IN THE SUPREME COURT OF OHIO

PROGRESSIVE PLASTICS, INC.,	)	Case No. 2011-1793
	)	
Appellant,	)	
v.	)	
	)	Appeal From the Ohio Board of Tax Appeals
RICHARD A. LEVIN [JOSEPH W. TESTA],	)	
Tax Commissioner of Ohio,	)	Case No. 2008-A-241
	)	
Appellee.	)	

REPLY BRIEF OF APPELLANT PROGRESSIVE PLASTICS, INC.

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I. INTRODUCTION.

This case is about the Tax Commissioner and Department of Taxation unilaterally and without justification imposing tax on an Ohio small business. The record in this case, and the Tax Commissioner's arguments on appeal, demonstrate that the Tax Commissioner believes that he has the authority to dictate the accounting method used by a taxpayer to calculate the value of its inventory. Not coincidentally, the accounting method mandated by the Tax Commissioner is the method which forces the taxpayer to incur the highest amount of tax possible. The Tax Commissioner has ignored this Court's ruling that a taxpayer can use whatever generally accepted accounting principal it chooses to value its inventory; the Tax Commissioner has ignored the clear mandate of R.C. § 5711.18 which provides that the value calculated by the taxpayer must be taken as the true value of the inventory for tax purposes unless the Tax Commissioner makes a "finding" that another value is the true value; and, finally, the Tax Commissioner has ignored the clear mandate of R.C. § 5711.21(A) that such "finding" must be supported by evidence pertinent to the taxpayer.

At the end of the day, the case is not about taxation. Rather, this case is about the Tax Commissioner declaring that he, not this Court nor the General Assembly, gets to decide how tax is assessed to Ohio taxpayers. The Tax Commissioner apparently believes that he is above the law: he tells taxpayers what tax they will pay and then shifts the burden to the taxpayer to prove him wrong, even when the law clearly provides otherwise. And when a taxpayer such as PPI exercises its right to seek the review of this Court, the Tax Commissioner files a Brief criticizing the taxpayer for wasting judicial resources.

The taxpayer argues that the Tax Commissioner cannot assess additional tax under R.C. § 5711.18 because the Tax Commissioner did not make a "finding" that the taxpayer's value of its inventory was not the true value of the same. The Tax Commissioner argues that it made such a finding, that finding being that the taxpayer utilized the LIFO method of accounting. But the use of a particular accounting method cannot be the sole basis for an increase of tax liability, as this Court has held that an Ohio taxpayer can use whatever generally accepted accounting principal it chooses. *R.H. Macy Co. v. Schneider* (1964), 176 Ohio St. 94, 96. So if the only "finding" made was the taxpayer's use of a particular accounting method, that "finding" cannot satisfy the Tax Commissioner's burden under R.C. §§ 5711.18 and 5711.21(A).

II. LAW AND ARGUMENT.

REPLY IN SUPPORT OF PROPOSITION OF LAW NO. 1

IN ORDER TO ISSUE AN ASSESSMENT INCREASING THE BOOK VALUE OF A TAXPAYER'S INVENTORY FOR THE PURPOSES OF PERSONAL PROPERTY TAX, THE BURDEN IS UPON THE TAX COMMISSIONER TO MAKE A FINDING, SUPPORTED BY EVIDENCE PERTINENT TO THE TAXPAYER, THAT THE BOOK VALUE OF THE INVENTORY AS REPORTED BY THE TAXPAYER IS NOT THE TRUE VALUE OF THAT INVENTORY.

R.C. § 5711.18 provides that a taxpayer's book value of inventory "shall be taken as the true value of such property, unless the assessor finds such depreciated book value is greater or less than the true value of such property in money." This has been held to mean that the book value as reported by the taxpayer on its personal property tax return is the *prima facia* true value of the inventory. *PPG Industries v. Kosydar* (1981), 65 Ohio St.2d 80, 82; *EX-cell O Corp. v. Kosydar* (3rd. Dist. 1976), 49 Ohio App.2d 131, 140, rev'd on other grounds by *General American Transp. Corp. v. Limbach* (1984), 15 Ohio St.3d 302, 304. R.C. § 5711.21(A) provides that in making a finding under R.C. § 5711.18, the Tax Commissioner must be guided by "the statements contained in the taxpayer's return and such other rules and evidence as will enable the assessor to arrive at such true value."

In his Brief, the Tax Commissioner argues that he "made comprehensive, independent findings at multiple stages of the audit and assessment regarding the valuation of Progressive Plastics' property." Appellee Br. at 9. However, after making this statement, the Tax Commissioner fails to explain exactly what his "findings" were. That is because the only "finding" made by the Tax Commissioner was that PPI uses the LIFO method of accounting. This is evidenced in no fewer than five (5) portions of the record in this case. First, the Department of Taxation's Preliminary Proposed Audit Results, submitted May 12, 2006, focuses entirely on the LIFO method of accounting and categorically concludes such method is inappropriate, without any mention of any facts or evidence specific to PPI. Record at 3, Statutory Transcript at 449-450. Next, in the Tax Commissioner's Final Determination, the Tax Commissioner simply states that "the Ohio Board of Tax Appeals and the Ohio Supreme Court have ruled that FIFO is the best method for valuing inventory . . ." (citing cases)[1] Record at 3, Statutory Transcript at 1-2. Again, there is nothing in the Final Determination which pertains to PPI specifically, or why the LIFO method is inappropriate for PPI in particular. Third, in a deposition conducted as part of the original 2002-2003 audit, the Audit Agent, Douglas Basista, testified that PPI's use of the LIFO method was the sole basis for

[1]Neither the BTA nor this Court has ever held that FIFO is the "best method" for valuing inventory. The cases cited by the Tax Commissioner in his Final Determination all held that FIFO better valued that particular taxpayer's inventory, based on evidence particular to the taxpayer. For a detailed analysis of these cases, see Appellant's Merit Brief at 11-15.

determining that PPI had undervalued its inventory.[2] Supp. at 41-44. In his Brief, the Tax Commissioner argues that the FIFO method "more nearly resembles Progressive Plastics' actual inventory [sic]." Appellee Br. at 10. However, Mr. Basista testified that the determination was made that PPI could not use the LIFO method without any consideration of PPI"s actual inventory practices. Supp. at 44. Fourth, in an in-house memorandum from Agent Basista to Ms. Cynthia Losey of the Department of Taxation (the date of which is redated for some reason in the Statutory Transcript), Mr. Basista acknowledges PPI's arguments as to why LIFO is appropriate, but concludes (again as a matter of law) that taxpayers cannot use the LIFO method, without any examination of the facts and circumstances particular to PPI. Statutory Transcript at 480. Finally, in another in-house communication between Elizabeth Karolyi and Joseph Catey, both of the Department of Taxation, Mr. Catey advised Ms. Karolyi not to grant PPI's requested stay of the audit (discussed *infra*), because the LIFO issue was "well settled" and a "legal issue." Statutory Transcript at 444-445. In sum, the Tax Commissioner's finding was merely that, as a matter of law, PPI could not use the LIFO method of accounting.[3]

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[2]In referencing Mr. Basista's testimony, PPI does not concede that information from the 2002-2003 audit is appropriate to consider in this case. The reference to Mr. Basista's deposition is merely to point out that the Tax Commissioner, through his agent Mr. Basista, has admitted that the accounting method chosen by PPI was the only basis for assessing additional tax.

[3]In this Brief, the Tax Commissioner attempts to fabricate a factual finding by making reference to a memorandum from the taxpayer to its counsel which suggests that PPI's actual inventory practices are consistent with the FIFO method. Appellee Br. at 17. However, a review of the Final Determination in this case demonstrates that the Tax Commissioner did not rely on this fleeting statement (or even reverence it) in assessing PPI. Nor did the Tax Commissioner make this argument in its briefs filed with the BTA and the BTA certainly did not rely on this statement when issuing its Decision and Order. Furthermore, this statement (which was made in a memorandum the subject of which being how the LIFO reserves were calculated) is at odds with the affidavit of PPI's Chief Operating Officer Rome P. Busa, Jr. as well as the arguments raised by the Taxpayer in their Petition for Reassessment and in every document filed by the Taxpayer thereafter.

After arguing that he made a "finding" that PPI could not use the LIFO method of accounting as a matter of law, the Tax Commissioner argues that his "findings" are presumed to be correct absent a showing that the same are "clearly unreasonable or unlawful." Appellee Br. at 11. The Tax Commissioner then cites a number of decisions from this Court he claims supports the proposition that his "findings" are presumed to be correct. *Id.* The problem with the Tax Commissioner's argument in this regard is that the cases cited deal with <u>factual</u> findings of the Tax Commissioner, not conclusions of law. For example, in *Hatchadorian v. Lindley* (1986), 21 Ohio St.3d 66, the issue was whether or not certain items of personal property were "used in business" such that the same were subject to personal property taxation. 21 Ohio St.3d at 68. This Court upheld the Tax Commissioner's <u>factual</u> finding that the "property is not capable of use in the taxpayer's business . . .." *Id.* at 69. In *Shiloh Automotive, Inc. v. Levin* (2008), 117 Ohio St.3d 4, the issue was whether or not the purchase of certain assets was an "arms length transaction" (a factual inquiry) such that the purchase price should be taken as the taxable value of the property. 117 Ohio St.3d at ¶ 17. In *Columbia Gas Transmission Corp. v. Levin* (2008), 117 Ohio St.3d 122, the issue was whether a company was properly classified as a "pipeline company" or "natural gas company" for the purposes of R.C. § 5727.01. 117 Ohio St.3d at ¶ 12. In each of those cases, the Tax Commissioner made a factual finding, supported by evidence contained in the record, and it was that <u>factual finding</u> that this Court held to be presumptively valid. None of those cases involve an erroneous conclusion of law, <u>e.g.</u>, that a taxpayer cannot use a certain accounting method to value its inventory. The Tax Commissioner also erroneously cites *Higbee Co. v. Evatt* (1942), 140 Ohio St. 325, for the proposition that the Tax Commissioner's findings are presumed to be valid "regardless of whether the Tax Commissioner has affirmatively produced evidence in support of his findings." However, the *Higbee* decision dealt with a taxpayer's claim for a tax deduction. 140 Ohio St. at 332. This Court held that "the burden is upon a taxpayer *to prove his right to a deduction* and he is not entitled to the full amount of deduction claimed merely because no evidence is induced contra his claim." *Id.* (emphasis added). But this case does not involve a deduction claimed by PPI, and R.C. § 5701.18, and the case law interpreting the same, are clear that the taxpayer's calculated value of inventory "shall be taken as the true value" unless the taxpayer's value is rebutted by the Tax Commissioner. Thus, the rule announced by this Court in *Higbee* has no bearing on this case.

The Tax Commissioner then proceeds to argue that he was qualified to make a legal determination that PPI could not use the LIFO method because he is a "tax expert." Appellee Br. at 10. Thus, the Appellee's Brief goes, "in the Tax Commissioner's expert judgment, Progressive Plastics had underreported the value of its manufacturing inventory in 2004 and 2005." But the Revised Code does not allow the Tax Commissioner to merely assert his "expert opinion" when making a finding under R.C. § 5711.18; rather, R.C. § 5711.21(A) provides that the Tax Commissioner must rely on "rules and evidence" to support his findings. If the Tax Commissioner were entitled to rely on his "expert opinion" in assessing additional tax to Ohio taxpayers in lieu of considering rules and evidence, R.C. § 5711.21(A) would be rendered meaningless.

In the end, we have a case where the only "finding" made by the Tax Commissioner was a legal conclusion that PPI cannot use the LIFO method of accounting. But this Court has held that a taxpayer can use whatever generally accepted accounting principal it chooses in valuing its inventory. PPI's choice of accounting method simply cannot be the basis for an assessment of tax.

REPLY IN SUPPORT OF PROPOSITION OF LAW NO. 2

EACH TAX YEAR STANDS ON ITS OWN, SUCH THAT THE TAX COMMISSIONER CANNOT RELY ON INFORMATION OBTAINED IN A PRIOR YEAR'S AUDIT TO ASSESS ADDITIONAL TAX FOR A SUBSEQUENT YEAR.

PPI has argued that the Tax Commissioner cannot rely on information from the 2002-2003 audit in assessing tax for 2004-2005. The Tax Commissioner disagrees. However, the Tax Commissioner fails to cite even a single case which holds that he can rely on information obtained through a prior year's audit. Conversely, PPI has pointed out that it has been universally held that "each taxable year stands on its own and must be separately considered." *United States v. Skelly Oil Company* (1969), 24 U.S. 678, 684. Taken to its logical extreme, the Tax Commissioner's argument would allow him to conduct a single audit (say in 2002) and use that audit to assess tax for subsequent years, for example 2003, 2004, 2005, 2006, 2007 and 2008. Of course, that is <u>exactly what the Tax Commissioner did in this case</u>, as PPI has been assessed tax not only for the initial tax period (2002-2003) but for each of the following years thereafter until the personal property tax was phased out after 2008. While only the years 2004 and 2005 are at issue in this case, the Tax Commissioner is attempting to create a dangerous precedent that he will subsequently use to support his assessment against this particular taxpayer in the appeals to come.

The Tax Commissioner argues that *Olmsted Falls Bd. of Education v. Cuyahoga Cty. Board of Revision* (2009), 122 Ohio St.3d 134, cited by PPI in its Merit Brief, is inapplicable in this case. The Tax Commissioner argues that *Olmsted Falls* and its progeny merely stand for the proposition that the Tax Commissioner may not carry forward a "determination of value" from one year to the next. This is so because the determination of value is the "ultimate issue." Appellee Br. at 19. But the Tax Commissioner ignores that the underlying reasoning in the *Olmsted Falls* decision is that each tax year constitutes a new cause of action or new claim. 122 Ohio St.3d at 137. And the Tax Commissioner has failed to address the decision (cited by PPI) in *Fogg-Akron Associates, L.P. v. Summit County Board of Revision* (2009), 124 Ohio St.3d 112, wherein this Court held that a taxpayer could not argue that a value of property from one year must be the value of the property for a subsequent year absent a showing of a change in circumstances. The rationale in *Olmsted Falls* and *Fogg-Akron* is that each taxable year stands on its own and is a separate cause of action and separate claim.

The Tax Commissioner next argues that R.C. § 5711.26 actually <u>requires</u> him to consider information from past audits to the extent that Section charges him to utilize "all facts or information he possesses" in making a final assessment of tax liability for personal property. Appellee Br. at 20. The Tax Commissioner's reliance on R.C. § 5711.26 is misplaced, however, by virtue of the fact that Section repeatedly makes reference to a final assessment in connection <u>with a specific tax year</u>.

Admittedly, the issue of whether the Tax Commissioner can view prior year information in connection with a personal property tax audit is a case of first impression with this Court. However, this Court has consistently held that prior year's information is irrelevant in connection with real property tax cases. There is no logical reason why the Tax Commissioner should be precluded from using prior year's information in connection with the assessment of real property tax, but be permitted to do so in connection with the assessment of personal property tax. And the language of R.C. § 5711.26, insofar as it repeatedly refers to the "preliminary or amended assessment . . . for such [tax] year," makes it clear that the Tax Commissioner cannot do what he has done in this case, namely rely on prior year audit findings to assess tax in a subsequent year.

The Tax Commissioner argues that he needed to rely on information from the 2003 audit to the extent PPI failed to provide information as part of the 2004-2005 audit. Appellee Br. at 6-7. However, PPI certainly did not refuse to provide information to the Tax Commissioner. What occurred here is that PPI had made a reasonable request to stay the 2004-2005 audit to the extent the 2002-2003 audit was still ongoing. Statutory Transcript at 454-456. PPI never received a response to its request to stay the audit. Statutory Transcript at 465-467. Instead, PPI received a Notice of Assessment. *Id.* The Department of Taxation continued to refuse to stay the 2004-2005 audit until the conclusion of the 2002-2003 audit, and, accordingly, on August 31, 2006 PPI provided approximately 260 pages of documentation to the Department of Taxation. Statutory Transcript at 6-7. The Tax Commissioner does not dispute that those documents are contained in the record of this case. Appellee Br. at 7, fn 3. It should be pointed out that the documents requested and received by the Department of Taxation have nothing to do with the issue of whether or not the inventory was properly valued under the LIFO method of accounting. Rather, the documents were only relevant to the extent it was <u>presumed</u> by Tax Commissioner that PPI should have used the FIFO method. That is, the documents were only necessary so that the Department of Taxation could <u>recalculate</u> the value of PPI's inventory under the FIFO method. Appellee Br. at 21 ("in order to come up with the true value in dollars and cents of Progressive Plastics' taxable inventory [under the FIFO method], the Tax Commissioner requested Progressive Plastics "inventory schedules," "chart of accounts," "fixed asset records" and other documents that would enable him to derive the true values that should have been reported on the tax returns.") Thus, the (alleged) failure to provide documents was not the reason <u>why</u> the Tax Commissioner determined that the FIFO method was appropriate (or that LIFO was inappropriate, for that matter); rather, the documents were requested to allow the Tax

Commissioner to recalculate the listed value of the inventory, having declared that PPI must use the FIFO method.

<u>REPLY AND SUPPORT OF PROPOSITION OF LAW NO. 3</u>

THE DOCTRINE OF COLLATERAL ESTOPPEL DOES NOT APPLY IN TAX CASES TO PREVENT A TAXPAYER FROM ARGUING IN SUBSEQUENT YEARS THAT ITS ACCOUNTING METHOD YIELDS THE TRUE VALUE OF ITS INVENTORY.

The Tax Commissioner concedes that collateral estoppel is not applicable in this case. Appellee Br. at 24. Abandoning the collateral estoppel argument (which, as the Tax Commissioner confirms in his Brief, was never raised in the first place) the Tax Commissioner argues that *stare decisis* is the appropriate standard.

The doctrine of *stare decisis* requires Courts to "stand by things decided, and not to disturb settled points." *Allstate Ins. Co. v. Campbell* (2010), 128 Ohio St.3d 186, 202. The doctrine "is designed to provide continuity and predictability in our legal system. [Courts] adhere to *stare decisis* as a means of thwarting the arbitrary administration of justice as well as providing a clear rule of law by which the citizenry can organize their affairs." *Westfield Ins. Co. v. Galatis* (2003), 100 Ohio St.3d 216, 226. As stated by the United States Supreme Court, "*stare decisis* permits society to presume that bedrock principals are founded in the law rather than in the proclivities of individuals, and thereby contributes to the integrity of our constitutional system of government, both in appearance and in fact." *Pollock v. Farmers' Loan & Trust Co.* (1895), 157 U.S. 429, 652.

Stare decisis is not appropriate in this case for several reasons. First, this Court has not ruled on any of the issues presented and certainly the Tax Commissioner is not arguing that *stare decisis* prevents this Court from overturning the decision of the Board of Tax Appeals. Moreover, *stare* *decisis* has no application in this case because no tribunal had ever determined that the Tax Commissioner had properly assessed tax to PPI for tax years 2004 and 2005. Incredibly, the Tax Commissioner appears to not only argue that it only has to conduct a single audit and then bind a taxpayer to the audit results for years to come, but also that once a taxpayer has gone to the BTA for a given year it is precluded from exercising its right to administrative and judicial appeal for future audits.

III. CONCLUSION.

In conclusion, the decision of the BTA must be reversed. The Tax Commissioner's own Brief demonstrates that the only "finding" it made in support of its assessment was a legal conclusion that PPI cannot use the LIFO method of accounting. As PPI could use whatever method of accounting it chose, the use of a particular accounting method without more cannot be the basis for the assessment of additional tax. Next, even if the Tax Commissioner had made a "finding" any such "finding" would have been part of the 2002-2003 audit as the Tax Commissioner did not even conduct an audit relative to 2004 or 2005. As "each tax year stands on its own," the Tax Commissioner cannot rely on audit findings from the 2002-2003 audit to assess additional tax to PPI for 2004-2005. Finally, the Tax Commissioner's argument regarding *stare decisis* has no application in this case.

Respectfully submitted,
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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true copy of the foregoing *Reply Brief of Appellant Progressive Plastics, Inc.* was served via Overnight Mail this 2nd day of April, 2012 upon the following:

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