05-0317
SALES TAX
TAX YEARS: 2001, 2002, 2003
SIGNED: 01-11-2007
COMMISSIONERS: P. HENDRICKSON, R. JOHNSON, M. JOHNSON, D. DIXON,
GUIDING DECISION

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER,	)	**FINDINGS OF FACT, CONCLUSIONS OF LAW, AND FINAL DECISION**
Petitioner,	)	
	)	Appeal No.: 05-0317
v.	)	
	)	Account No.: #####
AUDITING DIVISION OF THE	)	Tax Type: Sales Tax
UTAH STATE TAX COMMISSION,	)	Audit Period: 01/01/01 – 12/31/03
	)	
Respondent.	)	Judge: Chapman

Presiding:
Marc B. Johnson, Commissioner
Kerry Chapman, Administrative Law Judge

Appearances:
For Petitioner: PETITIONER REP. 1, Attorney for Petitioner
PETITIONER REP. 2, Attorney for Petitioner
PETITIONER REP. 3, General Manager, PETITIONER
For Respondent: RESPONDENT REP., Assistant Attorney General

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for a Formal Hearing on November 8, 2006. On November 7, 2006, Auditing Division (the "Division") submitted a Motion in Limine to Limit the Testimony of PETITIONER REP. 3 ("Motion in Limine"), in which it argued that portions of PETITIONER REP. 3' testimony would violate the parol evidence rule. At the Formal Hearing, the parties presented oral arguments concerning the Division's Motion in Limine. In addition, PETITIONER REP. 3 was allowed to testify on all issues, so that his testimony would be available for consideration in case the Commission denied the Division's Motion.

The Division argued that PETITIONER REP. 3, who is the general manager of

PETITIONER ("PETITIONER"), should not be allowed to testify that the terms of a contract between the Petitioner and one of its customers was different than shown on two written invoices that the Petitioner prepared and sent to its customer. Although courts generally do not allow parol evidence to contradict the terms of an integrated agreement, they must first determine whether the written document was an integrated contract, i.e., a writing that was the final and complete expression of the agreement. *See The Cantamar, L.C.C. v. Champagne*, 142 P.3d 140 (Utah App. 2006); *In re Armstrong*, 292 B.R. 678 (10th Cir. 2003). In determining whether the writing was intended by the parties to be an integrated contract, any relevant evidence, including parol evidence, is admissible. *See Novell, Inc. v. The Canopy Group, Inc.*, 92 P.3d 768 (Utah App. 2004).

The Commission must determine whether the two invoices at issue are integrated contracts. Accordingly, PETITIONER REP. 3' testimony is relevant to these proceedings. For this reason, the Commission denies the Division's Motion in Limine and will consider PETITIONER REP. 3' testimony in determining whether the invoices at issue are integrated contracts. If that determination is yes, the testimony will be limited to clarify any ambiguity that may exist in the contracts. If that determination is no, PETITIONER REP. 3' testimony will be considered in its entirety.

Based upon the evidence and testimony presented at the hearing, the Tax Commission hereby makes its:

FINDINGS OF FACT

1. The tax in question is sales and use tax.

2. The audit period in question is January 1, 2001 through December 31, 2003.

3. The Division issued a Statutory Notice – Sales and Use Tax ("Statutory Notice") to PETITIONER on February 18, 2005, in which it imposed $$$$$ in additional tax for the audit period, plus interest.

4. PETITIONER is in the business of locating and selling heavy equipment to construction companies and other businesses.

5. On Amended Schedule 2 of the Statutory Notice, the Division assessed additional tax on the Petitioner's sales of 13 pieces of equipment, determining that all of the transactions were "disallowed exempt sales." The Division included comments on the schedule, which stated that "[t]he transactions listed are exempt sales for which valid exemption documentation was not provided. Acceptable documentation may include: exemption certificates, verification of out-of-state shipment, or purchase order information."

6. PETITIONER is contesting two of the 13 disallowed exempt sales, specifically two sales the Petitioner made to COMPANY A ("COMPANY A"), a now defunct STATE 1 company.

7. In 2001, the Petitioner made three sales to COMPANY A, as shown on the invoices submitted as Exhibit P-1. The three sales include the two disallowed sales that the Petitioner is contesting , as well as a third sale that the Division did not assess. All three sales occurred approximately four years prior to the issuance of the Statutory Notice.

8. The two COMPANY A sales that the Petitioner is contesting are: 1) the February 19, 2001 sale of a EQUIPMENT A for a total of $$$$$; and 2) the April 13, 2001 sale of another EQUIPMENT B for $$$$$. The third sale to COMPANY A, which the Division did not assess, is the February 21, 2001 sale of a EQUIPMENT C for $$$$$$.

9. The invoices for all three COMPANY A sales indicate that the sales were "FOB[1]

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1 Utah Code Ann. §70A-2-319(1) provides that the term "F.O.B. (which means "free on board") at a named place" is a delivery term under which:

> (a) when the term is F.O.B. the place of shipment, the seller must at that place ship the goods in the manner provided in this chapter (Section 70A-2-504) and bear the expense and risk of putting them into the possession of the carrier; or
> (b) when the term is F.O.B. the place of destination, the seller must at his own expense and risk transport the goods to that place and there tender delivery of them in the manner provided in this chapter (Section 70A-2-503);
> . . . .

Utah," as found in the top section of each invoice. However, the information in the bodies of the invoices differed, as follows:

a. In the body of the February 19, 2001 invoice for one of the EQUIPMENT A & EQUIPMENT B at issue, the phrase "FOB: CITY, UT" appears.

b. In the body of the April 13, 2001 invoice for the other EQUIPMENT B at issue, there is no additional information.

c. In the body of the February 21, 2001 invoice for the EQUIPMENT C, which is the sale not assessed, the phrase "CIF[2] CITY 2, CO" appears.

10. The Division determined that the two contested COMPANY A sales were taxable Utah sales because the invoice for each transaction shows FOB Utah and because the Petitioner was unable to locate and provide records indicating that the equipment at issue was shipped for delivery outside of Utah.

Black's Law Dictionary (5th ed. 1979) provides that the term "FOB" is an abbreviation for "free on board." The definition of "free on board" provides that the seller assumes all responsibilities and costs up to the point of delivery. The definition of "FOB" provides that title to goods usually passes from seller to buyer at the FOB location.

2 UCA §70A-2-320 defines the term "C.I.F" as follows:

> 1) The term C.I.F. means that the price includes in a lump sum the cost of the goods and the insurance and freight to the named destination. . . .
> (2) Unless otherwise agreed and even though used only in connection with the stated price and destination, the term C.I.F. destination or its equivalent requires the seller at his own expense and risk to
>
> > (a) put the goods into the possession of a carrier at the port for shipment and obtain a negotiable bill or bills of lading covering the entire transportation to the named destination; and
> > (b) load the goods and obtain a receipt from the carrier (which may be contained in the bill of lading) showing that the freight has been paid or provided for;
> > . . . .

Black's Law Dictionary (5th ed. 1979) provides that the term "CIF" is an abbreviation for "costs, insurance, and freight" and means that the "[q]uoted sales price . . . includes cost of goods, freight, and insurance."

11. In the Explanation of Audit Findings that accompanied the Statutory Notice, the Division explained that "[t]he Preliminary Notice dated January 3, 2006 has been amended to reflect our concurrence with additional information provided. . . . One sale to COMPANY A was deleted since the equipment was shipped out-of-state."

12. The Petitioner could only locate a shipping document for one of its three sales to COMPANY A. This shipping invoice from COMPANY B ("COMPANY B"), submitted as Exhibit P-2, is dated February 23, 2001 and relates to the February 21, 2001 sale of the EQUIPMENT C, which was not assessed. The shipping invoice shows that the Petitioner was charged to have the EQUIPMENT C shipped to STATE 1.

13. The Petitioner asserts that all three sales to COMPANY A (i.e, the two contested sales and the third sale that was not assessed) were nontaxable sales made in interstate commerce, because in each instance, the equipment was shipped for delivery outside of Utah.

14. The Petitioner argued that it could not locate any documents directly related to shipping the equipment at issue in the two contested sales, not only because COMPANY A had gone out of business, but also because the sales were approximately four years old by the time the Statutory Notice was issued. The Petitioner contends that COMPANY B, the company hired to deliver the equipment, did not employ a four-year retention policy for shipping documents. As a result, the Petitioner relied on the testimony of PETITIONER REP. 3 as evidence that the equipment was shipped to STATE 1.

15. PETITIONER REP. 3 is the general manager of PETITIONER and works under the direction of OWNER, the company's owner. As general manager, PETITIONER REP. 3' duties include overseeing the day-to-day operations of the company, seeing that machinery clears customs, and buying and selling equipment. PETITIONER REP. 3 Testimony.

16. OWNER negotiated with and entered into an oral contract with COMPANY A for

the sale of the equipment at issue. The Petitioner's bookkeeper, OWNER'S SPOUSE, prepared the invoices sent to COMPANY A (Exhibit P-1). PETITIONER REP. 3 did not participate in negotiating the contracts with COMPANY A or preparing the invoices that the Petitioner sent to COMPANY A. PETITIONER REP. 3 Testimony.

17. PETITIONER REP. 3 has been employed at PETITIONER for ten years, including 2001, the year the two COMPANY A transactions at issue occurred. PETITIONER REP. 3 arranged for COMPANY B to pick up the equipment at issue in the two contested transactions and deliver it to STATE 1. PETITIONER REP. 3 Testimony.

18. PETITIONER REP. 3 was present when COMPANY B loaded the equipment at issue for delivery to COMPANY A. COMPANY B billed PETITIONER for the costs to ship the equipment at issue to STATE 1. PETITIONER REP. 3 Testimony.

APPLICABLE LAW

1. Utah Code Ann. §59-12-103(1) provides that "[a] tax is imposed on the purchaser as provided in this part for amounts paid or charged for the following transactions: (a) retail sales of tangible personal property made within the state; . . ."

2. Utah Admin. Rule R865-19S-44 ("Rule 44") provides guidance in determining when a sale is made in interstate commerce, as follows:

> A. Sales made in interstate commerce are not subject to the sales tax imposed. However, the mere fact that commodities purchased in Utah are transported beyond its boundaries is not enough to constitute the transaction of a sale in interstate commerce. When the commodity is delivered to the buyer in this state, even though the buyer is not a resident of the state and intends to transport the property to a point outside the state, the sale is not in interstate commerce and is subject to tax.
> B. Before a sale qualifies as a sale made in interstate commerce, the following must be complied with:
> 1. the transaction must involve actual and physical movement of the property sold across the state line;

> 2. such movement must be an essential and not an incidental part of the sale;
> 3. the seller must be obligated by the express or unavoidable implied terms of the sale, or contract to sell, to make physical delivery of the property across a state boundary line to the buyer;
>
> C. Where delivery is made by the seller to a common carrier for transportation to the buyer outside the state of Utah, the common carrier is deemed to be the agent of the vendor for the purposes of this section regardless of who is responsible for the payment of the freight charges.
>
> . . . .

3. UCA §59-12-106(2) (2001), which is currently found at Section 59-12-106(3), provided that a seller must obtain an exemption certificate, as follows:

> For the purpose of the proper administration of this chapter and to prevent evasion of the tax and the duty to collect the tax, it shall be presumed that tangible personal property or any other taxable transaction under Subsection 59-12-103(1) sold by any person for delivery in this state is sold for storage, use, or other consumption in this state unless the person selling the property, item, or service has taken from the purchaser an exemption certificate signed by and bearing the name and address of the purchaser to the effect that the property, item, or service was exempted under Section 59-12-104. The exemption certificates shall contain information as prescribed by the commission.

4. Utah Admin. Rule R865-19S-23 ("Rule 23") provides guidance concerning a seller's responsibility to obtain exemption certificates, as follows:

> A. Taxpayers selling tangible personal property or services to customers exempt from sales tax are required to keep records verifying the nontaxable status of those sales. Records shall include:
> 1. sales invoices showing the name and identity of the customer; and
> 2. exemption certificates for exempt sales of tangible personal property or services if the exemption category is shown on the exemption certificate forms.
>
> . . . .
>
> E. The burden of proving that a sale is for resale or otherwise exempt is upon the vendor. If any agent of the Tax Commission requests the vendor to produce a valid exemption certificate or other similar acceptable evidence to support the vendor's claim that a sale is for resale or otherwise exempt, and the vendor is unable to comply, the sale will be considered taxable and the tax shall be payable by the vendor."

5. Utah Code Ann. §59-12-111(A) requires a sales tax licensee to keep records, as follows:

> Each person engaging or continuing in any business in this state for the transaction of which a license is required under this chapter shall: (a) keep and preserve suitable records of all sales made by the person and other books or accounts necessary to determine the amount of tax for the collection of which the person is liable under this chapter in a form prescribed by the commission;
> (b) keep and preserve for a period of three years all such books, invoices, and other records; and
> (c) open such records for examination at any time by the commission or its duly authorized agent.

6. Utah Admin. Rule R865-19S-22(A) ("Rule 22") provides guidance concerning the sales tax records a seller is required to keep, as follows in part:

> Every retailer, lessor, lessee, and person doing business in this state or storing, using, or otherwise consuming in this state tangible personal property purchased from a retailer, shall keep and preserve complete and adequate records as may be necessary to determine the amount of sales and use tax for which such person or entity is liable. . . .

DISCUSSION AND CONCLUSIONS OF LAW

As explained earlier, the Commission has denied the Division's Motion in Limine and will consider PETITIONER REP. 3' testimony in determining whether the invoices relating to the two contested sales are integrated contracts that express, in writing, the final and complete expression of the agreement between the Petitioner and COMPANY A. PETITIONER REP. 3 testified that the Petitioner and COMPANY A entered into an oral contract or contracts for the purchase of the equipment at issue. As a result, neither party was able to produce a written document that the Petitioner and COMPANY A both signed and that showed the terms to which they agreed. Although the Petitioner prepared the invoices, there is no evidence to suggest that COMPANY A participated in their preparation or concurred with their contents. For these reasons, the Commission finds that the invoices are not written documents that the parties adopted as the final and complete expression of their agreements and, thus, are not integrated contracts. Accordingly, the Commission will consider PETITIONER REP. 3' testimony and give it the weight it deems appropriate in deciding whether or not the two

contested sales are taxable Utah sales or nontaxable sales made in interstate commerce.

Under Rule 44(B), a transaction is deemed to be a sale made in interstate commerce if the following conditions are met:

> 1. the transaction must involve actual and physical movement of the property sold across the state line;
> 2. such movement must be an essential and not an incidental part of the sale; [and]
> 3. the seller must be obligated by the express or unavoidable implied terms of the sale, or contract to sell, to make physical delivery of the property across a state boundary line to the buyer;

In accordance with the rule, a sales contract for equipment qualifies as a nontaxable sale made in interstate commerce, if the seller delivers the equipment or has the equipment delivered out-of-state. The Division did not assess the Petitioner's sale of the EQUIPMENT C to COMPANY A because a shipping invoice showed that the Petitioner arranged and paid to have the truck delivered out-of-state, even though the "FOB Utah" and "CIF STATE 1" terms listed on the sales invoice do not conclusively show where title passed and where delivery occurred.

Similarly, the Petitioner claims that the "FOB Utah" terms that exist on the invoices for the two contested sales were not intended to mean that COMPANY A took physical possession of the equipment in Utah. The Petitioner argues that it arranged and paid to ship the equipment at issue to STATE 1 in the same manner as the EQUIPMENT C, which was not assessed. Although the shipping invoices and other documents associated with the two contested sales were not available, the Petitioner had PETITIONER REP. 3 provide oral testimony to support its argument that the equipment at issue was delivered out-of-state and, thus, nontaxable sales made in interstate commerce.

The Division argues, however, that oral testimony is insufficient to show that the two contested sales were nontaxable sales made in interstate commerce, citing the Utah Supreme Court's decision in *Tummurru Trades, Inc. v. Utah State Tax Comm'n*, 802 P.2d 715 (Utah 1990). In that case, a taxpayer did not collect sales

tax on its sales for resale and out-of-state sales. The taxpayer also failed to keep adequate records and could not produce exemption certificates concerning the transactions. Instead, the taxpayer substituted oral testimony to prove that the sales were exempt. Under these circumstances, the Court found:

> It is clear from the record that Tummurru failed to keep adequate records with regard to its sales and that it was unable to produce the necessary exemption certificates. The purpose for the statutory requirement that merchants keep records of their sales and exemptions is to prevent tax evasion and tax fraud. In the instant case, the Tax Commission properly determined that where Tummurru could not uphold its burden of proving that the sales were made in interstate commerce or for resale by providing records of exemption certificates, the sales tax would be levied. Tummurru's failure to keep records necessarily requires this result because oral testimony is not an adequate substitute for accurate record keeping.

When the *Tummurru* decision was issued in 1990, a specific provision existed in Section 59-12-104(12)(1987) that exempted "sales of use of property which the state is prohibited from taxing under the Constitution or laws of the United States or under the laws of this state,"[3] which include sales made in interstate commerce. Prior to the legislature deleting the exemption in the mid-1990's, the Court found in *Tummurru* that a seller was obligated to keep exemption certificates or other records, as set forth in Section 59-12-106(2) and Rule 23, to prove that an out-of-state sale was not subject to Utah taxation.

It is arguable that the exemption in Section 59-12-104(12)(1987) was never necessary to preclude the taxation of out-of-state sales, as the exemption has been deleted. However, the record keeping requirements of Section 59-12-106(2) and Rule 23 are specifically tied to the exempt sales listed in Section 59-12-104. As long as the exemption for out-of-state sales was among the exemptions listed in Section 59-12-104, it was clear that those record keeping requirements applied to a seller's out-of-state sales, in addition to its other exempt sales. Once the legislature deleted the out-of-state sales exemption from Section 59-12-104, however, the connection between out-of-state sales and the record keeping requirements of Section 59-12-106(2) and Rule 23

3 This provision was deleted from Utah law in the mid-1990's and, thus, no longer existed as of the audit period.

ceased to exist. For this reason, the Petitioner argues that a seller who makes out-of-state sales is no longer required to procure an exemption certificate.

The Commission agrees that a seller is not required to procure an exemption certificate to prove that a sale qualifies as an out-of-state sale. Moreover, the Commission's exemption certificate, USTC Form TC-721 (Rev. 5/06), does not list out-of-state sales as a specific exemption. Nevertheless, the Commission is hesitant to find that the portion of the *Tummurru* decision relating to oral testimony no longer applies to a seller's duty to keep records concerning its sales to customers in other states. The Commission notes that Section 59-12-111 requires a seller to maintain records for three years and Rule 22(A) requires a seller to maintain "adequate records as may be necessary to determine the amount of sales and use tax for which such person may be liable." Both of these provisions require the Petitioner to maintain the necessary records to determine a seller's sales tax liability. For these reasons, the Commission finds that *Tummurru* still applies to sales made in interstate commerce and that oral testimony *alone* is not an adequate substitute for accurate records to prove that a sale is a nontaxable out-of-state sale.[4]

The Commission finds PETITIONER REP. 3' testimony to be credible and to show that the Petitioner arranged and paid to ship the equipment at issue to STATE 1. Were there no documentary evidence to corroborate his testimony, the Commission would likely find that, pursuant to the principles stated in *Tummurru*, the Petitioner had failed to provide adequate evidence to prove that the two contested sales were nontaxable out-of-state sales. However, in this matter, the Petitioner submitted documentary evidence that indirectly supports PETITIONER REP. 3' oral testimony. In addition, because of the statutory changes that have occurred since *Tummurru*, the controlling record keeping statute that now applies to nontaxable out-of-sales is Section 59-12-111, not Section 59-12-106(2). These factors appear to differentiate this matter from the circumstances described

4 As a result, the burden of proof to prove that a sale is not subject to Utah sales and use tax is the same, whether a sale made in interstate commerce is a nontaxable sale, as the Petitioner argues, or an exempt sale, as the Division argues.

in *Tummurru.*

The Petitioner made three sales to COMPANY A within a two-month period in early 2001, with two of the sales occurring within two days of one another. The Commission finds it credible that the parties would have entered into a similar contract for all three sales. The existence of the invoice for the sale of the EQUIPMENT C and its related shipping invoice are records that show that Petitioner arranged and paid to ship at least one of the items sold to COMPANY A to STATE 1. Furthermore, all three invoices to COMPANY A contained the term "FOB Utah," and yet the one sale for which the shipping document could be located was shown to be a nontaxable out-of-state sale. Moreover, although title for a sale that is FOB Utah may pass in Utah, Rule 44(C) makes it clear that a sale that is FOB Utah is still in interstate commerce if the delivery in Utah is made to a common carrier.

The connection between the three COMPANY A sales, the availability of documentary evidence showing that one of the COMPANY A sales was a nontaxable out-of-state even though its invoice contained the term "FOB Utah," the oral testimony, and the three-year retention policy required under Section 59-12-111 are all factors that convince the Commission that the circumstances in this matter differentiate it from the circumstances in *Tummurru*. For these reasons, the Commission finds that sufficient documentary evidence exist to corroborate PETITIONER REP. 3' testimony that the Petitioner arranged and paid to have the equipment at issue shipped to STATE 1. Accordingly, the Commission finds that the two contested COMPANY A sales are nontaxable out-of-state sales.

DECISION AND ORDER

Based upon the foregoing, the Commission finds that the two contested COMPANY A sales, specifically the February 19, 2001 sale of a EQUIPMENT A for a total of $$$$$ and the April 13, 2001 sale of another EQUIPMENT B for $$$$$, are nontaxable out-of-state sales. Accordingly, the Commission orders that these two sales be removed from the Division's assessment. It is so ordered.

DATED this _____ day of _____, 2007.

_____
Kerry Chapman
Administrative Law Judge

BY ORDER OF THE UTAH STATE TAX COMMISSION:

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this _____ day of _____, 2007.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

Marc B. Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

Notice of Appeal Rights: You have twenty (20) days after the date of this order to file a Request for Reconsideration with the Tax Commission Appeals Unit pursuant to Utah Code Ann. §63-46b-13. A Request for Reconsideration must allege newly discovered evidence or a mistake of law or fact. If you do not file a Request for Reconsideration with the Commission, this order constitutes final agency action. You have thirty (30) days after the date of this order to pursue judicial review of this order in accordance with Utah Code

Ann. §§59-1-601 and 63-46b-13 et seq.

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