

COLUMBIA SOUTHERN EDUCATION §
GROUP, F/K/A COLUMBIA SOUTHERN
UNIVERSITY, INC. §
P.O. BOX 3110
ORANGE BEACH, AL 36561, §

APPEAL OF USE TAX REFUND
DENIAL
MAY 2003 – APRIL 2009
TAX I.D. #351

Taxpayer, §

v. §

BALDWIN COUNTY, ALABAMA §
SALES & USE TAX DEPARTMENT.

**FINAL ORDER ON TAXPAYER'S
APPLICATION FOR REHEARING**

This appeal involves a denied refund of Baldwin County use tax requested by the above Taxpayer for May 2003 through April 2009. A Final Order was entered on May 30, 2013 affirming the County's denial of the refund. The Final Order concluded that private schools in Alabama are not exempt from State or local sales or use tax, and consequently, that Department Reg. 810-6-3-.47.02, which specifies that private schools are exempt from sales and use tax, is invalid. "The Department's unsupported declaration in Reg. 810-6-3-.47.02 that private schools are exempt is thus clearly invalid and a wrongful usurpation of legislative authority by the Department." Final Order at 7. The Taxpayer timely applied for a rehearing.

The May 30, 2013 Final Order found that the private school exemption in Reg. 810-6-3-.47.02 was without statutory support. As discussed below, however, the Taxpayer correctly points out on rehearing that when Reg. 810-6-3-.47.02 was promulgated in 1961, Alabama law did include an exemption from sales tax for sales to private schools.

Alabama enacted a sales tax in 1959 pursuant to Act 100 in the 1959 Second Special Session of the Alabama Legislature. Act 100 became effective on October 1, 1959. Section 33 of Act 100 specified various exemptions, but did not include an exemption for sales to private schools. But later in the same Special Session, and specifically on November 6, 1959, the Legislature amended Section 33 of Act 100 by Act 371 to include an exemption for sales of tangible personal property to private schools. The Department accordingly promulgated Reg. 810-6-3-.47.02 in March 1961 in accordance with the private school exemption included in Act 371.

The Legislature again amended Section 33 of Act 100 in 1963 by Act 425, 1963 Ala. Acts. The preamble to Act 425 indicated that Section 33 was being amended to include an exemption for sales of fuel and supplies for use or consumption on certain ships and towing vessels. The private school exemption was not mentioned in the preamble to Act 425, but as reenacted, that exemption was deleted from Section 33.

The Taxpayer asserts that “[o]ne might conclude that 1963 Act 425 effected an *implicit repeal* of the private school exemption. . . .” Taxpayer’s Application for Rehearing at 3. It contends, however, that an implicit repeal of the exemption is contradicted by three key points. First, the preamble to Act 425 did not mention that the private school exemption was being deleted. Second, Act 425 amended “Section 33 of Act No. 100,” and not “Section 33 of Act No. 100, as amended by Act No. 371.” Based thereon, the Taxpayer claims that “[t]he logical conclusion is that the Legislature *simply forgot*” about the private school exemption added to Section 33 by Act 371. Taxpayer’s Application for Rehearing at 4. Third, the Department amended the private school regulation after Act 425 was enacted, which, according to the Taxpayer, indicated that

the private school exemption was still valid.

To begin, the fact that the Revenue Department amended Reg. 810-6-3-47.02 after the private school exemption was deleted from the statute in 1963 is of no consequence. The Taxpayer argues that "one would presume that if there was an implicit repeal of the private school statutory exemption, the Alabama Department of Revenue would have been well aware of that fact because the repeal (if one occurred) occurred two months prior to the (Department's) 1963 amendment to the Private School Exemption Regulation." Taxpayer's Application for Rehearing at 5. The Taxpayer presumes too much.

The Department employees that were charged with interpreting and administering the State's sales and use tax laws in 1963 have long since passed. Consequently, we can never know what those individuals were aware of concerning Act 425 and the deletion of the private school exemption pursuant to that Act. But the fact remains that the exemption was excluded by the Act, so I presume that the Department administrators simply were unaware that the exemption was no longer in the law, and thus incorrectly assumed when they subsequently amended Reg. 810-6-3-47.02 that the exemption was still applicable. I agree with the County that "[a]t best the Department of Revenue's actions in amending the rule after the statute was repealed simply indicates inattentiveness on the part of the department to the tax laws of the state, or at worst, a willful failure to follow existing law by substituting the judgment of the Department of Revenue for that of the legislature." County's Response Brief at 11.

There is no evidence that the issue was ever raised from 1963 until 1989, when the Administrative Law Division ruled in *State of Alabama v. Roberts' Cafeteria, Inc.*,

Docket S. 87-179 (Admin. Law Div. Recommended Order 1/3/1989), that the private school regulation, Reg. 810-6-3-.47.02, was invalid.¹ See, Final Order at 4, 5. The holding in *Roberts Cafeteria* was later cited with approval in *Ward International Trucks, Inc. v. State of Alabama*, Docket S. 00-216 (Admin. Law Div. F.O. 11/16/2000; F.O. on Rehearing 12/5/2000); F.O. Denying Department's App. for Rehearing 12/18/2000). Neither *Roberts Cafeteria* nor *Ward International* were appealed, yet even after being on notice that Reg. 810-6-3-.47.02 was invalid, the Department has, without explanation, failed to repeal the erroneous provision.

After Act 425 was enacted in 1963, there has been no statutory basis for the private school exemption. As discussed at length in the Final Order, a Department regulation that is contrary to or unsupported by a statute enacted by the Legislature is invalid. The Department cannot by regulation continue the life of an exemption that has been repealed by the Legislature. "It is not within the power of the State Department of Revenue to add to or take from the statute by administrative construction. Only the legislative branch of our state government is vested by the Constitution with lawmaking authority." *State v. Robinson Land & Lumber Co. of Ala.*, 77 So.2d 641, 647 (Ala. 1954).

I agree with the Taxpayer that it "is not entirely clear" why the private school exemption was removed from the statute pursuant to Act 425 in 1963. Taxpayer's Application for Rehearing at 2. Perhaps the drafters of Act 425 did forget or were unaware that the private school exemption was added by Act 371. The fact remains, however, that it was removed by Act 425, and the sales tax and use tax exemption

¹ It is not surprising that private schools, as the beneficiaries of the invalid regulation, did not challenge the regulation.

statutes, now Code of Ala. 1975, §§40-23-4 and 40-23-62, respectively, have been reenacted in their entirety on numerous occasions since 1963 without the private school exemption provision. If a statute is revised, and a part of the prior statute is omitted, such omitted part has been repealed. "But, if parts of the original act are omitted from that which is a complete revision of the law on the subject, such omitted parts are annulled and repealed." *American Standard Life Ins. Co. v. State*, 149 So. 168 (1933).

Even assuming that the deletion of the private school exemption in Act 425 and the subsequent reenactments of the exemptions provisions without that exemption did not act to repeal the exemption, the Alabama Legislature conclusively settled the issue in 1977 when it adopted the recodified Alabama Code of 1975.

The Alabama Legislature adopted the Code of Alabama 1975 pursuant to Act No. 20, §4, Ala. Acts 1977. That 1977 Act included a repealing provision – "All statutes of a general and permanent nature not included in the CODE OF ALABAMA 1975, are repealed on the date on which such Code becomes operative and effective." Code of Ala. 1975, §1-1-10 also provides that "all statutes of a public, general, or permanent nature, not included in this Code, are repealed." See generally, *State Dept. of Revenue v. MGH Management Inc. and Manderson Associates, Inc.*, 627 So.2d 408 (Ala. Civ. App. 1993).

In *MGH Management*, two corporate taxpayers petitioned the Department for refunds of corporate income tax for 1986 through 1988. The case turned on whether the Multistate Tax Compact ("MTC") was in effect in Alabama in those years. The MTC was created in 1966 to establish a uniform income tax system for allocating and apportioning the income and deductions of taxpayers doing business in more than one

state. Alabama adopted the MTC in 1967 pursuant to Act No. 395, Ala. Acts 1967. Section 8 of Act 395 also provided that the MTC shall become effective upon approval by the Governor and the passage of an act by Congress authorizing the various states to enter into such a Compact.

Congress never passed an act that authorized the states to enter into the Compact, and in 1978 the U.S. Supreme Court concluded that the MTC did not require congressional approval. *United States Steel Corp. v. Multistate Tax Comm'n*, 98 S. Ct. 799 (1978).

As indicated, the Alabama Legislature adopted the Code of Ala. 1975 by Act No. 20, §4, Ala. Acts 1977. The new Code, at Code of Ala. 1975, §40-27-1 et seq., contained the entire text of the MTC, as enacted in Alabama pursuant to Act 395 in 1967, except that it deleted §8 of Act 395 that required congressional approval before the MTC became effective in Alabama.

The Administrative Law Division held in *MGH Management* that the MTC was in effect in the subject years, and accordingly entered a recommended order granting the refunds. The Commissioner of Revenue reviewed the recommended order and issued a final, appealable order denying the refunds.² The taxpayers appealed to circuit court, which reversed and held that the MTC was in effect, and that refunds were due.

² When *MGH Management* was decided in 1991, the Administrative Law Division was governed by the procedures in the Alabama Administrative Procedures Act, Code of Ala. 1975, §41-22-1 et seq. That Act required the issuance of a recommended order if a hearing was conducted by a hearing officer. The agency head, the Commissioner of Revenue, was then authorized to issue the final, appealable order in the case. The current procedures followed by the Revenue Department, and also specifically the Administrative Law Division, were adopted pursuant to Acts 1992, Act 92-186, effective October 1, 1992, see Code of Ala. 1975, §40-2A-7, et seq.

The Department appealed to the Court of Civil Appeals. That Court held that by omitting the requirement of congressional approval in the readopted Code, the Legislature clearly intended to repeal that provision.

In 1977 by Act No. 20, §4, Ala. Acts 1977, the Alabama legislature adopted the Code of Alabama 1975, the first official recodification since 1940. The new Code of Alabama, at §§ 40-27-1 to -6, contained the entire text of the Tax Compact but deleted § 8 of Act No. 395, which contained the necessity of Congressional approval before becoming effective. The 1977 act included a repealing provision, which states: "All statutes of a general and permanent nature not included in the CODE OF ALABAMA 1975, are repealed on the date on which such Code becomes operative and effective. . . ." (Emphasis in original.) Section 1-1-10, Code 1975, also provides that "all statutes of a public, general, and permanent nature, not included in this Code are repealed.

* * *

In holding that the Tax Compact was in effect in this state, the trial court held that, by adopting the 1975 Code, the legislature repealed the portion of the original legislation limiting its effective date and that the Tax Compact had been enacted by its own terms.

We agree. The 1977 recodification of the Alabama code contained absolutely no condition to the immediate effectiveness of the Tax Compact. The absence of such conditional language evidences clear legislative intent: that the Tax compact be enacted in 1977 and not be contingent upon Congressional approval. We find that the legislature clearly, and not by implication, repealed the Congressional approval requirement of the 1967 act by excluding it in the 1975 recodification of the Alabama Code.

MGH Management, 627 So.2d at 410.

The rationale of *MGH Management* applies in this case. When the Legislature adopted the recodified Code of Alabama 1975 in 1977, the private school exemption was not included in the sales and use tax exemptions statutes, §§40-23-4 and 40-23-62, respectively. Consequently, even if the private school exemption was not repealed by being omitted from the exemptions statute pursuant to Act 425 in 1963, and also

from the later amended versions of the statute, it clearly was repealed by being omitted from the recodified Code of Alabama 1975 in 1977.

The Taxpayer on rehearing repeats its argument that the County is required to follow Reg. 810-6-3-.47.02 based on Code of Ala. 1975, §§11-3-11.2(b) and 40-12-4(b). That argument was adequately addressed and rejected in the Final Order at 10, 11. A Department regulation must be followed if it is a reasonable interpretation of the underlying statute. See generally, *White v. Shellcast*, 477 So.2d 422 (Ala. 1985). But if a regulation is not supported by a statute, then the regulation must be rejected.

All local taxing jurisdictions in Alabama must follow all valid Department sales and use tax regulations that are reasonable and supported by a statute duly enacted by the Legislature, but a local jurisdiction is not required to follow a patently invalid regulation that is contrary to Alabama law, as is the private school exemption regulation.

As stated in the Final Order, at 12:

It is important that the Court in *Yelverton's* found that the Department's local nexus regulation was reasonable and not contrary to any statute. Clearly in such cases, a Department regulation must be followed because it is a correct interpretation of the underlying law. And it necessarily follows that because county and municipal sales and use tax laws must parallel the State sales and use tax provisions, any Department regulation that correctly interprets a State sales and use tax statute must also be followed for local tax purposes.

It does not follow, however, that a Department regulation that is contrary to or not supported by a statute must still be followed by the Department and all local taxing jurisdictions. To the contrary, as discussed, such a regulation must be rejected.

I recognize that the Department's long-standing interpretation of a statute should be given favorable consideration by the courts. But that "rule of construction is to be laid aside where it seems reasonable certain that the administrator's interpretation has

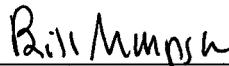
been erroneous and that a different construction is required by the language of the statute.” *Boswell v. Abex Corporation*, 317 So.2d 317, 319 (Ala. 1975). While the private school exemption was in effect when Reg. 810-6-3-.47.02 was promulgated in 1961, it arguably was repealed by Act 425 in 1963, and without question was clearly repealed in 1977 by being excluded from the recodified Code of Alabama 1975. The regulation thus is unsupported by statute and must be rejected.

The holding in this case is based on a simple premise. The Revenue Department cannot create an exemption from tax through its rule making authority. The Department may, of course, issue a regulation interpreting a statute, and such a regulation will be affirmed if reasonable and consistent with the underlying statute that it seeks to interpret. But if the substance of the regulation is unsupported by a statute, as is the private school exemption regulation, then the regulation must be rejected, regardless of how long it has been in existence. An invalid regulation does not somehow become valid through the passage of time.

The May 30, 2013 Final Order is affirmed.

This Final Order on Taxpayer’s Application for Rehearing may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered August 15, 2013.



BILL THOMPSON

Chief Administrative Law Judge

bt:dr

cc: Shirley M. Justice, Esq.
Donald E. Johnson, Esq.
David J. Conner, Esq.
Kim Creech