

IEC ARAB ALABAMA, INC. 350 11th Street SW Arab, AL 35016-1770,	§ §	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
Taxpayer,	§	DOCKET NO. U. 98-507
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

**FINAL ORDER DENYING DEPARTMENT'S  
APPLICATION FOR REHEARING**

This case involves the above Taxpayer's liability for State and City of Arab use tax for January 1990 through December 1997. The Department entered preliminary assessments against the Taxpayer for the above period on September 11, 1998. It later entered final assessments, which the Taxpayer paid to prevent default under various loan agreements. The Taxpayer also timely appealed the final assessments to the Administrative Law Division.<sup>1</sup>

The Department assessed the Taxpayer based on Act 97-301, which was enacted in May 1997. As discussed below, the Legislature passed Act 97-301 in response to the Administrative Law Division's holding in *Bluegrass Bit Co., Inc. v. State of Alabama*, U. 96-294 and S. 96-287 (Admin. Law Div. 1/16/97). The Act amended Code of Ala. 1975, §40-23-62(1) to provide that the use tax exemption provided therein applied only to property used, stored, or consumed in Alabama on which Alabama sales tax had actually been paid. Before the amendment, §40-23-62(1) exempted all property subject to Alabama sales tax, whether the sales tax was paid or could be assessed and collected. Section 3 of Act 97-

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<sup>1</sup> A taxpayer is authorized to appeal a final assessment to the Administrative Law Division or circuit court, even if the taxpayer pays the final assessment before taking the appeal. Code of Ala. 1975, §40-2A-7(b)(5)b.

301 provided that the amendment shall be effective for all open tax years. Based on that retroactive provision, the Department assessed the Taxpayer back to January 1990 because the Taxpayer would have owed use tax during that period pursuant to the amended version of §40-23-62(1).

The parties agreed to hold the case in abeyance pending the outcome of *Monroe v. Valhalla Cemetery, Inc.*, which involved the constitutionality of the retroactive application of Act 97-301. As discussed in more detail below, the Court of Civil Appeals upheld the retroactive provision in Act 97-301. *Monroe v. Valhalla Cemetery, Inc.*, 749 So.2d 470 (Ala. Civ. App. 1999). The parties in this case thereafter attempted to settle, but finally submitted the case on a joint stipulation of facts in February 2005. Blake Madison represented the Taxpayer. Assistant Counsel Wade Hope represented the Department.

The two substantive issues raised by the parties were (1) whether the retroactive application of Act 97-301, as applied to the Taxpayer, constituted a denial of equal protection and due process; and (2) whether the Department was barred from assessing the Taxpayer beyond the general three year statute of limitations at Code of Ala. 1975, §40-2A-7(b)(2).

The Administrative Law Division issued an Opinion and Preliminary Order on May 19, 2005 holding that the retroactive application of Act 97-301 was not unconstitutional, citing the Court of Civil Appeals' decision in *Valhalla Cemetery*. The Administrative Law Division also held that under the circumstances, the Department was barred from assessing the Taxpayer beyond the general three year statute at §40-2A-7(b)(2). The Opinion and Preliminary Order reads in pertinent part at 4 – 5:

Generally, the Department must assess tax "within three years from the due date of the return, or three years from when the return is filed with the department, whichever is later, . . ." Section 40-2A-7(b)(2). However, a preliminary assessment may be entered at any time "if no return is filed as required . . ." Section 40-2A-7(b)(2)a.

In this case, the Department, presumably relying on subparagraph (b)(2)a., assessed the Taxpayer back to 1990 because the Taxpayer had never filed use tax returns with the Department. However, the open-ended statute of limitations in subparagraph (b)(2)a. applies only if a taxpayer is required to file a return and fails to do so. The Taxpayer in this case was not required to file use tax returns before Act 97-301 was enacted because the subject property was exempt from use tax pursuant to §40-23-62(1). Consequently, because the Taxpayer was not required to file use tax returns before May 1997, the open-ended statute in subparagraph (b)(2)a. does not apply. See, *Alexander v. State of Alabama*, U. 97-333 (Admin. Law Div. 1/9/98). Rather, the general three year statute applies.

The Department entered the preliminary assessments against the Taxpayer on September 11, 1998. The Department thus timely assessed the Taxpayer for the use tax due from August 1995 through December 1997. (footnote omitted) The tax due before August 1995 is time-barred.

A Final Order was entered on August 15, 2005 holding that the Department should refund the State use tax overpaid by the Taxpayer for the pre-August 1995 periods, and that the City of Arab was liable to refund the City tax overpaid for those periods. The Administrative Law Division also added the City as an intervenor in the case pursuant to Code of Ala. 1975, §40-2A-9(l).

The Department timely applied for a rehearing. It also requested that the City of Arab be allowed to respond. The Taxpayer and the City both subsequently filed well-written briefs on rehearing.

In *Bluegrass Bit*, the Administrative Law Division ruled that Alabama use tax was not owed on property sold by out-of-state vendors to customers in Alabama because the sales were closed in Alabama, and thus subject to Alabama sales tax, in which case the property

was exempt from use tax pursuant to §40-23-62(1). After the ruling gained national attention, the Alabama Legislature enacted Act 97-301. That Act closed the loophole pointed out in *Bluegrass Bit* by amending §40-23-62(1) so that only property on which Alabama sales tax is actually paid is exempt from Alabama use tax. To prevent taxpayers from claiming refunds based on the pre-amendment version of §40-23-62(1), the Legislature made Act 97-301 retroactive for all open tax years.

Valhalla Cemetery and others sued the Department in Montgomery County Circuit Court seeking to have the retroactive provision in Act 97-301 declared unconstitutional. The Circuit Court held that the provision was unconstitutional, and ordered refunds.

The Court of Civil Appeals reversed. In so holding, the Court stated that “Act No. 97-301 is retroactive for two to three years.” *Valhalla Cemetery*, 749 So.2d at 474. The two to three years referred to by the Court related to the statute of limitations within which a refund must be claimed. See, Code of Ala. 1975, §40-2A-7(c)(2). The Court reasoned that the retroactive application of Act 97-301, which effectively barred taxpayers from obtaining refunds for the statutory two or three year refund period, was reasonable and served a legitimate legislative purpose, i.e., it closed a loophole in Alabama’s sales and use tax structure.

While *Valhalla Cemetery* involved the retroactive application of Act 97-301 as it applied to refunds, the Department is now attempting to assess the Taxpayer for a pre-1997 period based on the retroactive application of Act 97-301. The Department may do so, but only for “all open tax years.” That is, the Department can assess any pre-May 1997 period only if it is not barred by the various time limitations for entering preliminary assessments at Code of Ala. 1975, §40-2A-7(b)(2).

Section 40-2A-7(b)(2) generally allows the Department three years from the due date of the return or the due date of the tax within which to assess additional tax due. The retroactive application of Act 97-301 clearly allowed the Department to assess the Taxpayer for additional tax due within three years from the effective date of the Act. (Contrary to the Department's claim in its application for rehearing, the general three year statute allows the Department to assess tax whether a taxpayer files a return or not.)

Section 40-2A-7(b)(2) also includes various exceptions to the general three year statute. The relevant exception in this case is the first clause of §40-2A-7(b)(2)a., which allows the Department to assess tax "at any time if no return is filed as required, . . ."

The City concedes that the Taxpayer was not required to file use tax returns before the enactment of Act 97-301. It argues, however, that Act 97-301 imposed a new duty on the Taxpayer by requiring it to file returns for the pre-May 1997 periods. Consequently, the City contends that because the Taxpayer was required by the retroactive application of Act 97-301 to file use tax returns for January 1990 forward, the open-ended statute of limitations at §40-2A-7(b)(2)a. thus applies. I disagree.

Act 97-301 did not and could not reopen a previously closed tax period for purposes of assessment. The Act applied retroactively to only those tax periods that were open on the effective date of the Act. Because the periods more than three years before May 1997 were closed on the effective date of the Act, the Act could not be applied retroactively, relative to the Taxpayer, for more than three years, i.e., the general statute of limitations for assessing tax.<sup>2</sup>

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<sup>2</sup> If the Taxpayer had filed fraudulent returns for the pre-1997 periods, the Department  
(continued)

The Alabama Supreme Court ruled in *Ex parte State of Alabama, Dept. of Revenue*, 667 So.2d 1372 (Ala. 1996), that while the Alabama Legislature can retroactively extend or reduce a statute of limitations period, it can do so only for periods not already barred.

Thus the legislature has the power to retroactively alter, extend, or curtail an existing limitations period. However, the power to extend a limitations period can be exercised only where the bar was not complete before the enactment of the statute extending the period, because if the statute extending the period was applied to a cause of action already barred, then the effect of the statute would be to revive a cause of action. A statute extending a limitations period can apply only to a cause of action not already barred. Ala. Const. 1901, §95; *Tyson v. Johns-Manville Sales Corp.*, 399 So.2d 263, 268-69 (Ala. 1981).

*Ex parte State*, 667 So.2d at 1374.

Because the statute of limitations for assessing the Taxpayer beyond the general three year statute at §40-2A-7(b)(2) had expired before the enactment of Act 97-301, that Act could not retroactively apply to extend the statute to prior periods.

The City contends that the “Administrative Law Division’s construction of Act No. 97-301 essentially nullifies the retroactive effect of Act No. 97-301, . . .” City’s Brief at 6. I again disagree.

As discussed, the Legislature included the retroactive provision in Act 97-301 to prevent taxpayers from obtaining refunds based on the holding in *Bluegrass Bit*. The provision effectively served that purpose, see *Valhalla Cemetery*. The retroactive provision also allowed the Department to assess use tax on property that was previously exempt

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could have assessed it back to 1990 (and earlier) based on the second clause of §40-2A-7(b)(2)a. Likewise, the Department could have assessed the Taxpayer back six years if the Taxpayer had underreported by at least 25 percent on its returns, see §40-2A-7(b)(2)b. However, like the first clause in §40-2A-7(b)(2)a., those provisions also do not apply in this case.

from use tax under the pre-amendment version of §40-23-62(1), but the express intent of the Legislature was that such tax could only be assessed for open tax periods. The Legislature clearly did not intend to allow the Department to assess tax for periods closed before the effective date of the Act, which in this case is the period before August 1995.<sup>3</sup>

Finally, if the Department's position is correct that Act 97-301 may be applied back to 1990 (and presumably beyond), then the constitutionality of the provision is again in issue. The Court held in *Valhalla Cemetery* that applying the Act back two to three years to bar refunds was constitutional because it served a legitimate legislative purpose and the period of retroactivity was modest, as required by the U.S. Supreme Court's holding in *U.S. v. Carlton*, 114 S.Ct. 2018 (1994). Certainly, applying the Act back for over eight years to January 1990 cannot be deemed a "modest" period.

The Department's application for rehearing is denied. The August 15, 2005 Final Order is affirmed.

This Final Order Denying Department's Application for Rehearing may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered January 5, 2006.

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BILL THOMPSON  
Chief Administrative Law Judge

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<sup>3</sup> When Act 97-301 became effective on May 7, 1997, the general three year statute was open for periods back to April 1994 because the May 20, 1994 due date of the April 1994 return was within three years from the effective date of the Act. However, when the Department finally entered preliminary assessments against the Taxpayer in September 1998, the Department could only assess the Taxpayer back three years from that date, or August 1995 forward.