



The *Equifax* Fallout Begins

Mississippi's Proposed Regulation to Codify a 300% Sales Tax Penalty, Alter Legal Standard for Imposition of 50% Penalty

The Mississippi Department of Revenue (the "Department") recently proposed [a regulatory amendment](#) that would reflect new statutory sales tax penalty rates, which in some cases would levy sanctions at a 300% rate! In 2012, the Mississippi Legislature amended Mississippi Code section 27-65-39 to provide for fixed 10% and 50% penalty rates as opposed to the since-rescinded 10%, 15%, 25% and 50% rates still reflected in the Department's regulations. The Department now proposes to revise Regulation 35.IV.01.02 to reflect the new rates, as well as an alarming "trust fund monies" penalty, as follows:

- for negligent failure to file or timely pay without the intent to defraud—10%
- for intentional disregard of the law or intent to defraud—50%
- for failure to remit tax collected from customers—300% (*in addition* to the 10% and 50% penalties)

The proposed regulations raise several important questions that taxpayers should consider before the rules are finalized. This is especially important in light of the recent holding of the Mississippi Supreme Court in [Equifax, Inc. v. Mississippi State Tax Commission](#) that courts are seemingly powerless now to review the Department's decision to impose those sanctions. (See our prior Client Alerts discussing this case [here](#), regarding the Mississippi Supreme Court's denial of rehearing and [here](#), regarding the decision.)

What exactly does "intentional disregard" now mean? In the proposed amendments, the Department stated that the 50% penalty "will be used in cases where the taxpayer continually files and/or pays late, *or where the taxpayer continues to disregard instruction given through an audit and is subsequently audited and found to owe on the same issue.*" However, this new standard appears to conflict with the underlying statute, Section 27-65-39, which states that the 50% penalty may be applied in instances of "intentional disregard of the provisions of this chapter *or authorized rules and regulations promulgated under the provisions of this chapter.*"

Noticeably absent from that statute is any reference to failure to follow an auditor's advice or instructions, which often is oral, lacks sufficiently detailed documentation and may not necessarily reflect the Department's officially-adopted formal policy on an issue. By enacting standards governing when the Department could use such a big "stick," the Mississippi Legislature intended that the Department put the public on notice of its position by adhering to the formal rule making process of the Administrative Procedures Act; by substituting an auditor's informal and unofficial opinion in

place of formal rules and regulations, the proposed regulation would potentially circumvent that legislative requirement.

Taxpayers may recall that earlier this year the Mississippi Legislature amended Section 27-65-37 to provide that if a sales tax taxpayer is being audited following an earlier "no-change" audit, the Department may be estopped from holding the taxpayer responsible for any tax found due in that second audit. See [Miss. H.B. 892 \(2013\)](#). This new regulation appears to be the Department's reaction to that new law.

Are these penalties now mandatory? With respect to the 10% penalty, the regulation closely tracks the new statutory language of Section 27-65-39, albeit with one potentially important exception. Whereas the statute provides that the penalty "may" be levied, the regulation states that the Department "will" assess the penalty. If this distinction was intentional and reflects a new policy that penalties will automatically be imposed in all cases, a consequence may be that it could make it more difficult for both parties to informally resolve future audits.

Does Mississippi still maintain the concept of "trust fund monies"? The 300% "trust fund monies" penalty is an entirely new addition to the regulation, but is supported by language in Section 27-65-31 which provides that the Department "*may*" assess a penalty of up to "three times the amount of the taxes due." The regulation adopts the "will" standard as it did with the 10% penalty noted above, again raising the issue of whether the penalty will henceforth be treated as mandatory rather than permissive.

The 300% trust fund monies penalty is also particularly interesting in light of the Mississippi Supreme Court's recent holding in [Mobility Medical, Inc. v. Mississippi State Tax Commission](#). (See our prior Client Alert discussing this case [here](#)). In that case, the Department argued and the Court agreed that Mississippi's sales tax is not really a pass-through tax. The Court further held that a seller may or may not - at his sole discretion - add the tax to the sales price. This conclusion is difficult to square with the plain language of Section 27-65-31, which mandates sellers add the tax to the sale price and explicitly renders failure to do so a criminal offense. It is also directly contrary to several Mississippi Supreme Court decisions dating back to the earliest days of Mississippi's sales tax construing the nature of that new system and upholding the mandatory requirement to pass the tax along to the customer.

One of the more important questions resulting from the *Mobility Medical* decision is what consequences it holds for the entire "trust fund monies" concept, upon which this 300% penalty rests. Even though the Supreme Court never discussed (or even acknowledged) Section 27-65-31, is that statute still operative in light of its holding? Because a seller is not required by any law to collect it from the customer and may even negotiate to absorb the tax directly, is that collection now just a private contractual matter between the seller and buyer? Because the Supreme Court clearly stated that a seller is the only taxpayer and is solely responsible for this tax, presumably that seller is no longer the collection agent on behalf of the State, as the Supreme Court acknowledged they were as early as 1940. Consequently, the state's claim to hold a seller legally responsible for funds purportedly held in trust for a party that is no longer its principal appears to be without any principled foundation.

From an immediate and more practical standpoint, however, taxpayers should be concerned that the Department on audit will "deem" sales taxes to have been collected even if none were separately stated on an invoice. Indeed, it is routine audit practice for the Department to calculate the tax base "net of" sales taxes "deemed" collected; therefore, it is possible that an auditor will use this "net of" sales tax as a basis for threatening to assess the 300% penalty.

Speak now or forever hold your peace. A public hearing on this and several other proposed regulatory changes will be held in Jackson, Mississippi on **Wednesday, December 11, 2013, at 3:30 p.m.** Taxpayers are encouraged to participate in this hearing and to raise these and other issues regarding this proposed regulation.

— [John F. Fletcher](#) and [Justin B. Stone](#)

Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, contact:

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