division was directed to file a motion to dismiss protest on jurisdictional grounds. The *Motion to Dismiss* of the Division was filed August 9, 2007. A *Notice of Hearing on Motion to Dismiss and Order Setting Hearing* was served on the parties on August 10, 2007.[6] Protestant filed a response to the *Notice* on September 4, 2007.

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[1] 68 O.S. 2001, § 201 et seq.

[2] Rules 710:1-5-20 through 710:1-5-47 of the *Oklahoma Administrative Code* ("*OAC*").

[3] *OAC*, 710:1-5-22(b).

[4] *OAC*, 710:1-5-28.

[5] *OAC*, 710:1-5-30.

[6] *OAC*, 710:1-5-46(d).

The *Motion to Dismiss* was heard on September 10, 2007. On September 25, 2007, an *Order Recommending the Denial of the Division's Motion to Dismiss* was issued by the undersigned. By Order No. 2007-11-01-25, the Commission adopted the findings of fact, conclusions of law and recommendations entered on September 25, 2007.

A hearing on the merits of the protest was scheduled for December 19, 2007, by *Notice of Hearing* issued November 2, 2007. A closed hearing was held as scheduled with all parties present[7]. Protestant testified with respect to the business and the missing inventory. SUPERVISOR, Audit Supervisor testified with respect to the conduct of the audit and the records of the Division. Division's Exhibits A through H were identified, offered and admitted into evidence. Upon conclusions of the hearing, the record was closed and the protest was submitted for decision.[8]

FINDINGS OF FACT

Upon review of the file and records, including the tape recording of the hearing, the Exhibits received into evidence and the pleadings of the parties, the undersigned finds:

1. Protestant owns and operates a retail package liquor store known as LIQUOR STORE located at BUSINESS ADDRESS in CITY, Oklahoma. Division's Exhibit A.

2. Two (2) requests for Protestant's records "to determine if the proper amount of retail sales have been reported on your monthly sales tax returns" were made by the Division. Division's Exhibit B. The second records request shows that the period selected for audit was January 1, 2004 through December 31, 2005, and that Protestant's 2004 and 2005 federal and state income tax returns had been secured by the Division. Division's Exhibit B-2. According to SUPERVISOR, the income tax returns were obtained from the records of the Tax Commission and Protestant's beginning and ending inventories were determined from the tax returns.

3. Protestant testified that he delivered three (3) boxes which contained the requested records to a Tax Commission building and left them with an individual. According to SUPERVISOR, the Division did not receive the records. She testified that the purpose of the records was to verify the accuracy of the sales tax reports filed by Protestant.

4. A cost mark-up depletion audit of Protestant's inventory for the periods inclusive of January, 2004 through December, 2005 ("audit period") was performed by the Division. Protestant's beginning and ending inventory, and purchases of product for the audit period were taken from Protestant's 2004 and 2005 income tax returns and the reports by Protestant's wholesalers, respectively. The "product available for sale" during the audit period was determined by adding the beginning inventory to Protestant's purchases during the audit period, and subtracting the ending inventory. Testimony of SUPERVISOR. The wholesale cost of Protestant's "product available for sale" during the audit period totaled $665,501.01.

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[7] Protestant invoked his right to a confidential hearing in accordance with 68 O.S. 2001, § 205.

[8] *OAC*, 710:1-5-39(a).

5. The "average weighted cost mark-up" percentage of 12.35 was derived from a comparison of the wholesale prices and a shelf inspection of Protestant's retail prices and an interview with Protestant. Testimony of SUPERVISOR; Division's Exhibit C.

6. The "mark-up" was applied to the "product available for sale" to arrive at a retail value of the inventory. Protestant's reported sales of $465,735.00 for the audit period was subtracted from the retail value of the product available for sale of $747,690.38 to arrive at under-reported sales of $281,955.38 for the audit period. Testimony of SUPERVISOR; Division's Exhibit D.

7. As a result of the audit, the Division by letter dated August 24, 2006 proposed the assessment of additional sales tax, interest and penalty against Protestant in the aggregate amount of $31,548.79, consisting of tax in the amount of $23,613.77, interest at fifteen percent (15%) through October 31, 2006, in the amount of $5,573.64, for a total of tax and interest due within thirty (30) days of $29,187.41, and a thirty (30) day delinquent penalty at ten percent (10%) of $2,361.38. Exhibit F.

8. Protestant timely protested the proposed assessment. Oklahoma Tax Commission Order No. 2007 11 01 25.

9. The latest revision to the proposed assessment which was done to comply with Oklahoma Tax Commission Order No. 2008 04 10 02, proposes an aggregate amount due of $35,361.38, consisting of sales tax in the amount of $22,361.38 on the proposed under-reported sales of $267,001.58 during the audit period, interest accrued through July 31, 2008, in the amount of $11,185.05 and penalty in the amount of $2,236.13. *Notice of Sales Tax Adjustment* filed May 27, 2008.

10. Protestant is at his store a majority of the time, but has a couple of women who watch the store while he runs errands. Protestant accuses an employee of his brother's liquor store for the theft of merchandise equal to the under-reported sales. Protestant testified that he hired this person to be on call, gave him a key to the store and the alarm code; but doesn't recall ever calling him to come to work except he showed up one day to help unload a delivery truck. Protestant speculated that the theft occurred over a year and one-half period, but doesn't remember when he noticed the product was missing. Protestant accuses his brother for the theft because he noticed a lot of the product he had purchased that he could not account for on his brother's shelves in large quantities. He stated that prior to this his brother's inventory was always low. He further stated that he confronted his brother concerning the theft and their dad recovered approximately a truck load of liquor valued between $4,000.00 and $5,000.00. Protestant also stated that he didn't report the theft to the police or file an insurance claim, and doesn't know whether he reported the loss as a business expense deduction on his income tax returns.

ISSUE AND CONTENTIONS

The issue presented for decision is whether Protestant sustained his burden of proving that the audit is incorrect in any respect.

Protestant contends that the under-reported sales are attributable to the theft of product by an employee of his brother's liquor store. Protestant admits that he purchased the product shown to have been purchased by him, but that the stolen inventory was sold at his brother's liquor store and the state received the tax from those sales. Protestant argues that without the audit of his brother's liquor store, he can't show where his missing inventory went.

The Division contends that Protestant has not come forward with any evidence to sustain his allegation that the product was stolen. In support of this contention, the Division argues that there are ways to document theft and meet your burden of proof; however Protestant has failed to do so. The Division further argues that the proposed assessment was revised to factor in a two percent (2%) margin of error for undocumented losses, including theft.

CONCLUSIONS OF LAW

WHEREFORE, premises considered, the undersigned concludes as a matter of law that:

1. Jurisdiction over the parties and the subject matter of this proceeding is vested in the Tax Commission. 68 O.S. Supp. 2002, § 221(D).

2. The collection and remittance of sales tax is governed by the Oklahoma Sales Tax Code ("Code").[9] An excise tax is levied upon the gross receipts or gross proceeds[10] of all sales,

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[9] 68 O.S. 2001, § 1350 et seq.

[10] The terms "gross receipts" or "gross proceeds" are defined to mean "the total amount of consideration for the sale of any tangible personal property or service taxable under the Oklahoma Sales Tax Code, whether the consideration is in money or otherwise. "Gross receipts" or "gross proceeds" shall include, but not be limited to:

a. cash paid,
b. any amount for which payment is charged, deferred, or otherwise to be made in the future, regardless of the time or manner of payment,
c. any amount for which credit or a discount is allowed by the vendor,
d. any amount of deposit paid for transfer of possession, and
e. any value of a trade-in or other property accepted by the vendor as consideration, except for used or trade-in parts excluding tires or batteries for a motor vehicle, bus, motorcycle, truck-tractor, trailer, semitrailer or implement of husbandry, as defined in Sections 1-105, 1-125, 1-134, 1-135, 1-162, 1-180 and 1-183 of Title 47 of the Oklahoma Statutes, if the used or trade-in parts are taken in trade as exchange on the sale of new or rebuilt parts.

There shall not be any deduction from the gross receipts or gross proceeds on account of cost of the property sold, labor service performed, interest paid, or losses, or of any expenses whatsoever, whether or not the tangible personal property sold was produced, constructed, fabricated, processed, or otherwise assembled for or at the request of the consumer as part of the sale.

Amended and renumbered by Laws 2003, c. 413, § 1, eff. Nov. 1, 2003. See, 68 O.S. Supp. 2004, § 1352(11) which provides:

a. "Gross receipts", "gross proceeds" or "sales price" means the total amount of consideration, including cash, credit, property and services, for which personal property or services are sold, leased or rented, valued in money, whether received in money or otherwise, without any deduction for the following:

(1) the seller's cost of the property sold,

not otherwise exempted by the Code. 68 O.S. 2001, § 1354(A). Incorporated cities, towns, and counties are authorized to levy taxes as the Legislature may levy for purposes of state government, including a consumer sales tax. 68 O.S. 2001, §§ 2701 et seq. and 1370 et seq., as amended.

3. The sale of "tangible personal property"[11] is expressly made subject to sales tax. 68 O.S. 2001, § 1354(A)(1). "Sale" is defined to mean "the transfer of either title or possession of tangible personal property for a valuable consideration regardless of the manner, method, instrumentality, or device by which the transfer is accomplished in this state * * *". 68 O.S. 2001, § 1352(15).[12] See, *OAC*, 710:65-1-2. "The taxable event is the sale itself * * *." ***Pioneer Telephone Cooperative, Inc. v. Oklahoma Tax Commission***, 1992 OK 77, 832 P.2d 848; citing with approval, *Phillips v. Oklahoma Tax Commission*, 1978 OK 34, 577 P.2d 1278, 1282, ("In discussing sales tax, it must be emphasized that sales tax is imposed upon the sale itself * * *"); and *Liberty Steel Co. v. Oklahoma Tax Commission*, 1976 OK 83, 554 P.2d 8, 10, ("A sales tax, as opposed to a use tax, is imposed on the sale itself and is collectable from the seller"). "For the purpose of proper administration of the provisions of the sales and use tax laws, it is presumed that all gross receipts are subject to tax until they are shown to be tax exempt." *OAC*, 710:65-1-4(a).

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(2) the cost of materials used, labor or service cost,
(3) interest, losses, all costs of transportation to the seller, all taxes imposed on the seller, and any other expense of the seller,
(4) charges by the seller for any services necessary to complete the sale, other than delivery and installation charges,
(5) delivery charges and installation charges, unless separately stated on the invoice, billing or similar document given to the purchaser, and
(6) the value of exempt personal property given to the purchaser where taxable and exempt personal property have been bundled together and sold by the seller as a single product or piece of merchandise.

b. Such term shall not include:

(1) discounts, including cash, term, or coupons that are not reimbursed by a third party that are allowed by a seller and taken by a purchaser on a sale,
(2) interest, financing, and carrying charges from credit extended on the sale of personal property or services, if the amount is separately stated on the invoice, bill of sale or similar document given to the purchaser, and
(3) any taxes legally imposed directly on the consumer that are separately stated on the invoice, bill of sale or similar document given to the purchaser.

See, *OAC*, 710:65-1-2. Amended at 21 Ok Reg 2581, eff 6-25-04. See also, *OAC*, 710:65-1-9. Amended at 21 Ok Reg 2581, eff 6-25-04.

[11] Defined by the Code to mean "personal property which may be seen, weighed, measured, felt, or touched or which is in any other manner perceptible to the senses". 68 O.S. 2001, § 1352(17). Amended and renumbered by Laws 2003, c. 413, § 1, eff. Nov. 1, 2003, to include within the meaning "electricity, water, gas, steam and prewritten computer software" and to provided that "[t]his definition shall be applicable only for purposes of the Oklahoma Sales Tax Code". See, 68 O.S. Supp. 2004, § 1352(23). See also, *OAC*, 710:65-1-2. Amended at 21 Ok Reg 2581, eff 6-25-04.

[12] Renumbered as § 1352(21) by Laws 2003, c. 413, § 1, eff. Nov. 1, 2003.

4. The excise tax levied by the Code is required to be paid by the consumer or user to the vendor, who is required to collect from the consumer or user the full amount of the tax levied or an amount equal as nearly as possible or practicable to the average equivalent thereof, 68 O.S. 2001, § 1361(A); and remit the same to the Tax Commission, 68 O.S. 2001, § 1362(A). The amount to be collected by the vendor on each sale is the applicable percentage of the gross receipts or gross proceeds thereof as provided by § 1354 of the Code which applicable percentage shall equal the combination of the state and any applicable municipal and county sales tax rates rounded to a whole cent. 68 O.S. 2001, § 1362(B). A vendor may elect to compute the tax due on transactions on an item or invoice basis. Id. The tax levied by the Code shall be added to the gross receipts not included in the gross receipts. ***Duncan Medical Services v. Oklahoma Tax Commission***, 1994 OK 91, 911 P.2d 247, at 253.

5. In ***Pioneer Telephone***, *supra.*, Pioneer sought a refund of sales taxes on the receipts from its telephone services which it determined were in excess of that necessary to provide the services and which were credited on a pro-rata basis to its customers' capital accounts in accordance with its end-of-year accounting. In denying the refund, the Supreme Court of Oklahoma held:

> The taxable event is the sale itself, and not the cost of operations determined by an accounting method at a future date. The taxable event, the sale of the service, occurs when the cooperative member receives the service and incurs the obligation to pay consideration, the monthly charge, for telephone service.

Id., at 851. In so holding, the Court construed the meaning of "gross receipts" as defined by the Code and according to its plain meaning, and found that "gross receipts includes the consideration for the sale of the service" which includes the cost of the service and any amount allowed as a credit by the seller[13] and that "[t]hus gross receipts refers to the total amount of money or the value of other considerations received from selling property or performing services", citing *County of Sacramento v. Pacific Gas and Electric Co*., 193 Cal.App.3d 300, 238 Cal.Rptr. 305, 311 (3 Dist.1987). See, ***Duncan Medical***, *supra*. at 251, wherein the Supreme Court of Oklahoma concluded that "[t]he plain meaning of gross receipts or gross proceeds upon which the sales tax shall be calculated is the total consideration received by the seller or the total obligation incurred by the purchaser at the time of the transaction, if greater than the monetary consideration received by the seller", citing *Pioneer Telephone, supra*. Id.

6. A proposed assessment is presumed correct and the taxpayer bears the burden of showing that it is incorrect, and in what respect. *OAC*, 710:1-5-47. See, ***Enterprise Management Consultants, Inc. v. State ex rel. Oklahoma Tax Commission***, 1988 OK 91, 768 P.2d 359. In sales tax matters, "[t]he burden of proving that a sale was not a taxable sale shall be upon the person who made the sale." 68 O.S. 2001, § 1365(E). See, ***Dunn v. State ex rel. Oklahoma Tax Commission***, 1993 OK CIV APP 105, 862 P.2d 1285. Section 1365(E) further provides in pertinent part:

[13] It should be noted that as of November 1, 2003, discounts are excluded from "gross receipts" or "gross proceeds" if they are not reimbursed by a third party. See, Note 12.

> It shall be the duty of every tax remitter required to make a sales tax report and pay any tax under [the Code] to keep and preserve suitable records of the gross daily sales together with invoices of purchases and sales, bills of lading, bills of sale and other pertinent records and documents which may be necessary to determine the amount of tax due hereunder and such other records of goods, wares and merchandise, and other subjects of taxation under [the Code] as will substantiate and prove the accuracy of such returns. * * * All such records shall remain in Oklahoma and be preserved for a period of three (3) years, unless the Tax Commission, in writing, has authorized their destruction or disposal at an earlier date, and shall be open to examination at any time by the Tax Commission or by any of its duly authorized agents.

See, ***Kifer v. Oklahoma Tax Commission***, 1998 OK CIV APP 34, 956 P.2d 162.

7. In administrative proceedings, the burden of proof standard is "preponderance of evidence." 2 Am.Jur.2d Administrative Law § 357. See, Oklahoma Tax Commission Order No. 91-10-17-061. "Preponderance of evidence" means "[e]vidence which is of greater weight or more convincing than the evidence which is offered in opposition to it; that is, evidence which as a whole shows that the fact sought to be proved is more probable than not." Black's Law Dictionary 1064 (5th ed. 1979). It is also defined to mean "evidence which is more credible and convincing to the mind * * * [T]hat which best accords with reason and probability." Id.

8. Here, Protestant failed to come forward with any credible evidence to show the product representing the under-reported sales was stolen. A two percent (2%) variance has been factored into the revised assessment for unsubstantiated losses. The evidence does not support any further reduction to the proposed amount of under-reported sales.

9. Protestant's protest to the latest revision of the proposed sales tax assessment should be and the same is hereby denied.

DISPOSITION

Based on the above and foregoing findings of fact and conclusions of law, it is ORDERED that the protest of Protestant, PROTESTANT d/b/a LIQUOR STORE, be denied. It is further ORDERED that the latest revision to the proposed assessment, inclusive of any additional accrued and accruing interest, be fixed as the deficiency due and owing.

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.