

ARIZONA TAXPAYER BILL OF RIGHTS RULING

TBR 00-1

This substantive policy statement is advisory only. A substantive policy statement does not include internal procedural documents that only affect the internal procedures of the agency and does not impose additional requirements or penalties on regulated parties or include confidential information or rules made in accordance with the Arizona administrative procedure act. If you believe that this substantive policy statement does impose additional requirements or penalties on regulated parties you may petition the agency under Arizona Revised Statutes § 41-1033 for a review of the statement.

ISSUE:

Whether certain tanning facility operators understated their transaction privilege tax obligations as a result of an extensive misunderstanding or misapplication of the tax laws and, if so, what is the affected class of taxpayers and what are the terms of the closing agreements.

APPLICABLE LAW:

Arizona Revised Statutes (A.R.S.) § 42-2056.A provides that the Arizona Department of Revenue ("Department") may enter into closing agreements with taxpayers if the Department determines that, as a result of the same extensive misunderstanding or misapplication of the tax laws, taxpayers failed to properly account for their taxes.

A.R.S. § 42-2056.A.1 states that an extensive misunderstanding or misapplication occurs if the Department determines that more than sixty percent of the affected class failed to properly account for their taxes owing to the same extensive misunderstanding or misapplication of the tax laws.

A.R.S. § 42-2056.A.2 requires the Department to publicly declare the nature of the possible misunderstanding or misapplication and the proposed definition of the class of affected taxpayers and to conduct a public hearing to hear testimony regarding the extent of the misunderstanding or misapplication of the affected class.

A.R.S. § 42-2056.A.3 requires the Department to issue a tax ruling and publish its findings in a newspaper of general circulation if it determines after the public hearing that the affected class of taxpayers has failed to properly account for their taxes due to an extensive misunderstanding or misapplication of the tax law.

Pursuant to A.R.S. § 42-2056.A.4, the Department may abate some or all of the penalties, interest and tax in a closing agreement, or the closing agreement may provide for prospective treatment of the matter. All taxpayers in the affected class will be offered the opportunity to enter into a similar closing

agreement for the same tax periods.

A.R.S. § 42-2056.A.5 requires the Department to offer taxpayers who have correctly computed their tax obligations the opportunity to enter into closing agreements, which provide for a pro rata credit or refund of the tax previously paid, subject to the applicable statute of limitations provisions.

To comply with A.R.S. § 42-2056.B, the Department must secure the approval of the tax ruling and closing agreements from the attorney general before entering into closing agreements.

A.R.S. § 42-2056.C provides that a closing agreement, signed under this section and subject to the taxpayer's accounting for and paying such taxes in the future, is final and conclusive except upon the showing of fraud, malfeasance or misrepresentation of a material fact and cannot be reopened as to the matters agreed upon nor modified by any officer, employee or agent of the state. The agreement or any determination, assessment, collection, payment abatement, refund or credit made pursuant to the agreement shall not be annulled, modified, set aside or disregarded in any suit, action or proceeding.

A.R.S. § 42-5002.A.1 provides, in part, that a person that imposes an added charge to that is identified as being to cover transaction privilege tax shall not remit less than the amount collected to the Department.

DISCUSSION:

On May 5, 1999, the Director of the Department issued Transaction Privilege Tax Ruling 99-5 ("Ruling") that expressed the Department's position regarding the taxability of tanning facilities. The Ruling stated that "income derived by tanning facility businesses and other establishments from their customer's use of tanning equipment is subject to transaction privilege tax under the personal property rental classification." The Department will allow a reasonable time for the Ruling to be disseminated to the affected taxpayers, and for the affected taxpayers to begin remitting the required transaction privilege tax.

The Department received a letter from a taxpayer requesting that the Assistant Director of the Transaction Privilege Tax Division ("Division") determine that as a result of the same extensive misunderstanding or misapplication of the tax laws more than 60 percent of the businesses operating tanning facilities in Arizona unintentionally or inadvertently failed to report or pay transaction privilege tax on certain revenues received. The Division researched the issue and found that less than 10% of the tanning facilities were remitting transaction privilege tax on the revenues received for the use of tanning machines. As a result of this finding, a Notice of Public Hearing (Notice) was published in the *Arizona Capitol Times*, a newspaper of general circulation, on March 31, 2000. The Notice stated that a public hearing would be held on April 27, 2000, at 1:30 p.m. at the Industrial Commission, 800 W. Washington, Phoenix, Arizona. The class of taxpayers was defined as those entities who have receipts from engaging in the business of providing tanning equipment for use by others. Letters, similar to the Notice, were also sent to all known businesses that operated tanning facilities. The Notice provided that copies of relevant, non-confidential documents could be obtained and reviewed from 8:00 a.m. to 5:00 p.

m. at the reception desk in the lobby of the Revenue Building located at 1600 West Monroe, Phoenix, Arizona. It also indicated that if additional information was needed, the taxpayer could contact Robert Ridenour at (602) 542-4656, or by writing him at 1600 W. Monroe, Phoenix, Arizona 85007.

On April 27, 2000, at 1:30 p.m. in the Industrial Commission Amphitheater, a public hearing was held, pursuant to the Taxpayer Bill of Rights, A.R.S. § 42-2056, regarding the failure of tanning bed operators to file returns and pay transaction privilege tax.

John D. Sylvester, Problem Resolution Officer for the Department of Revenue and designated hearing officer, presided at the hearing (which was recorded), announced that under A.R.S. § 42-2056 the Department of Revenue may enter into closing agreements with the members of a class of taxpayers if the department determines that, as a result of the same extensive misunderstanding or misapplication of the tax laws, more than 60 percent of the persons in the affected class of taxpayers failed to properly account for their taxes. In addition, he stated that the Department of Revenue defined the proposed class of affected taxpayers as those businesses that have receipts from engaging in the business of providing tanning equipment for use by others. All relevant portions of the notice of public hearing were read. He also disclosed that the Department of Revenue anticipated a decision within the next 60 days and that a tax ruling and closing agreements would be forthcoming if the department determined that the affected class qualified under the provisions of A.R.S. § 42-2056.

Robert Ridenour, Director's Office of Tax Policy and Legal Support, testified that, after the receipt of a letter from a taxpayer requesting relief under A.R.S. § 42-2056, the Division researched the issue and found that there was greater than 60% of the affected taxpayers not complying with the taxing statute, as expressed by the Department in Transaction Privilege Tax ("TPR") Ruling 99-5. He further stated that the public hearing was to determine the reason or reasons for the non-compliance.

The hearing officer heard testimony from taxpayers and taxpayer representatives. They testified that they had concluded that the activity was a service business. The hearing officer also heard testimony from Robert Ridenour, who testified that research by the Division also revealed that taxpayers who failed to comply had done so because they had concluded that they were engaged in a service business. The hearing officer found that the testimony was relevant and credible, and that a substantial misunderstanding therefore existed.

RULING:

The Hearing Officer found that more than sixty percent of the tanning business operators had understated their Arizona transaction privilege and use tax liability by failing to report or pay transaction privilege tax on certain revenues through an extensive misunderstanding or misapplication of the tax laws and that the class of affected taxpayers is those businesses that have receipts from engaging in the business of providing tanning equipment for use by others.

At the recommendation of the Hearing Officer and in the interest of fair dealing and equity, the

Department will provide to members of the affected class an opportunity to enter into closing agreements under which tax, penalties and interest otherwise due will be waived in accordance with A.R.S. § 42-2056 for tax periods prior to August 31, 1999, subject to the applicable statute of limitations. Tanning facility operators who correctly reported and paid transaction privilege tax on revenues may also enter into closing agreements for the same tax periods, and the Department will refund the amount of tax, penalties and interest paid as a result of their proper reporting and payment of tax. Taxpayers entering into the closing agreements must in the future properly account for and pay any transaction privilege taxes due. Tanning facility operators that want to avail themselves of this Ruling must enter into closing agreements within sixty (60) days of receiving notice of this Ruling.

To request additional information concerning closing agreements, please contact Robert Ridenour, Department of Revenue, 1600 West Monroe, by telephone at (602) 542-4656, Ext. 7671 or by facsimile at (602) 542-5005.

Mark W. Killian, Director

In accordance with A.R.S. §42-2056(C), the above ruling is hereby approved this day of August 14, 2000.

Janet A. Napolitano
Attorney General
By: Michael P. Worley