WALTER W. MUNCASTER MUNCASTER & ASSOCIATES P.O. Box 291 Elmore, AL 36025, Taxpayer, v. STATE OF ALABAMA DEPARTMENT OF REVENUE.	'	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION DOCKET NOS. S. 98-273 S. 98-408

OPINION AND PRELIMINARY ORDER

The Revenue Department assessed State sales and rental tax and Autauga County sales tax against Walter W. Muncaster (ATaxpayer@), d/b/a Muncaster & Associates, for September 1993 through June 1997. The Taxpayer appealed to the Administrative Law Division pursuant to Code of Ala. 1975, '40-2A-7(b)(5)a. The appeal was docketed as S. 98-273. The Department later assessed State sales and rental tax and Autauga County sales tax against the Taxpayer for July 1997 through February 1998. The Taxpayer again appealed to the Administrative Law Division. That appeal was docketed as S. 98-408. The cases were consolidated, and a hearing was conducted on May 10, 2000. Kenneth Hemphill represented the Taxpayer. Assistant Counsel Wade Hope represented the Department.

ISSUES

The issues in this case are:

(1) Did the Department timely file its Answer in both appeals as required by Code of Ala. 1975, '40-2A-9(c); and

(2) Did the Department properly compute the Taxpayer=s liability for the subject periods using the best information available.

FACTS

The Taxpayer sold computers and related equipment at retail in Alabama during the periods in issue. The Taxpayer failed, however, to obtain an Alabama sales tax license, or file returns and pay sales tax to the Department on those sales.

The Department discovered when it audited various businesses in Central Alabama that the Taxpayer had made taxable retail sales to those businesses during the subject periods. The Taxpayer failed, however, to charge and collect sales tax on those sales.

The Department contacted the Taxpayer for the purpose of auditing his records. The Taxpayer adamantly refused to allow the Department to review his records, or otherwise provide information concerning his sales tax liability.[1] The Department consequently computed the Taxpayer=s taxable sales during the subject periods using copies of sales invoices obtained from his customers. Because the Taxpayer failed to cooperate, the Department was aware of only those customers it discovered by independent audit.

The Taxpayer had three primary customers during the periods in issue. One had a

[1]The Taxpayer claimed in a letter to the Department examiner that AI am not (the Revenue Department=s) personal tax collector nor have I ever agreed to function as such, either explicitly or implicitly.@ Dept. Ex. 10.

direct pay permit which allowed it to purchase tangible property tax-free. The Taxpayer=s sales to that customer thus were not included in the audit.

The two other primary customers will be referred to as Customer A and Customer B for confidentiality purposes. The Taxpayer failed to charge sales tax on his sales to Customer A. However, the Department=s audit of Customer A showed that Customer A had reported and remitted sales tax to the Department on those items purchased from the Taxpayer. The Taxpayer=s representative stated at the May 10 hearing that the Taxpayer and his customers had agreed that the customers, not the Taxpayer, would report and pay sales tax to the Department.

The Department determined that Customer A had erroneously paid the sales tax because the Taxpayer, as seller, and not Customer A, as purchaser, was obligated to collect and remit sales tax to the Department. The Department accordingly refunded the tax to Customer A, plus applicable interest. The Department in turn included the gross receipts received by the Taxpayer from his sales to Customer A in the audit.

Customer B reported its monthly sales tax to the Department on an estimated basis pursuant to Code of Ala. 1975, '40-23-7(c). The Department thus could not verify that Customer B had reported and paid sales tax to the Department on its purchases from the Taxpayer. Consequently, Customer B did not receive a refund relating to its purchases from the Taxpayer. As with Customer A, the Department included the gross receipts received by the Taxpayer from his sales to Customer B in the audit.

The Department totaled the Taxpayer=s taxable sales to Customers A and B, and also a few taxable sales to other customers identified by audit. The Department also

computed the Taxpayer=s rental gross receipts using those customers= records. The Department then tripled the sales and rental gross receipts to arrive at taxable gross receipts. The Department tripled the amounts to (1) encourage the Taxpayer to provide records so that a more accurate figure could be determined, and (2) protect the State=s interest and ensure that the Taxpayer paid all tax due.

The Department entered the final assessments for September 1993 through June 1997 on April 7, 1998. The Taxpayer timely appealed. The Administrative Law Division docketed the appeal as S. 98-273, and notified the Legal Division of the appeal on May 11, 1998. The Department filed its Answer in S. 98-273 on July 30, 1998.

The Department entered the final assessments for July 1997 through February 1998 on August 12, 1998. The Taxpayer again appealed. The Administrative Law Division docketed the appeal as S. 98-408, and notified the Legal Division of the appeal on September 11, 1998.

When it received the Taxpayer=s second appeal, the Administrative Law Division continued a hearing previously scheduled in S. 98-273. The Preliminary Order stated that Aas soon as the Department files its Answer in S. 98-408, the cases will be consolidated and set for hearing.@

The Department filed a Motion To Consolidate Cases with the Administrative Law Division on March 3, 2000. The motion stated in part that the AAnswer filed in Docket No. S. 98-273 is also applicable to the action filed and docketed as Docket No. S. 98-408.@

The Administrative Law Division entered an Order Consolidating Appeals and Setting Hearing on March 6, 2000. The Order stated in part that the AAnswer previously

filed in S. 98-273 will serve as an Answer in both cases.@

ANALYSIS

Issue (1) Were the Department=s Answers timely filed?

The Revenue Department is required to file an Answer with the Administrative Law Division within 30 days. A 60 day extension may be granted, giving the Department a combined 90 day Answer period. Code of Ala. 1975, '40-2A-9(c).

The Department was notified of the appeal in S. 98-273 on May 11, 1998. The Department timely filed its Answer on July 30, 1998, within the combined 90 day Answer period.

The Department was notified of the appeal in S. 98-408 on September 11, 1998. The Department failed to file an Answer per se, but rather filed a Motion To Consolidate Cases on March 3, 2000. That motion stated that the Answer in S. 98-273 is applicable to S. 98-408. But even treating the March 3 motion as an Answer in S. 98-408, the Answer was not timely filed within the 90 day deadline.

What is the effect of the Department=s failure to timely file an Answer as required by '40-2A-9(c)? That issue was addressed in State of Alabama v. Sungard Business Systems, Inc., U. 94-310 (Admin. Law Div. Order Dismissing Final Assessment 1/10/95); and State of Alabama v. Bishop-Parker Furniture Co., Inc., S. 93-252 (Admin. Law Div. Final Order Denying Department=s Application for Rehearing 3/31/94). The final assessments in issue in those cases were dismissed because the Department failed to timely file its Answer within the 90 day period. The rationale for dismissing the final assessments was explained in Sungard, as follows:

The Department does not dispute that it failed to file its answer in this case within 90 days as required by '40-2A-9(c). Rather, the Department argues that even though its answer was late, '40-2A-9(b) does not give the Administrative Law Judge authority or jurisdiction to dismiss the final assessment in issue. I disagree.

This same issue was decided in a prior Administrative Law Division case, State v. Bishop-Parker Furniture Company, Docket No. S. 93-252, decided March 31, 1994. In that case, the Department failed to file its answer within the required 90 days. As in this case, the Department conceded that the answer had not been timely filed, but nonetheless argued that '40-2A-9(b) did not give the Administrative Law Judge authority to dismiss the final assessments in issue. The Department's argument was rejected, as follows:

> The cardinal rule of statutory construction is that a statute must be construed to fulfill the intent of the Legislature. Gulf Coast Media, Inc. v. The Mobile Press Register, Inc., 470 So.2d 1211. The purpose and object of the statute must be considered, and the plain language of the statute should not be followed when the practical consequences will lead to unjust results and is contrary to the purpose of the statute. Smith v. Alabama Medicaid Agency, 461 So.2d 817; Birmingham News Co. v. Patterson, 202 F.Supp 881. The plain-meaning rule of statutory construction should not be followed where the result is inconsistent with the intent of the statute. Bailey v. USX Corp., 850 F.2d 1506.
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> The clear intent of the Taxpayers' Bill of Rights and Uniform Revenue Procedures Act, of which ''40-2A-9(b) and (c) are a part, is to provide "equitable and uniform procedures for the operation of the department and for all taxpayers when dealing with the department." See Code of Ala. 1975, '40-2A-2(1). Certainly the Legislature did not intend nor would it be equitable to penalize a taxpayer for failing to comply with a statute or regulation concerning administrative appeals, but not hold the Department to the same standard.
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> The Legislature required the Department to answer within 30 days to protect taxpayers from undue delay by the Department. However, if a taxpayer cannot be granted relief when the Department fails to answer within the required 30 days, or at least within the additional 60 days allowed by '40-2A-9(c), then in practical effect the time limits imposed by that section

> would be meaningless. The Department could ignore the time requirements without penalty.
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> In light of the above, '40-2A-9(b) must be construed to allow the administrative law judge authority to grant relief to either party where the opposing party fails to comply with a statute, regulation or preliminary order concerning an appeal before the Administrative Law Division, either by dismissing the taxpayer's appeal if the taxpayer fails to comply, or by granting the relief sought by a taxpayer if the Department fails to comply. That legislative intent is recognized in Department Reg. 810-14-1-.24(3), which specifies that if either party fails to comply ". . . the Administrative Law Judge shall have discretion to dismiss the appeal, grant all or part of the relief sought by the taxpayer, or take any other action appropriate under the circumstances."
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> The above logic is equally applicable in this case. If a taxpayer cannot be granted relief under '40-2A-9(b), then in practical effect the time limits imposed by '40-2A-9(c) would be meaningless. The Department could ignore the statutory time requirements without penalty. Clearly, that was not the intent of the Legislature. As noted in Bishop-Parker, numerous taxpayer appeals have been dismissed on motion by the Department because the taxpayer failed to timely file a notice of appeal. The intent of the Legislature and fairness requires that the Department must be held to the same standard.

Sungard, at 2.

The Department failed to file its Answer (Motion To Consolidate Cases) in S. 98-408 until March 3, 2000, almost 18 months after being notified of the appeal in September 1998. Applying the rationale of Sungard, the final assessments entered against the Taxpayer for July 1997 through February 1998 must be dismissed.[2]

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[2]It is irrelevant that the Administrative Law Division=s March 6, 2000 Order stated

Issue (2) - Did the Department properly compute the Taxpayer=s liability?

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that the Answer in S. 98-273 will serve as the Answer in S. 98-408. The 90 day Answer period had already expired when that Order was entered.

A person making retail sales in Alabama is required to obtain a sales tax license from the Department. Code of Ala. 1975, '40-23-6. A licensed retailer is required to add sales tax to the retail sales price, and collect the tax from the purchaser. Code of Ala. 1975, '40-23-26. The retailer is then required to file monthly sales tax returns with the Department and remit all tax collected during the subject month. Code of Ala. 1975, '40-23-7.[3]

A retailer is also required to maintain adequate records from which his sales tax liability can be verified. Code of Ala. 1975, '40-23-9; see also, Code of Ala. 1975, '40-2A-7(a)(1). If a retailer fails to provide adequate records, the Department is authorized to compute the retailer=s liability using the best information available. Section 40-2A-7(b)(1)a. Having failed to keep records, the retailer cannot then complain that the Department=s calculations based on the best information available are not exact. Jones v. C.I.R., 903 F.2d 1301 (10th Cir. 1990); Denison v. C.I.R., 689 F.2d 777 (10th Cir. 1982); and Webb v. C.I.R., 394 F.2d 366 (5th Cir. 1968).

The Department=s calculations must, however, be reasonable under the circumstances and based on some minimum evidentiary foundation. Otherwise, the usual presumption of correctness does not apply. Yoon v. C.I.R., 135 F.3d 1007 (5th Cir. 1998); Denison v. C.I.R., 689 F.2d 771 (1982); Leonard Jackson v. C.I.R., 73 T.C. 394 (1979); United States v. Janis, 96 S.Ct. 3021 (1976).

> AWhere the record reflects no reasonable basis for the Commissioner=s assessment, where the assessment cannot be deemed

[3]A retailer may file quarterly returns if its sales tax liability averages less than $200 per month during the prior calendar year. Code of Ala. 1975, '40-23-7(d).

> reasonable on its face, and where no finding is made in that regard, we cannot afford a presumption of correctness to attach automatically to the assessment.@

Denison, 689 F.2d at 773.

In this case, the Taxpayer failed to file returns, and failed to provide records from which the Department could compute his correct liability. Under those circumstances, the Department was clearly authorized to compute the Taxpayer=s taxable gross receipts using invoices obtained from his customers.[4]

However, the Department then tripled the gross receipts in an effort to force the

[4]The Department examiners did an excellent job in attempting to compute the Taxpayer=s liability using the customer invoices. However, perhaps the Department could also have reviewed the Taxpayer=s vendor records to determine total purchases by the Taxpayer, and then applied a reasonable markup. The Department could have perhaps identified the Taxpayer=s vendors by determining who manufactured the equipment sold by the Taxpayer to his customers. But again, depending on whether the Taxpayer used one or a number of vendors, the Department could not know for sure if all of the Taxpayer=s vendors had been identified.

Taxpayer into cooperating. I understand the Department=s concern that the Taxpayer may have had other customers that were not discovered by the Department. But there is no evidence to support that suspicion. Consequently, tripling the Taxpayer=s known gross receipts was arbitrary and not based on any evidentiary foundation.[5]

In Dial Bank v. State of Alabama, Inc. 95-289 & F. 95-308 (Admin. Law Div. Opinion and Preliminary Order 8/10/98), the Department tripled the numerators in Dial Bank=s franchise tax apportionment factors because Dial Bank failed to provide a 50 state spreadsheet as requested by the Department. The Administrative Law Division rejected the tripled numerators because they were not based on any evidentiary foundation. Dial Bank, at 21. Likewise, the arbitrarily tripled gross receipts in this case must also be rejected.

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[5]Ironically, if the invoices of Customers A and B did not show sales by the Taxpayer in a particular month, the Department did not estimate or project sales for that month because, according to the examiner, A. . . we really had no evidence that they had made any sales at all during that -- those months.@ Transcript, at 31. The same rationale should apply concerning the tripled gross receipts. The Department has no evidence that the Taxpayer made sales to other unidentified customers during the subject periods.

This holding does not endorse the Taxpayer=s actions in this case. The Taxpayer violated several statutes in Title 40, Chapter 2A, Code of Ala. 1975. For example, the Taxpayer was required to keep accurate records reflecting his tax liability. Section 40-2A-7(a)(1). Because the Taxpayer failed to keep or permit inspection of those records, he was subject to contempt proceedings in circuit court. Section 40-2A-7(a)(3). The Department could also have subpoenaed the records from the Taxpayer. The Taxpayer would have again been subject to contempt proceedings if he had failed to obey the subpoena. Section 40-2A-7(a)(4).

The Taxpayer also violated numerous sales tax statutes in Title 40, Chapter 23, Code of Ala. 1975. The Taxpayer failed to obtain a sales tax license as required by '40-23-6, failed to file returns as required by '40-23-7, failed to keep records as required by '40-23-9, and failed to charge and collect sales tax from his customers as required by '40-23-26. Any person that fails to file returns or keep records is guilty of a misdemeanor, and shall be fined from $25 to $500 for each offense. Code of Ala. 1975, '40-23-11. Any person that willfully refuses to file returns or permit examination of records shall also be guilty of a misdemeanor, shall be fined from $50 to $500 for each offense, and may be imprisoned for up to 6 months. Code of Ala. 1975, '40-23-12.

The Department could enjoin the Taxpayer from continuing in business until he complies with all relevant statutes. Code of Ala. 1975, '40-23-27. The Taxpayer may also be subject to various criminal provisions in Title 40, Chapter 29, Article 6; specifically Code of Ala. 1975, '40-29-110 (attempt to evade or defeat tax); '40-29-111 (willful failure to collect or pay over tax); and '40-29-112 (willful failure to file return, supply information, or

pay tax).

The Department assessed the Taxpayer for the 10 percent failure to timely pay penalty and the 5 percent negligence penalty. See, Code of Ala. 1975, ''40-2A-11(a) and 40-2A-11(c). However, the Department may have instead assessed the Taxpayer for the 50 percent fraud penalty at Code of Ala. 1975, '40-2A-11(d). Wade v. C.I.R., 185 F.3d 876 (1999) (AThere is no dispute (taxpayer) kept inadequate books and records, further suggesting fraud.@); United States v. Hahn, 182 F.3d 919 (1999) (AFraud is defined as an intent to avoid taxes; in finding fraud, the failure to file a return is a factor of particular weight. (cite omitted.) When coupled with other circumstantial evidence of fraud such as failure to keep adequate records . . ., the failure to file a return is persuasive evidence.@); Soloman v. C.I.R., 732 F.2d 1459 (1984) (AA number of indicia of fraud have been relied on in cases under Subsection 6653(b) (26 U.S.C.). These include, first, taxpayer=s failure to file returns . . . A second factor is a taxpayer=s failure to report income over an extended period of time . . . A taxpayer=s failure to furnish the Government with access to his records is also a factor . . . Another consideration is a taxpayer=s failure to keep adequate books and records.@)[6]

[6]The Alabama fraud penalty statute at '40-2A-11(d) adopts by reference the federal fraud penalty at 26 U.S.C. '6663. Consequently, the above cited federal cases control for

Alabama purposes.

The Taxpayer claims he was not the Department=s personal tax collector. See, footnote 1, *infra*. However, Alabama law obligated the Taxpayer, as a retailer, to add to and collect from his customers a 4 percent State sales tax on all retail sales. Section 40-23-26.

At least one of the Taxpayer=s customers (Customer A) paid sales tax on its purchases from the Taxpayer. However, '40-23-26(b) makes it unlawful for a retailer not to charge and collect sales tax from a customer. Consequently, the Taxpayer, not his customers, was obligated to collect and remit sales tax to the Department. The tax erroneously paid by Customer A was thus correctly refunded by the Department. If the Taxpayer and Customer A had agreed that Customer A would pay the tax, the Taxpayer may recover against Customer A.

The final assessments for July 1997 through February 1998 are dismissed. The Department is directed to recompute the Taxpayer=s liabilities for September 1993 through June 1997 as indicated herein, based on the tax due as reflected in the records of the Taxpayer=s customers, plus applicable penalty and interest.

This Opinion and Preliminary Order is not an appealable Order. The Final Order, when entered, may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, '40-2A-9(g).

Entered June 16, 2000.

BILL THOMPSON
Chief Administrative Law Judge