

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

ADMINISTRATIVE DECISION

IN THE MATTER OF [REDACTED]
DOCKET NO.: 21-228
ACCT. NO.: [REDACTED]

**GROSS RECEIPTS TAX
ASSESSMENT
AUDIT PERIOD: APRIL 1, 2018
THROUGH APRIL 30, 2018**

AUDIT NO.: [REDACTED]

[REDACTED]¹

TODD EVANS, ADMINISTRATIVE LAW JUDGE

APPEARANCES

This case is before the Office of Hearings and Appeals upon a written protest received December 1, 2020, 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”).

A hearing was held in this matter on February 26, 2021, at 9:00 a.m. in Little Rock, Arkansas. The Department was represented by Kevin Christian, Attorney at Law, Office of Revenue Legal Counsel (“Department’s Representative”). Also present for the Department was Rachel Bowen, DFA Technician, and Matthew Crane, Audit Supervisor. The Taxpayer appeared at the hearing and represented himself. All individuals appeared at the hearing by telephone.

¹ This amount represents [REDACTED] (tax) and [REDACTED] (interest).

ISSUE

Whether the Taxpayer has proven entitlement to the farm machinery and equipment exemption by a preponderance of the evidence. No.

PARTIES' FACTUAL AND LEGAL CONTENTIONS

Prehearing Filings

Within his Answers to Information Request, the Taxpayer provided the following statement:

██████████ say I'm an active farmer. ██████████ markets ██████████. " " ██████████ sold to ██████████.

Ar ST says eq used and ██████████ no sale tax – How would I know statute?

Within his Answers to Information Request, the Department's Representative provided a summary of the relevant facts, stating in pertinent part as follows²:

On or about April 16, 2018, ██████████ ("Taxpayer") purchased a 2018 ██████████. ██████████ hereafter "██████████" from ██████████ in ██████████. See **Exhibit 1**, Purchase Invoice. The purchase price of the ██████████ was ██████████. **Exhibit 1**.³ At the time of the purchase, Taxpayer claimed entitlement to the farm exemption. See **Exhibit 2**, Commercial Farming Sales Tax Exemption. On the face of the exemption certificate, the Taxpayer certified that he was engaged in, or provided services for, the production of ██████████. There is an additional hand-written word in the "products grown or raised" space on the form that undersigned believe states ██████████. Taxpayer also certified that the farm machinery and equipment he purchased would be used exclusively and directly in the agricultural production of food and fiber to be sold in the commercial marketplace or used directly in the agricultural production of farm products to be fed to livestock that will be sold in processed form at retail. Because the Taxpayer claimed the farm exemption, he paid no sales tax on the transaction.

² All Exhibits support the statements for which they are cited.

³ This document also lists a trade-in (S/N ██████████) valued at ██████████.

On October 15, 2020, the Department sent a letter to the Taxpayer requesting that he provide documentation that the exemption claimed on the purchase of the [REDACTED] was correctly applied. See **Exhibit 3**, Farm Exemption Inquiry Letter. Specifically, the Department requested documentation of Taxpayer's commercial farming venture, including “[i]ndividual [i]ncome [t]ax returns and related schedules verifying farming activities, depreciation schedules for this machinery/equipment, or other documentation indicating direct or exclusive farm use of this machinery/equipment.”

The Taxpayer responded by sending a USDA Payment Statement dated October 7, 2020, demonstrating that Taxpayer received funds through an agricultural program. See **Exhibit 4**, USDA Payment Statement Form. The Taxpayer included a hand-written note on the Payment Statement stating that “[t]his doc. shows that I am an [REDACTED]. One has to demonstrate participation in order to qualify for USDA help.” A subsequent call between the Department’s Representative and Taxpayer revealed that [REDACTED] leases some land to other individuals to farm and that he receives compensation from the government.

Lacking sufficient documentation to demonstrate the exemption was properly claimed, the Department disallowed the commercial farming sales tax exemption and assessed [REDACTED] in tax and [REDACTED] in interest, totaling [REDACTED], against the Taxpayer. Interest has continued to accrue. A Summary of Findings and Basis for Adjustment was sent to the Taxpayer on November 12, 2020. See **Exhibit 5**, Summary of Findings. A Notice of Proposed Assessment was sent to the Taxpayer on November 13, 2020. See **Exhibit 6**, Notice of Proposed Assessment.

Thereafter, on December 8, 2020, Taxpayer filed a timely protest of the assessment, stating that he is an active farmer and that he works on a farm five to six days a week. See **Exhibit 7**, Protest Form.

The Department contends that its assessment of tax, penalty, and interest was proper.

Within his Answers to Information, the Department’s Representative asserted that the item purchased by the Taxpayer represents tangible personal property and, thus, is generally taxable. He further asserted that the Taxpayer has failed to prove entitlement to the farm machinery and equipment exemption. Specifically, he asserted that the Taxpayer has not demonstrated that he is

engaged in the production of food or fiber as a commercial business or that the machinery/equipment is directly and exclusively used in farming. Additionally, he averred that the Taxpayer has not proven he is engaged in farming for profit. He also claimed that the assessment of interest was appropriate under Ark. Code Ann. § 26-18-508 (Repl. 2020).

Hearing Testimony

A. DFA Technician's Testimony

The DFA Technician agreed with the Department's Representative's rendition of the issue. The DFA Technician also certified the exhibits attached to the Department's Answers to Information Request. The DFA Technician further testified that Arkansas Gross Receipts Tax Rule GR-51 requires exempt farm machinery to be used directly and exclusively within commercial farming. Taxpayer contacted the Department in response to the Department's inquiry letter but provided no supporting documentation. The Taxpayer later provided evidence on November 6, 2020 that he sold produce to [REDACTED]. She noted that Taxpayer did not file a Schedule F. She ultimately decided that the Taxpayer failed to prove he was a commercial farmer.

The Department decided to assess the Taxpayer on his purchase. During the audit, the Taxpayer stated that he uses the [REDACTED] to check power around the farm and destroy beaver dams. He asserted that both of these uses are indirect uses. The DFA Technician acknowledged that she is not familiar with farming. She reasserted, however, that the stated maintenance activities are not direct and exclusive to the creation of the produce. She conceded that the activities were beneficial. The DFA Technician agreed that the Taxpayer worked the land but

stated that she is bound by the requirements under Arkansas law. Additionally, she instructed a trade-in deduction is only allows for motor vehicles, trailers, and motorcycles.

B. Audit Supervisor's Testimony

The Audit Supervisor agreed with the testimony and conclusions reached by the DFA Technician. He explained that the Taxpayer's lack of a Schedule F within his income tax return was a significant factor. He testified that the Taxpayer reported no farm income or losses during 2018. He noted that the [REDACTED] and [REDACTED] invoices from the Taxpayer are for the 2020 and 2021 growing season, not the current year. Additionally, the documentation from the Department of Agriculture is also dated 2020. The relevant purchase occurred in 2018. No documentation has been provided by the Taxpayer for 2018. The Taxpayer did not receive a trade-in deduction because no deduction is allowed under Arkansas Gross Receipts Tax Rule GR-12.1.

C. Taxpayer's Testimony

The Taxpayer testified that his uses of the [REDACTED] are necessary to maintain water irrigation. He used the [REDACTED] to maintain electricity for the irrigation system, destroy beaver dams, and spray weeds. He helps another individual [REDACTED]. He also uses the [REDACTED] to maintain [REDACTED] trees by clearing limbs and other activities. When he purchased the [REDACTED] the dealer only asked if he would use the [REDACTED] in farming. He did not fully read the exemption claim. The process has frustrated him since he is not an attorney. [REDACTED]⁴

⁴ The Taxpayer provided a report (dated October 26, 2020) for a [REDACTED] [REDACTED] that stated the Taxpayer had [REDACTED] pounds of [REDACTED] for the 2020 to 2021 Season.

is paid by him through crop share rent and market [REDACTED] [REDACTED]⁵ then purchases his crop. The Report of Commodities Listing⁶ details the stipend assistance that he receives for [REDACTED]. That stipend is based upon an average sales price. He asserted that this document demonstrates that he is an active farmer. The Taxpayer has [REDACTED] and an [REDACTED]. The Taxpayer questioned why he was not allowed to claim a trade-in deduction upon his trade-in of a [REDACTED] towards the purchase. If the trade-in deduction was properly disallowed, he stated that the law should be amended to allow such a deduction.

D. Assertions of Department's Representative

The Department's Representative asserted that the Taxpayer bore the burden of proof in this matter and failed to prove entitlement to the farm machinery and equipment exemption.

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

CONCLUSIONS OF LAW

A. Standard of Proof

Ark. Code Ann. § 26-18-313(c) (Repl. 2020) provides, in pertinent part, as follows:

⁵ The Taxpayer provided an invoice (dated October 21, 2020) from [REDACTED] Inc. that stated the Taxpayer sold [REDACTED] to [REDACTED] Inc. from October 17-18, 2020. The Taxpayer owned twenty-five percent (25%) of this lot.

⁶ The Taxpayer provided a [REDACTED] (dated January 26, 2021, and listing his name as a producer of each in various percentages of ownership) for the 2020 program year, which listed [REDACTED]. The Taxpayer also included a [REDACTED] listing a potential payment to the Taxpayer under the 2020 [REDACTED]

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**. [Emphasis Added.]

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) (Repl. 2020). 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) (Repl. 2020). 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) (Repl. 2020).

B. Sales Tax Assessment

1. Sales Tax

Arkansas Gross Receipts (Sales) Tax generally applies to the entire gross proceeds for all sales of tangible personal property and certain specifically enumerated taxable services. Ark. Code Ann. § 26-52-301 (Repl. 2020). The machinery purchased by the Taxpayer represents tangible personal property and is subject to Arkansas sales tax unless the Taxpayer demonstrates that an exemption applies.

Generally, the liability for collection and remittance of sales tax is upon the seller. Ark. Code Ann. § 26-52-508 (Repl. 2020). A seller, however, may be relieved of this liability if the customer makes an exemption claim. Ark. Code Ann. § 26-52-517(a) (Repl. 2020). At that point, the purchaser will become liable for the sales tax liability if the Department ultimately determines that the purchaser improperly claimed an exemption. Ark. Code Ann. § 26-52-517(e) (Repl. 2020). Here, the Department has demonstrated that the Taxpayer made exemption claims at the time of the purchases of the relevant machinery or equipment. Consequently, the liability for payment of sales tax on the purchase of the [REDACTED] has shifted to the Taxpayer if the exemption was improperly claimed.

2. Farm Equipment and Machinery Exemption

Ark Code Ann. §26-52-403(b) (Repl. 2020) exempts the sale of certain farm equipment and machinery from sales tax. Pursuant to Ark. Code Ann. § 26-52-105(b) (Repl. 2020), the Secretary 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 or the agricultural production of grass sod or nursery products as a commercial business. Farm equipment and machinery does not include implements used in the production and severance of timber, motor vehicles that are subject to registration, airplanes, or hand tools.
- . . .
- 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:
 - a. Containers or storage facilities;
 - b. Implements used in the production or severance of timber (except as exempted by GR-51(F) of this rule), or any motor vehicle of a type subject to registration for use on the highway, or airplanes, or hand tools;

- c. Attachments to and accessories not essential to the operation of the implement itself (except when sold as part of an assembled unit);
- d. Items which are incorporated into real property; and
- e. Repair labor and repair parts.
- 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 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;
 - b. The items of farm machinery and equipment are used exclusively and directly to provide those services; and
 - c. The items of farm 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.

Example: A fertilizer spreader or seed spreader, or chemical applicator purchased by a farmer would qualify for the farm machinery exemption if used exclusively by a farmer in applying fertilizer, planting seed, or applying agricultural chemicals as part of the agricultural production of food, fiber, grass, sod, or nursery products as a business. The farm machinery exemption will also be available to a fertilizer dealer, seed company, or other similar business upon the purchase of these same items provided the items are used exclusively and directly by the business in applying fertilizer, planting seed, or applying agricultural chemicals for farmers. [Emphasis supplied.]

Tax deductions and credits, like tax exemptions, exist as a matter of legislative grace. *Cook, Commissioner of Revenue v. Walters Dry Good Company*, 212 Ark. 485, 206 S.W.2d 742 (1947); and *Kansas City Southern Ry. Co. v. Pledger*, 301 Ark. 564, 785 S.W.2d 462 (1990). A taxpayer claiming a deduction or credit bears the burden of proving that he or she is entitled to the deduction or credit by bringing himself or herself clearly within the terms and conditions imposed by the statute that contains the deduction or credit. *Weiss v. American Honda Finance Corp.*, 360 Ark. 208, 200 S.W.3d 381 (2004).

Here, even if I were to treat the Taxpayer's uses of the [REDACTED] to maintain the irrigation system, treat for weeds, and maintain the [REDACTED] as direct uses and with consideration of the presumption under Arkansas Gross Receipts Tax Rule GR-51(C)(1)(a), the record still lacks any evidence that the Taxpayer was engaged in the commercial [REDACTED] during the audit period of August 2018. All provided records to establish the Taxpayer's commercial farming operation involved later periods during 2020 and 2021. Additionally, the Taxpayer claimed no farming income or expenses during the 2018 tax year upon his income tax return. I am unable to find that the Taxpayer was engaged in the commercial production of food during August 2018 based on the provided evidence, preventing satisfaction of a threshold requirement for the farm machinery and equipment exemption. Consequently, based on the record presented at this stage in the administrative process for reviewing the assessment, the exemption was properly denied.⁷

⁷ The remaining arguments raised by the Department's Representative as reasons for denying the Taxpayer's exemption claim shall not be addressed as they are rendered moot.

The Taxpayer has asserted that a deduction should still be allowed for his trade-in of an [REDACTED]. While Ark. Code Ann. § 26-52-510(b)(1)(A) (Repl. 2020) does allow a trade-in deduction for motor vehicles, trailers, and semi-trailers, a similar deduction is not allowed for other items. An [REDACTED] does not qualify as a motor vehicle⁸, trailer, or semitrailer, for purposes of the referenced deduction. The Taxpayer has provided no authority allowing for a similar deduction with respect to [REDACTED] purchases. While the Taxpayer argued that a similar deduction should be allowed for farm machinery, 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. Consequently, this argument is not persuasive.

The assessment of tax is sustained.

C. 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. 2020). Consequently, the assessment of interest on the tax balance is sustained.

DECISION AND ORDER

The proposed assessment of sales tax and interest is sustained. 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 (Repl. 2020), unless the Taxpayer

⁸ See Ark. Code Ann. § 26-52-103(20) (Repl. 2020).

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, 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 (Repl. 2020) 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.⁹

OFFICE OF HEARINGS & APPEALS

A handwritten signature in blue ink, appearing to read "T. Evans", is written over a horizontal line. There is a small handwritten number "3" above the signature.

TODD EVANS
ADMINISTRATIVE LAW JUDGE

DATED: March 8, 2021

⁹ See *Board of Trustees of Univ. of Arkansas v. Andrews*, 2018 Ark. 12.