

FREEDOM TRAIL VENTURES, LTD. §
6967 US HIGHWAY 80 W.
HAYNEVILLE, AL 36040-4428, §

STATE OF ALABAMA
DEPARTMENT OF REVENUE
ADMINISTRATIVE LAW DIVISION

Taxpayer, § DOCKET NO. W. 06-421

v. §

STATE OF ALABAMA §
DEPARTMENT OF REVENUE.

FINAL ORDER

The Revenue Department assessed Freedom Trail Ventures, Ltd. (“Taxpayer”) for withholding tax for various months from September 2004 through October 2005.¹ The Taxpayer appealed to the Administrative Law Division pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. A hearing was conducted on December 13, 2006. Warren Matthews represented the Taxpayer. Margaret McNeill represented the Department.

The Taxpayer contracted to manage the White Hall Gaming Center in Lowndes County, Alabama in mid-2004. The Gaming Center operates for-profit bingo games.

The Taxpayer hired an accountant in Oklahoma to handle the Gaming Hall’s gambling-related tax filings. It hired an Alabama accountant to handle the Hall’s wage withholding and other tax-related obligations. The Alabama accountant has always timely filed monthly withholding tax returns and remitted the tax withheld from the Taxpayer’s employees.

The Oklahoma accountant contacted the Department in mid-2004 concerning the Taxpayer’s duty to withhold Alabama tax from bingo payouts. She was unable to obtain a definite answer. Consequently, she assumed that Alabama law was similar to federal law,

¹ The Department entered five final assessments against the Taxpayer for March and June 2005; July, August, and October 2005; September 2004 through September 2005; August 2005; and October 2005.

and that tax withheld from gambling winnings should be reported and paid annually. She accordingly filed an annual 2004 withholding return with the Department concerning the Taxpayer's gambling withholding in January 2005 and remitted the tax due.

In mid-2005, the Department notified the Taxpayer that it owed penalties and interest from mid-2004 through December 2004 because it had not properly reported and paid its withholding tax to the Department. The notice did not explain why or how the tax had been improperly reported and paid. The Taxpayer's Alabama accountant paid the interest due and requested a waiver of the penalties. The Department accepted the interest and closed the file, i.e., waived the penalties, without comment.

The Department also informed the Alabama accountant in mid-2005 that tax withheld from gambling payouts must be reported and paid monthly. The Alabama accountant relayed the information to the Oklahoma accountant, who began filing separate monthly withholding tax returns and remitting the tax due concerning the Taxpayer's gambling-related withholding. The accountant understood that the monthly returns were due by the end of the subsequent month. Consequently, she filed some of the monthly returns by the end of the subsequent month, but after the 15th of the month due date.

The Taxpayer's accountants continued to file separate withholding returns relating to the Taxpayer's wage withholding and gambling withholding, and also pay the amounts due with separate checks, until the Department notified the Taxpayer in December 2005 that only one return and one check should be submitted. The Taxpayer has timely remitted one monthly withholding return and paid the tax due since that time.

The Department subsequently assessed the Taxpayer for the penalties in issue because the Taxpayer had not timely filed its withholding returns and remitted the tax due

during the months in issue. All but one of the final assessments also includes interest.

The Taxpayer's representative argues that the penalties should be waived for reasonable cause pursuant to Code of Ala. 1975, §40-2A-11(h). He contends that the Taxpayer relied on its accountants to timely report and pay the tax due, and that its reliance on those competent tax advisors constitutes reasonable cause pursuant to Rev. Proc. 97-003.

If a taxpayer relies on a lawyer, accountant, or other tax advisor to timely file a return and/or pay the tax due, the advisor's negligent failure to do so will not relieve the taxpayer from any related late penalties. That is, the advisor's negligence will be attributed to the taxpayer. See, *U.S. v. Boyle*, 105 S.Ct. 687 (1985). In this case, however, the Taxpayer's accountants did not correctly report and pay the Taxpayer's gambling-related withholding due to a misunderstanding of law, not because of negligence.

A similar situation arose in *Tiger Steak, Inc. v. State of Alabama, Inc.* 05-722 (Admin. Law Div. 12/28/05). In that case, the taxpayer's accountants filed an extension to file the taxpayer's S corporation return. They did not file a separate extension concerning the taxpayer's non-resident composite return because they believed, incorrectly, that only one extension was required. The Department subsequently penalized the taxpayer for not timely filing the composite return. The Administrative Law Division waived the penalty.

The Department strenuously argues that the penalties should not be waived. It contends that it was the Taxpayers' duty to timely file the returns, and that their reliance on their CPA to do so does not constitute reasonable cause, citing *U.S. v. Boyle*, 105 S.Ct. 687 (1985). The Department also contends that "Taxpayer's reliance of a tax advisor is not reasonable cause." Department's Answer, at 2 – 3.

In *Boyle*, an executor of an estate relied on his attorney to timely file the estate's tax return. The attorney negligently failed to do so. The IRS

subsequently assessed the executor for late penalties. The issue was whether reliance on the attorney constituted reasonable cause to waive the penalties.

The U.S. Supreme Court held that the executor's reliance on the attorney was, under the circumstances, not reasonable cause to waive the late penalties. The executor was under a legal duty to timely file the return, or ensure that the attorney timely filed the return, by the known due date. The late penalty applied because the executor failed in that duty. The negligence of the attorney was thus attributed to the executor.

In *Boyle*, the Court distinguished the situation where a taxpayer is advised, as a matter of law, that it is unnecessary to file a return.

This case is not one in which a taxpayer has relied on the erroneous advice of counsel concerning a question of law. Courts have frequently held that "reasonable cause" is established when a taxpayer shows that he reasonably relied on the advice of an accountant or attorney that it was unnecessary to file a return, even when such advice turned out to have been mistaken. (cites omitted) This Court also has implied that, in such a situation, reliance on the opinion of a tax adviser may constitute reasonable cause for failure to file a return. (cites omitted)

Boyle, 105 S.Ct. at 631.

The rationale of *Boyle* does not apply in this case because the Taxpayers' CPA understood that filing an extension request concerning Form 20S also constituted an extension request for Form 20SC. The CPA in effect "advised" the Taxpayers that as a matter of law both the 20S and 20SC returns were not due until the extended April 15, 2004 due date. The Taxpayers' reliance on that advice thus constituted reasonable cause. Unlike the situation in *Boyle*, where the attorney failed to file the return because of negligence, the CPA in this case failed to timely file the Form 20SC returns through a misunderstanding of law. The Taxpayers were not negligent in failing to file the returns by a known due date, as in *Boyle*, because they relied on their CPA's advice that as a matter of law, the due date to file the returns had been extended.

Tiger Steak at 4 – 5.

The above rationale also applies in this case. The Taxpayer's Oklahoma accountant contacted the Department and attempted in good faith to determine how and when the

Taxpayer's gambling withholdings should be reported and paid. She was not told to report and pay the gambling withholding with the wage withholding on a single return. Consequently, she assumed that it should be paid on a separate annual return, the same as required by federal law. When she later learned that the gambling-related withholding return should be filed monthly, she began filing a separate return and remitting a separate check for the tax due. Not until the end of 2005 did the Taxpayer's accountants learn that a single return and check should be submitted.

In short, the Taxpayer's accountants misunderstood an issue of law, i.e., when and how the gambling withholding should be reported and paid. Under the circumstances, the Taxpayer's reliance on the accountants constitutes reasonable cause to waive the penalties in issue.

The final assessment for September 2004 through September 2005 is voided. The final assessment for March and June 2005 is reduced to interest of \$1,209.77. The final assessment for July, August, and October 2005 is reduced to interest of \$69.75. The final assessments for October 2005 is reduced to interest of \$21.26. The final assessment for August 2005 is reduced to interest of \$58.06. Judgment is entered accordingly. Additional interest is also due on the above amounts from April 3, 2006.

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

Entered January 4, 2007.

BILL THOMPSON
Chief Administrative Law Judge

bt:dr

cc: Margaret Johnson McNeill, Esq.
Warren C. Matthews, Esq.
Neal Hearn