UT 17-01
Tax Type: Use Tax
Tax Issue: Aircraft Use Tax

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS

THE DEPARTMENT OF	)	Docket No.	XX-ST-XXXX
REVENUE OF THE	)	NTL Nos.	CNXX […],
STATE OF ILLINOIS	)	CNXX […],	CNXX […],
v.	)	CNXX […],	CNXX […],
	)	CNXX […],	CNXX […]
PARENT CO. LLC,	)	John E. White,	
Taxpayer	)	Administrative Law Judge	

RECOMMENDATION FOR DISPOSITION

Appearances: Daniel Hefter, Hefter Law, Ltd., appeared for PARENT CO., LLC; Seth Schriftman, Special Assistant Attorney General, appeared for the Illinois Department of Revenue.

Synopsis:

This matter involves the Department's issuance of seven Notices of Tax Liability (NTLs), one to each of seven different LLCs, to wit: NUMBER 1 COMPANY, LLC; NUMBER 2 COMPANY, LLC; NUMBER 3 COMPANY, LLC; NUMBER 4 COMPANY, LLC; NUMBER 5 COMPANY, LLC; NUMBER 6 COMPANY, LLC; NUMBER 7 COMPANY, LLC; all of which are subsidiary LLCs of the LLC named as the representative Taxpayer in the caption of this contested case. Each NTL assessed aircraft use tax (AUT) to one of the subsidiary LLCs, following an audit by the Department. For convenience, in this recommendation, I will generally refer to the seven subsidiary LLCs in the singular, as Taxpayer, unless otherwise indicated. The issue is

whether Taxpayer ever used any of the aircraft in Illinois, incident to its ownership of them.

The hearing was held at the Department's offices in Chicago. Taxpayer presented the testimony of a witness, as well as stipulated and other documentary exhibits. I have reviewed the evidence, and I am including in this recommendation findings of fact and conclusions of law. For reasons that follow, I recommend that the NTLs be finalized as issued.

Findings of Fact:

1. Each of the Stipulated Exhibits admitted into evidence is an affidavit of, respectively, JOHN DOE, JOE SMITH, and Annette Simmons, with attached documents, which each affiant identifies, and refers to within his/her affidavit, as a sub-exhibit. In this recommendation, a citation to, for example, Stip. Ex. 1.4, will refer to the document identified by the affiant as sub-exhibit 4 of Stipulation Exhibit 1.
2. Prior to the transactions at issue and after, JOHN DOE (DOE) was an owner of three separate entities that have operated a flight school at an airport in the northwest suburbs of Chicago. Stipulated Exhibit (Stip. Ex.) 1 (Affidavit of DOE), ¶¶ 1-5. The three entities are: CORP. 1, Inc. (hereafter, CORP. 1), The CORP. 2, Inc. (hereafter, CORP. 2), and CORP. 3, LLC. *Id*., ¶ 1.
3. On the following dates, CORP. 1, Inc., and/or CORP. 2 purchased aircraft bearing the following United States registration numbers, which are commonly referred to as tail numbers:

U.S. Reg. No.	Purchase date	Purchaser
NUMBER 1	November 23, 1994	CORP. 1
NUMBER 2	January 23, 1995	CORP. 2
NUMBER 3	March 4, 1997	CORP. 2

NUMBER 4	July 29, 1998	CORP. 2
NUMBER 5	December 13, 2004	CORP. 2
NUMBER 6	December 28, 2004	CORP. 2
NUMBER 7	June 16, 2005	CORP. 2

Stip. Ex. 1, ¶ 6; Stip. Ex. 1.4 (copies of recorded Aircraft Bills of Sale for purchases described above).

4. The aircraft listed in the table above are the aircraft at issue (hereafter collectively referred to as "the Aircraft") in this contested case. Stip. Ex. 3, *passim*.
5. When CORP. 2 purchased the Aircraft described in lines 2 through 6 of the above table, it did so with monies borrowed from JOE SMITH (SMITH). Stip. Ex. 2 (SMITH Affidavit), ¶ 2; Stip. Ex. 1.5 (copy of completed Aircraft Security Agreement form recorded with the FAA showing a security interest SMITH Realty had in Aircraft NUMBER 2), 1.6 (copies of completed Aircraft Security Agreement forms recorded with the FAA showing a security interest SMITH had in Aircraft NUMBER 3, NUMBER 4, NUMBER 5, and NUMBER 6).
6. CORP. 2 prepared and filed Aircraft Security Agreement forms with the FAA to record that SMITH Realty had a security interest in Aircraft NUMBER 2, and that JOE SMITH had a security interest in Aircraft NUMBER 3, NUMBER 4, NUMBER 5, and NUMBER 6. Stip. Exs. 1.5-1.6.
7. Between August of 2008 and March of 2009, CORP. 2 had not made any payments to SMITH regarding the loans. Stip. Ex. 2, ¶ 3; Stip. Ex. 1.7 (copy of schedule showing loan payment information prepared by DOE); Hearing Transcript (Tr.) pp. 55-59 (DOE).
8. During the months of March and April 2009, two separate sets of Aircraft Bill of Sale forms and Aircraft Registration Application forms were filed with the FAA regarding

each of the Aircraft at issue. Stip. Ex. 1.8 (copies of recorded Aircraft Bills of Sale dated March 13, 2009); Stip. Ex. 2.2 (copies of recorded Aircraft Bills of Sale dated April 21, 2009); Stip. Ex. 3, ¶¶ 6-7; Stip. Ex. 3.1 (copies of completed Aircraft Registration Application forms, dated March 13, 2009); Stip. Ex. 3.2 (copies of completed Aircraft Registration Application forms, dated April 21, 2009).

9. On March 13, 2009, a set of Aircraft Bill of Sale forms were filed and recorded with the FAA, notifying it that ownership of the following Aircraft had been transferred between the following parties:

U.S. Reg. No.	**Seller**	**Purchaser**
NUMBER 1	JOHN DOE DBA CORP. 2	JOE SMITH
NUMBER 2	CORP. 2	JOE SMITH
NUMBER 3	CORP. 2	JOE SMITH
NUMBER 4	CORP. 2	JOE SMITH
NUMBER 5	CORP. 2	JOE SMITH
NUMBER 6	CORP. 2	JOE SMITH
NUMBER 7	CORP. 2	JOE SMITH

Stip. Ex. 1.8; Stip. Ex. 3, ¶ 6.

10. Also on March 13, 2009, JOE SMITH, the purchaser named on the Aircraft Bill of Sale forms referred to immediately above, completed and signed an Aircraft Registration Application form regarding each of the seven Aircraft, and submitted those Aircraft Registration Application forms to the FAA. *See* Stip. Ex. 3, ¶ 5; Stip. Ex. 3.1.

11. SMITH completed and signed each of the seven Aircraft Registration Application forms under a certification which provides, in pertinent part, as follows:

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[ ] **CHECK HERE IF YOU ARE ONLY REPORTING A CHANGE OF ADDRESS**

ATTENTION! Read the following statement before signing this application. This portion MUST be completed.

A false or dishonest answer to any question in this application may be grounds for punishment by fine and / or imprisonment (U.S. Code, Title 18, Sec. 1001).

CERTIFICATION

I/WE CERTIFY:

(1) That the above aircraft is owned by the undersigned applicant, who is a citizen (including corporations) of the United States

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(2) That the aircraft is not registered under the laws of any foreign country; and

(3) That legal evidence of ownership is attached or has been filed with the [FAA]

NOTE: If executed for co-ownership all applicants must sign. Use reverse side if necessary.

TYPE OR PRINT NAME BELOW SIGNATURE

SIGNATURE	TITLE	DATE
[signature] JOE SMITH	Owner	03/13/2009

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Stip. Ex. 3.1.

12. On or about April 21, 2009, another set of Aircraft Bill of Sale forms were filed and recorded with the FAA, notifying it that ownership of the following Aircraft had been transferred between the following parties:

U.S. Reg. No.	Seller	Purchaser
NUMBER 1	JOE SMITH	NUMBER 1 COMPANY, LLC
NUMBER 2	JOE SMITH	NUMBER 2 COMPANY, LLC
NUMBER 3	JOE SMITH	NUMBER 3 COMPANY, LLC
NUMBER 4	JOE SMITH	NUMBER 4 COMPANY, LLC
NUMBER 5	JOE SMITH	NUMBER 5 COMPANY, LLC
NUMBER 6	JOE SMITH	NUMBER 6 COMPANY, LLC
NUMBER 7	JOE SMITH	NUMBER 7 COMPANY, LLC

Stip. Ex. 2.2 (copies of recorded Aircraft Bills of Sale dated April 21, 2009); Stip. Ex. 3, ¶ 7 & 3.1.

13. Together with the April 21, 2009 Aircraft Bill of Sale forms submitted to the FAA, the purchaser named on each of those forms completed an Aircraft Registration Application form regarding each of the seven Aircraft, and submitted those Aircraft Registration Application forms to the FAA. *See* Stip. Ex. 3, ¶ 7; Stip. Ex. 3.2 (copies of completed Aircraft Registration Applications for the Aircraft, dated April 21, 2009).
14. SMITH signed each of the Aircraft Registration Application forms dated April 21, 2009. Stip. Ex. 3, ¶ 7; Stip. Ex. 3.2.
15. Each of the Aircraft Registration Application forms dated April 21, 2009 contain the identical certification which was included on the Aircraft Registration Application forms dated March 13, 2009. Stip. Exs. 3.1-3.2. The principle difference between the two sets of Aircraft Registration Application forms is that SMITH signed each of the Aircraft Registration Application forms dated April 21, 2009 not as an individual owner/applicant, as he had on the set dated March 13, 2009, but as the member of the corporate applicant/owner. *Id*.
16. The Department conducted an audit of the transactions recorded with the FAA in March and April 2009 regarding the Aircraft. Stip. Ex. 3, ¶¶ 1-3. Annette Simmons (Simmons) conducted the audit for the Department. *Id*.
17. During the course of the audit, Simmons spoke with both DOE and SMITH. Stip. Ex. 3, ¶¶ 17-19. Later, she spoke with and received information from a power of attorney regarding her initial valuation of the Aircraft. Stip. Ex. 3, ¶ 21.
18. Simmons used the valuations she received from Taxpayer's power of attorney when preparing the determination of tax due for each of the Aircraft. Stip. Ex. 3, ¶¶ 21-23,

26, 31; Stip. Exs. 3.14-3.15, 3.17.

19. No AUT transaction returns were filed regarding either of the two sets of transactions which took place on March 13, and/or on April 21, 2009, for any of the Aircraft. Stip. Ex. 3, ¶ 20.

20. Although Simmons determined that the purchasers named on the March 13, 2009 and on the April 21, 2009 Aircraft Bills of Sale for the Aircraft could have been assessed tax regarding their respective purchases, a decision was made to assess AUT regarding only the April 21, 2009 purchases/transfers. Stip. Ex. 3, ¶ 10.

21. Following audit, the Department issued seven NTLs to Taxpayers to assess AUT for the transfers of the seven Aircraft from SMITH to the seven subsidiary LLCs.

NTL No.	U.S. Reg. No.	Tax	Amnesty Penalty	Audit Late Penalty	Late Pay Penalty	Late Filing Penalty	Interest	Amnesty Interest	Total
CNXX [...]	NUMBER 1	[…]	[…]	[…]	[…]	[…]	[…]	[…]	[…]
CNXX [...]	NUMBER 2	[…]	[…]	[…]	[…]	[…]	[…]	[…]	[…]
CNXX [...]	NUMBER 3	[…]	[…]	[…]	[…]	[…]	[…]	[…]	[…]
CNXX [...]	NUMBER 4	[…]	[…]	[…]	[…]	[…]	[…]	[…]	[…]
CNXX [...]	NUMBER 5	[…]	[…]	[…]	[…]	[…]	[…]	[…]	[…]
CNXX [...]	NUMBER 6	[…]	[…]	[…]	[…]	[…]	[…]	[…]	[…]
CNXX [...]	NUMBER 7	[…]	[…]	[…]	[…]	[…]	[…]	[…]	[…]

Stip. Ex. 1.17 (copies of NTLs). Each NTL was addressed to the subsidiary owner/applicant on whose behalf the Aircraft Bills of Sale and Aircraft Registration Application was submitted to the FAA on April 21, 2009. *Id*.

Conclusions of Law:

The Aircraft Use Tax Act (AUTA) imposes a tax "on the privilege of using, in this State, any aircraft as defined in Section 3 of the Illinois Aeronautics Act acquired by gift, transfer, or purchase after June 30, 2003." 35 ILCS 157/10-15. The AUTA is one of two tax statutes the Illinois General Assembly enacted ─ the other being the Watercraft Use Tax Act (WUTA) ─ which were modeled after the previously enacted Vehicle Use Tax Act (VUTA). *Compare* 35 ILCS 157/10-1 *et seq*. (effective June 20, 2003) *and* 35 ILCS 158/15-1 *et seq*. (effective July 30, 2004) *with* 625 ILCS 5/3-1001 *et seq*. (*formerly* Ill. Rev. Stat. ch. 95½, ¶¶ 3-1001 to 3-2006 (1980)). Each of those respective statutes impose a tax on the privilege of using, in Illinois, certain types of tangible personal property that are acquired in transactions that would not constitute a sale at retail, as that phrase is defined within the Retailers' Occupation Tax Act (ROTA) and the Use Tax Act (UTA). 35 ILCS 157/10-15; 35 ILCS 158/15-1; 625 ILCS 5/3-1001; 35 ILCS 105/2; 35 ILCS 120/1; *see also* Greenwalt v. Department of Revenue, 198 Ill. App. 3d 129, 555 N.E.2d 775 (2d Dist. 1990) (MVUT upheld as constitutional).

The legislative intent underlying the AUTA, the VUTA and the WUTA is to tax the privilege of using aircraft, motor vehicles and watercraft in Illinois, *each and every time* such items are subsequently acquired by a different person by gift, transfer, or purchase, unless one of the expressed statutory exceptions or exemptions apply. 35 ILCS 157/10-15; 35 ILCS 158/15-1; 625 ILCS 5/3-1001; Greenwalt v. Department of Revenue, 198 Ill. App. 3d 129, 132, 555 N.E.2d 775, 777 (2d Dist. 1990) ("Accordingly, section 3-1001 [of the VUTA] imposes a tax only on the use of vehicles not purchased at retail, whereas retail sales are taxed under the Use Tax Act.").

Issue and Arguments

Taxpayer asserts that, in this case, the Department is impermissibly applying the AUTA as though it imposes a tax on mere transfers of title to aircraft, instead of on the use of aircraft in Illinois. Tr. pp. 86-87 (closing argument). Taxpayer contends that the evidence shows that it never made any actual, physical use of the Aircraft in Illinois, including any substantive or economic use of them. *Id*. Taxpayer also argues that, based on an unwritten agreement between and SMITH and DOE, Taxpayer held only a security interest in the Aircraft, implying that Taxpayers do not, in fact, own any of the Aircraft. *Id*., p. 86.

In response to Taxpayer's argument, the Department counters that the evidence admitted at hearing shows both that Taxpayer owned the Aircraft, and that it used them in Illinois. Regarding the issue of ownership, the Department reasons that the FAA title documents carry more weight than DOE's mere testimony that he and SMITH had an oral agreement that Taxpayer would hold only a security interest in the Aircraft. As to the question of use, the Department argues that the legislative definition of "use" in the UTA was intended to be read broadly, and was not intended to be limited to the exercise of rights and powers by persons who actually operate, are transported in, or who physically manipulate, an aircraft. Tr. p. 94. It concludes that, under the statutory definition of use, Taxpayer's admitted agreement to allow DOE's flight school to continue to operate the Aircraft, in Illinois, constituted Taxpayer's exercise of rights and powers over such aircraft which was incident to its ownership of them. *Id*.

Analysis

Section 10-35 of the AUTA, provides, in pertinent part:

> Sec. 10-35. Powers of Department. *** In the administration of, and compliance with, this Law, the Department and persons who are subject to this Law shall have the same rights, remedies, privileges, immunities, powers, and duties, and be subject to the same conditions, restrictions, limitations, penalties, and definitions of terms, and employ the same modes of procedure, as are prescribed in the Use Tax Act, as now or hereafter amended (except for the provisions of Section 3-70), which are not inconsistent with this Law, as fully as if the provisions of the Use Tax Act were set forth in this Law. In addition to any other penalties imposed under law, any person convicted of violating the provisions of this Law, shall be assessed a fine of $1,000.

35 ILCS 157/10-35.

Since the AUTA incorporates the UTA's definition of terms, the word "using," within AUTA § 10-15's phrase, "the privilege of using, in this State, any aircraft … acquired by gift, transfer, or purchase after June 30, 2003", should be construed consistent with the UTA's definition of "use" ─ unless some particular aspect of the UTA's definition is inconsistent with the AUTA. 35 ILCS 157/10-35. Within § 2 of the UTA, the Illinois General Assembly defined "use" to mean:

> ***
>
> the exercise by any person of any right or power over tangible personal property incident to the ownership of that property, except that it does not include the sale of such property in any form as tangible personal property in the regular course of business to the extent that such property is not first subjected to the use for which it was purchased, and does not include the use of such property by its owner for demonstration purposes. … "Use" does not mean the demonstration use or interim use of tangible personal property by a retailer before he sells that tangible personal property. ***

35 ILCS 105/2.

As indicated above, the AUTA also incorporates the "same modes of procedure, as are prescribed in the Use Tax Act …." 35 ILCS 157/10-35. Section 11 of the UTA incorporates into the UTA certain provisions of the complementary Retailers' Occupation Tax Act (ROTA). 35 ILCS 105/11. Among them is § 4 of the ROTA, which provides that

the Department's determination of tax due constitutes prima facie proof that tax is due in the amount determined by the Department. 35 ILCS 105/12; 35 ILCS 120/4.

In this case, Taxpayers position is essentially that the subsidiary LLCs are not subject to AUT regarding the transactions, because they neither used the Aircraft in Illinois, nor did they own the Aircraft. More specifically, they argue that "[t]here is no question that what we have here is a security arrangement, a loan and security arrangement, and the titles were transferred for one reason and one reason only: Security." Tr. p. 86. A particularly good description of the applicable burden in a case like this was described by the court in Balla v. Department of Revenue, 96 Ill. App. 3d 293, 421 N.E.2d 236 (1st Dist. 1981):

> Ordinarily, the taxing authority has the burden of proof regarding a taxpayer's liability to the government. (Cornett-Lewis Coal Co. v. C. I. R. (6th Cir. 1944), 141 F.2d 1000.) For example, the taxing authority bears the burden of proving that the taxpayer actually received income (Thomas v. C. I. R. (6th Cir. 1955), 223 F.2d 83), and that such income is properly subject to taxation (Miller v. United States (7th Cir. 1961), 296 F.2d 457). The Illinois legislature, in order to aid the Department in meeting its burden of proof in this respect, has provided that the findings of the Department concerning the correct amount of tax due are prima facie correct. (Ill.Rev.Stat.1979, ch. 120, par. 9-904(a).) When the taxpayer introduces credible evidence to the contrary, the burden is again placed on the Department to prove its contentions by a preponderance of the evidence. Goldfarb v. Department of Revenue (1952), 411 Ill. 573, 104 N.E.2d 606.

Balla, 96 Ill. App. 3d at 296, 421 N.E.2d at 238.

In this case, the Department established its prima facie case when it introduced copies of the NTLs as a stipulated exhibit. Stip. Ex. 3.17. That exhibit, without more, constitutes prima facie proof that Taxpayer owes AUT in the amount determined by the Department. 35 ILCS 157/10-35; 35 ILCS 105/12; 35 ILCS 120/4. The Department's prima facie case is overcome, and the burden shifts to the Department to prove its case,

only after a taxpayer presents evidence that is consistent, probable and identified with its books and records, to show that the Department's determinations were not correct. Copilevitz v. Department of Revenue, 41 Ill. 2d 154, 157-58, 242 N.E.2d 205, 207 (1968).

The documentary evidence in this case, however, clearly establishes that, as of April 21, 2009, each of the subsidiary LLCs had notified the FAA— and the general public — that it was a registered owner of one of the Aircraft. Stip. Exs. 2.2, 3.2. Each of the two sets of Aircraft Bill of Sale and Aircraft Registration Application forms completed regarding the April 21, 2009 transactions constitute written statements by SMITH, acting as each Taxpayer's member, in which he swears that one of the subsidiary LLCs was the owner of an Aircraft. Stip. Exs. 2.2, 3.2. I presume these sworn, written statements were made within the scope of his duties of each subsidiary LLC, because he identified himself as the member of each LLC on the Aircraft Registration Application forms. *Id*. Generally, any statement made by a party or on his behalf which is inconsistent with his position in litigation may be introduced into evidence against him. Quincy Trading Post, Inc. v. Department of Revenue, 12 Ill. App. 3d 725, 731-32, 298 N.E.2d 789, 794 (4th Dist. 1973) ("Statements made by an agent in the exercise of his duties pertaining to matters within the scope of his authority may constitute an admission as an exception to the hearsay rule."). The two sets of Aircraft Bill of Sale and Aircraft Registration Application forms constitute written statements which are inconsistent with the subsidiary LLC's position at hearing.

For the following reasons, I give no weight to DOE's testimony that an unwritten agreement between DOE and SMITH provides the better evidence of ownership of the

Aircraft on April 21, 2009. First, SMITH already had a recorded security interest in five of the Aircraft. Stip. Exs. 1.5-1.6. If the agreement between SMITH and DOE was intended only to provide SMITH with a security interest in the Aircraft, DOE could have just recorded another such security interest for SMITH regarding the remaining two Aircraft. Second, and more fundamentally, if DOE intended only to provide SMITH with a security interest in the Aircraft, why would both DOE and SMITH have knowingly made sworn, material misrepresentations to the FAA about the ownership of all of the Aircraft? I will not presume such fraud.

To rebut the Department's prima facie case, a taxpayer must present credible evidence, which is closely tied to its regularly kept books and records. Copilevitz, 41 Ill. 2d at 157-58, 242 N.E.2d at 207; Balla, 96 Ill. App. 3d at 296, 421 N.E.2d at 238. Here, all of the documentary evidence shows that the subsidiary LLCs owned the Aircraft on and after April 21, 2009. On the issue of ownership, I find that DOE's contradictory testimony is not credible. Each Taxpayer's sworn statements to the FAA constitute substantive evidence that each subsidiary LLC owned one of the Aircraft on April 21, 2009. Stip. Exs. 2.2, 3.2.

The next issue is use. The evidence makes clear that each subsidiary LLC's member knew that, after the April 21, 2009 transfers of title and ownership of an Aircraft, DOE's flight school would continue to operate each of the Aircraft, in Illinois. Stip. Ex. 1, ¶ 8; Stip. Ex. 1.7; Stip. Ex. 2, ¶ 6; Tr. p. 83 (DOE). When an owner of tangible personal property knowingly permits another person to have custody of the property, and operate such property in Illinois, whether for business or other purposes, the owner is exercising rights and powers over that property which are incident to its ownership of it.

Miller Brewing Co. v. Korshak, 35 Ill. 2d 86, 93, 219 N.E.2d 494, 497-98 (1966) ("The power to allow property one owns to be used [by others] for one's benefit in this manner is the 'exercise' of 'an incident of ownership' under the act."). What I infer and reconcile from the evidence is that Taxpayers permitted DOE's flight school to continue to possess and operate the Aircraft, in Illinois, to give DOE a better opportunity to repay the loan amounts DOE owed Taxpayers' individual member, and which amounts exceeded the fair market value of the Aircraft. Stip. Ex. 1, ¶ 8; Stip. Ex. 1.7; Stip. Ex. 2, ¶ 6; Tr. p. 83 (DOE).

But it is not necessary to establish a reason why Taxpayers permitted another to have custody of and operate the Aircraft in Illinois. What does matter is that Taxpayers knowingly permitted the Aircraft to remain in DOE's flight school's custody, and knowingly permitted DOE to retain possession of them, and to operate them, in Illinois, for the flight school's operation. Stip. Ex. 1, ¶ 8; Stip. Ex. 2, ¶ 6. By doing so, Taxpayers exercised rights and powers over the Aircraft, in Illinois, which were incident to their ownership of them, and thereby used them, in Illinois, as use in defined in the UTA. 35 ILCS 105/2; Miller Brewing Co., 35 Ill. 2d at 93, 219 N.E.2d at 497-98.

Conclusion:

I recommend that the Director finalize the NTLs as issued, with penalties and interest to accrue pursuant to statute.

May 10, 2017
Date

John E. White, Administrative Law Judge