

SALES AND USE TAX

Tax Tribunal Issues First Ruling Regarding Scope of Authority of Tax Tribunal Judge

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Chief Judge Bill Thompson of the newly-established Alabama Tax Tribunal ("the Tribunal") issued his first, and a key, ruling involving the scope of his authority when the taxpayer, Stone Bridge Farms of Cullman, Alabama, does not specifically raise a viable argument or defense in its notice of appeal. This raises the question of whether a tax tribunal judge may invalidate an Alabama Department of Revenue (the "Department") regulation, even though the taxpayer challenging the underlying assessment did not attack the regulation in its pleadings or at the hearing. *Stone Bridge Farms, LLC v. State of Alabama Department of Revenue*, Ala. Tax Tribunal Docket No. S. 14-510 (January 27, 2015).

The case involves a taxpayer that owns and rents facilities for special events such as weddings, rehearsal dinners, and receptions in rural Cullman County. Initially, the facility included only a wedding chapel, a banquet room, and other buildings. It was undisputed that the rental proceeds from these specific facilities were not subject to the lodgings tax. However, beginning in January 2013, the taxpayer began renting three nearby chalets on the property to overnight guests, typically those involved with a wedding at the adjacent facility. At that point, the taxpayer began filing lodgings tax returns and paying lodgings tax on the chalet rentals.

The Department audited the taxpayer and assessed it for additional lodgings tax on the proceeds from the rental of the wedding chapel, banquet room and any other facility on the property used by the guests that previously had not been subject to lodgings tax. The Department relied on its Regulation 810-6-5-.13, which requires the collection of lodgings tax on all rented facilities "where rooms or other accommodations are offered for the use

of travelers, tourists or other transients . . ." That is, pursuant to the regulation, once any part of the taxpayer's facilities became subject to lodgings tax, the rentals from *all* facilities became subject to the tax.

The taxpayer's CEO, who had appealed the final assessment, did not attend the hearing or file a brief. Nevertheless, Chief Judge Thompson ruled that the regulation was invalid because it expanded the scope of the lodgings tax beyond the levy permitted by the statute, and voided the final assessment. Instead of challenging the substance of the ruling, the Department raised a procedural defense in its application for rehearing. It argued that the taxpayer's failure to raise the issue of the overbroad regulation barred the Tax Tribunal from ruling in favor of the taxpayer on that ground.

This procedural challenge has broad implications to tax practitioners and, of course, to the authority of the new Alabama Tax Tribunal. If the Department's position was correct, then the burden would presumably be on both the taxpayer and the Department to raise every argument in their pleadings or at the hearing before the Tribunal; otherwise, the Tribunal would lack jurisdiction to even consider these questions of law. This would create a heavy burden for any taxpayer, especially *pro se* taxpayers (including in-house counsel or tax managers of corporate taxpayers) who frequently appear before the Tribunal. It would also deliver a significant blow to the new Tribunal as a "user-friendly" forum to resolve tax disputes.

Chief Judge Thompson rejected the Department's attempt to limit the Tribunal's scope of authority and ability to review questions of law:

I agree that if a taxpayer disputes a final assessment on factual grounds, the taxpayer must present evidence that the final assessment is incorrect. . . . This case can be distinguished, however, because the relevant facts, as stated in the Department's answer, are not disputed, and the case involves a purely legal issue. That is, the case does not involve a disputed issue of fact.

He ruled that by appealing in a timely manner, the taxpayer had invoked the jurisdiction of the Tribunal, and that the validity of the regulation was also before the Tribunal because the Department cited the regulation as the basis for the assessment in its answer. He also added that "the Alabama Legislature has empowered the Tax Tribunal to increase or decrease a final assessment upon appeal 'to reflect the correct amount due.'" See Ala. Code § 40-2A-7(b)(5)d.1.

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As additional support for the distinction between questions of law versus fact, the judge also cited new Tax Tribunal Regulation 887-X-1-.6, which provides that the Tribunal's final order may "grant such relief and invoke such remedies as deemed necessary by the tribunal judge for a fair and complete resolution" of the case. He added: "[f]undamental fairness mandates that a taxpayer should not be required to pay a tax that is not due under Alabama law."

The Department's attorneys argued that the Tribunal was in essence placing the burden of proof on the Department to justify the validity of its assessments, and that the Tribunal had "effectively become an advocate for the [t]axpayer." The judge flatly rejected both arguments, referring to the fundamental premise for the establishment of the Tribunal last year: "By establishing an independent Alabama Tax Tribunal . . . this chapter provides taxpayers with a means of resolving controversies that ensures both the appearance and the reality of due process and fundamental fairness." Ala. Code § 40-2B-1(a).

The judge asserted that if the Department's position was upheld, it would cause the taxpayer to pay "a tax that is not due under Alabama law, because the taxpayer's *pro se* representative may not have properly plead the taxpayer's case... If that position is accepted, then small businesses and non-lawyer taxpayers could fall prey to procedural and other legal traps, and would in practical effect be forced to hire an experienced attorney to represent them in an appeal before the Tribunal, which is clearly contrary to the intent of the Legislature." To buttress that statement, the judge cited a recent article in *Business Alabama Monthly* in which one of the principal authors and sponsors of the bill made essentially the same point.

Citing the Department's mission statement to administer Alabama's revenue laws in an equitable manner, the judge added a strong personal note:

In my 38-plus years as an employee of the Revenue Department, first as an assistant counsel and then for 31-plus years as the Department's Chief Administrative Law Judge, I personally observed that the Department's employees, and especially those in its operating divisions, almost universally applied the proverbial Golden Rule and took the position that a taxpayer should only pay the correct tax due, nothing more or less. Unfortunately, it appears that this case is an exception to that commendable mindset... Rather, the Department's position is that the [t]axpayer should be required to pay

lodging tax that isn't due ... based on what most citizens of Alabama would consider a procedural or technical trap.

In conclusion, he pointed out the potential waste of resources since the taxpayer could appeal an adverse ruling of the Tribunal to circuit court, raise the validity of the regulation in question at that level, and have a trial *de novo*. "Not resolving an issue while it is before the Tribunal would thus cause an unnecessary waste of time and expense for the [t]axpayer and the Department and also waste the circuit court's time and resources."

As Chief Judge Thompson's ruling makes clear, one of the overriding goals of a state-level tax tribunal, court, board or commission is to provide a system that is fair to both the taxpayer and the state department of revenue – in appearance and in reality. While it is unknown whether the Department will appeal this ruling to circuit court, this case is especially instructive for any state considering establishing an independent tax tribunal or court. According to Eileen Sheer and the AICPA's State and Local Tax Technical Resource Panel (TRP), only sixteen states still lack some form of an independent tax tribunal. While Alabama joined the majority of states last year with the passage of the Alabama Taxpayer Fairness Act, there are similar proposals currently pending in New Mexico and Washington.

The states considering an independent tax tribunal, as well as states with existing tax tribunals of whatever stripe, should consider clarifying the authority of their tribunal with respect to questions of law or legal arguments not raised by the taxpayer in its pleadings but yet relevant to the ultimate issue of determining the taxpayer's correct liability. And this authority should not be limited to appeals involving *pro se* taxpayers.

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