

DECISION OF MUNICIPAL TAX HEARING OFFICER

January 25, 2013

Taxpayer
Taxpayer's address

Taxpayer
MTHO # 733

Dear *Taxpayer*:

We have reviewed the arguments presented by *Taxpayer* in its protest and by the City of Tucson (Tax Collector or City) in its Response to the Protest and at the hearing held on November 2, 2012. Taxpayer did not appear at the hearing and the hearing was held in Taxpayer's absence. Taxpayer's explanation for its absence at the hearing established good cause. Therefore the additional evidence submitted by Taxpayer and the Tax Collector's response were included as part of the record. The review periods covered were December 2006, February 2007, January 2008, July 2008, August 2008, January 2009 and June 2010. Taxpayer's protest, Tax Collector's response, and our findings and ruling follow.

Taxpayer's Protest

Taxpayer's records were destroyed. Taxpayer has not been able to obtain the necessary information from its customers. Taxpayer agrees it was a construction contractor on three of the projects that were assessed. Taxpayer believes the City's estimate of the cost of the projects is about 30% too high. With respect to the other four projects the City assessed, Taxpayer was a construction manager, not a construction contractor. Taxpayer would like to obtain additional information in support of its position.

Tax Collector's Response

Taxpayer agrees it is taxable on three of the projects. Taxpayer has not substantiated that it was a construction manager on the remaining projects. Taxpayer was requested to provide records to determine gross income and allowable deductions. The Tax Collector made several requests but Taxpayer failed to provide any records. The Tax Collector therefore based the assessment on an estimate of income. Taxpayer has not presented records or other documents to show that the Tax Collector's estimate of gross receipts was not reasonable and correct. The City's assessment should be upheld as issued.

Discussion

Taxpayer obtained building permits for seven projects in the City. Taxpayer was listed as the contractor on the building permits. Taxpayer did not file City privilege tax reports with respect to any of the projects.

The Tax Collector sent Taxpayer an initial audit letter on November 2, 2010. A follow-up letter was sent January 4, 2011. A final notice was sent Taxpayer on June 8, 2011. Because Taxpayer

did not respond to previous correspondence, a tentative assessment was mailed to Taxpayer on June 20, 2011 and was again mailed to an alternative address on June 30, 2011. An updated tentative assessment was mailed to Taxpayer on September 29, 2011. Each tentative assessment informed Taxpayer that it was based on an estimate, but could be revised if Taxpayer provides records for the audit period. Taxpayer did not provide any records.

A final estimated assessment was mailed to Taxpayer on February 8, 2012. The estimated assessment was computed by doubling the amounts listed on the building permits and not allowing any deductions. Taxpayer protested and requested that the auditor contact Taxpayer's customers for job costs and the amounts paid to Taxpayer. The auditor attempted to contact the customers but did not receive any documentation.

The auditor again requested documentation from Taxpayer. Taxpayer requested additional time to obtain the records previously requested. The matter was then forwarded to the Municipal Tax Hearing Office in July 2012 and a hearing was scheduled. Taxpayer failed to appear at the hearing. Taxpayer was allowed to make a post-hearing submission.

The Tax Collector was Authorized to Issue an Estimated Assessment.

Starting in November 2010 the Tax Collector made several requests to Taxpayer for records to determine gross income and allowable deductions for the projects where Taxpayer obtained the building permits. Taxpayer has not provided any business records or other documentation showing Taxpayer's receipts and any allowable deductions for the audit period. The auditor tried to obtain documentation from Taxpayer's customers but was not successful.

It was Taxpayer's responsibility to keep books and records showing Taxpayer's gross income attributable to its activities in the City. Regulation § 19-350.1(g) requires a taxpayer's books and records to indicate both individual transaction amounts and totals for each reporting period for each category of taxable, exempt, and excluded income. Taxpayer did not provide the necessary records to permit the Tax Collector to ascertain Taxpayer's gross receipts and any applicable deductions or exemptions for the review periods.

Because Taxpayer did not have the required records, Tucson City Code (TCC) §§ 19-545(b) and 19-555(e) authorize the Tax Collector to estimate Taxpayer's income, on a reasonable basis, to determine the correct tax. Taxpayer obtained the building permits for the projects at issue and was listed as the contractor. The building permit listed the estimated cost of the construction project. In the absence of other information, it was reasonable for the Tax Collector to base its estimated assessment on the building permits taken out by Taxpayer.

Taxpayer has not Shown that the Tax Collector's Estimate was not Reasonable or Correct.

TCC § 19-545(b) requires that any estimate made by the Tax Collector be made on a reasonable basis. The Tax Collector computed its estimated assessment by doubling the amount of the building permit and not allowing for any deductions such as the 35% standard deduction. The Tax Collector doubled the building permit value because at times the permit value understates the real cost of the construction. This would help ensure the assessment was not understated and would allow the Tax Collector to revise the assessment down if supported by records.

It is the responsibility of the taxpayer to prove that the Tax Collector's estimate is not reasonable and correct. TCC § 19-545(b). In support of its position that the estimate is overstated, Taxpayer provided copies of bank statements and other information relating to costs of construction for seven of the seventeen month period of January 2008 through May 2009. A total of \$288,138.13 was paid for construction of the *LP Projects* during those seven months, a monthly average of \$41,162.59.

No evidence was presented and there is no basis in the record to assume that construction only occurred during the seven months for which information was provided. It is also possible that construction on the *LP Projects* was conducted each month during the period January 2008 through May 2009. Assuming the monthly average construction cost of \$41,162.59 applied to each month during the period January 2008 through May 2009, a total cost of construction for the *LP Projects* would be \$699,764.03. Twice the building permit values for the *LP Projects* was \$680,916.50. Taxpayer has not met its burden to prove that the Tax Collector's estimate of gross income is not reasonable and correct.

Taxpayer was Entitled to the 35% Standard Deduction.

The Tax Collector did not allow Taxpayer a 35% standard deduction because Taxpayer did not report gross receipts. TCC § 19-415(a) imposes the City privilege tax measured by the taxpayer's gross income from the business activity of construction contracting within the city. Subsection (b) allows certain deductions. Once all other available deductions have been applied, TCC § 19-415(b)(2) allows a deduction of 35% against the remaining gross income subject to tax. There are no qualifications to the 35% deduction other than all other deductions have to be applied first. Taxpayer was entitled to the 35% deduction from the gross income the Tax Collector determined was otherwise subject to the City privilege tax under TCC § 19-415.

Taxpayer has not Shown it was a Construction Manager.

Taxpayer contends it was a construction manager for *LP Projects* on four of the projects included in the assessment. Taxpayer however was listed as the contractor on the building permits. Whether a Taxpayer is a construction contractor or a construction manager begins with a review of the agreement between the parties. Taxpayer has not provided contracts relating to the four projects for which Taxpayer contends it was a construction manager. *LP Projects* has not provided any documentation confirming whether Taxpayer was acting as a construction manager.

In its post-hearing submission Taxpayer provided copies of six bank statements for *LP Projects* and 14 cancelled checks. The bank statements showed receipts and payments but did not identify any transactions with Taxpayer or transactions relating to the projects at issue for any month. There was no correlation between the bank statements and the projects at issue. The cancelled checks did not identify any of the projects at issue. Even if the cancelled checks showed that *LP Projects* paid some of the project expenses, that does not address whether Taxpayer was acting as a construction manager. While the checks may indicate that they were signed by *Taxpayer*, Taxpayer's principal, no information was submitted regarding *Taxpayer's* or Taxpayer's capacity with *LP Projects*. Taxpayer has therefore not shown that it was a construction manager with respect to the four *LP Projects*.

Taxpayer's Request for Additional Time to Obtain Documents.

Taxpayer requested in its post-hearing submission that it be allowed additional time to obtain documentation. The Tax Collector first contacted Taxpayer by letter in November 2010. The Tax Collector's listing of attempted contacts with Taxpayer and various requests for information indicated that Taxpayer was not responsive in providing information. The auditor tried to obtain information from Taxpayer's customers but was not successful. The cancelled checks and bank statements Taxpayer did provide in its post-hearing submission do not shed light either on Taxpayer's gross receipts or Taxpayer's capacity as a construction manager. Taxpayer has had over two years to obtain and provide records and other information. Nothing has been provided indicating that additional time will produce useful results. No further delay is warranted and this matter is ready for decision.

Based on the foregoing, the Tax Collector's assessment is upheld except that the Tax Collector shall allow Taxpayer the 35% standard deduction.

Findings of Fact

1. Taxpayer is a limited liability company.
2. Taxpayer obtained building permits for seven construction projects in the City.
3. Taxpayer was listed as the contractor on the building permits.
4. Taxpayer did not file City privilege tax reports with respect to any of the projects.
5. The Tax Collector sent Taxpayer an initial audit letter dated November 2, 2010 and a follow-up letter dated January 4, 2011.
6. Taxpayer did not respond to the letters.
7. A final notice was sent Taxpayer on June 8, 2011 asking Taxpayer to make available books and records listed in the letter such as cash receipts, general ledger, check register, bank statements, cancelled checks and any other records pertinent to the business. Taxpayer did not respond.
8. The Tax Collector sent two tentative assessments to Taxpayer, first on June 20, 2011 (and on June 30, 2011 to an alternate address) and the second on September 29, 2011. Each tentative assessment informed Taxpayer that it was based on an estimate, but could be revised if Taxpayer provides records for the audit period.
9. Taxpayer did not provide any records.
10. A final audit assessment was mailed to Taxpayer on February 8, 2012.
11. The estimated assessment was computed by doubling the value listed on the building permits and not allowing any deductions.
12. The Tax Collector doubled the building permit value because at times the permit value understates the real cost of the construction.
13. Taxpayer protested the assessment.
14. Taxpayer provided customers' names to the auditor and requested that the auditor contact the customers for job costs and the amounts paid to Taxpayer.
15. The auditor attempted to contact the customers but did not receive any documentation from the customers.
16. The auditor again requested documentation from Taxpayer. Taxpayer requested additional time to obtain the records previously requested.
17. The matter was forwarded to the Municipal Tax Hearing Office in July 2012 and a hearing was scheduled and held.
18. Taxpayer did not appear at the hearing.
19. In its post-hearing submission Taxpayer:
 - a. requested additional time to provide documentation.
 - b. agreed it was subject to tax on three of the projects in the assessment.

- c. contended it was a construction manager for **LP Projects** on the other four projects located at **123 N. Street, 456 E. Street, 789 N. Street** and **987 E. Street**.¹
- d. provided copies of six bank statements for **LP Projects** and 14 cancelled checks.
- e. contended that the checks paid as shown on the bank statements were for construction on the **LP Projects**.

20. The bank statements showed the following disbursements by checks and electronic and other withdrawals:

Statement Date	Checks/ Debit Paid	Electronic Withdrawal	Other Withdrawal
June 2008	45,951.44	136.92	330,274.50
Sep 2008	67,440.55	3,650.00	1,827.50
Dec 2008	38,260.49	1,310.51	4,991.40
Feb 2009	36,367.04	1,310.51	4,000.00
Mar 2009	40,429.18	1,310.51	320.00
May 2009	<u>13,359.43</u>	<u>1,310.51</u>	<u>0.00</u>
Totals	241,808.13	9,028.96	341,413.40

- 21. Taxpayer also listed \$46,330 as the amount of checks paid for January 2009.
- 22. No bank statements, financial records or other information were provided for the other months from January 2008 through May 2009 other than those listed above.
- 23. Taxpayer did not address the use of the funds withdrawn electronically or by other means.
- 24. Taxpayer's submission shows that the amounts paid for construction on the **LP Projects** during the listed months, including January 2009, totaled \$288,138.13.
- 25. The average monthly construction cost shown for the **LP Projects** is \$41,162.59.
- 26. The **LP Projects** located at **123 N. Street** was assessed for the month of January 2008.
- 27. Taxpayer's submission indicates that construction on **LP Projects** continued through at least May 2009, a seventeen month period from January 2008.
- 28. Applying the average monthly construction cost shown for the **LP Projects** to each month of the period January 2008 through May 2009 totals \$699,764.03.
- 29. The building permit values for the four **LP Projects** totaled \$340,458.24.
- 30. Two times the building permit values totaled \$680,916.50.
- 31. Taxpayer has not provided any other documents.

Conclusions of Law

- 1. The City privilege tax is imposed on persons engaging in certain business activities. Tucson City Code, Chapter 19, Article II.

¹ Taxpayer's submission also referenced a project at **321 E. Street**. That project was not listed in the City's final audit assessment.

2. The privilege tax is measured by the person's gross income from the taxable business activity. TCC § 19-400(a)(1).
3. TCC § 19-415(a) imposes the City privilege tax measured by the taxpayer's gross income from the business activity of construction contracting within the city.
4. All construction contracting gross income subject to the tax and not otherwise deductible is allowed a deduction of thirty-five (35) percent. TCC § 19-415(b)(2).
5. Taxpayer is a person subject to the City privilege tax.
6. Every person subject to the City privilege tax is required to keep records showing the gross income of the taxpayer attributable to any activity occurring in whole or in part in the City. TCC § 19-350(a); Regulation 19-350.1(a).
7. The books and records of the taxpayer are required to indicate both individual transaction amounts and totals for each reporting period for each category of taxable, exempt, and excluded income. Regulation 19-350.1(g).
8. Taxpayer did not have the required records for the audit periods showing Taxpayer's income attributable to the projects in the City.
9. Taxpayer did not make any records available to the Tax Collector for the Tax Collector to correctly determine the amount of tax owed by Taxpayer.
10. The Tax Collector was authorized to estimate Taxpayer's income to determine the correct tax. TCC § 19-555(e).
11. The Tax Collector's estimate is required to be made on a reasonable basis. TCC § 19-545(b).
12. It is the responsibility of the taxpayer to prove that the Tax Collector's estimate is not reasonable and correct. TCC § 19-545(b).
13. An estimate of income based on the building permit value listed on building permits which listed Taxpayer as the contractor was reasonable.
14. It was reasonable for the Tax Collector to assume that the building permit value may understate the real cost of construction.
15. Taxpayer provided copies of bank statements or other information relating to costs of construction for seven of the seventeen month period of January 2008 through May 2009.
16. Based on the facts presented, it can reasonable be assumed that construction on the **LP Projects** were conducted during the period January 2008 through May 2009.
17. Taxpayer has not presented evidence to prove that the Tax Collector's estimate of gross income was not reasonable and correct.
18. Taxpayer was entitled to the 35% standard deduction from any income the Tax Collector determined was otherwise subject to the City privilege tax under TCC § 19-415. TCC § 19-415(b)(2).
19. The Tax Collector's assessment to Taxpayer is upheld in part and denied in part. The Tax Collector shall modify the assessment by allowing Taxpayer the 35% standard deduction.
20. The Tax Collector's Notice of Assessment is proper in all other respects.

Ruling

Taxpayer's protest of the assessment for the periods December 2006, February 2007, January 2008, July 2008, August 2008, January 2009 and June 2010 is granted in part and denied in part.

The Tax Collector shall modify the assessment by allowing Taxpayer the 35% standard deduction.

The Tax Collector's Notice of Assessment is upheld in all other respects.

The Parties have timely rights of appeal to the Arizona Tax Court pursuant to Model City Tax Code Section -575.

Sincerely,

Hearing Officer

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c: ***Tax Audit Supervisor***
Municipal Tax Hearing Office