

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)
[Redacted],) DOCKET NO. 24442
)
)
Petitioner.) DECISION
)
_____)

On July 8, 2011, the Sales Tax Audit Bureau (Bureau) of the Idaho State Tax Commission (Commission) issued a Notice of Deficiency Determination (Notice) to [Redacted] (taxpayer). The Notice proposed additional use tax, penalty, and interest in the total amount of \$12,919 for taxable periods April 2009 through December 2009. The taxpayer filed a timely appeal and petition for redetermination on August 18, 2011, and requested an informal hearing, which was held on July 24, 2012.

The Commission, having reviewed the audit file and considered the points discussed during the informal hearing, hereby modifies the audit findings for the reasons detailed below.

The taxpayer is a [Redacted] that constructs and improves real property in Idaho and throughout the [Redacted].

The Bureau initiated a limited scope audit of a single project in which the taxpayer undertook a contract to install [Redacted]. The taxpayer operated as a subcontractor to [Redacted], the general contractor, which had a contract with the [Redacted]. The materials installed by the taxpayer were purchased by [Redacted] and supplied to the taxpayer for the project. As Idaho state agencies can make purchases of tangible personal property exempt from tax, no sales or use tax had been paid prior to the taxpayer taking possession of and installing the materials.

The Bureau held the taxpayer, as a contractor constructing real property, liable for use tax on the value of the materials consumed on the project. The general contractor provided information from [Redacted] that indicated the price which [Redacted] paid for the materials. The Bureau relied on this price in asserting the use tax liability. The taxpayer's use of the installed materials is the only item held subject to tax by the Bureau.

The taxpayer protests the Bureau's imposition of tax arguing that the general contractor should be held liable for tax on the use of the materials. The taxpayer believes that because the general contractor entered into the contract with [Redacted] and the contract explicitly outlines the use tax liability arising from installation of materials supplied by [Redacted], the taxpayer cannot be held liable for tax on its own use of the materials. In addition, the taxpayer points out that the general contractor took possession of the materials prior to the taxpayer's work on the project. Based on the above, the taxpayer argues that the general contractor is the only one which exercised control over the material sufficient to incur a use tax liability.

In the event that the Commission disagrees with its first argument, the taxpayer also asserts that it had installed less material than the contract originally set. The taxpayer provided documentation indicating that it had only installed 53.8 percent of the materials originally called for in the contract. Consequently, the taxpayer argues that the tax liability should be reduced by 46.2 percent to account for the contract reduction.

Finally, the taxpayer originally disagreed with the materials value used by the Bureau in calculating the use tax owed. However, the taxpayer received confirmation directly from the materials supplier that indicated the value used by the Bureau was correct. The taxpayer no longer disputes the value of the materials.

For sales and use tax purposes, a contractor improving real property is the consumer of any materials that become part of the realty and owes sales or use tax on such materials (Idaho Code § 63-3609(a)):

(a) All persons engaged in constructing, altering, repairing or improving real estate, are consumers of the material used by them; all sales to or use by such persons of tangible personal property are taxable whether or not such persons intend resale of the improved property.

Based on the above, if a contractor has used materials in the construction of real property, the contractor will owe sales or use tax. The term “use” as utilized here is a specially defined term for the purposes of the use tax (Idaho Code § 63-3615(b)):

(b) The term “use” includes the exercise of any right or power over tangible personal property incident to the ownership or the leasing of that property or the exercise of any right or power over tangible personal property by any person in the performance of a contract, or to fulfill contract or subcontract obligations, whether the title of such property be in the subcontractor, contractor, contractee, subcontractee, or any other person, or whether the titleholder of such property would be subject to the sales or use tax...

The Commission concludes that the above definition clearly covers the facts before it in this case. The taxpayer exercised power over tangible personal property in fulfilling its obligations as a subcontractor constructing real property. Though the project owner [Redacted] never owed a use tax, it is clear in the definition that a subcontractor still does owe a use tax regardless of this fact. An administrative rule addresses this issue specifically and further supports the Bureau’s position (IDAPA 35.01.02.12.10):

10. Materials Provided by Project Owner.

a. If a project owner who is not exempt from tax buys materials for a job and hires a contractor to install them, he must pay sales or use tax when he buys the material. If the owner does not pay tax on the materials, the contractor may be held liable for the tax.

b. If material needed for a contract is purchased or supplied by an owner who is exempt from sales and use taxes, then the use by the contractor is subject to use tax. This is true even if the property is owned by an exempt entity such as the federal government or a state government agency. For example, if a

contractor has a public works contract to build a structure using materials owned and supplied by the government, whether federal, state, or local, he is the consumer of the materials and is subject to a use tax on their value. This tax falls directly upon the contractor and not the owner of the property

c. A contractor who buys tangible goods cannot avoid tax just because the goods will be built in to a structure which will belong to, or be used by an exempt entity. Contractors and subcontractors may not avoid paying sales or use tax due to a contract which allows invoices to be made out in the name of the exempt entity, such as the U.S. Government, and designate the contractor or subcontractor as an agent of the exempt entity. In this case, the contractor or subcontractor is the user or consumer of the material and its use, while it is in his possession and subject to his labor, is taxable.

Therefore, the Commission confirms the Bureau's assertion that the taxpayer is liable for tax on its use of all materials installed on the project.

The Commission acknowledges the point that the general contractor likely could have been held liable for the use tax as well. However, that does not change the fact that the taxpayer as a subcontractor incurred a use tax liability of its own. Of course, use tax can only be imposed once on the materials consumed for a given project, but, as is evident in this case, there are situations in which multiple parties could be held liable for that tax. In addition, contractual obligations between two private parties do not generally have any impact on the Commission's authority to assert a tax against someone who rightfully owes the tax.

Though the Commission confirms the Bureau's imposition of use tax, the documentation provided by the taxpayer clearly indicates that the taxpayer only installed 53.8 percent of the materials set forth in the original contract. The remaining materials were retained by [Redacted] and used by a different contractor for another project. Therefore, the Commission agrees that the tax liability should be reduced by 46.2 percent and this reduction is reflected below.

Finally, interest has been imposed per Idaho Code § 63-3045(6).

THEREFORE, the Notice dated July 8, 2011, and directed to [Redacted], is MODIFIED by this decision.

IT IS ORDERED that the taxpayer pay the following amount of tax, penalty, and interest (calculated through June 21, 2013):

<u>TAX</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
\$6,950	\$0	\$932	\$7,882

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of the taxpayer's right to appeal this decision is enclosed.

DATED this _____ day of _____ 2013.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this _____ day of _____ 2013, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[Redacted]

Receipt No.
