

STATE OF FLORIDA
DIVISION OF ADMINISTRATIVE HEARINGS

TRUE BLUE POOLS CONTRACTING,)
INC.,)
)
Petitioner,)
)
vs.) Case No. 10-8807
)
DEPARTMENT OF REVENUE,)
)
Respondent.)
_____)

RECOMMENDED ORDER

Administrative Law Judge Eleanor M. Hunter conducted a final hearing in this case by video teleconference between sites in Tallahassee and Miami, Florida, on October 27, 2010.

APPEARANCES

For Petitioner: Samuel B. Reiner, II, Esquire
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For Respondent: John Mika, Esquire
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STATEMENT OF THE ISSUE

The issue is whether Petitioner collected and remitted to Respondent the correct amount of sales and use taxes during the audit period from October 1, 2004, through September 30, 2007,

and, if not, what additional amount of tax plus penalty and interest is due.

PRELIMINARY STATEMENT

On October 26, 2009, Respondent issued a Notice of Proposed Assessment to Petitioner to collect \$113,632.17 in taxes, plus \$28,408.05 as a penalty, and \$43,050.38 in interest (through October 26, 2010), or a total of \$185,090.60 for the audit period. On February 16, 2010, Respondent received the challenge to the proposed assessment in a Petition for Formal Hearing, which was forwarded to the Division of Administrative Hearings (DOAH) on February 26, 2010, and assigned DOAH Case Number 10-1005.

A hearing was scheduled for May 21, 2010, but it was cancelled after the parties filed a Joint Motion for Continuance and a Joint Motion for Provisional Closing Order to allow the parties to try to settle their dispute. Having been unable to do so, the parties filed a Joint Motion to Reopen File and Schedule Final Hearing on August 23, 2010. The case was reopened and assigned DOAH Case Number 10-8807. By Notice of Hearing, the case was set for final hearing, and the hearing was held on October 27, 2010.

At the hearing, Respondent presented the testimony of an auditor, Linda Johnson-Smith. Respondent's Exhibits 1-11 were received in evidence. Petitioner presented the testimony of

Peter Vigil. Petitioner's Composite Exhibit 1 was received in evidence. The Transcript of the hearing was filed November 15, 2010. Proposed Recommended Orders were received from Respondent on December 6, 2010, and from Petitioner on December 13, 2010.

FINDINGS OF FACT¹

1. Petitioner True Blue Pools (Petitioner, taxpayer, or TBP) is a domestic corporation headquartered in Miami-Dade County, Florida.

2. TBP services, repairs, and renovates swimming pools and constructed some pools during the audit period.

3. Respondent, Florida Department of Revenue (Respondent or DOR), is the agency of state government authorized to administer the tax laws of the State of Florida, pursuant to section 213.05, Florida Statutes.²

4. DOR is authorized to prescribe the records to be kept by all persons subject to taxes under chapter 212, Florida Statutes. Such persons have a duty to keep and preserve their records, and the records shall be open to examination by DOR or its authorized agents at all reasonable hours pursuant to section 212.12(6), Florida Statutes.

5. DOR is authorized to conduct audits of taxpayers and to request information to ascertain their tax liability, if any, pursuant to section 213.34, Florida Statutes.

6. On November 2, 2007, DOR initiated an audit of TBP to determine whether it was properly collecting and remitting sales and use taxes to DOR.

7. The audit period was from October 1, 2004, through September 30, 2007.

8. On December 15, 2008, DOR sent TBP its Notice of Intent to Make Audit Changes (NOI), with schedules, showing that TBP owed to DOR additional sales and use taxes in the amount of \$113,632.17, penalty in the amount of \$28,406.05, and interest through December 16, 2008, in the amount of \$34,546.59, making a total assessment in the amount of \$176,586.81.

9. On October 26, 2009, DOR issued its Notice of Proposed Assessment.

10. TBP timely challenged the Notice of Proposed Assessment, filing its petition with DOR and requesting an administrative hearing.

11. Subsequent to the petition being filed, additional documentation was provided by TBP resulting in a revision to the tax, interest, and penalty amount due. DOR's revised work papers, dated May 27, 2010, claim Petitioner owes \$64,430.83 in tax, \$16,107.71 in penalty, and interest through May 27, 2010, in the amount of \$27,071.99, with an assessment of \$107,610.53.

12. The assessed penalty, \$16,107.71, was calculated after 25% of the penalty was waived, pursuant to subsection

213.21(3) (a), Florida Statutes, based on DOR's determination that there is no evidence of willful negligence, willful neglect, or fraud.

13. The audit was conducted to determine liability in four categories: improper sales tax exemptions, unpaid sales taxes for taxable expenses, unpaid use taxes on fixed assets, and unpaid use taxes on taxable materials used to fulfill contracts to improve real property.

Sales Tax Exemptions

14. Due to the large volume of invoices and other records, the auditor conducted a random sampling of invoices for three months during the audit period, October 2004, January 2005, and September 2007.³ If no sales tax was collected and the Petitioner claimed that the transaction was exempt from the requirement to pay taxes, the auditor looked for proof that either the TBP customer was an exempt organization, for example, a school or a church, or that TBP had provided its suppliers with a DOR Form DR-13 to exempt from taxes products acquired for resale.

15. In the absence proof of either type of exemption, DOR assumed taxes should have been paid. Using the difference between taxes collected and taxes due for the three months, the auditor determined that the percentage of error was .016521. When .016521 was applied to total sales of \$1,485,890.79 for the

36-month audit period, the results showed that an additional \$24,548.41 in sales taxes should have been collected from customers, and is due from TBP.

16. Although a business is required to pay taxes for the materials it purchases to use in its business, it is not required to collect taxes from its customers when it enters into lump sum contracts to perform a service for customers.

17. At least one invoice for \$9,500.00 that the auditor treated as an improper exemption was, in fact, a partial payment on a lump-sum contract. The invoice referenced a "shotcrete draw," which represented the collection of funds after the concrete part of pool construction was completed. TBP is not required to collect taxes when it uses lump-sum contracts.

18. Other invoices for pool repair and services were also mischaracterized as exempt by the TBP, but it is not clear that all were payments related to lump-sum contracts. DOR's auditor, nevertheless, testified as follows:

With the knowledge that I have for True Blue Pools, being a lump-sum contractor, True Blue Pools should not charge their customer any sales tax.

Transcript at pages 67-68.

19. DOR concedes that some of TBP's transactions are also exempt from taxes as improvements to real property. In its Proposed Recommended Order, DOR asserted that TBP's use of the

term "improvements to real property" is overbroad, but it did not specify how or why this is the case. During cross-examination of the owner of TBP, only one invoice for \$500.00 for leak detection on the Delgado property was shown to have been for a service rather than for swimming pool construction.

Taxable Expenses

20. DOR audited TBP's purchases of tangible personal property used in the daily operation of its business. The products included chlorine and other chemicals, office supplies, and vehicle parts, expenses, and repairs. The ledger for a 12-month period, calendar year 2006, showed an average monthly additional tax due of \$111.18, or a total of \$4,002.48 in additional taxes for the 36-month audit period. As noted in Petitioner's Proposed Recommended Order, "[t]he representative of TBP did not dispute DOR's allegation that no tax may have been paid on the purchase of all of these items"

Fixed Assets

21. TBP's list of fixed assets was taken from the depreciation schedule on Internal Revenue Service Form 4562. The items listed are computer- and software-related. TBP provided no proof that it had paid a use tax. The additional tax due equals \$419.94. Petitioner's Proposed Recommended Order includes the statement that "[a]gain, the representative of TBP

did not dispute DOR's allegation that no tax may have been paid on the purchase of these items"

Taxable Materials

22. Taxable materials, those purchased to fulfill a contract to improve real property, included items used to build, renovate, and repair pools. The items included concrete, meters, drains, and valves.

23. For the 12-month sample period, calendar year 2006, TBP failed to pay taxes on material purchases in the total amount of \$168,310.05, or an average of \$14,078.96 a month. For the 36-month audit period, the total of the purchases was \$506,842.56. With a 6 percent tax due for the state and 1 percent for the county, the total additional tax due on materials is \$35,460.00.

24. TBP conceded that it improperly used a resale exemption to purchase taxable materials from suppliers without paying taxes. The materials were used to provide services and were not resold. Acknowledging again that TBP uses lump-sum contracts, this time to support the collection of additional taxes, the auditor testified as follows:

And the law states that the taxpayer's [sic] an ultimate consumer of all materials purchased to fulfill a lump-sum contract, and that's what they told me they operate under, a lump-sum contract.

Transcript at page 58.

25. At the hearing, TBP used its actual profit and loss statement to show that the cost of goods it sold (general purchases and taxable materials) in the amounts of \$18,360.77 in October 2004, \$8,519.22 in January 2005, and \$4,818.65 in September 2007. Corresponding taxes for each of those months should have been \$1,285.25, \$596.35, and \$337.31, or an average of \$739.63 a month, or a total of \$26,626.68 for 36 months. The goods that it sold were not at issue in the audit of taxable materials, rather it was TBP's purchases from vendors that should have been taxed that resulted in DOR's audit results.

Total Additional Sales and Use Taxes Due

26. The three categories of additional taxes due, \$4,002.48 for taxable expenses, \$419.94 for fixed assets, and \$35,460.00 for taxable materials, equal \$39,882.42 in additional taxes due during the audit period.

Taxes Paid

27. TBP filed DOR Forms DR-15, monthly sales and use tax reporting forms, and paid sales and use taxes during the audit period. For the sample months used by DOR to examine sales tax exemptions, TBP paid \$1,839.10 in taxes in October 2004, \$1,672.73 in January 2005, and \$1,418.13 in September 2007. Using the three months to calculate an average, extended to 36 months, it is likely that TBP paid \$59,712 in taxes.

28. TBP asserted that DOR was required to, but did not, offset the deficiency of \$39,882.42, by what appears to be an overpayment of \$59,712.00 in sales and use taxes.

29. Other than pointing out that the amount reported on the DR-15s differed, being sometimes more and sometimes less than the amount shown on the profit and loss statements, DOR did not dispute TBP's claim that it had paid sales and use taxes. TBP's representative explained that end-of-the-year adjustments for additional collections or for bad debt could cause the amounts on the DR-15s and profit and loss statements to differ.

30. With regard to the taxes paid, DOR took the following position in its Proposed Recommended Order:

Petitioner's DR-15's [sic] for the collection periods October 2004, and January 2005, [and September 2007] (Petitioner's Composite Exhibit 1) do reflect sales tax being collected and remitted to DOR. DOR does not allege that Petitioner never paid tax on its purchases, or made bona fide exempt sales for which no tax was collected. DOR's audit findings identify just those which occurred within the sample period, scheduled in the auditor's workpapers, and applied over the entire audit period.

31. The DR-15s are taken from the sample months selected by DOR within the audit period, and DOR does not address TBP's claim that a set off for taxes paid was mandatory, pursuant to subsection 213.34(4), Florida Statutes. Using the audit schedules, DOR showed credit for taxes paid in the amounts of

\$20.63 for taxable expenses, \$0 for fixed assets, and \$24.31 in state taxes and \$1.03 for county taxes on taxable materials. The amounts are far less than the \$59,712.00 in sales/use taxes TBP showed that it paid during the audit period.

CONCLUSIONS OF LAW

32. The Division of Administrative Hearings has jurisdiction over the parties to and subject matter of this proceeding pursuant to sections 72.011(1), 120.569, and 120.57(1), Florida Statutes (2003).

33. DOR has the burden of proof in this proceeding, but that burden is "limited to a showing that an assessment has been made against the taxpayer and the factual and legal grounds upon which the . . . department made the assessment." See § 120.80(14)(b)2., Fla. Stat.

34. The standard of proof is a preponderance of the evidence. See § 120.57(1)(j), Fla. Stat. A "preponderance" of the evidence means the greater weight of the evidence. See Fireman's Fund Indemnity Co. v. Perry, 5 So. 2d 862 (Fla. 1942).

35. Florida Administrative Code Rule 12A-1.051 applies to sales to or by contractors who repair, alter, improve and construct real property. Rule 12A-1.051(4) provides the following:

General rule of taxability of real property contractors. Contractors are the ultimate consumers of materials and supplies they use

to perform real property contracts and must pay tax on their costs of those materials and supplies, unless the contractor has entered a retail sale plus installation contract. Contractors performing only contracts described in paragraphs (3)(a) . . . do not resell the tangible personal property used to the real property owner but instead use the property themselves to provide the completed real property improvement. Such contractors should pay tax to their suppliers on all purchases. . . . They should charge no tax to their customers, regardless of whether they itemize charges for materials and labor in their proposals or invoices, because they are not engaged in selling tangible personal property.

36. As referenced in the general rule, the specific provision applicable to lump-sum contracts is as follows:

(3) Classification of contracts by pricing. The taxability of purchases and sales by real property contractors is determined by the pricing arrangement in the contract. Contracts generally fall into one of the following categories:

(a) Lump sum contracts. These are contracts in which a contractor or subcontractor agrees to furnish materials and supplies and necessary services for a single stated lump sum price.

37. TBP is not required to collect taxes when it performs work pursuant to a lump-sum contract.

38. In response to DOR's claim that TBP's use of the term "improvement to real property" is overbroad, Technical Assistance Advisement 03A-025R on Sales and Use Tax -- Service Warranties, was issued by DOR to interpret sections: 212.0506,

212.06, Florida Statutes, and Rule 12A-1.051, and provides, in relevant part, the following taxpayer guidance:

FACTS:

According to the petition, Taxpayer sells service warranty contracts for the repair and/or replacement of certain swimming pool equipment and provides certain services. The service contract identifies the covered equipment as pumps, motors, filters, underwater light fixtures, transformers, skimmers, main drains, and valves. The contract identifies the covered services as leak detection and leak repair . . .

REQUESTED ADVISEMENT:

Advice is requested whether the sale of the service warranty is subject to tax.

LAW AND DISCUSSION:

Section 212.06(14), Florida Statutes, defines certain terms to help determine whether a person is working with an improvement to real property. . . (c) "Improvements to real property" includes the activities of building, erecting, constructing, altering, improving, repairing, or maintaining real property. Pumps, motors, filters, underwater light fixtures, transformers, main drains, valves and timer boxes on an in-ground pool are classed as improvements to real property. Leak detection and repair of an in-ground pool are also improvements to real property.

Revised Technical Assistance Advisement No. 03A-025R Department of Revenue, 2003 Fla. Tax LEXIS 47 (July 14, 2003).

39. TBP's interpretation of leak detection as an improvement to real property is not overbroad.

40. DOR failed to demonstrate that it has a factual or legal basis to collect sales taxes on lump-sum contracts for constructing or repairing in-ground swimming pools.

41. TBP does not contest DOR's assessment of \$4,002.48 in sales taxes, \$419.94 in use taxes on fixed assets, and \$35,460.00 in use taxes on materials, or a total of \$39,882.42.

42. DOR did not contest TBP's claim that it paid sales and use taxes during the audit period, nor its use of the sampling method to determine that, over the 36-month audit period, it paid \$59,712.00 in use/sales taxes. TBP asserted that subsection 213.34(4), Florida Statutes, mandates a setoff of taxes paid against taxes owed.

43. DOR took the position that TBP should file a request for a refund rather than have a deficiency offset against taxes paid.

44. TBP's position is supported by the decision in Dep't of Revenue v. Kemper Investors Life Ins. Co., 660 So. 2d 1124, at 1129-1130 (Fla. 1st DCA 1995) in which the court ruled as follows:

Here, although there was no audit of an alleged overpayment of insurance premium taxes in the audit period under review, we are of the view that this omission works against the Department, rather than against the taxpayer. By reference to section 215.26, the language of section 213.34(4) appears to place a responsibility upon the state, through its departments and

officials, correctly and timely to determine the tax burden falling upon the taxpayer, over and above its responsibilities in merely responding to claims for a refund. We view these amendments as remedial legislation, and therefore applicable to the resolution of the case before us.
(citations omitted)

As shown above, section 213.34 specifically states that the Department shall offset the overpayment of any tax during an audit period against a deficiency of any tax determined to be due during the same audit period.

45. Because the deficiency is less than the taxes paid, the assessment should be voided.

RECOMMENDATION

Based upon the forgoing findings of fact and conclusions of law, it is recommended that the Department of Revenue issue a final order dismissing the Notice of Intent to Make Audit Changes dated December 15, 2010.

DONE AND ENTERED this 20th day of January, 2011, in Tallahassee, Leon County, Florida.



ELEANOR M. HUNTER
Administrative Law Judge
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Filed with the Clerk of the
Division of Administrative Hearings
this 20th day of January, 2011.

ENDNOTES

¹ Findings of Fact 1 through 11 are taken from the Joint Pre-Hearing Stipulation.

² Unless otherwise indicated, all references to Florida Statutes are to the 2010 edition.

³ The taxpayer never signed the Sampling Agreement, a consent form for the use of the sampling method, but the auditor said the taxpayer agreed verbally. Any objection to the sampling method is assumed to have been waived at hearing when the Petitioner used the same method to estimate the taxes it had paid. See Finding of Fact 27.

COPIES FURNISHED:

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NOTICE OF RIGHT TO SUBMIT EXCEPTIONS

All parties have the right to submit written exceptions within 15 days from the date of this Recommended Order. Any exceptions to this Recommended Order should be filed with the agency that will issue the Final Order in this case.