

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 24880
[Redacted],)	
)	
Petitioner.)	DECISION
)	
_____)	

On December 28, 2011, the Sales Tax Audit Bureau (Bureau) of the Idaho State Tax Commission (Commission) issued a Notice of Deficiency Determination (Notice) to [Redacted]. The Notice proposed additional sales and use tax, penalty, and interest in the total amount of \$96,565 for taxable periods June 2008 through May 2011. The taxpayer filed a timely appeal and petition for redetermination on February 13, 2012, and requested an informal hearing, which was held on August 1, 2012.

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

The taxpayer is a franchise retailer for a national corporation primarily selling [Redacted]. The taxpayer also repairs and services [Redacted] equipment for its customers.

The Bureau undertook a routine comprehensive audit of the taxpayer's sales and use tax returns. After its review, the Bureau asserted errors in both sales and purchases resulting in the above mentioned sales and use tax liability. The only errors relevant to this discussion are related to sales made by the taxpayer to customers who claimed the production exemption. In the opinion of the Bureau, many of these customers did not qualify for the claimed exemption and therefore, the taxpayer was held liable for the sales tax it should have collected on those transactions.

The taxpayer protested the Notice arguing that many of the sales for which the Bureau had denied the customer's production exemption claim were actually valid exempt sales. The taxpayer agreed with the remainder of the liability asserted and consequently, no further discussion of those issues is necessary in this decision.

By statute, all sales in Idaho are presumed to be subject to sales tax (Idaho Code § 63-3622(a)):

- (a) To prevent evasion of the sales and use tax, it shall be presumed that all sales are subject to the taxes imposed by the provisions of this chapter and the retailer shall have the burden of establishing the facts giving rise to such exemption unless the purchaser delivers to the retailer, or has on file with the retailer, an exemption or resale certificate.

Based on the above, the taxpayer argues that it has fulfilled its obligation as a retailer, and cannot be held liable for tax on any of its sales to customers for which the taxpayer has an exemption certificate on file. In this case, all parties agree that the taxpayer had the proper exemption certificates related to all exempt sales in question. However, for those sales held taxable by the Bureau, the Bureau's denial of the customer's exemption claim is not an issue of documentation, but is based on the following (Idaho Code § 63-3622(g)):

- (g) It shall be presumed that sales made to a person who has completed an exemption or resale certificate for the seller's records are not taxable and the seller need not collect sales or use taxes unless the tangible personal property or services purchased are taxable to the purchaser as a matter of law in the particular instance claimed on the exemption certificate.

The Bureau argues that many of the taxpayer's nontaxed sales to its customers were "taxable as a matter of law" and therefore, the taxpayer should have collected sales tax. Almost all of the nontaxed sales held taxable by the Bureau were claimed by the customer as exempt under the production exemption. As established by Idaho Code § 63-3622D, the production exemption exempts the sale and use of certain tangible personal property used in production of tangible personal property for resale. A discussion of the details of the exemption is unnecessary here

with one exception. There is a particular exclusion from the production exemption which the Bureau relies upon as the reason for denying the customer's exemption claim (Idaho Code § 63-3622D(f)):

(f) The exemptions allowed in this section do not include machinery, equipment, materials and supplies used in a manner that is incidental to the manufacturing, processing, mining, farming or fabricating operations such as maintenance and janitorial equipment and supplies.

The Bureau argues that the equipment sold by the taxpayer ([Redacted] equipment) is used by the customer in maintenance or janitorial activities, or some other activity incidental to, or entirely outside the production operation. On that basis, the Bureau held the taxpayer liable for sales tax on those transactions for which the customer claimed the production exemption.

In addition to Idaho Code § 63-3622(a) quoted previously, another subsection of the same statute emphasizes the obligation placed upon the retailer and the method by which a retailer can meet that obligation (Idaho Code § 63-3622(d)):

(d) ...Other than as provided elsewhere in this section, when an exemption or resale certificate, properly executed, is presented to or is on file with the seller, the seller has no duty or obligation to collect sales or use taxes in regard to any sales transaction so documented, regardless of whether the purchaser properly or improperly claimed an exemption.

These subparts of the statute are not entirely consistent. On one hand, if the purchaser provides a certificate, the seller has no duty or obligation to determine the validity of the claimed exemption, even if the purchaser improperly claimed the exemption. In contrast, a seller must collect the tax if the sale is taxable as a matter of law, even if the purchaser has filled out the exemption certificate claiming the exemption.

In interpreting statutes, all words of the statute must be harmonized and read together. All sections of the applicable statute must be read together to determine the intent of the legislature.

Davaz v. Priest River Glass Co., Inc. 125 Idaho 333, 870 P.2d 1292 (1994). If the statute is

ambiguous, then it must be construed to mean what the legislature intended for it to mean. Miller v. State, 110 Idaho 298, 715 P.2d 968 (1986). To determine that intent, not only are the literal words of the statute examined, but also the reasonableness of proposed constructions, the public policy behind the statute, and its legislative history. Lopez v. State Industrial Special Indemnity Fund, 136 Idaho 174, 30 P.3d 952 (2001).

In considering the interpretation of Idaho Code § 63-3622, the Commission must consider the language of the statute by giving effect to every subsection and construing each subsection so that it is harmonized with the other subsections of the statute. When considering these factors, it is clear that the legislature intended a low threshold for the acceptance of certificates by sellers. Unless the transaction is taxable as a matter of law, the seller has no duty or obligation for the collection of tax. This means that unless the facts show that the seller knows unequivocally that the buyer's purchase is taxable, or if the representations on the invoice and certificate disclose that the claim of exemption is invalid as a matter of law, the certificate will relieve the seller from any potential liability. The seller can rely on the representations of the buyer, even if the representations are not reasonable and the seller has no duty to question or challenge the representations. The seller can only be held liable if the seller's actual knowledge is such that he knows the buyer cannot claim the exemption at the time of sale, or if the purchase is taxable as a matter of law.

The Commission is not convinced that the taxpayer had unequivocal knowledge regarding its customers' use of the equipment, nor is it absolutely clear that the sale and use of the equipment qualify for the production exemption. Therefore, the taxpayer will not be held liable for exempt sales to customers for which the customer claimed the production exemption, and the proper exemption certificate is on file with the taxpayer.

The Commission agrees that a detailed review of the customer's actual use of tangible personal property would be relevant in an audit of that customer. As the end user of the tangible personal property, that customer is obligated to provide detailed evidence that its continued use of the property in question qualifies for the claimed exemption. However, the Commission does not agree that a retailer must have a detailed knowledge of the intended, or actual use to which its customer will put a given item of tangible personal property sold to that customer. For that matter, the Commission finds no law requiring the retailer to have any knowledge of the customer's actual use of the tangible personal property. As noted above, the only statutory reason that the Commission may deny an otherwise valid exemption claim made by a customer is if the use of that tangible personal property is "taxable as a matter of law."

In closing, it should be noted that the Commission does not have sufficient evidence before it to take a position on whether any of the taxpayer's customers use the equipment in such a manner that actually qualifies for the production exemption. As has already been emphasized, the retailer is not obligated to know whether the claimed exemption actually applies, it only has to demonstrate that the production exemption could possibly apply. This threshold has been met and therefore, any further review of the claimed exemption must be taken up with the individual customers.

Finally, the Commission finds the imposition of interest appropriate per Idaho Code § 63-3045(6).

THEREFORE, the Notice dated December 28, 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:

<u>TAX</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
\$16,008	\$0	\$2,491	\$18,499

Interest is calculated through June 26, 2013, and will continue to accrue at the rate set forth in Idaho Code § 63-3045(6) until the liability is paid in full. During 2013, interest accrues on the tax amount at a rate of \$1.32 per day. For each day payment is made prior to June 26, 2013, this amount can be subtracted from the total interest noted above.

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.