

STATE OF MICHIGAN
COURT OF APPEALS

KC TRANSPORTATION, INC.,
Plaintiff-Appellant,

UNPUBLISHED
July 9, 2013

v

DEPARTMENT OF TREASURY,
Defendant-Appellee.

No. 310428
Tax Tribunal
LC No. 00-314982

Before: BOONSTRA, P.J., and SAAD and HOEKSTRA, JJ.

PER CURIAM.

Petitioner, KC Transportation, Inc., appeals the final judgment of the Michigan Tax Tribunal. The Tax Tribunal denied KC Transportation’s appeal of an assessment for unpaid motor fuel taxes pursuant to the International Fuel Tax Agreement (IFTA). For the reasons set forth below, we affirm.

I. FACTS AND PROCEEDINGS

IFTA is “the interstate agreement on collecting and distributing fuel use taxes paid by motor carriers.” 49 USC 31701(3). It is designed to encourage cooperation in the administration and collection of motor fuel taxes throughout multiple jurisdictions. *May Trucking Co v Oregon Dep’t of Transportation*, 388 F3d 1261, 1262 (CA 9, 2004). The member jurisdictions impose the fuel taxes, and IFTA organizes the administration of the taxes among the jurisdictions. *Id.* at 1262-1263. “[A]n interstate motor carrier pays all its state fuel taxes quarterly to the ‘base jurisdiction’ in which it registers as a licensee,” then IFTA requires the base jurisdiction to apportion the necessary tax to each state in which the motor carrier travels. *Id.* at 1263. “Federal law requires all states that have a fuel-tax reporting requirement to conform those requirements to IFTA.” *Id.*, citing 49 USC 31705. Through legislative act, Michigan entered into IFTA. MCL 207.212a(1).

KC Transportation runs a fleet of approximately 150 trucks that travel throughout 49 jurisdictions in North America. Respondent, Department of Treasury, performed an IFTA audit on KC Transportation for the period of October 1, 1999 to September 30, 2004. From the beginning of the audit, it was evident that there were problems with KC Transportation’s record keeping, including its failure to keep daily trip sheets with odometer readings, which the auditor testified were required by IFTA. Because KC Transportation was unable to provide the odometer readings, respondent used a random sample of trucks that had maintenance records

containing odometer readings. Respondent concluded that KC Transportation's mileage was understated and KC Transportation agreed. Accordingly, KC Transportation and respondent adjusted KC Transportation's mileage by 3.4 percent.

Respondent also found problems with KC Transportation's accounting system for fuel purchases because, along with other irregularities, there were some trucks with mileage but no gallons of fuel purchased. The auditor testified that the IFTA allowed him to recalculate the fuel usage to determine tax liability once he concluded that KC Transportation had inadequate records. He explained that the IFTA allowed him to assess KC Transportation a liability with the base of 4.0 MPG if there were inadequate records. However, he was hoping to avoid using the 4.0 MPG alternative, to avoid a harsh result for KC Transportation. Respondent eventually calculated a 6.21 MPG rate after removing certain outliers from the audit. Using this rate, respondent concluded that KC Transportation owed taxes on an additional 1,515,647 gallons of fuel. Respondent issued an assessment to petitioner for unpaid motor fuel taxes in the amount of \$335,552.29, plus \$33,614.95 in penalties and \$148,867.09 in interest.

II. ANALYSIS

We review a decision of the tribunal to determine "whether the tribunal committed an error of law or applied the wrong legal principles." *AERC of Michigan, LLC v Grand Rapids*, 266 Mich App 717, 722; 702 NW2d 692 (2005). The tribunal's factual findings should be upheld if there is competent, material, and substantial evidence to support the findings. *Wexford Med Group v Cadillac*, 474 Mich 192, 201; 713 NW2d 734 (2006).

Michigan's Motor Carrier Fuel Tax Act (MCFTA), MCL 207.211, *et seq.*, provides that "[a] motor carrier licensed under this act shall pay a road tax calculated on the amount of motor fuel consumed in qualified commercial motor vehicles on the public roads or highways within this state." MCL 207.212(1). It further states that "qualified commercial motor vehicles licensed under this act that travel in interstate commerce will be subject to the definition of taxable motor fuels and rates as defined by the respective international fuel tax agreement member jurisdictions." *Id.* The MCFTA sets forth the methods to determine the amount of fuel consumed and average MPG:

The amount of motor fuel consumed in the operation of a motor carrier on public roads or highways within this state shall be determined by dividing the miles traveled within Michigan by the average miles per gallon of motor fuel. The average miles per gallon of motor fuel shall be determined by dividing the miles traveled within and outside of Michigan by the total amount of motor fuel consumed within and outside of Michigan. [MCL 207.212(2).]

The IFTA Articles of Agreement, R1210.100, states that the base jurisdiction has the authority to determine a licensee's tax liability on the basis of the best information available if the licensee "fails, neglects, or refuses to file a tax return when due; . . . fails to make a record available upon written request by the base jurisdiction; [or] fails to maintain records from which the licensee's true liability may be determined." It further provides, in relevant part:

The assessment made by a base jurisdiction pursuant to this procedure shall be presumed to be correct and, in any case where the validity of the assessment is questioned, the burden shall be on the licensee to establish by a fair preponderance of evidence that the assessment is erroneous or excessive. [*Id.*, R1210.300.]

The IFTA Audit Manual provides that the audit must be conducted on a sample that is representative of the licensee's operations. *Id.*, A530.100.¹ If a legitimate reason exists, the Treasury Department should allow the licensee input on the sample-selection process. *Id.*, A530.300. Further,

If the licensee's records are lacking or inadequate to support any tax return filed by the licensee or to determine the licensee's tax liability, the base jurisdiction shall have authority to estimate the fuel use upon (but is not limited to) factors such as the following:

- .005 Prior experience of the licensee;
- .010 Licensees with similar operations;
- .015 Industry averages;
- .020 Records available from fuel distributors; and
- .025 Other pertinent information the auditor may obtain or examine.

Unless the auditor finds substantial evidence to the contrary by reviewing the above, in the absence of adequate records, a standard of 4 MPG/1.7KPL will be used. [*Id.*, A550.100.]

Therefore, if the auditor determines that the petitioner's records were lacking or inadequate, then the auditor has the authority to estimate the fuel use. *Id.*

¹ Along with the IFTA Procedures Manual, the IFTA Articles of Agreement and Audit Manual "shall be equally binding upon the member jurisdictions and IFTA licensees and are known as the IFTA governing documents." IFTA Articles of Agreement, R120.

The IFTA Audit Manual, A100; A540.200, states that respondent should "audit the tax returns and supporting documents of licensees based in that jurisdiction" and that "the audit will be completed using the best information available to the base jurisdiction." Moreover, the audit must be conducted on a sample that is representative of the licensee's operations. *Id.*, A530.100. If a legitimate reason exists, respondent should allow the licensee input on the sample-selection process. *Id.*, A530.300. "An agreement that the sampling methodology is appropriate should be signed by the licensee and the auditor." *Id.*, A530.400.

KC Transportation asserts that the tribunal erred in upholding the assessment despite the fact that it submitted evidence of all of its fuel purchases. However, the tribunal found that there were various problems with fuel reporting and an absence of required records. These findings were supported by material, substantial, and competent evidence. The auditor testified (and the tribunal found his testimony competent) that it was apparent from the beginning of the audit that KC Transportation did not have adequate records. As noted, evidence showed that fuel purchases were underreported because some vehicles had mileage but no gallons of fuel purchased, while others were apparently achieving 30 MPG, an improbably high mileage rate for the trucks at issue. KC Transportation's submission of evidence regarding fuel it purchased in no way resolves respondent's inquiry into unreported fuel purchases. Respondent accepted the tax credits paid and the fuel purchases submitted for those tax credits; at issue was the unreported fuel purchases and inadequate reporting. Accordingly, the tribunal did not err when it affirmed the assessment despite KC Transportation's submission of its fuel purchase records because respondent had the authority to estimate fuel use once it determined that there were inadequate records.

KC Transportation further argues that respondent failed to utilize the best evidence available when it demanded trip sheets instead of using KC Transportation's information from the electronic control modules in the trucks.

The IFTA Procedures Manual, P540-P570, details the records that are required, as well as what information the records must contain. It provides as follows:

- .100** Licensees shall maintain detailed distance records which show operations on an individual-vehicle basis. The operational records shall contain, but not be limited to:
 - .005 Taxable and non-taxable usage of fuel;
 - .010 Distance traveled for taxable and non-taxable use; and
 - .015 Distance recaps for each vehicle for each jurisdiction in which the vehicle operated.

- .200** An acceptable distance accounting system is necessary to substantiate the information reported on the tax return filed quarterly or annually. A licensee's system at a minimum, must include distance data on each individual vehicle for each trip and be recapitulated in monthly fleet summaries. Supporting information should include:
 - .005 Date of trip (starting and ending);
 - .010 Trip origin and destination;
 - .015 Route of travel (may be waived by base jurisdiction);

- .020 Beginning and ending odometer or hubodometer reading of the trip (may be waived by base jurisdiction);
- .025 Total trip miles/kilometers;
- .030 Miles/kilometers by jurisdiction;
- .035 Unit number or vehicle identification number;
- .040 Vehicle fleet number;
- .045 Registrant's name; and
- .050 may include additional information at the discretion of the base jurisdiction [*Id.*, P540 (emphasis added).]

The manual further provides that a licensee may use electronic data recording systems in lieu of handwritten trip reports. *Id.*, P610. If an electronic data recording system is used, it must collect a variety of information, including “[b]eginning and ending odometer or hubodometer reading of the trip (may be waived by base jurisdiction).” *Id.*, P640.100.

These provisions make clear that odometer readings are in fact required by IFTA, unless the base jurisdiction waives the requirements. The auditor testified that Michigan has not waived the odometer readings and in fact requires them, and KC Transportation provides no evidence to contradict this assertion.

KC Transportation contends that respondent erred in seeking daily trip sheets and excluding all other evidence it submitted, but this argument mischaracterizes respondent's requests. Respondent sought daily trip sheets, as required by IFTA. When KC Transportation did not have those, respondent sought any other information that contained odometer readings in order to comply with IFTA. Respondent eventually used the maintenance records of certain trucks because the odometer readings were recorded when the trucks were repaired.

KC Transportation argues that the tribunal erred in finding that IFTA did not require respondent to examine the fuel records it submitted to respondent. KC Transportation asserts that the IFTA requires an auditor to review supporting documentation, which would include the fuel reports. The tribunal concluded that respondent did not need to audit fuel records. “Although not required to calculate an error rate for fuel,” the tribunal reasoned, “in this case a more equitable outcome would probably arise from such a calculation since the auditor calculated a highly improbable amount of missing gallons.”

While it is true that IFTA requires an auditor to review supporting documentation, the auditor determined early on that there were potentially unreported fuel purchases and that the fuel records were incomplete. The auditor accepted KC Transportation Comdata fuel-purchase reports as proof of the tax paid credits, but concluded that the data simply did not show the amount of total fuel purchased.

KC Transportation argues that the tribunal erred in affirming respondent's audit method. The IFTA provides broad latitude for auditors who have determined that there are inadequate records. The IFTA Articles of Agreement, R1210.100, provide that the base jurisdiction has the authority to determine a licensee's tax liability *on the basis of the best information available*. (Emphasis added.) Consistently, the IFTA Audit Manual, A100 and A540.200, provide that respondent should "audit the tax returns and supporting documents of licensees based in that jurisdiction" and that "the audit will be completed *using the best information available to the base jurisdiction*." (Emphasis added.)

Moreover, the audit must be conducted on a sample that is representative of the licensee's operations. *Id.*, A530.100. The manual further provides:

If the licensee's records are lacking or inadequate to support any tax return filed by the licensee or to determine the licensee's tax liability, the base jurisdiction shall have authority to estimate the fuel use upon (but is not limited to) factors such as the following:

- .005 Prior experience of the licensee;
- .010 Licensees with similar operations;
- .015 Industry averages;
- .020 Records available from fuel distributors; and
- .025 Other pertinent information the auditor may obtain or examine.

Unless the auditor finds substantial evidence to the contrary by reviewing the above, in the absence of adequate records, a standard of 4 MPG/1.7KPL will be used. [*Id.*, A550.100.]

KC Transportation asserts that the standard audit method involves reviewing distance and fuel records and computing an error rate for each factor. This may be true in the IFTA Best Practices Audit Guide, but the guide itself states that jurisdictions are in no way required to implement the guide. Rather, again, IFTA provides respondent with broad latitude once it has determined that a licensee's records are inadequate. *Id.* The audit is to be conducted on the "best information available" over a sample that is representative of the licensee's fleet. *Id.*, A100, A530.100, A540.200. Respondent is entitled to use any pertinent information when estimating a licensee's fuel use. *Id.*, A550.100.

In sum, the auditor testified that at the beginning of the audit he determined that miles were understated, which KC Transportation accepted as true. At this point, the auditor also determined that there were unreported fuel purchases based on these extra miles. KC Transportation and respondent stipulated to a mileage adjustment of 3.4 percent, and the auditor determined that, on the basis of those extra miles, there was unreported fuel. The auditor testified that because KC Transportation failed to keep the required source documents for the quarter, he was forced to look outside the quarter. The auditor eventually used 32 or 33 vehicles as a sample and used the available odometer readings. Asked about the reliability of this

approach, he stated that he used the best information available, and this methodology was within his discretion.

Affirmed.

/s/ Mark T. Boonstra
/s/ Henry William Saad
/s/ Joel P. Hoekstra