

**STATE OF ARKANSAS
DEPARTMENT OF FINANCE & ADMINISTRATION
OFFICE OF HEARINGS & APPEALS**

ADMINISTRATIVE DECISION

IN THE MATTER OF [REDACTED]
[REDACTED]
ACCT. NO.: [REDACTED]

**COMPENSATING USE TAX
ASSESSMENT
AUDIT NO.** [REDACTED]
**AUDIT PERIODS: JUNE 1, 2017
THROUGH JUNE 30, 2017**

DOCKET NOS.: 19-272

USE TAX ([REDACTED])¹

TODD EVANS, ADMINISTRATIVE LAW JUDGE

APPEARANCES

This case is before the Office of Hearings and Appeals upon written protest dated October 28, 2018, signed by [REDACTED], the Taxpayer. The Taxpayer protested an assessment issued by the Department of Finance and Administration (“Department”).

A hearing was held in this matter on May 30, 2019 at 1:56 p.m. in Little Rock, Arkansas. The Department was represented by David Scott, Attorney at Law, Office of Revenue Legal Counsel. Also present for the Department was Patti Gilliland, Audit Supervisor. The Taxpayer was represented by [REDACTED], Attorney at Law – [REDACTED] (“Taxpayer’s Representative”). The Taxpayer was also present at the administrative hearing.

ISSUE

¹ This amount represents [REDACTED] (tax), [REDACTED] (failure to file penalty), and [REDACTED] (interest) and does not include adjustments agreed to by the Department. During the administrative hearing, the Taxpayer’s Representative explained that, after the Department’s adjustment, the Taxpayer was only continuing to protest the assessment of penalty and interest because the aircraft was not sold within two (2) years of its purchase.

Whether the Department's Assessment in this matter is correct under Arkansas law. Yes.

LEGAL AND FACTUAL CONTENTIONS OF THE PARTIES

Prehearing Filings

The Department provided the following factual information in its Answers to Information Request:

On May 10, 2017, [REDACTED], ("Taxpayer") bought a [REDACTED] ["Aircraft A"] from [REDACTED] located in [REDACTED].² Taxpayer did not report the out-of-state purchase or pay the compensating use ("use") tax at the time of purchase of the [REDACTED] and the tax remains unpaid. Taxpayer has not obtained and maintained an Arkansas gross receipts tax permit as required for any person acting as an aircraft dealer. Taxpayer did not file the required monthly tax reports.

On January 22, 2018, Rayni McCool, DFA Service Representative, ("Ms. McCool"), sent an inquiry letter regarding the purchase of the [REDACTED].³ Ms. McCool requested a copy of the [REDACTED] sales invoice showing the sales price and date of sale along with proof of use tax payment. The Taxpayer did not provide the requested sales price or proof of payment of use tax.

On February 2, 2018, Taxpayer stated in his letter that is a FAA registered aircraft dealer.⁴ Taxpayer had the [REDACTED] flown to [REDACTED] Arkansas for storage and use. Taxpayer further stated, "My aircraft spend most of their time in [REDACTED], although I usually bring an aircraft that has been repaired to [REDACTED] AR, so I can advertise it and personally meet with potential customers who fly in. The [REDACTED] you reference in your letter just arrived from [REDACTED]" Taxpayer stated in his October 28, 2018 letter⁵, "So [REDACTED] aircraft now sits in hangar at [REDACTED] while [REDACTED] tries to figure out what they broke." Taxpayer further stated in his February letter." I prefer not to have a formal AR [sic] Sales/Use tax account because I only sell [REDACTED] a year and having to fill out "zero" returns monthly or quarterly drives me nuts plus I can't every [sic] member [sic] my password on your Sales/Use tax website which is why I walk into your office and hand you a check each time I sell an [REDACTED]."

² A copy of the Bill of Sale was attached as Exhibit 1.

³ A copy of that letter was attached as Exhibit 2.

⁴ A copy of that letter was attached as Exhibit 3.

⁵ A copy of that letter was attached as Exhibit 4.

October 12, 2018, Ms. McCool sent a second letter⁶ which asked the Taxpayer to provide a copy of his Arkansas Retail Sales Tax Permit to purchase aircraft exempt for resale and the FAA Dealer's Aircraft Registration Certificate to exempt the purchase. Further, in the letter, Ms. McCool requested a copy of the Aircraft Bill of Sale, Aircraft Sales Contract, and purchase price. Taxpayer did not supply the requested information.

October 31, 2018, Ms. McCool sent a third letter⁷ which contained a Summary Of Findings and Use tax assessment. A mathematical computation error was subsequently discovered by the Department and an adjustment was made to the assessment. An adjusted Summary Of Findings was mailed to the Taxpayer on January 25, 2019.⁸ Due to the lack of proof of purchase price of the [REDACTED] after repeated requests, the 2018 Blue Book value for the average retail price plus the average overhaul was used as the basis of the assessment.⁹

On October 31, 2018, Michael Yancey, DFA Sales and Use Tax Division Supervisor, (Mr. Yancey"), sent a Notice of Proposed Assessment to the Taxpayer.¹⁰ The Taxpayer timely protested the assessment on August 20, 2018.¹¹

On January 9, 2019, the Department requested purchase price information for the [REDACTED] and specifically, proof of the [REDACTED] purchase price. This purchase price was not found on the [REDACTED] Bill of Sale, but was present in an email exchange between the Taxpayer and [REDACTED].¹² On February 14, 2019, the Department made an additional request for proof of the purchase price and the wire-transfer thereof. Taxpayer provided an executed Aircraft Purchase Offer and an executed Acceptance of the aircraft, both of which are DocuSign validated, which reflect the aircraft purchase price of [REDACTED] and a processing fee of [REDACTED] for a total purchase price of [REDACTED].¹³

On January 29, 2019, Mr. Yancey sent an adjusted Notice of Proposed Assessment to the Taxpayer.¹⁴

On February 26, 2019, based upon the receipt of the Taxpayer's proof of purchase price, the Department issued a second adjusted Summary Of

⁶ A copy of that letter was attached as Exhibit 5.

⁷ A copy of that letter was attached as Exhibit 6.

⁸ A copy of that letter was attached as Exhibit 7.

⁹ A copy of that letter was attached as Exhibit 8.

¹⁰ A copy of that letter was attached as Exhibit 9.

¹¹ A copy of the protest was attached as Exhibit 10.

¹² A copy of this exchange was attached as Exhibit 11.

¹³ Copies of these document are attached as Exhibit 12.

¹⁴ A copy of this letter was attached as Exhibit 13.

Findings which reflects a total amount of tax, penalty, and interest due of [REDACTED].¹⁵

In accordance with Ark. Code Ann. § 26-18-403 (Supp. 2017), a liability has been determined by the Director of the Department of Finance and Administration (“Department”) against Taxpayer in the amount of [REDACTED] for use tax, penalty, and interest on his purchase of the [REDACTED] (Second Adjusted Summary Of Findings reflects an amount of [REDACTED]). [Citations to Exhibits Omitted.]

Within his Answers to Information Request, the Department’s Representative asserted that, since the Taxpayer collected sales tax within the sales prices contained in its invoices, the tax must be remitted to the Department before a Taxpayer may assert that its services were nontaxable and the tax was incorrectly collected from its customers pursuant to the binding authority of *Cook v. Sears Roebuck & Co.*, 212 Ark. 308, 206 S.W.2d 20 (1947). Additionally, he argued that any portions of the assessment that were estimated due to insufficient Taxpayer records were reasonable, explaining that the Taxpayer bears the burden of refuting an estimated assessment under Ark. Code Ann. § 26-18-305(a)(1)(B) (Repl. 2012). He further noted that an estimated assessment may not be rebutted through the use of its employees’ testimony, standing alone. *Leathers v. A & B Dirt Movers, Inc.*, 311 Ark. 320, 844 S.W.2d 314 (1992). Regarding any materials that could have been purchased exempt as sales for resale, he declared that, pursuant to Arkansas Gross Receipts Tax Rule GR-81.1, the Taxpayer was required to either make his refund claim with his vendors or obtain assignments of the vendors’ rights to obtain those refunds. He explained this requirement was mandatory even though refund claims with respect to those purchases is now barred by the applicable statute of limitations. He concluded his

¹⁵ A copy of this document was attached as Exhibit 14.

analysis averring that the failure to pay penalty was appropriate under Ark. Code Ann. § 26-18-208(2)(A) (Repl. 2012) and interest is warranted under Ark. Code Ann. § 26-18-508 (Repl. 2012).

Within her Answers to Information Request, the Taxpayer's Representative explained the Taxpayer paid sales tax to vendors on its material purchases even if those items were ultimately resold through the performance of taxable services and an independent contractor had improperly wrote "sales tax was included" on various invoices involving the performance of nontaxable services even though the Taxpayer did not believe its services were taxable. Additionally, she asserted that any estimated sales amounts based on later taxable sales that are not adjusted for sales tax paid on material purchases and include "sales tax paid" invoices for nontaxable services are unreasonable and must be adjusted.

Hearing Testimony

A. Audit Supervisor's Testimony

The Audit Supervisor testified the Department assessed the Taxpayer for his purchase of Aircraft A on May 10, 2017. After receipt of a report for Arkansas aircraft sales from the FAA, the Department noticed that the Taxpayer had purchased Aircraft A. Initially, the Department sent a letter to the Taxpayer, requesting information regarding his aircraft purchase including evidence that taxes were paid on the purchase.¹⁶ On February 2, 2018, the Taxpayer provided a letter stating: he had been ill, was an aircraft dealer under the name of [REDACTED] [REDACTED] ("Taxpayer's S-Corporation"), and his dealer license and sales tax

¹⁶ The Department's Representative provided an additional copy of all exhibits previously attached to his Answers to Information Request as Department's Hearing Exhibit 1.

permit had lapsed during his illness. The Taxpayer also provided evidence that he had reapplied for an aircraft dealer's license and demonstrated that the Taxpayer's S-Corporation had a valid aircraft dealer's license from August 2011 to August 2012 and May 2018 to May 2019. He did not have a valid dealer's license or sales tax permit at the time of the Aircraft's purchase. Ms. McCool¹⁷, an employee of the Department, then sent a second letter on October 12, 2018, that explained the requirements for aircraft held for resale and requested a bill of sale, aircraft dealer's license, and a copy of the Taxpayer's sales tax permit. The Taxpayer then hand delivered a letter on October 28, 2018, that stated the Aircraft was purchased for repair and resale. That letter also stated that the Aircraft was brought to Arkansas for repairs in [REDACTED].

When Ms. McCool prepared the assessment utilizing Blue Book values in the absence of the actual sales records, she incorrectly summed the retail and wholesale values for Aircraft A, resulting in an assessed purchase price of [REDACTED]. Ms. McCool discovered her error in the valuation and adjusted the audit using a [REDACTED] Blue Book average retail value and an average overhaul cost of [REDACTED]. The Taxpayer sent a letter to the Department's Representative on December 20, 2018. That letter noted that the purchase price was [REDACTED], and the Taxpayer also purchased [REDACTED] in refurbishment services. These prices were supported by additional documentation provided by the Taxpayer. The assessment was again adjusted to utilize the lower purchase price. The assessment was reduced to [REDACTED] (tax), [REDACTED] (failure to file penalty), and [REDACTED] (interest). Interest will continue to accrue until the tax is

¹⁷ Ms. McCool no longer works for the Department.

paid in full. Without a valid sales tax permit, the Audit Supervisor averred that a seller cannot operate as an aircraft dealer and purchase aircraft exempt as sales for resale. She is unsure of how many transactions the Taxpayer has discussed with the Department. She does not know how earlier transactions were handled with the Taxpayer.

B. Taxpayer's Testimony

The Taxpayer testified that he has bought and [REDACTED] aircraft within Arkansas¹⁸ prior to his purchase of Aircraft A. He previously had a sales tax permit, but it was regularly cancelled¹⁹ and had to be reactivated due to inactivity. The Taxpayer asserted that [REDACTED], another employee of the Department, told him: "Just bring the money in [from aircraft sales] when you get it." That instruction was provided around 2011 or 2012. He visited the Department's [REDACTED] Office many times before his 2011 or 2012 discussion with [REDACTED] as well. During an earlier visit, he testified that he was [REDACTED] at that time. Simply visiting the Office was extremely

¹⁸ He has sold aircraft within other states as well. See Taxpayer's Hearing Exhibit 7, an inquiry letter dated June 17, 2008, on a different aircraft sale that he testified never entered Arkansas. Also contained within that Exhibit is a letter to the State Sales and Use Department dated June 22, 2008, discussing the charitable aims of his aircraft business, explaining that the aircraft are held as inventory not as assets, and asserting that he does not feel a city business license is necessary. Another letter within that Exhibit is a letter from the Department dated October 24, 2008, that informs the Taxpayer that aircraft sales within the state are generally subject to Arkansas sales tax and providing applicable tax rates at the time of that letter. The Taxpayer explained that these letters were provided as evidence that he regularly speaks with the Department and attempts to follow the law. He also provided a letter to the [REDACTED] County Property Assessor as further evidence that he is not trying to evade his tax liabilities. See Taxpayer's Hearing Exhibit 8.

¹⁹ He provided evidence of a prior permit that was issued to him by letter from the Department dated April 17, 2009. See Taxpayer's Hearing Exhibit 9. He explained that he did not know that permit was cancelled. The Audit Supervisor explained the prior permit was issued to the Taxpayer's S-Corporation and was cancelled on December 31, 2014. The Audit Supervisor explained that, under state law, a sales tax permit will generally be automatically cancelled if a taxpayer reports zero sales for twelve months. She advised that the Sales Tax Department may be able to change his filing status to that of an occasional filer to avoid this issue in the future. See Ark. Code Ann. § 26-52-210(a) (Supp. 2017). The Auditor further noted Aircraft A was not purchased by the Taxpayer's S-Corporation.

difficult for him. He owned a [REDACTED] (“Aircraft B”) that he purchased for personal use and intended to pay applicable taxes at the time of that earlier visit. He wanted to pay those taxes to put his affairs in order. At that time, another Departmental employee, named [REDACTED], told him that the Department did not operate that way. He testified that he knew this statement was false due to his experience, being an accountant since 1975. He, however, lacked the strength to argue at that time and did not pay the taxes on Aircraft B. He intended to use Aircraft B for personal use since it was cheaper to operate but ultimately could not use it. He eventually sold Aircraft B but regrets that decision.

He explained that, to reestablish his corporation with the FAA after his license was cancelled in 2014, he would be required to file S-Corporation 1120S’s for 2015 and 2016.²⁰ He decided to operate as an individual going forward rather than reactivating the S-Corporation. Between 2014 and the end of 2016, he was fighting his cancer and did not focus on his business activities.

He further explained that he reported and paid applicable taxes on earlier aircraft sales within the Department’s [REDACTED] Office.²¹ One of those meetings also occurred with [REDACTED] who helped him report and pay applicable taxes on the sale of a [REDACTED] in the amount of [REDACTED]²² (including taxes) in [REDACTED] Arkansas.²³ He later sold Aircraft B to [REDACTED] in

²⁰ A copy of the Taxpayer’s S-Corporation’s Income Tax Returns for the 2014 tax year were entered as Taxpayer’s Hearing Exhibit 5.

²¹ The Audit Supervisor acknowledged that many aircraft sellers choose to remit the taxes on their sales in person but stated that behavior is not indicative of a statement that the Taxpayer was instructed he may purchase aircraft exempt from tax.

²² See the FAA Aircraft Bill of Sale entered as Taxpayer’s Hearing Exhibit 6.

²³ It seems that this meeting occurred after his prior conversation with [REDACTED] in 2011 or 2012.

the amount of [REDACTED], collecting an additional [REDACTED] in sales tax.²⁴ He explained that [REDACTED] set up each of the tax payments as audits.

He purchased Aircraft A in March of 2017. Aircraft A was picked up in July 2017 in [REDACTED] in a ferriable condition²⁵ after some cylinder work was completed within [REDACTED]. The aircraft was flown to [REDACTED] Arkansas. After a week in [REDACTED] Arkansas, he sent Aircraft A to [REDACTED]²⁶ in [REDACTED] (his “loose partner” since 2008). His aircraft stay at that location most of his period of ownership. Aircraft A then returned to [REDACTED] Arkansas for a couple of days and was then sent to [REDACTED] for repairs to its autopilot. After [REDACTED], Aircraft A was returned to [REDACTED] and has been on sale since September 2017. In July 2018, Aircraft A became due for an annual inspection, which occurred in [REDACTED] Arkansas. That inspection lasted one month and ruined the aircraft. Aircraft A was then transported to [REDACTED] for repairs. The repairs were not completed in [REDACTED]. Aircraft A was returned to [REDACTED] and he believes repairs to the autopilot are finally completed. Aircraft A is now located in [REDACTED]. Sometimes, Aircraft A returns to [REDACTED] Arkansas to be shown to local potential purchasers.

Now, he has listed Aircraft A with [REDACTED] in [REDACTED] (a known seller of [REDACTED] aircraft). A copy of Aircraft A’s current listing was entered as Taxpayer’s Hearing Exhibit 3. The longest

²⁴ A copy of the associated sales tax assessment dated April 2017 regarding the aircraft sale by the Taxpayer’s S-Corporation was entered as Taxpayer’s Hearing Exhibit 4. The associated checks for payment of the applicable taxes were also included within that exhibit and dated April 2017.

²⁵ Only having partial functionality.

²⁶ This organization trains [REDACTED] and provides mechanic’s training to [REDACTED]. He provides planes for [REDACTED] to repair for a low cost. The Taxpayer then eventually sells the aircraft and purchases a different aircraft for [REDACTED] to repair.

continuous period of time that Aircraft A remained within ██████ Arkansas was one month. Additionally, it has only been present in the State for a period exceeding three days twice. The second time lasted about ten (10) days. He can still make money off of the sale of Aircraft A, even after expenses. His pilot's license expired in ██████ due to an inability to complete his biennial checkup and he has not personally used Aircraft A, nor could he, due to his license status. He could operate under his partner's license, but he has not done that. Aircraft A was intended to be used only for eventual sale. Because more than two (2) years has now elapsed since his purchase of Aircraft A, he reported his purchase of Aircraft A and paid applicable taxes on May 12, 2019.²⁷ He asserted that he had two years to sell the aircraft under Arkansas law. He acknowledged that he did not have a sales tax permit at the time of his purchase of Aircraft A. He testified that he has followed the instructions of ██████.

The Taxpayer further stated that he registered for a new sale tax permit in February 2019 and the Department is currently attempting to cancel that permit as well. As evidence of the new registration, the Taxpayer provided a copy of the sales tax return filed for the month of March 31, 2019. *See Taxpayer's Hearing Exhibit 10.* As evidence of the current attempt to cancel his permit, the Taxpayer provided a letter from the Department dated May 20, 2019.²⁸ He noted that there is not a federal aircraft dealer's license. Instead, he asserted that the FAA issues

²⁷ A copy of the associated return and cancelled check were entered as Taxpayer's Hearing Exhibit 2. The Taxpayer's Representative explained that only the penalty and interest remain under protest.

²⁸ This letter explains that the Taxpayer failed to report a sales total for his aviation sales for the month of March 2019 and warns that an estimated assessment may be issued if this error is not corrected. A review of that return (entered as Taxpayer's Hearing Exhibit 10) demonstrates that the Taxpayer indeed failed to include a sales total for his aviation sales. The Audit Supervisor explained that, as a registered aircraft seller, the Taxpayer must include an amount for aircraft sales, even if that amount is zero.

Dealer's Aircraft Registration Certificates which indicate to the FAA that he buys and sells aircraft.²⁹ Those certificates have to be included within the aircraft that he purchases.

C. Hearing Assertions of Taxpayer's Representative

The Taxpayer's Representative asserted that there exists a long-standing course of conduct between the Taxpayer and the Department. She asserted that the Taxpayer was instructed to operate differently than the Department now advises. While those directions are contrary to the applicable law, she explained that the Taxpayer is entitled to rely on that course of conduct. She requested that any penalty and interest be waived.

D. Hearing Assertions of Department's Representative

The Department's Representative asserted that the Taxpayer has not provided actual proof of any official statements contrary of the Department's position in this matter. He further doubted whether a statement so contrary to Arkansas law would be provided to taxpayers. Since the Taxpayer lacked a Sales and Use Tax Permit, the Department's Representative asserted that taxes were due on the purchase of Aircraft A. He also asserted that the assessment of penalty and interest was correct.

After a general discussion of the burdens of proof in tax proceedings, a legal analysis shall follow.

CONCLUSIONS OF LAW

Standard of Proof

²⁹ See Taxpayer's Hearing 1. He had earlier Dealer's Aircraft Registration Certificates but has not found them.

Ark. Code Ann. § 26-18-313(c) (Supp. 2017) 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 means the greater weight of the evidence.

Chandler v. Baker, 16 Ark. App. 253, 700 S.W.2d 378 (1985). In *Edmisten v. Bull Shoals Landing*, 2014 Ark. 89, at 12-13, 432 S.W.3d 25, 33, the Arkansas Supreme Court explained:

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. 2017). 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. 2017). 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 application of the tax, exemption, deduction, or credit. Ark. Code Ann. § 26-18-313(f)(2) (Supp. 2017).

Further, it is the duty of every taxpayer to make a return of any tax due under any state tax law and to preserve suitable records to determine the amount due. Ark. Code Ann. § 26-18-506(a) (Repl. 2012). The taxpayer's records may be examined by the Department at any reasonable time, and, when the Taxpayer fails to maintain or provide adequate records, the Department may make an estimated assessment based on the information that is available. Ark. Code Ann. § 26-18-506(b) and (d) (Repl. 2012). The burden is on a taxpayer to refute an estimated assessment and self-serving testimony, standing alone, is insufficient to refute an estimated assessment. Ark. Code Ann. § 26-18-506(d); *cf. Leathers v. A. & B. Dirt Mover, Inc.*, 311 Ark. 320, 844 S.W.2d 314 (1992). Specifically, the Arkansas Supreme Court stated as follows when analyzing an estimated assessment:

In short, we find Mr. Nabholz's testimony insufficient, standing alone, to meet the taxpayer's statutory burden in refuting the reasonableness of the assessment. To hold otherwise would be to permit a taxpayer to maintain scant records and after an unsatisfactory tax audit, avoid taxation by merely verbalizing his transactions unsupported by appropriate documentation made at the time of the transactions or by testimony from other parties to the transactions.
Id. at 330, 844 S.W.2d at 319.

Assessment

A. Tax Assessment

Arkansas Compensating (Use) Tax, however, generally applies to the privilege of storing, using, distributing, or consuming tangible personal property and taxable services within the State of Arkansas that were purchased outside this state. Ark. Code Ann. § 26-53-106(a) (Supp. 2017). A purchaser is generally liable for Arkansas Use Tax unless a seller pays the tax on the purchaser's behalf.

Ark. Code. Ann. § 26-53-123 (Supp. 2017). Tangible personal property means personal property that may “be seen, weighed, measured, felt, or touched or is in any other manner perceptible to the senses.” Ark. Code Ann. § 26-53-102(25)(A) (Supp. 2017). Here, the Taxpayer has testified that Aircraft A has been flown into the State of Arkansas multiple times and stored within Arkansas during those trips. For purposes of the application of the tax, the short duration of those events is of no effect. Aircraft A is tangible personal property and its storage and use within the State is generally taxable. Consequently, the Department has bore its burden of proof by demonstrating that a generally taxable transaction occurred. This tax portion of the assessment was conceded.

B. Application of the Exemption Under Ark. Code Ann. § 26-52-409 (Repl. 2014)

When transactions are exempted from Arkansas sales tax, those services are likewise exempted from the Arkansas Compensating Use Tax. Ark. Code Ann. § 26-53-112(2) (Repl. 2014). Ark. Code Ann. § 26-52-409(a) (Repl. 2014) discusses the ability of aircraft sellers to purchase aircraft exempt for resale, stating as follows:

(1) Any person, whether an established business or an individual, engaged in the business of selling aircraft in this state **and holding a retail sales tax permit** may purchase aircraft exempt for resale and use the aircraft for rental or charter service without payment of sales or use tax for a period of not to exceed one (1) year from the date of purchase of the aircraft.

(2) In the case of aircraft purchased for resale which require substantial modification or substantial refurbishing prior to resale, the purchaser may use the aircraft for rental or charter service without payment of sales or use tax for a period of not to exceed two (2) years from the date of purchase of the aircraft. [Emphasis supplied.]

The requirements of the sale for resale exemption are also discussed at Ark. Code Ann. § 26-52-401(12) (Supp. 2017), which provides as follows:

(A) Gross receipts or gross proceeds derived from sales for resale to persons regularly engaged in the business of reselling the articles purchased, whether within or without the state **if the sales within the state are made to persons to whom gross receipts tax permits have been issued** as provided in § 26-52-202.

(B)(i) Goods, wares, merchandise, and property sold for use in manufacturing, compounding, processing, assembling, or preparing for sale can be classified as having been sold for the purposes of resale or the subject matter of resale only in the event the goods, wares, merchandise, or property becomes a recognizable integral part of the manufactured, compounded, processed, assembled, or prepared products.

(ii) The sales of goods, wares, merchandise, and property not conforming to this requirement are classified for the purpose of this act as being “for consumption or use”; [Emphasis supplied.]

It is clear that the Taxpayer must possess a sales tax permit to qualify for the sale for resale exemption. Since the Taxpayer did not possess a Sales and Use Tax Permit at the time of the purchase of Aircraft A, he was not entitled to the sale for resale exemption on his purchase. To the extent that the Taxpayer was not aware of this requirement, lack of knowledge of a publicly stated legal requirement cannot be recognized as a defense to its enforcement as all individuals are presumed to know the law. *Barlow v. US*, 32 U.S. 404, 411 (1833); *see also State v. Simmons*, 1 Ark. 265, 266 (1839). While the Taxpayer appears to believe permit requirement is unreasonable, the Arkansas Supreme Court has explained that the Arkansas General Assembly is the sole arbiter of policy decisions within Arkansas and it would be inappropriate for an administrative agency or court to refuse to enforce a state law as it reads based on a policy disagreement. *Snowden v. JRE Investments, Inc.*, 2010 Ark. 276, 370 S.W.3d 215.

C. Taxpayer's Estoppel Claim

While the Taxpayer's storage and use of Aircraft A within the State of Arkansas is generally taxable, the Taxpayer has asserted that he relied on certain actions by employees of the Department. Specifically, he explained that the Department has regularly accepted payments from him for aircraft sales without requiring him to obtain a sales tax permit. This assertion potentially implicates an estoppel defense.

A long line of Arkansas Supreme Court precedent provides that the State is not bound by the actions of agents that are not in compliance with the law and the agents' granted authority. *Southwestern Distilled Products v. State ex. Rel. Humphrey*, 199 Ark. 761, 136 S.W. 2d 166 (1940), *Arkansas State Highway Commission v. McNeil*, 222 Ark. 643, 645, 262 S.W.2d 129 (1953); *Terminal Oil Co. v. McCarroll, Commr. of Revenues*, 201 Ark. 830, 835, 147 S.W.2d 352 (1941); *Superior Bathhouse Co. v. McCarroll, Commr. of Revenues*, 200 Ark. 233, 237, 139 S.W.2d 378 (1940); *Sherman v. Hallmark Loan & Investment Corp.*, 249 Ark. 964, 462 S.W.2d 840 (1971) (1976).

Within *Foote's Dixie Dandy, Inc. v. McHenry*, 270 Ark. 816, 822-825, 607 S.W.2d 323, 325-327 (1980), the Court addressed the assertion that the State may never be estopped by the action of its agents, stating as follows:

We do not overrule those cases but we do abandon the principle stated in those cases that the state can never be estopped by the actions of its agents. Estoppel is not a defense that should be readily available against the state, but neither is it a defense that should never be available. Estoppel of the state is a principle of law recognized in more and more jurisdictions.

...

In *Gestuvo v. District Director of the United States Immigration and Naturalization Service*, 337 F.Supp. 1093 (C.D.Cal.1971), the court recognized estoppel when certain essential elements were present. As the court stated:

Four elements are necessary: (1) the party to be estopped must know the facts; (2) he must intend that his conduct shall be acted on or must so act that the party asserting the estoppel had a right to believe it is so intended; (3) the latter must be ignorant of the true facts; and (4) he must rely on the former's conduct to his injury.

In explaining the application of estoppel, the court, in *Gestuvo*, continued:

(T)he requirements of morals and justice demand that our administrative agencies be accountable for their mistakes. Detrimental reliance on their misrepresentations or mere unconscientiousness should create an estoppel, at least in cases where no serious damage to national policy would result ... The contrary conclusion sacrifice 'to form too much of the American spirit of fair play in both our judicial and administrative processes.'

...

Arkansas has not abandoned the doctrine of sovereign immunity which is in our constitution. Ark. Const. art. 5, s 20. However, we recently, in effect, applied the doctrine of estoppel against the state where justice required such a finding. In *Hammers v. State*, 261 Ark. 585, 550 S.W.2d 432 (1977), the appellant had agreed to testify against an accomplice in return for the prosecuting attorney's promise to nolle prosequi the charge against her. As a result, she made an oral statement incriminating herself. The trial court found that the appellant was not entitled to immunity because the agreement between the appellant and the prosecuting attorney had not been approved by the court. In vacating and remanding, we determined that the appellant was entitled to a determination whether the agreement made, even though unauthorized, should be enforced on equitable principles. We stated that:

Although the state is not estopped by the unauthorized act of its agent, (citations omitted) appellant should be equitably entitled to have her agreement with the prosecutor enforced if she complied with its terms in good faith and made a full, fair, free and candid disclosure of all facts pertaining to the crimes charged, even though that requires barring her prosecution for the crimes. *Hammers v. State*, supra, 261 Ark. at 600, 550 S.W.2d 432.

Estoppel will protect the citizen only to the extent that he relied upon actions or statements by an agent. In the present case there was good faith reliance by Foote's C.P.A. on the advice of the Employment Security

Division's field agent. There was no reason for the C.P.A. to question the agent's credibility since he had dealt with him frequently on Employment Security Division matters and no problems had arisen. Fairness has to be a two edged sword. People who deal with the state must be fair and the same principle should apply to the state. Justice Holmes made the remark many years ago that "Men must turn square corners when they deal with the government." *Rock Island, Arkansas & Louisiana R.R. v. United States*, 254 U.S. 141, 143, 41 S.Ct. 55, 56, 65 L.Ed. 188 (1920). Years later, two commentators added the logical corollary to Holmes' remark: "It is hard to see why the government should not be held to a like standard of rectangular rectitude when dealing with its citizens." Mcquire & Limet, *Hobson's Choice and Similar Practices in Federal Taxation*, 48 Har.L.Rev. 1281, 1299 (1935). We agree with both ideas.

We are satisfied that all the circumstances of this case warrant applying the doctrine of equitable estoppel. The facts are that only a form was not filed which would have been routinely approved if it had been filed; that there was not a scintilla of evidence of bad faith; and that an important agent of the State of Arkansas, clothed with considerable authority, had told Foote's that it did not have to file any further documentation. These elements were important criteria in *United States v. Georgia-Pacific Co.*, 421 F.2d 92, 96 (9th Cir. 1970). The State had all the necessary information in the present case-the name of the new corporation, the record of the older corporation and timely filed reports. The Footes were ignorant of the true facts as required in *Smale & Robinson v. United States*, 123 F.Supp. 457 (S.D.Cal.1954). These factors, as well as others, satisfy us that estoppel should be applied in this case.

Subsequent guidance from the Arkansas Supreme Court has explained that an estoppel claim should not lie in the absence of "clear proof of an affirmative misrepresentation by the agency." *Ark. Dept. of Human Services v. Estate of Lewis*, 325 Ark. 20, 922 S.w.2d 712 (1996). Applying those principles within that case, the Court provided:

In the case at hand, there was no affirmative misrepresentation by the State but only silence on the part of DHS of its right to recoup Medicaid benefits after Ruby Lewis's death. It necessarily follows that under these conditions, there can be no evidence that Ruby Lewis in any way relied on the State's silence regarding Act 415 to her detriment. For us to conclude otherwise would be to engage in guesswork and rank speculation which we will not do.

Id. at 25, 922 S.W.2d at 714. In rejecting an estoppel claim based on acquiescence of city officials to a zoning violation, the Arkansas Court of Appeals has explained that, absent a misrepresentation of law or fact by a government official, all individuals are presumed to know the law and, thus, are implicitly aware its requirements, preventing those individuals from demonstrating ignorance of the true facts (the third element of an estoppel claim). *Duchac v. City of Hot Springs*, 67 Ark. App. 98, 992 S.W.2d 174 (1999).

Here, the Taxpayer explained that the Department regularly accepted his tax payments for aircraft sales and created some billings associated with those payment. It does not appear, however, that the Department's employees ever discussed the applicability of the sale for resale exemption to the Taxpayer's aircraft purchases when accepting those sales tax payments. To the extent that those individuals should have discovered his error during their conversations, the Arkansas Supreme Court has explained that an affirmative misrepresentation is necessary to prove an estoppel claim against the State. The record does not provide evidence of an affirmative misrepresentation with respect to the relevant issue. Consequently, the Taxpayer's estoppel claim is not persuasive and does not bar the Department's use tax assessment in this matter.

Interest

Interest must be assessed upon tax deficiencies for the use of the State's tax dollars. See Ark. Code Ann. § 26-18-508 (Repl. 2012). Consequently, the assessment of interest on the sustained tax balance is likewise sustained and cannot be waived by this Office.

B. Failure to File Penalty

With respect to the failure to file penalty, Ark. Code Ann. § 26-18-208(1) (Repl. 2012) provides as follows:

In the case of a taxpayer's failure to file any return required by any state tax law on or before the date prescribed determined with regard to any extension of time for filing the return, unless it is shown that the failure is due to reasonable cause and not to willful neglect, there shall be added to the amount required to be shown as tax on the return five percent (5%) of the amount of the tax if the failure is not more than one (1) month, with an additional five percent (5%) for each additional month or fraction of a month during which the failure continues, not to exceed thirty-five percent (35%) in the aggregate . . .

Based on the above analysis, the Taxpayer was liable for payment of use tax on his aircraft purchases and could not claim the sale for resale exemption due to his lack of a Sales and Use Tax Permit. The Taxpayer was responsible for the reporting and remitting use tax on his purchase of Aircraft A. Further, lack of knowledge of this requirement cannot be recognized as a defense to the assessment of the failure to file penalty. Based on the record, the assessment of the failure to file penalty is sustained.


DECISION AND ORDER

The assessment is sustained in full. 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. 2017), 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 Administrative Decision shall be effective and become the action of the agency. The revision request may be mailed to the Assistant Commissioner of Revenues, P.O. Box 1272, Rm. 2440,

Little Rock, Arkansas 72203. A revision request may also be faxed to the Assistant Commissioner of Revenues at (501) 683-1161 or emailed to revision@dfa.arkansas.gov. 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.

Ark. Code Ann. § 26-18-406 (Supp. 2017) provides for the judicial appeal of a final decision of an Administrative Law Judge or the Commissioner of Revenues on a final assessment or refund claim denial; however, the constitutionality of that code section is uncertain.³⁰

DATED: July 10, 2019

OFFICE OF HEARINGS & APPEALS

TODD EVANS
ADMINISTRATIVE LAW JUDGE

³⁰ See *Board of Trustees of Univ. of Arkansas v. Andrews*, 2018 Ark. 12.