DECISION OF MUNICIPAL TAX HEARING OFFICER

July 11, 2011

Taxpayer's Representative
Address for Taxpayer's Representative

Taxpayer
MTHO # 602

Dear Taxpayer:

We have reviewed the evidence and arguments presented by ***Taxpayer*** and the City of Surprise (Tax Collector or City) at the hearing on June 15, 2011. The review period covered was January 2007 through July 2010. Taxpayer's protest, Tax Collector's response and our findings and ruling follow.

Taxpayer's Protest

Taxpayer was assessed City privilege tax under the amusement classification for Taxpayer's operation of a fitness facility. Taxpayer obtained state and City privilege tax licenses from the Arizona Department of Revenue (Department) when the business was established.[1] Taxpayer contacted the Department regarding filling out the tax return forms and was verbally told by a representative that the services provided by Taxpayer were not subject to a privilege tax. The license was subsequently cancelled and the Department stopped sending Taxpayer the return forms. Taxpayer believed it was in compliance. Taxpayer was not aware that the City taxed the operation of fitness facilities and Taxpayer was not informed by either the City or by the Department that city privilege taxes are due. Taxpayer should not be liable for any tax prior to 2010 because of oversight by the City and the Department. Taxpayer should only be liable for tax after it was informed by the City that tax should be collected on the operation of a fitness facility.

Tax Collector's Response

Taxpayer operates a fitness facility within the City. The City has adopted Local Option H which imposes the privilege tax on the operation of health spas and fitness centers. Because Taxpayer's activities were taxable during the review period, the full amount of the assessment, including interest, is due for the review period.

Discussion

Taxpayer operates a fitness facility in the City. The City imposes a privilege tax on the business activity of providing amusements, including health spas, fitness centers, dance related activities or instruction, whether on a per-event use, or for long-term usage, such as membership fees. Surprise City Code (SCC) § 3.14-410(a)(2).

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[1] The City's privilege tax is collected by the Arizona Department of Revenue.

The Tax Collector conducted an audit assessment of Taxpayer for the period January 2007 through July 2010 and issued an assessment under the amusement classification for Taxpayer's operation of the fitness facility. Taxpayer timely protested the assessment contending that it was told by a Department representative that its services were not subject to privilege tax. Thereafter its license was cancelled and Taxpayer stopped receiving the privilege tax return forms. Taxpayer believed it was in compliance with the tax laws.

Taxpayer also argued that the City did not question Taxpayer's failure to file returns or pay tax when Taxpayer submitted the annual renewal of its business license. When Taxpayer was told by the City that it was taxable, Taxpayer promptly complied. Taxpayer would have complied earlier had Taxpayer not been mislead by the Department. Taxpayer therefore contends it should only have to pay tax after the City informed Taxpayer that it was subject to the City privilege tax.

It is not disputed that SCC § 3.14-410(a)(2) imposes the City privilege tax on persons engaging in the business of operating health spas and fitness centers or that Taxpayer's operation of its fitness facility is subject to the City privilege tax. The question is whether the City is nevertheless precluded from enforcing the tax during the review period because Taxpayer made a good faith attempt to be licensed and his failure to pay the tax was due to erroneous information he received from the Department.

Generally, it is a taxpayer's responsibility to be familiar with the code of the jurisdiction where it will be operating. Every person is presumed to know the law and its requirements, and a mistake as to such requirements is no excuse for failure to meet them. *Newman v. Fidelity Savings and Loan Association,* 14 Ariz. 354, 128 P. 53 (1912). However, there are limited exceptions to the general rule.

First, equitable estoppel may lie against a taxing authority in rare situations if certain conditions are met. Two of the conditions are (1) the taxpayer actually and reasonably relied (2) on prior inconsistent conduct of the taxing authority. *Luther Construction Co., Inc., v. Arizona Department of Revenue,* 205 Ariz. 602, 605, 74 P.3d 276, 279 (2003). A taxpayer's reliance is not reasonable however "if the law clearly precluded the Taxpayer's theory of nontaxability." *Valencia Energy Company, v. Arizona Department of Revenue,* 191 Ariz. 565, 580, 959 P.2d 1256, 1271 (1998). Here, SCC § 3.14-410(a)(2) clearly imposes the City's privilege tax on persons engaging in the business of operating health spas and fitness centers. Therefore, Taxpayer's reliance in this case was not reasonable.

In addition, to meet the requirement for an inconsistent act, an action by the government must bear some considerable degree of formalism. *Valencia,* 191 Ariz. at 577, 959 P.2d at 1268. Generally, the state action would need to be in writing." *Valencia,* 191 Ariz. at 577, 959 P.2d at 1268. Here, there was no formalism to the information Taxpayer received from the Department. The information was not in writing. The record does not disclose the identity of the person providing the information or the person's capacity and authority with the Department. The information Taxpayer received from the Department does not give rise to equitable estoppel.

Second, it may be possible to preclude including interest and penalty in an assessment if the deficiency assessed is directly attributable to erroneous written advice furnished to the taxpayer by an employee of the City acting in an official capacity in response to a specific request from the taxpayer and not from the taxpayer's failure to provide adequate or accurate information. SCC § 3.14-541(a)(1). The record in this case does not contain a specific request for information from Taxpayer, any written advice that was furnished to Taxpayer by or on behalf of the City or the

identity and capacity of the employee who gave advice to Taxpayer. Therefore SCC § 3.14-541(a)(1) is not applicable here.

Taxpayer also stated that if the assessment were upheld, the business would have to be closed. The purpose of the protest and hearing process is to determine whether the assessment was valid under the City code. *See,* SCC § 3.14-570(b)(1). Taxpayer's ability or inability to pay the assessment does not bear on the validity of the assessment and is not a question to be considered by the Hearing Office.

The City's assessment of privilege tax and interest against Taxpayer was proper.

Findings of Fact

1. Taxpayer operates a fitness facility within the City.
2. The City privilege tax is collected by the Department.
3. The City has adopted Appendix IV of the Model City Tax Code pursuant to which it performs supplementary local audits.
4. The Tax Collector conducted an audit assessment of Taxpayer for the period January 2007 through July 2010 and issued an assessment for additional city privilege tax of $70,188.72 and interest through June 2010 of $5,431.53.
5. No penalties were assessed.
6. Taxpayer timely protested the assessment stating:
    a. The Department administers the City privilege tax.
    b. Taxpayer obtained city and state privilege licenses from the Department.
    c. Taxpayer also obtained a city business license from the City.
    d. Taxpayer asked the Department how to fill out the privilege tax return.
    e. Taxpayer was verbally informed by a Department representative that the services provided by Taxpayer were not subject to the privilege tax.
    f. Taxpayer's privilege license was subsequently cancelled by the Department and Taxpayer no longer received the monthly reporting forms.
    g. Taxpayer believed that his business was not taxable in the City and that he was in compliance with the law.
    h. Had Taxpayer been informed that his services were taxable, Taxpayer would have complied.
7. The Department representative's identity, capacity with the Department or authority to act has not been disclosed.
8. The state does not tax Taxpayer's activities of operating a fitness center.
9. Taxpayer did not receive anything in writing from either the state or the city stating that Taxpayer's fitness facility was not subject to the City privilege tax.
10. Prior to the audit the City did not contact Taxpayer to inform Taxpayer that fitness centers were subject to the City privilege tax.

11. The City did not inform Taxpayer that he was not in compliance when Taxpayer renewed his city business license each year.

12. The Department does not routinely provide the City copies of privilege tax returns for business located in the City.

13. Taxpayer did not look at the City Tax Code or inquire at the City regarding the taxability of the operation of a fitness facility.

14. Taxpayer stated at the hearing that it did not have the ability to pay the assessment.

15. Taxpayer has not requested that he be allowed to make installment payments.

16. The Tax Collector testified that the option to make installment payments is available with the City.

Conclusions of Law

1. The City imposes a privilege tax on the activity of providing amusements that begins in the city or takes place entirely within the City, including health spas and fitness centers. SCC § 3.14-410(a)(2).

2. Taxpayer's fitness center business is subject to the City privilege tax under the amusement classification. SCC § 3.14-410(a)(2).

3. Taxpayers are presumed to know the law and its requirements, and a mistake as to such requirements is no excuse for failure to meet them. *Newman v. Fidelity Savings and Loan Association,* 14 Ariz. 354, 128 P. 53 (1912).

4. Equitable estoppel may lie against a taxing authority if, among other requirements, the taxing authority engaged in affirmative conduct inconsistent with a position it later adopted that is adverse to the taxpayer and the taxpayer actually and reasonably relied on the taxing authority's prior conduct. *Luther Construction Co., Inc., v. Arizona Department of Revenue,* 205 Ariz. 602, 604-605, 74 P.3d 276, 278-279 (2003).

5. Inconsistent conduct sufficient to invoke equitable estoppel must be absolute, unequivocal, bear some considerable degree of formalism under the circumstances and be taken by or have the approval of a person authorized to act in the area. *Valencia Energy Company, v. Arizona Department of Revenue,* 191 Ariz. 565, 577, 959 P.2d 1256, 1268 (1998).

6. The taxing authority may not generally be estopped due to the casual acts, advice, or instructions issued by non-supervisory personnel. *Valencia,* 191 Ariz. at 577, 959 P.2d at 1268.

7. To meet the requirement for an inconsistent act, an action by the government must bear some considerable degree of formalism. *Valencia,* 191 Ariz. at 577, 959 P.2d at 1268.

8. "It is rare that satisfactory evidence of an absolute, unequivocal, and formal state action will be found unless it is in writing." *Valencia,* 191 Ariz. at 577, 959 P.2d at 1268.

9. A taxpayer's reliance is not reasonable if the law clearly precludes the taxpayer's theory of nontaxability." *Valencia,* 191 Ariz. at 580, 959 P.2d at 1271.

10. SCC § 3.14-410(a)(2) clearly imposes the City's privilege tax on Taxpayer's business activity of operating a fitness facility.

11. The law clearly precludes any theory of nontaxability.

12. The City is not estopped from assessing Taxpayer for taxes due during the review period.

13. Interest and penalty may not be included in a assessment if the deficiency assessed is directly attributable to erroneous written advice furnished to the taxpayer by an employee of the City acting in an official capacity in response to a specific request from the taxpayer and not from the taxpayer's failure to provide adequate or accurate information. SCC § 3.14-541(a)(1).

14. The record in this case does not show that an employee of the City, or of the Department on behalf of the City, furnished written advice to Taxpayer that its activities were not subject to City privilege tax.

15. SCC § 3.14-541(a)(1) is not applicable in this case.

16. Under the administrative review process a taxpayer may contest the applicability or amount of the tax imposed on him. SCC § 3.14-570(b)(1).

17. Taxpayer's inability to pay is not relevant regarding the validity of the assessment.

18. The City may enter into an agreement with a taxpayer to allow the taxpayer to satisfy a liability for any tax imposed by this Chapter by means of installment payments. SCC § 3.14-596(a)

19. The City's assessment of privilege tax and interest against Taxpayer for the period January 2007 through July 2010 is proper.

Ruling

Taxpayer's protest of an assessment of privilege tax and interest made by the City of Surprise for the period January 2007 through July 2010 is denied.

The Tax Collector's Notice of Assessment to Taxpayer for the period January 2007 through July 2010 is upheld.

The parties have timely rights of appeal to the Arizona Tax Court pursuant to Model City Tax Code Section –575.

Sincerely,

Hearing Officer

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c: Revenue & Utility Billing Manager
Municipal Tax Hearing Office