

Revenue Ruling

No. 01- 005, Issued August 21, 2001

Question: Should the Louisiana Department of Revenue reevaluate its interpretation of R.S. 47:305.1(A) following the Louisiana Supreme Court's ruling in *Showboat Star Partnership, Showboat of Louisiana, Inc., and Lake Ponchartrain Showboat Inc. versus Ralph Slaughter?*

Answer: On April 3, 2001, the Louisiana Supreme Court issued a decision on the application of R.S. 47:305.1(A) to purchases for vessels. This law exempts materials used in constructing vessels with at least 50-ton load displacement from sales tax. Information about the case and the department's analysis follow.

Name of Case: *Showboat Star Partnership, Showboat of Louisiana, Inc., and Lake Ponchartrain Showboat Inc. versus Ralph Slaughter, Secretary of the Department of Revenue and Taxation, State of Louisiana*

Court: Louisiana Supreme Court No. 00-C-1227

Date: April 3, 2001

Type of Tax: Sales and Use

Statute at Issue: R.S. 47:305.1(A)

"A. The tax imposed by R.S. 47:302(A)(1), 321(A)(1), and 331(A)(1) shall not apply to sales of materials, equipment, and machinery which enter into and become component parts of ships, vessels, or barges, including commercial fishing vessels, drilling ships, or drilling barges, of fifty tons load displacement and over, built in Louisiana nor to the gross proceeds from the sale of such ships, vessels, or barges when sold by the builder thereof."

Facts

The plaintiffs owned and operated a riverboat gaming vessel in New Orleans, Louisiana. On August 3, 1993, Department of Revenue employees notified the plaintiffs that the exemption allowed under R.S. 47:305.1(A) applied to purchases of all original and replacement equipment placed on the vessel for serving their patrons. This included slot machines, gaming tables, seating, barware, cookware, cabinets, currency conveyor systems, surveillance equipment, illuminated signs, and any other expendable tangible personal property used to outfit the vessel for gaming. In January 1994, the department reversed its position limiting the exemption to materials used in the construction of the vessel. The department then audited the owners and issued a substantial assessment because sales tax had not been paid on purchases of slot machines, roulette tables, cabinets, currency

conveyor systems, surveillance equipment, illuminated signs, etc. in accordance with the department's original advice. The taxpayers paid \$278,628.12 under protest and filed suit against the department for recovery.

Issues Before the Louisiana Supreme Court

1. Does gaming equipment installed on vessels qualify for exemption under R.S. 47:305.1(A) as "component parts" of vessels?
2. Can taxpayers assert detrimental reliance or judicial estoppel when they have claimed a tax exemption based upon the department's original statement that the exemption was valid, if the department changes its position after the purchase and disallows the exemption?

Decision of the Court

1. The Supreme Court agreed with the lower courts that slot machines, the cabinets on which the slot machines were placed, the roulette wheels, etc. were not component parts of the gaming vessels. Removing these items could be done by simply unplugging and unbolting them and would not damage the vessel or the equipment. Therefore, the gaming devices had not become permanently installed components of the vessel.
2. The court also disagreed with the taxpayers' "societal expectation" argument that the machines were part of the vessel because one would reasonably expect to see gaming equipment on a gaming riverboat. The court ruled that the appropriate question is whether society expects to see gaming equipment when it enters any vessel, not if it expects to see gaming equipment when it enters a gaming riverboat. The court concluded that in the absence of specific contractual provisions to the contrary, the average prudent business entity does not expect gaming equipment to be permanently attached when buying a vessel. However, the court remanded the case to the trial court to determine if the signs and surveillance systems on the vessel were component parts.
3. The Supreme Court reviewed the four-factor test cited by the Louisiana First Circuit Court of Appeal in determining whether the legal and jurisprudential requirements for an "equitable estoppel or detrimental reliance" defense against a government agency are met:
 - the receipt of unequivocal advice from an unusually authoritative source;
 - reasonable reliance on that advice by the person receiving it;
 - extreme harm to the person receiving the advice from having relied on that advice; and

- gross injustice to the person relying on the advice in the absence of judicial estoppel.

The trial court, the Court of Appeal, and the Louisiana Supreme Court all ruled that taxes were due on the disputed purchases. They agreed that paying the sales tax because the department reversed its original position was not a detriment to the taxpayers. However, the two lower courts also concluded that the interest payable on the tax did harm the taxpayers, the tax and interest are always due (or not due) together, and one could not be collected without the other. Since the two courts saw the interest as harm to the taxpayer, they ordered the refund to the taxpayer of the tax and the interest that had been remitted under protest.

The Supreme Court obtained a different result regarding the plaintiff's detrimental reliance in the *Showboat Star* case. It agreed with the lower courts that payment of the sales tax, due to the department's change of position, was not detrimental. However, it disagreed with the lower courts on whether payment of the interest created an extreme harm to the taxpayers. The Louisiana Supreme Court adopted the reasoning of the Arizona Supreme Court in *Valencia Energy Co. v. Arizona Dept. of Revenue* [191 Ariz. 565, 959 P.2d 1256 (1998)]. The Arizona Supreme Court stated at 1268-69:

“No detriment is incurred when the party's only injury is that it must pay taxes legitimately owed under the correct interpretation of the law. Nor will liability for non-punitive interest on the tax legitimately due constitute detrimental reliance. Non-punitive interest is, after all, nothing more than compensation for the use of money. The taxpayer had the benefit of using the funds before paying the tax claim and, in the legal sense, suffers no loss by reason of paying interest on the money it retained in its possession.”

The High Court concluded that the plaintiffs failed to prove a detriment from their reliance on the department's advice. Since the issue of detrimental reliance and judicial estoppel were inapplicable, it chose to not rule, or to pretermite, on the department's argument that the doctrine of detrimental reliance cannot be invoked against the government. No extreme harm had come to the taxpayers from the department's change of position concerning the taxability of the gaming equipment and other property at issue.

Department's Position

The department acquiesces with the Louisiana Supreme Court. The exemption provided by R.S. 47:305.1(A) will be allowed for:

1. The sale of a vessel of 50 tons or more load displacement when sold by the builder. The exemption is limited to the vessel structure and equipment that is permanently installed to it. If a contract for the sale or construction of a vessel

includes the structure and additional items that are not component parts of the vessel, sales or use tax is due on the portion attributable to the property that does not qualify as component parts.

2. Purchases, by the vessel owner, of movable property that will be incorporated into and become an original component of a vessel of 50 tons or more load displacement.

Component parts of a vessel are items attached in such a way that removing them would damage the items or the vessel from which they are removed. This does not include property installed on a vessel to modify it for a specific function (e.g., fishing nets aboard a fishing vessel). Also, equipment necessary to meet government safety or navigation standards (e.g., life jackets, fire extinguishers, life boats, etc.) will not be exempt. Unless equipment is permanently installed onto the vessel structure as discussed by the Louisiana Supreme Court in *Showboat Star*, it will not be considered a component part eligible for exemption under R.S.

47:305.1(A). The Court determined that the bolting of gaming machines to keep them from tilting over when vessels are moving does not constitute the permanent installation of that property as components of vessels.

Also, the exemption under R.S. 47:305.1(A) only applies to components added during the construction of vessels. Replacement components and vessel repair services are not eligible for exemption under the statute. This issue was decided by Louisiana courts in *Compass Offshore, Inc. v. McNamara*, (App. 4 Cir. 1988, 526 So.2d 425), *Canal Barge Co. Inc. v. McNamara*, App. 4 Cir. 1987, 511 So.2d 1196), and *McNamara v. Central Marine Service, Inc.* (Sup.1987, 507 So.2d 207).

Purchases of original property to be placed aboard eligible vessels must be considered individually to determine whether they qualify as components are eligible for exemption under R.S. 47:305.1(A). Buyers can seek private letter rulings from the department if, after reviewing the statutes, rules, jurisprudence, and declaratory rulings on the matter, they are still uncertain about the exemption eligibility of their purchases.

When Is Department Advice Binding and When Is It Not?

In *Showboat Star*, the Supreme Court assessed the department's change of position subsequent to providing informal advice to the litigating taxpayers. Fortunately, such situations are rare. Through formal and informal communication with its employees, the department strives to provide to taxpayers with information that has a sound basis in law, formal administrative rule, and jurisprudence.

On February 20, 2001, the Department of Revenue promulgated Louisiana Administrative Code 61:III.101, which describes the agency's procedures for providing tax advice or other information.

1. "Rules" are promulgated through the Louisiana Administrative Procedure Act (R.S. 49:950 et seq.). R.S. 47:1511 authorizes the Secretary of Revenue to promulgate, make, and publish reasonable rules and regulations related to the taxes that the department administers. The rules must be consistent with the Constitution and laws of the state. They have the force and effect of law.
2. "Private Letter Rulings" (PLR) are declaratory rulings defined within LAC 61:III.101.C.2.a. A "PLR" provides guidance to a specific taxpayer at the taxpayer's request. It is a written statement that applies the principles of law to a specific set of facts or tax situation. It does not have the force and effect of law, and is not binding on the person who requested it or on any other taxpayer. The PLR is binding on the department for the taxpayer to whom the PLR is addressed provided the facts presented were truthful and complete and the transaction was carried out as described. It retains authority of the department's position unless a subsequent declaratory ruling, rule, court case, or statute supersedes it.
3. A "Revenue Ruling" is a declaratory ruling from the department written to provide guidance to the public and Department of Revenue employees. It is issued under Section 61:III.101.C.2.b of the Louisiana Administrative Code and applies principles of law to a specific set of facts. A Revenue Ruling does not have the force and effect of law and is not binding on the public. It is a statement of the department's position and is binding on the department until superseded or modified by a subsequent change in statute, regulation, declaratory ruling, or court decision. Temporary Revenue Rulings may be released on emerging issues when a quick response is critical. If the final Revenue Ruling produces a result different from the Temporary Revenue Ruling, the department will honor the one more favorable to the taxpayer for transactions that occurred after the Temporary Ruling was issued and before the final Revenue Ruling.
4. A "Statement of Acquiescence or Nonacquiescence" (SA/SNA) is another type of declaratory ruling intended to provide guidance to the public and to department employees. An "SA/SNA" is a written statement to announce the department's acceptance or rejection of a specific court or administrative decision. If a decision covers several disputed issues, the SA/SNA may apply to one or more issues, as specified. An SA/SNA is not binding on the public,

but is binding on the department unless superseded by a later SA/SNA, declaratory ruling, rule, statute, or court case.

5. A “Revenue Information Bulletin” (RIB) is an informal statement issued to publicize general information needed to comply with the laws administered by the department. A “RIB” will typically include information about filing deadlines, department office hours, website features, and statistical information. It will not be used for declaratory rulings, interpretations of law, or procedural guidance. A RIB does not have the force and effect of law and is not binding on the public or the department.

6. The department will also provide “informal advice” to taxpayers. Informal advice may be provided to an individual taxpayer directly in person or by telephone, through e-mail, or in a letter. It can also be provided to the general public through newsletters, pamphlets, and publications. Although the department strives to assure the quality of informal advice it provides, informal advice does not have the force of law and is not binding on the department, the public, or the person who asked for the advice. Informal advice will not affect an audit.