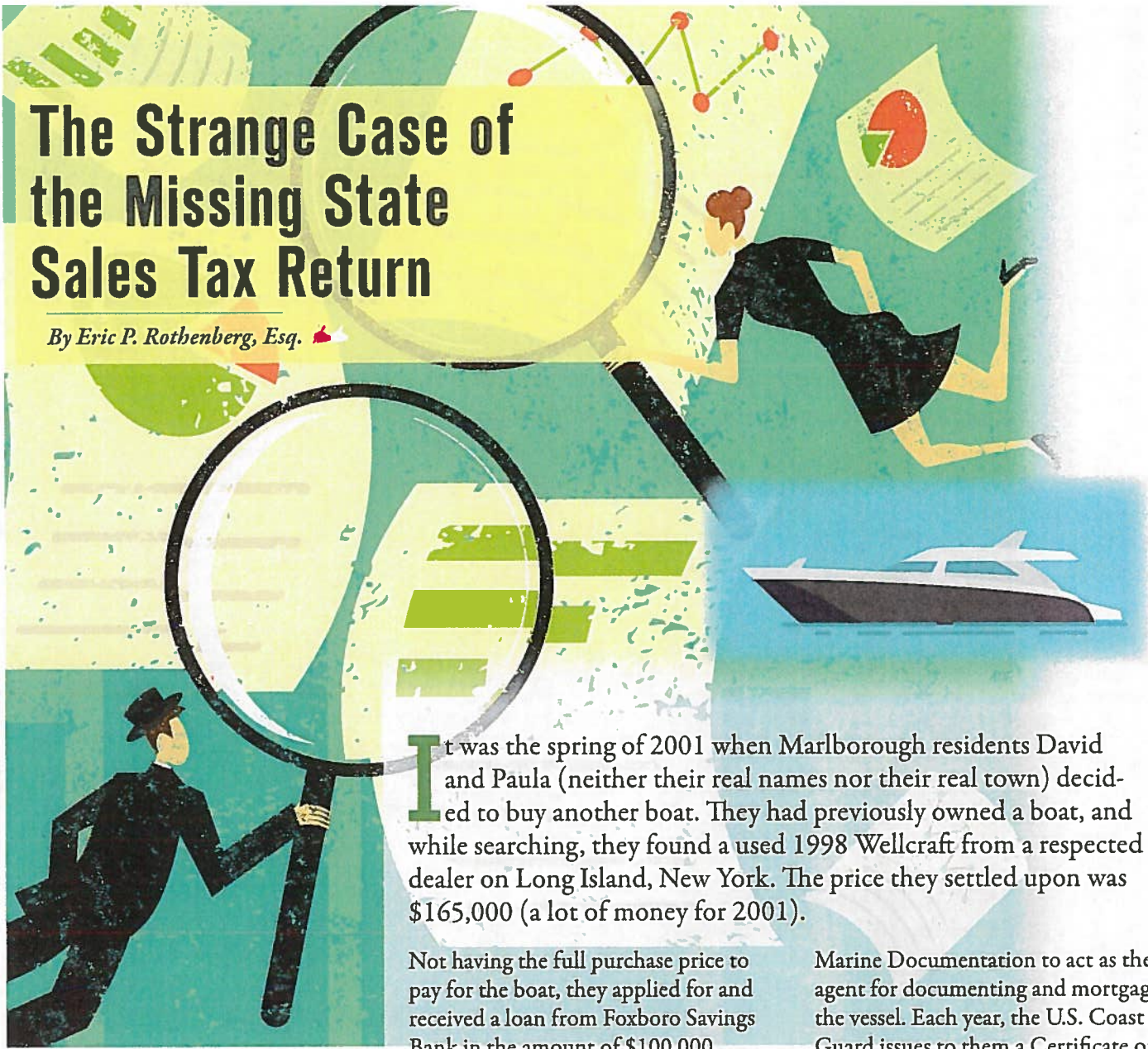


# The Strange Case of the Missing State Sales Tax Return

By Eric P. Rothenberg, Esq. 



**I**t was the spring of 2001 when Marlborough residents David and Paula (neither their real names nor their real town) decided to buy another boat. They had previously owned a boat, and while searching, they found a used 1998 Wellcraft from a respected dealer on Long Island, New York. The price they settled upon was \$165,000 (a lot of money for 2001).

Not having the full purchase price to pay for the boat, they applied for and received a loan from Foxboro Savings Bank in the amount of \$100,000.

As a condition of the loan, the bank said David and Paula had to provide proof they paid the sales tax to the Commonwealth of Massachusetts and provide them an affidavit that there were no liens on the boat.

Obtaining the title to a boat is not as simple as a car. It can be done through either the U.S. Coast Guard or through the state's Department of Motor Vehicles (DMV). Since this was a used boat that had been previously registered though the U.S. Coast Guard, it didn't make sense to change from that, as the Coast Guard's numbers were already on the boat. To facilitate purchasing the vessel, David and Paula hired Marine Documentation Service (not its real name). David and Paula had to sign an authorization document to permit

Marine Documentation to act as their agent for documenting and mortgaging the vessel. Each year, the U.S. Coast Guard issues to them a Certificate of Documentation, which is like a registration for a car and expires yearly.

The boat was shipped to David and Paula in May 2001, and they kept it at the marina where they lived in Marblehead (not where they really lived). Every year since 2001, they had to pay an excise tax to Marblehead based upon the value of the boat, just as they did on cars they had. In 2003, they paid off their loan to Foxboro Savings Bank. And things sailed along well for a decade.

That is until September of 2012. They received a letter from the Massachusetts Department of Revenue (DOR) informing them that the state determined they owed a sales or use tax on the boat for the period ending May 31, 2001, more than 11 years earlier. The letter said they would be assessed a tax of \$8,250,

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and with interest and penalties it now totaled over \$22,000. David and Paula knew they had paid the sales tax, as they vividly recalled the bank requiring proof it was paid *before* a loan would close. But that documentation was 11 years ago, and so they hoped they could show the DOR it was fully paid then. You might be saying to yourself, why did the DOR suddenly dredge up (pun intended) this issue from so long ago? Massachusetts is very aggressive with tax evaders (not to be confused with avoiders). The Commonwealth has, for decades now (I had such a case in the 1980s), sent tax collectors to marinas looking for *out-of-state* registrations of boats, especially by Massachusetts residents. They then look up to see if a sales or use tax return was filed and if not, assess the tax. In the case of David and Paula, they must have seen the Coast Guard registration, looked up the owner's name and address, and decided no sales tax was paid. And so they issued the Notice of Intent to Assess (NIA) to my clients, even though it was from 11 years earlier!

Upon receiving that notice in September 2012, my clients immediately tried to document the payment of the tax. They contacted the lender bank (now owned by another bank, and since the loan was paid in full in 2003, the bank had no records.). Their CPA, who prepared their income tax returns and the sales tax return, also didn't keep records that long. The bank where they kept their checking account also had no documents going back that far. They also contacted Marine Documentation Service, who documented the boat, and they had no records going back 12 years. They had very little to prove that they paid the tax besides their memory. *But (you might ask) isn't there a statute of limitations of going back that far?*

Yes, there are three basic statutes on assessing taxes. The general rule is no assessment may be made more than three years after the return is filed. The second rule says if the state is saying you left off more than 25% of your income, and then the three years becomes six years. BUT, (the third rule) if you don't file a return at all, then the statute never begins and the state (even the IRS) can assess you at ANY time. And here's the real Catch-22: If you did file, but so much time has gone by that you cannot prove you did file, then the state (and the IRS) can assert you did not file and now assess you, as in David and Paula's case. So much time has gone by that no one could reasonably now prove they did file. So, what could David and Paula do?

They protested the NIA with the tax examiner. In October 2012, they had a conference with the examiner and explained their facts to him and he listened, but determined that since they had no evidence to prove they paid the tax, they did not. In January 2014, more than a year later, they received a notice that their appeal was denied. They then received a Notice of Assessment dated February 12, 2014. Their only recourse at that time was to file an abatement



**It's best to advise your clients to keep the sales tax payment proof until after they no longer have the boat.**

request with Massachusetts (on Form CA-6) and so they did in May 2014. They were denied a hearing request in July 2015 because they had "no new evidence" so their abatement was denied. By November of 2015, the amount assessed was over \$25,000.

My clients independently filed a petition at the Appellate Tax Board (the equivalent at the state level of the U.S. Tax Court). Soon after that, they felt they needed to stop representing themselves and came to see me. My first reaction was outrage at the DOR. How could they assess my clients more than a decade after the return would have been due? Who keeps records that long? Being a tax lawyer for 40 years, I know the record keeping requirements for my clients and how long we can get records from the DOR, IRS, our banks, etc. It's just not that long. So what could I do for my clients?



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I knew my clients would make great witnesses at trial, so if I had nothing more than the few papers they brought to me, I would take a chance and put them on the stand to testify that they paid the tax. But I also thought, if I could muster up any type of circumstantial evidence to present, it would add credibility to their testimony. I asked my client if Marblehead collected excise taxes, which they did. So I asked them to ask the treasurer's office for a letter stating that my clients paid the excise tax on the boat every year since it was purchased. I asked them if they kept a copy of the affidavit the bank required of them to lend them the \$100,000, and they had that too. They also had a copy of the contract they signed with New England Documentation Service. I was able to get a letter from the marina in Marblehead stating that the boat was kept there every year. I also found the law on the Commonwealth of Massachusetts' own obligations for record keeping. It turns out



the state publishes these record retention requirements in the Massachusetts Statewide Records Retention Schedule (02-11 is the most recent one) for each state department. For sales tax reports it says: "Retain one year after audit or seven years, whichever is sooner." So even the DOR would not have records at the time they assessed David and Paula, if they had filed a sales tax return for their boat purchase. Obviously, it made little sense for the DOR to assess my clients more than seven years after such records were no longer retained by them for all taxpayers.

Since I was late to this dispute, I filed an appearance at the Appellate Tax Board and contacted the attorney for the Commonwealth to request that we get rid of this ridiculous case. He

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agreed that if I provided to him all the documentation I had gathered, and gave him an affidavit from my clients that they paid the tax, that he would recommend settling the case with no tax being due. It took three more months of trial date extensions for his supervisor to agree with me, but the case was settled in favor of David and Paula.

This case demonstrates the extent that Massachusetts will go to try to raise revenue, even where it places a terrible burden on the taxpayers. These taxpayers were assessed a tax that was paid more than 10 years prior to any contact from the DOR. Who can defend such old items? Most cannot. Luckily they could afford to hire me to stop the nonsense. But not every case turns out this well for the taxpayers. Even my own clients were willing to pay the DOR a significant portion of the tax bill until they came to see me. So what is the takeaway from this for your practice? First, keep in mind the state is willing to assert assessments many years after their own records are destroyed. If the amount at stake is high, it's best to advise your clients to keep the sales tax payment proof until *after* they no longer have the boat. Second, while auditors are pressured to assess taxes, taxpayers will do much better if they move on to the Appellate Tax Board to press their case. My experience is that the lawyers there are quite reasonable in resolving cases. And finally, the statute of limitations never runs out unless you file and can prove you filed. ♦


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