IN THE MATTER OF
GROSS RECEIPTS
TAX ASSESSMENT

DOCKET NO.: 16-086
AUDIT NO.: 12/14/2012 – 12/31/2012

JESSICA DUNCAN, ADMINISTRATIVE LAW JUDGE

APPEARANCES

This case is before the Office of Hearings and Appeals upon a written protest dated April 27, 2015, signed by [redacted], the Taxpayer. The Taxpayer protested an assessment of gross receipts tax (“sales tax”) resulting from an audit conducted by the Department of Finance and Administration (“Department”).

At the request of the Taxpayer, this case was taken under consideration of written documents submitted by the parties. A briefing schedule was mailed to the parties on September 14, 2015. The Department was represented by Lisa Ables, Attorney at Law, Office of Revenue Legal Counsel. The Department’s Opening Brief was filed on September 16, 2015. The Taxpayer’s Response Brief was filed on November 16, 2015. This matter was submitted for decision on December 3, 2015.

ISSUE

Whether the assessment made by the Department should be sustained?

Yes, in part.
FINDINGS OF FACT/CONTENTIONS OF THE PARTIES

On December 14, 2012, the Taxpayer purchased a 2013 Polaris Ranger (“UTV”) from [redacted] in [redacted], Arkansas. See Department’s Opening Brief – Exhibit A. At the time of purchase, the Taxpayer claimed the farm machinery and equipment sales tax exemption and did not pay sales tax. The Taxpayer completed and signed a Commercial Farming Machinery and Equipment Sales Tax Exemption Certificate (Form ST-403). Therein, the Taxpayer claimed he was engaged in the production of “Cattle” as a commercial farming business.

The Department conducted an audit and issued a proposed assessment in the amount of $[redacted]$ against the Taxpayer on February 27, 2015. See Department’s Opening Brief – Exhibit D. Taxpayer protested the assessment and included with the Protest Form a signed letter that stated:

In Dec. 2012, I purchased a UTV and [redacted] acres of land anticipating a cattle farm. The UTV was used to fix fence around the property. In [redacted] of [redacted], my circumstances changed and my wife and I divorced in [redacted]. In [redacted] I left the property and sold the acreage and the UTV. An amended return has been filed with Federal and Arkansas showing the farm use of the UTV for the last of December 2012. And an amended return for 2013 showing the sale of the UTV.

The Department’s Opening Brief provides, in part, as follows:

Taxpayer indicated he was engaged in or provided services for the production of cattle as a commercial farming business on the certification. However, when audited, Taxpayer failed to submit evidence showing he was engaged in the business of farming and that the UTV was used exclusively and directly in the agricultural production of food or fiber as a business.

1 The reflected amount included State Sales Tax ($[redacted]$ and interest ($[redacted]$), County Sales Tax ($[redacted]$ and interest ($[redacted]$), and Sales Tax ($[redacted]$ and interest ($[redacted]$).

The auditor requested that Taxpayer provide business records, including his 2012 Schedule F and depreciation schedules, to support and substantiate his entitlement to claim the farm exemption. Taxpayer failed to respond to the auditor’s first request so a second letter was sent on February 18, 2015. Taxpayer contacted field audit office by mail and advised that, pursuant to a divorce decree, his ex-wife is responsible for issues pertaining to this matter. Taxpayer included a copy of his divorce decree and referenced certain provisions contained therein; namely, the division of debts and a provision awarding the 2012 federal and state tax refund to wife. See Taxpayer letter and divorce decree attached as Exhibit C. A review of the divorce decree appears to provide no relevance to the sales tax issue involving the UTV. Taxpayer failed to provide any of the requested documentation. The auditor thereafter reviewed the parties’ 2012 joint tax return which reflected that no farm income had been earned for that year and no Schedule F had been filed.

Based upon the afore-facts, the farm machinery and equipment exemption was disallowed. Taxpayer was assessed gross receipts (sales) tax totaling $, plus interest of $ (10% per annum) assessed through February 27, 2015. No penalty was applied. See Summary of Findings, attached as Exhibit D. [P. 1–2]

In accordance with Arkansas law, in order to support a claim for entitlement to the farm exemption a taxpayer must provide clear and convincing evidence that he meets two requirements: (1) he is primarily engaged in the business of farming; and (2) the equipment is used exclusively and directly in the agricultural production of food or fiber.

The auditor requested Taxpayer’s business records, including Schedule F and depreciation schedule for 2012, demonstrating he was in the commercial farming business. Taxpayer failed to comply with the request and therefore failed to produce documentation substantiating that he was, or is, engaged in the commercial production of food or fiber. As a result, the auditor correctly concluded that the purchase failed to meet the criteria for the exemption pursuant to GR-51.

On April 27, 2015, Taxpayer filed an amended 2012 Arkansas Income Tax Return (AR1000) including Schedule F and depreciation schedules for the UTV. While the filing of a Schedule F and depreciation schedules is certainly one helpful indicator that Taxpayer intended to use the UTV in farming operations, the UTV
must still pass the “exclusivity” and “directly” requirements in order to fall within the exemption for farm machinery and equipment.

The Taxpayer has failed to establish entitlement to an exemption from tax on the purchase of the UTV by clear and convincing evidence. Therefore, the assessment of sales tax is proper. Finally, the assessment of interest is proper because the tax was due, but not paid, at the time the UTV was purchased. Accordingly, the Department respectfully requests that the assessment against the Taxpayer be sustained. [P. 4-5]

The Taxpayer provided documents to substantiate his entitlement to the claimed exemption including an amended 2012 Arkansas Income Tax Return which included a Schedule F – Profit or Loss from Farming and depreciation schedule (Form 4562). See Taxpayer’s Response Brief – Exhibit H. Also included in the Taxpayer’s Response Brief were, inter alia, the Taxpayer’s Decree of Divorce dated [redacted], email and letter correspondence between the Department and Taxpayer, the Bill of Sale, and four photographs depicting cattle and fencing on the Taxpayer’s formerly owned property. See Taxpayer’s Response Brief – Exhibit’s B, E, G, and I. The Taxpayer contends the following: (1) any tax debt from the tax year 2012 is the debt of his ex-wife pursuant to the divorce decree; (2) the amended Federal and Arkansas Income Tax Returns were accepted and refunds were issued, therefore the matter is settled; (3) the UTV was delivered to and utilized on the property depicted in the photographs until the UTV and land were both sold in 2013; and (4) the Department incorrectly assessed [redacted] and [redacted] local taxes because the UTV was delivered to his residence in [redacted] County.
CONCLUSIONS OF LAW

A. Standard of Proof

Ark. Code Ann. § 26-18-313(c) (Supp. 2015) provides, in pertinent part, as follows:

The burden of proof applied to matters of fact and evidence, whether placed on the taxpayer or the state in controversies regarding the application of a state tax law shall be by preponderance of the evidence.


A preponderance of the evidence is “not necessarily established by the greater number of witnesses testifying to a fact but by evidence that has the most convincing force; superior evidentiary weight that, though not sufficient to free the mind wholly from all reasonable doubt, is still sufficient to incline a fair and impartial mind to one side of the issue rather than the other.

The Department bears the burden of proving that the tax law applies to an item or service sought to be taxed, and a taxpayer bears the burden of proving entitlement to a tax exemption, deduction, or credit. Ark. Code Ann. § 26-18-313(d) (Supp. 2015). Statutes imposing a tax or providing a tax exemption, deduction, or credit must be reasonably and strictly construed in limitation of their application, giving the words their plain and ordinary meaning. Ark. Code Ann. § 26-18-313(a), (b), and (e) (Supp. 2015). If a well-founded doubt exists with respect to the application of a statute imposing a tax or providing a tax exemption, deduction, or credit, the doubt must be resolved against the

B. Sales Tax Assessment

Arkansas sales tax is generally imposed on sales of tangible personal property made by in-state vendors to in-state purchasers. Ark. Code Ann. §26-52-101 et seq. (Repl. 2014 & Supp. 2015). Ark Code Ann. § 26-52-103(21)(A) (Repl. 2014) defines “tangible personal property” as “personal property that can be seen, weighed, measured, felt, or touched or that is in any other manner perceptible to the senses.” The UTV purchased by the Taxpayer is tangible personal property. Consequently, the Department has satisfied its burden regarding the taxability of the UTV.

1. Farm Machinery and Equipment Exemption

Ark Code Ann. §26-52-403(b) (Repl. 2014) exempts the sale of farm machinery and equipment from sales tax. “Farm equipment and machinery” is defined as implements used exclusively and directly in farming. Ark. Code Ann. § 26-52-403(a)(1)(A) (Repl. 2014). “Farming” is defined as the agricultural production of food or fiber as a business. Ark. Code Ann. § 26-52-403(a)(2) (Repl. 2014). Pursuant to Ark. Code Ann. § 26-52-105(b) (Repl. 2014), the Director of the Department is directed to promulgate rules for the proper enforcement of the sales tax laws. Arkansas Gross Receipts Tax Rule GR-51 (“GR-51”) addresses the farm machinery and equipment exemption and provides, in pertinent part, as follows:

B. DEFINITIONS.
1. “Farm equipment and machinery” means the agricultural implements used exclusively and directly for the agricultural
production of food or fiber as a commercial business or the agricultural production of grass sod or nursery products as a commercial business...

C. The list of exempt items in GR-51(B)(1)(a) is not intended to be exclusive. Other agricultural implements may qualify for this exemption provided they meet the requirements of GR – 51(C)(1) and GR-51(C)(2).

1. An implement may not be treated as tax exempt unless it is used “exclusively” in the agricultural production of food or fiber as a business or the agricultural production of grass sod or nursery products as a business.

   a. An implement will be presumed to be used exclusively in the agricultural production of food, fiber, grass sod, or nursery products as a business if the implement is used on land owned or leased for the purpose of agricultural production of food, fiber, grass sod, or nursery products.

   b. A person who uses agricultural implements in the production of food, fiber, grass sod, or nursery products primarily for his own consumption is not entitled to this exemption.

2. An implement may not be treated as tax exempt unless it is used “directly” in the agricultural production of food or fiber as a business or the agricultural production of grass sod or nursery products as a business. The term “directly” limits the exemption to the following:

   a. Only those implements used in the actual agricultural production of food, fiber, grass sod, or nursery products to be sold in processed form or otherwise at retail; or
   b. Machinery and equipment used in the agricultural production of farm products to be fed to livestock or poultry which is to be sold ultimately in processed form at retail.

3. Implements which are not exempt include, but are not limited to, the following:

   f. Examples of non-exempt items include (i) a machine owned by a commercial farmer but also used at a location other than the farming property (such as a duck club or deer camp); (ii) a machine owned by a commercial farmer but also used for any other purpose at any time for activities other than commercial farming, even while located at the
commercial farm (such as pleasure riding, household activities, residential yard work, gardening, hunting, and fishing); and (iii) a machine purchased by a commercial farmer who also uses the machine to produce food or fiber primarily for his own consumption.

E. ENGAGED IN THE BUSINESS OF FARMING. A purchaser of farm machinery and equipment shall be considered to be engaged in the business of farming for purposes of the exemption if the purchaser meets the requirements in GR-51(E)(1) or GR-51(E)(2).

1. The purchaser is engaged in the agricultural production of food, fiber, grass sod, or nursery products as a business for profit as defined in Internal Revenue Code § 183 as adopted by Ark. Code Ann. §26-51-424; or

2. a. The purchaser provides services to farmers directly related to the production of food, fiber, grass sod, or nursery products; and

   b. The items of farm machinery and equipment are used exclusively and directly to provide those services; and

   c. The items of machinery and equipment would have otherwise qualified for the farm machinery exemption if purchased and used exclusively and directly by the farmer for the same activity.

The Taxpayer claimed the sales tax exemption for farm equipment and machinery on the purchase of the UTV in “anticipation of a cattle farm”. The record does not contain sufficient evidence to establish that the Taxpayer was currently engaged in the business of commercial farming at the time of purchase or that the UTV was used exclusively and directly in farming under GR-51. The Taxpayer’s contention that his ex-wife is responsible for any tax liability resulting from 2012 is improper. The Taxpayer was the sole purchaser of the UTV and is solely responsible for any sales tax due. The Taxpayer filed amended income tax returns to include a Schedule F and depreciation schedules. However, the information provided was limited to the UTV. The Taxpayer did not report any
purchases or sales of cattle, any farm income, or any other farming expenses to indicate that the Taxpayer was engaged in the business of farming. The Taxpayer failed to prove entitlement to the sales tax exemption for farm machinery and equipment on the purchase of the UTV. Consequently, the Department correctly assessed sales tax against the Taxpayer. Interest was properly assessed upon the tax deficiency for the use of the State’s tax dollars. See Ark. Code Ann. § 26-18-508 (Repl. 2012).

2. Local Tax

Pursuant to Ark. Code Ann. §26-52-521 (Repl. 2014), when a purchaser does not receive the purchased tangible personal property at the business location of the seller, the sale is sourced to the location of receipt by the purchaser of the tangible personal property. Arkansas Gross Receipts Tax Rules GR-76 (“GR-76”) defines “receive” and “receipt” as taking possession of tangible personal property or making first use of services. Here, the Taxpayer purchased the UTV in [ ], Arkansas. However, the UTV was delivered to the Taxpayer’s residence in [ ] County where he took possession of the UTV. Therefore, the Department incorrectly assessed [ ] County and [ ] City local sales tax.

DECISION AND ORDER

The proposed assessment of tax and interest is sustained, subject to the adjustments for the application of the appropriate local sales tax. The file is to be returned to the appropriate section of the Department for further proceedings in accordance with this Administrative Decision and applicable law. Pursuant to Ark. Code Ann. § 26-18-405 (Supp. 2015), unless the Taxpayer requests in writing within twenty (20) days of the mailing of this decision that the
Commissioner of Revenues revise the decision of the Administrative Law Judge, this decision shall be effective and become the action of the agency. The revision request may be mailed to the Assistant Commissioner of Revenues - Policy & Legal, P.O. Box 1272, Rm. 2440, Little Rock, Arkansas 72203. The Commissioner of Revenues, within twenty (20) days of the mailing of this Administrative Decision, may revise the decision regardless of whether the Taxpayer has requested a revision. The Taxpayer may seek relief from the final decision of the Administrative Law Judge or the Commissioner of Revenues on a final assessment of a tax deficiency by following the procedure set forth in Ark. Code Ann. § 26-18-406 (Supp. 2015).

DATED: February 22, 2016