

WIGLEY & CULP, INC.	§	STATE OF ALABAMA
P.O. BOX 912		DEPARTMENT OF REVENUE
LUCEDALE, MS 39452,	§	ADMINISTRATIVE LAW DIVISION
Taxpayer,	§	DOCKET NO. MISC. 03-658
v.	§	
STATE OF ALABAMA	§	
DEPARTMENT OF REVENUE.		

**FINAL ORDER ON  
TAXPAYER'S APPLICATION FOR REHEARING**

This appeal involves final assessments of State tobacco tax for November 1998 through January 2002 and Mobile County tobacco tax for May 2001 through January 2002. A Final Order was entered on April 25, 2006 affirming the State tobacco tax assessment.<sup>1</sup> The Taxpayer timely applied for a rehearing, which was conducted on July 13, 2006. Bob Galloway represented the Taxpayer. Assistant Counsel Wade Hope represented the Department.

The Taxpayer is based in Mississippi and sold cigarettes at wholesale to Alabama customers during the period in issue. The Department audited the Taxpayer, but the Taxpayer failed to provide its records to the Department examiner. The Department consequently assessed the Taxpayer based on the amounts the Taxpayer had reported as Alabama sales on Line 6 of its Mississippi tobacco tax returns. The Taxpayer appealed, contending that the Line 6 amounts on its Mississippi returns were its gross sales in Alabama, and that Alabama tax is due on only its net Alabama sales, i.e., gross Alabama sales less returned cigarettes.

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<sup>1</sup> The parties agreed that the Mobile County assessment was due to be dismissed because the subject tax was included in a prior settlement agreement in Mobile County Circuit Court.

After the initial hearing on December 21, 2004, the Administrative Law Division directed the Department to review the Taxpayer's records to verify "how (the Taxpayer) computed the number on Line 6 on the back of its Mississippi returns." December 28, 2004 Preliminary Order at 3. The Department examiner testified at the July 13 rehearing that when he returned to re-audit the Taxpayer, he requested the Taxpayer's records for two months, December 2000 and August 2001. The Taxpayer provided the examiner with its invoices, credit memos, and all other relevant records for those months.

The examiner used the Taxpayer's invoices to determine the Taxpayer's gross sales into Alabama in both months. He then subtracted the credit memo amounts, which reflected cigarettes previously sold into Alabama that were later returned to the Taxpayer. Using those records, the examiner confirmed that the Taxpayer's net Alabama sales in the two sample months almost exactly equaled the amounts reported by the Taxpayer on its Alabama returns for those months.

The examiner testified further, however, that he was still unable to reconcile the Mississippi returns because the Line 6 amounts did not equal the Taxpayer's gross Alabama sales as reflected on its records. The examiner consequently requested copies of the Taxpayer's Mobile County, City of Mobile, and Baldwin County tobacco tax returns. The Taxpayer refused to provide those returns because it did not deem the returns to be relevant to the issue in dispute. The Department subsequently notified the Administrative Law Division that because the Mississippi returns could not be reconciled with the Taxpayer's records, the final assessment should not be changed.

The ultimate issue in this case is whether the Taxpayer's Alabama returns for the subject period were correct as filed. After the December 2004 hearing, the Administrative

Law Division directed the Department to review the Taxpayer's records and determine the accuracy of the Line 6 amounts on the Mississippi returns only because the Administrative Law Division understood that that was the best method to verify the accuracy of the Taxpayer's Alabama returns. That is, reconciling the Line 6 amounts was an indirect method by which the Taxpayer's Alabama liabilities could be confirmed.

The Administrative Law Division was unaware at that time, however, that the Taxpayer had records from which its gross and net Alabama sales could be directly verified. As indicated, when the Department examiner reviewed the Taxpayer's records, he confirmed that the Taxpayer's gross Alabama sales less the Alabama credit memos (returned cigarettes) equaled the net amounts reported by the Taxpayer on its Alabama returns in the two sample months. Because the Taxpayer's records directly confirm that the Taxpayer had correctly reported its net Alabama sales on its Alabama returns, the accuracy of the amounts on Line 6 of the Taxpayer's Mississippi returns is irrelevant.<sup>2</sup>

The only evidence before the Administrative Law Division concerning the accuracy of the Taxpayer's Alabama returns is the examiner's finding that the returns for the two sample months were substantially correct. The Department argued at the July 13 rehearing that it did not review the Taxpayer's records for the purposes of determining the correctness of the Taxpayer's returns. That was, however, the practical effect of the review. The Department routinely uses sample periods in determining a taxpayer's liability. It randomly selected the two months in question, and without evidence that the two

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<sup>2</sup> The Taxpayer explained at the July 13, 2006 rehearing that the Line 6 amounts did not reconcile, i.e., did not equal its gross sales into Alabama, as initially argued by the Taxpayer, because of various miscellaneous mistakes by its clerical personnel.

months are not typical of the entire audit period, there is no reason the results should not be accepted.

The above holding does not condone the fact that the Taxpayer failed to initially provide the Department with its records for the subject period. The Taxpayer is required by Alabama law to maintain records and to provide the records to the Department on request. See, Code of Ala. 1975, §§40-2A-7(a) and (b) (generally) and 40-25-13 (specifically relating to tobacco tax). The Taxpayer's failure to permit inspection of its records also subjected it to contempt and various other penalty provisions. See, Code of Ala. 1975, §§40-2A-7(a)(3) and 40-25-1 et seq. If the Department elects to audit the Taxpayer for a subsequent period, the Taxpayer will be required to open its records to the Department or be subject to the above sanctions.

The Department was also authorized to calculate the Taxpayer's Alabama liability in the absence of records using the best information available, i.e., the Alabama sales reported by the Taxpayer on its Mississippi returns. See, Code of Ala. 1975, §40-2A-7(b)(1)a. The burden was then on the Taxpayer to show that the Department's calculations were incorrect. Code of Ala. 1975, §40-2A-7(b)(5)c. As indicated, however, the Taxpayer carried that burden when the Department determined from its review of the Taxpayer's records that the Line 6 amounts on the Mississippi returns did not accurately reflect the Taxpayer's liabilities, and that the Taxpayer had correctly reported its Alabama sales in the two sample months.

The April 26, 2006 Final Order and the final assessments of State and Mobile County tobacco tax in issue are voided.

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

Entered December 4, 2006.

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BILL THOMPSON  
Chief Administrative Law Judge

bt:dr

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