

STATE OF NORTH CAROLINA

**BEFORE THE ASSISTANT SECRETARY
OF REVENUE FOR ADMINISTRATIVE
TAX HEARINGS**

COUNTY OF WAKE

IN THE MATTER OF:

The Proposed Assessment of Sales and Use)
Tax for the period February 1, 2003 through)
November 30, 2005, by the Secretary of)
Revenue of North Carolina)
)
vs.)
)
Taxpayer)

FINAL DECISION
Docket No. 2007-1

This matter was heard before the Assistant Secretary of Administrative Hearings, Eugene J. Cella, in the City of Raleigh, on February 15, 2007, upon application for hearing by the Taxpayer wherein it protested the assessment of tax, penalty and interest for the period February 1, 2003 through November 30, 2005. The hearing was held by the Assistant Secretary pursuant to the provisions of G.S. 105-260.1. [Taxpayer and his wife] represented the business. Representing the Sales and Use Tax Division were Andrew Sabol, Director, and Dan R. Fulcher, Administration Officer.

Pursuant to G.S. 105-241.1, the Department mailed a Notice of Sales & Use Tax Assessment to the Taxpayer on February 21, 2006. The Taxpayer objected to the assessment in a letter dated February 26, 2006, and timely requested a hearing.

ISSUES

The issues to be decided are as follows:

- (1) Are prepared food, soft drinks and non-food items subject to the general State and local rate of tax during the audit period?
- (2) Is the assessment correct and properly proposed to be assessed against the Taxpayer based on the best information available?
- (3) Does the fact that the Department did not notify the Taxpayer that the rate of tax remitted through their sales and use tax returns on prepared foods and soft drinks was incorrect prevent the Department from assessing the tax?

EVIDENCE

The Sales and Use Tax Division introduced the following items into evidence at the hearing:

1. Copy of Memorandum dated May 16, 2001, from the Secretary of Revenue to the Assistant Secretary of Administrative Hearings, designated Exhibit E-1.
2. Copy of the auditor's report sales and use tax dated February 8, 2006 covering the period February 1, 2003 through November 30, 2005, designated Exhibit E-2.
3. Copy of Notice of Sales and Use Tax Assessment dated February 21, 2006, designated Exhibit E-3.
4. Copy of a letter dated February 26, 2006 from the Taxpayer to the Sales and Use Tax Division (Division), designated Exhibit E-4, with the following attachment:
 - a. Copy of Notice of Sales and Use Tax Assessment dated February 21, 2006.
5. Copy of a letter dated March 10, 2006 from the Division to the Taxpayer, designated Exhibit E-5.
6. Copy of a letter dated March 13, 2006, from the Taxpayer to the Division, designated Exhibit E-6, with the following attachments:
 - a. Letter of objection from [President the corporation] dated March 13, 2006.
 - b. Affidavit from [Co-manager] dated March 13, 2006.
 - c. Affidavit from [Co-manager] dated March 13, 2006.
 - d. Affidavit from [Taxpayer's CPA] dated March 13, 2006.
 - e. Affidavit from [President the corporation] dated March 13, 2006.
 - f. Copy of G. S. 105-471.
 - g. Copy of a letter dated March 10, 2006 from the Division to the Taxpayer.
7. Copy of a letter dated March 31, 2006 from the Division to the Taxpayer, designated Exhibit E-7.
8. Copy of a letter dated April 6, 2006 from the Taxpayer to the Division. designated Exhibit E-8.

9. Copy of a letter dated May 3, 2006 from the Division to the Taxpayer, designated Exhibit E-9.
10. Copy of a letter dated May 17, 2006 from the Division to the Taxpayer, designated Exhibit E-10.
11. Copy of a letter dated July 21, 2006 from the Division to the Taxpayer, designated Exhibit E-11.
12. Copy of a letter dated August 3, 2006 from the Taxpayer to the Division, designated Exhibit E-12, with the following attachment:
 - a. Copy of Form Gen 74 Offer In Compromise dated August 3, 2006.
13. Copy of a letter dated August 14, 2006 from the Division to the Taxpayer, designated Exhibit E-13.
14. Copy of a letter dated August 27, 2006 from the Taxpayer to the Division, designated Exhibit E-14.
15. Copy of Form E-505 Supplement, dated January 2002, designated Exhibit E-15.
16. Copy of Important Notice- Sales and use Tax Legislative Changes, dated July 2003, designated Exhibit E-16.
17. Copy of Important Notice- Food, dated July 2003, designated Exhibit E-17.
18. Copy of Form E-505, To Registered Taxpayers, dated October 2003, designated Exhibit E-18.
19. Copy of Department's Brief For Tax Hearing, dated February 15, 2007, designated Exhibit E-20.
20. Copy of a letter dated January 3, 2007 from the Assistant Secretary of Administrative Hearings to the Taxpayer, designated Exhibit E-19.

FINDINGS OF FACT

Based on the foregoing evidence of record, the Assistant Secretary makes the following findings of fact:

- (1) Throughout the assessment period, the Taxpayer operated a convenience store which included a restaurant.
- (2) The Taxpayer made retail sales of, amongst other things, food, non-food items, prepared food and soft drinks.
- (3) The assessment against the Taxpayer covers the period from February 1, 2003 through November 30, 2005.
- (4) Throughout the assessment period, State law required that, where local sales tax had been imposed, local sales tax be collected and remitted by retailers selling food.
- (5) Throughout the assessment period, State law required that state and local sales taxes be collected and remitted by retailers selling non-food items.
- (6) Until July 15, 2003, State law required that state and local sales taxes be collected and remitted by retailers selling prepared food and soft drinks unless the items were purchased for home consumption and would be exempt if purchased under the Federal Food Stamp Program.
- (7) From July 15, 2003 on, State law required that state and local sales taxes be collected and remitted by retailers selling prepared food and soft drinks.
- (8) The Taxpayer collected and remitted only the local sales tax on sales of prepared food, soft drinks and non-food items.
- (9) From February 1, 2003 through April 30, 2003 and from June 1, 2003 through September 30, 2003, the Taxpayer collected and remitted more local sales tax on sales of food than required.
- (10) During the assessment period, the Taxpayer failed to collect the state tax portion of the sales tax on sales of prepared food, soft drinks and non-food items.
- (11) The Taxpayer's manner of recording sales made it difficult to determine whether particular sales during the assessment period were of food (subject only to local sales tax) or prepared food, soft drinks or non-food items (subject to the state and local sales taxes).

- (12) To determine the amount of sales attributable to prepared food, soft drinks and non-food items, the auditors looked at the invoices from a sample three-month period showing how much the Taxpayer had spent purchasing food for resale.
- (13) The Taxpayer and the auditors agreed that the Taxpayer routinely applied a 35% mark up in pricing food for resale.
- (14) The auditors multiplied the cost of the purchased food by 1.35 to yield the estimated sales receipts generated during the sample period from sales of food. This number was then subtracted from the total sales receipts generated during the sample period to yield the estimated sales receipts generated from the sales of prepared food, soft drinks and non-food items.
- (15) Applying the estimated sales receipts generated from the sales of prepared food, soft drinks and non-food items to the entire assessment period, the Department assessed the Taxpayer state and local sales taxes on sales of prepared food, soft drinks and non-food items.
- (16) Credit was allowed for local sales tax that the Taxpayer had collected and remitted.
- (17) Credit was allowed for the overpayment of local sales tax during February 1, 2003 through April 30, 2003 and during June 1, 2003 through September 30, 2003.
- (18) The Taxpayer has not shown any documentation to support its contention that the amount of tax assessed on the retail sales of non-food, prepared food and soft drinks was incorrect.
- (19) The Taxpayer stated that it was never notified of the increase in the sales tax rate on prepared food and soft drinks
- (20) The Taxpayer provided affidavits from the co-managers of [Taxpayer], the president of the corporation and its Certified Public Accountant stating that they never received notification from the Department regarding the increase in sales tax rate on prepared food and soft drinks.
- (21) The following notices were mailed to registered taxpayers to notify them of changes in the Law regarding the rate of tax applicable for various types of food:
 - Form E505 Supplement dated 01-02 (Exhibit E-15) was mailed to registered taxpayers regarding changes in the tax rates on food in effect up to that date.
 - Important Notice-Sales and Use Tax Legislative Changes dated 7-03 (Exhibit E-16) was mailed to registered taxpayers and refers

them to the Department's website at www.dor.state.nc.us (now www.dornc.com) for expanded information regarding the changes in tax liability.

- Important Notice--Food dated 7-03 (Exhibit E-17) was posted on the Department's website to provide the expanded discussion of the changes in the tax liability for sale of food.
 - Form E505 dated 10-03 (Exhibit E-18) was mailed to registered taxpayers to provide a summary of law changes including the effect of the changes on food.
- (22) A notice of proposed sales and use tax assessment was mailed to the Taxpayer on February 21, 2006.
- (23) The Taxpayer notified the Department that it objected to the assessment and timely requested a hearing.

CONCLUSIONS OF LAW

Based on the foregoing findings of fact, the Assistant Secretary makes the following conclusions of law:

- (1) The Taxpayer operated as a retailer during the audit period as defined in G.S. 105-164.3(35).
- (2) As a retailer engaged in the business of making retail sales of tangible personal property, the Taxpayer was liable for collecting the applicable State and local sales tax on its retail sales pursuant to G.S. 105-164.4, G.S. 105-467, G.S. 105-483, and G.S. 105-498.
- (3) The Taxpayer is liable for the State rate and local sales tax on its retail sales of non-food items, prepared food and soft drinks during the audit period.
- (4) There is no provision in the Statutes for abatement of tax because a taxpayer did not receive a notice of change.
- (5) Notice of proposed sales and use tax assessment for the audit period was issued pursuant to G.S. 105-241.1.

DECISION

Therefore, the assessment of tax and interest is deemed correct under the law and the facts and is hereby declared to be finally determined and immediately due and payable as allowed by law. Because the failure to pay the tax was not the result of a negligent or intentional act by the Taxpayer, I find reasonable cause to waive the penalties. The proposed assessment of tax and accrued interest is hereby declared to be finally determined and immediately due and collectible with interest as allowed by law.

Made and entered this 12th day of June, 2007.

Eugene J. Cella
Assistant Secretary of Administrative Tax Hearings