

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

ADMINISTRATIVE DECISION

IN THE MATTER OF

████████████████████
████████████████████

**INDIVIDUAL INCOME
TAX ASSESSMENT**

ACCT. NO.: ████████████████████

DOCKET NO.: 21-239

**TAX YEAR 2019
(\$██████████)¹**

RAY HOWARD, ADMINISTRATIVE LAW JUDGE

APPEARANCES

This case is before the Office of Hearings and Appeals upon a written protest submitted on November 3, 2020, and signed by ██████████ (individually, “Taxpayer MM”), on behalf of himself and ██████████ (individually, “Taxpayer AM”), the Taxpayers. The Taxpayers protested the assessment of Individual Income Tax resulting from an audit conducted by the Individual Income Tax Section of the Department of Finance and Administration (“Department”). The Letter ID Number is ██████████.

A telephone hearing² was held in Little Rock, Arkansas, on March 12, 2021, at 10:00 a.m. The Department was represented by Kevin Christian, Attorney at Law, Office of Revenue Legal Counsel (“Department’s Representative”). Present for the Department was Juanita Breedlove – Tax Auditor. Taxpayer MM appeared at the hearing and represented the Taxpayers.

¹ The reflected amount included tax (\$██████████), penalty (██████████), and interest (\$██████████ as of October 14, 2020).

² All participants appeared at the hearing via telephone.

ISSUE

Whether the assessment issued by the Department against the Taxpayers (resulting from the disallowance of claimed deductions) should be sustained?

Yes.

FINDINGS OF FACT/CONTENTIONS OF THE PARTIES

The Department issued a proposed assessment against the Taxpayers on October 14, 2020. The Department's Answers to Information Request summarized the facts and issues involved in this case (including the basis for the Taxpayers' disagreement with the assessment as reflected by the handwritten portion of the Taxpayers' Protest Form) and stated, in pertinent part, as follows:

████████████████████ ("Taxpayers") jointly filed their 2019 Arkansas individual income tax return. See 2019 AR1000F, attached as **Exhibit 1**. On the return, Taxpayers claimed itemized deductions for medical and dental expenses, as well as for unreimbursed employee business expenses. See AR3 Itemized Deductions, attached as **Exhibit 2**. Having claimed these deductions, taxpayers reported no taxable income and claimed a refund.

On March 2, 2020, Juanita Breedlove, a tax auditor for the Department, sent Taxpayers an inquiry letter requesting that Taxpayers substantiate the deductions they claimed. See Individual Income Tax Inquiry Letter, attached as **Exhibit 3**. The letter asked Taxpayer to:

- Provide proof of payment of the medical and dental expense on line 1 of AR3 for tax year 2019.
- Provide proof of claim of line 20 unreimbursed employee business expenses on AR3 for 2019. This includes but is not limited to letter from employer concerning reimbursement of use of personal vehicle, mileage logs, receipts and explanation of expenses.

Exhibit 3.

On October 14, 2020, the Department issued a Summary of

Findings stating that the itemized deductions for medical and dental expense and unreimbursed employee business expense were being disallowed because they had not been substantiated. See Summary of Findings, attached as **Exhibit 4**. A Notice of Proposed Assessment was issued on October 14, 2020, stating that Taxpayers owe a balance of \$ [REDACTED] which includes \$ [REDACTED] in tax, \$ [REDACTED] in penalty amounts, and \$ [REDACTED] in interest as of that time. See Notice of Proposed Assessment, attached as **Exhibit 5**. Additional interest continues to accrue.

Taxpayers filed a timely Protest, stating:

I submitted each document by mail several months ago. Mileage, receipts, invoices. I called and was told that the documents requested were received but due to Covid at the time could not be given when or if I would hear anything.

See Protest Form, attached as **Exhibit 6**.

The day before the Protest form was received by the Department, the same e-mail address used to send the Protest form transmitted a PDF file to the Department, but no accompanying message, that appears to be an image of proof of insurance documents for an automobile. See Proof of Automobile Liability Insurance Documents, attached as **Exhibit 7**. The Department is not certain if Taxpayers intended this document to be considered as part of this protest; however, the Department attaches it to these Answers in the event Taxpayers consider the proof of insurance to be relevant to the subject protest.

...

The Tax Auditor requested proof of the deductions Taxpayers claimed for payment of the medical and dental expenses and for unreimbursed employee business expenses. While Taxpayers' Protest alleges to have sent certain items to the Department responsive to that request, the Department's records do not indicate that any such items supporting the claimed deductions were ever received. Undersigned counsel attempted to call the phone number listed on the protest form on the afternoon of December 1, 2020 to inquire about the documents, but the call was not answered. Undersigned counsel left a voice message but never received a return call. Even as for the items that Taxpayers' Protest form purports to have sent, none of those items enumerated on the form appear to relate to the medical or dental expenses claimed as deductions by the Taxpayers. Furthermore, standing alone, the proof of insurance document (**Exhibit 7**) does not demonstrate the

deductions were properly claimed.

Taxpayers failed to meet their burden to prove entitlement to claim the deductions for medical and dental expense and for unreimbursed business expenses. Accordingly, the Department's individual income tax assessment should be sustained and affirmed in its entirety. [P. 2 - 4].

The Tax Auditor presented testimony at the hearing consistent with the facts set forth in the Department's Answers to Information Request and she also testified that: (1) she reviews individual income tax returns for accuracy; (2) the Taxpayer's claimed itemized deductions in the amount of \$ [REDACTED] (this case involves medical/dental expenses of \$ [REDACTED] and unreimbursed employee business expenses of \$ [REDACTED]); (3) Department Exhibit 3 is an inquiry letter she mailed to the Taxpayers requesting documentation to prove entitlement to the claimed medical/dental expenses and the claimed unreimbursed employee business expenses; (4) the Taxpayers never provided any documents or records in response to her inquiry letter; (5) she never received any of the documents that Taxpayer MM stated in the Protest Form were mailed; (6) she never told Taxpayer MM that the documents listed in the Protest Form were received in the mail; (7) she never spoke with Taxpayer MM on the phone; (8) in cases where documents are received from taxpayers, the documents are imaged onto the Department's system by techs and then auditors are notified that the documents are on the system (even if someone else received the Taxpayers' records, she would be able to see the records on the system); (9) she has no notes or other documentation of any communication with the Taxpayers after she mailed the inquiry letter to them; (10) with respected to the medical/dental expenses, she needed documents showing that the Taxpayers paid the expenses such as

receipts; (11) with respect to the unreimbursed employee business expenses, she needed a mileage log, invoices, and a letter from the employer addressing reimbursement; (12) page 3 of Department Exhibit 7 is a copy of a proof of insurance card with an effective date of [REDACTED] and an expiration date of [REDACTED] but the audit period was 2019; and (13) to date, the Taxpayers have not submitted any proof to her of their entitlement to the claimed deductions.

Taxpayer MM testified that: (1) when he got the letter, he called and spoke to the Tax Auditor; (2) he asked the Tax Auditor what he needed to do; (3) he had all of his gas receipts and a mileage log; (4) the Tax Auditor told him that the Department was light-staffed due to Covid-19 but to send the records to the address she gave me and somebody would get back with me after the records were processed; (5) he does not know why the insurance card (page 3 of Department Exhibit 7) was sent to the Department; and (6) he can get copies of all of his gas and oil change receipts and he can contact the hospital about getting copies of medical bills.³

CONCLUSIONS OF LAW **Standard of Proof**

Ark. Code Ann. § 26-18-313(c) (Repl. 2020) 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.

³ At this point, the Department's Representative stated that: (1) he would object to the Taxpayers submitting records at some later date because the Department has put resources into this hearing; (2) attempts have been made to contact Taxpayer MM to find out if he had any supporting documentation; and (3) during the prehearing teleconference with Taxpayer MM on February 26, 2021, it came up that the Department would be willing to consider additional documentation but he has still not seen anything.

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).

Individual Income Tax Assessment

The State of Arkansas imposes an income tax upon “the entire income of every resident, individual, trust, or estate. The tax shall be levied, collected, and paid annually upon the entire net income as defined and computed in this chapter at the following rates . . .” See Ark. Code Ann. § 26-51-201(a) (Repl.

2020). “Net income” is the adjusted gross income of a taxpayer less allowed deductions. See Ark. Code Ann. § 26-51-403(a) (Repl. 2020).

Tax deductions and credits, like tax exemptions, exist as a matter of legislative grace. See 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 it is entitled to the deduction or credit by bringing herself or himself clearly within the terms and conditions imposed by the statute that contains the deduction or credit. See Weiss v. American Honda Finance Corp., 360 Ark. 208, 200 S.W.3d 381 (2004).

Ark. Code Ann. § 26-18-506(a) (Repl. 2020) requires the Taxpayers to maintain suitable records and states:

(a) It is the duty of every taxpayer required to make a return of any tax due under any state tax law to keep and preserve suitable records as are necessary to determine the amount of tax due or to prove the accuracy of any return.

The Department has statutory authority to “[a]udit and properly determine and compute the state tax payable by any taxpayer subject to taxation under any state law”⁴ and to “employ proper and reasonable audit methods.”⁵ The Taxpayers did not provide documentation to the Tax Auditor during the audit (or prior to the administrative hearing) to substantiate claimed deductions. The burden of proving entitlement to deductions is upon the Taxpayers and the Taxpayers failed to present sufficient evidence to establish the deductions were improperly disallowed by the Department. However, Taxpayer MM contended

⁴ See Ark. Code Ann. § 26-18-301(a)(2) (Repl. 2019).

⁵ See Ark. Code Ann. § 26-18-305(a)(2)(A) (Repl. 2020).

that records may exist which would allow for a determination of the appropriateness of the claimed deductions. In a Revision Decision issued in May of 2019, the Commissioner of Revenues delineated the authority of the Office of Hearings and Appeals and held that:

The duties of a hearing officer appointed by the Department are limited to reviewing written protests and making written findings as to the applicability of a proposed assessment or denial of a claim for refund. Accordingly, it is outside the scope of the duties of the hearing officer to provide taxpayers with guidance concerning the existence of programs to request a waiver of interest or penalties.

The Office of Hearings and Appeals does not have the authority to order or direct a re-audit of a matter submitted for consideration. The documents, which Taxpayer MM contends would substantiate the disallowed deductions, were not examined by the Tax Auditor or introduced into evidence for this proceeding. In light of the position taken by the Department's Representative, at this stage of the administrative review, the Taxpayers have failed to introduce sufficient evidence or documentation to establish that they were entitled to the denied deductions. Consequently, the Department correctly assessed Arkansas Individual Income Tax against the Taxpayers.

Interest and Penalty

Interest was properly assessed upon the tax deficiencies for the use of the State's tax dollars. See Ark. Code Ann. § 26-18-508 (Repl. 2020). A penalty was also properly assessed under Ark. Code Ann. § 26-18-208 (Repl. 2020).

DECISION AND ORDER

The assessment 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 Taxpayers request 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 Taxpayers have 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.⁶

OFFICE OF HEARINGS & APPEALS



RAY HOWARD
ADMINISTRATIVE LAW JUDGE

DATED: March 17, 2021

⁶ See Board of Trustees of Univ. of Arkansas v. Andrews, 2018 Ark. 12.