

05-1268
Audit
Signed 09/05/2006

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER 1 & PETITIONER 2,	)	ORDER	
)		
Petitioners,	)	Appeal No.	05-1268
)		
v.	)	Account No.	#####
	)	Tax Type:	Income Tax
AUDITING DIVISION OF THE	)	Tax Years:	2001
UTAH STATE TAX COMMISSION,)		
	)	Judge:	Chapman
Respondent.)		

STATEMENT OF THE CASE

The Petitioners are appealing an audit deficiency of additional Utah individual income tax and interest for the 2001 tax year. The Petitioners requested that the Commission issue its initial decision upon a review of the written record and have waived their right to proffer oral arguments at an Initial Hearing. Accordingly, the Commission makes its initial decision based solely on the documents that the Petitioners submitted on March 21, 2006 and that the Division submitted on April 3, 2006.

Auditing Division (“Division”) imposed its assessment in a Statutory Notice of Audit Change (“Statutory Notice”) dated August 11, 2005. The Division assessed additional Utah income tax in the amount of \$\$\$\$\$, plus interest. No penalties were assessed.

The Petitioners filed an amended Utah non-resident return for the 2001 tax year on March 2, 2004. The Division reviewed the amended return and assessed additional tax for three revisions: 1) it increased the amount of adjusted gross income that the Petitioners apportioned to Utah from \$\$\$\$\$ to \$\$\$\$\$; 2) it decreased the federal tax deduction that the Petitioners claimed from \$\$\$\$\$ to \$\$\$\$\$; and 3) it disallowed the \$\$\$\$\$ tax credit that the Petitioners claimed for research activities.

The Petitioners do not contest the revision that increased the amount of their adjusted gross income apportioned to Utah from \$\$\$\$\$ to \$\$\$\$\$. However, they contest the other two revisions that the

Division made. First, the Petitioners contest the revision that decreased their federal tax deduction from \$\$\$\$ to \$\$\$\$ (i.e., a reduction of \$\$\$\$). The Petitioners admit that they filed an Internal Revenue Service (“IRS”) Form 1045 (“Application for Tentative Refund”) in March 2002, in which they requested a credit and refund of federal income tax for the 2001 tax year in the amount of \$\$\$\$. The IRS refunded this amount. The Division claims that this refund decreased their federal tax liability for 2001 by \$\$\$\$\$, which would require a corresponding reduction of \$\$\$\$ (one-half the amount of the federal tax refund) from the amount of federal tax liability that may be deducted for Utah income tax purposes. The Petitioners do not contest that the total federal tax deduction that the Division allowed, \$\$\$\$\$, is one-half of their federal tax liability for the 2001 tax year. However, they ask the Commission to deny the Division’s revision because they believe the amount they deducted, \$\$\$\$\$, is the amount that is derived by following the instructions that accompanied the 2001 Utah income tax return.

Second, the Petitioners request that the Commission deny the Division’s disallowance of their \$\$\$\$ tax credit for research activities for the 2001 tax year. For federal tax purposes, the IRS allowed the Petitioners to take this credit on their 2001 federal tax return. The Division claims that for Utah income tax purposes, the credit must be claimed in a year that is subsequent to its being claimed for federal purposes, or, in this case, no sooner than the 2002 tax year. The Petitioners argue that even though Utah law may provide as the Division asserts, they called the “Technical Department of the Utah State Tax Commission” and were advised by a person named (X) to take the Utah credit in the same year that they took it for federal purposes. Furthermore, they contend that it would be costly and time consuming to amend returns and carry the credit forward to subsequent years.

APPLICABLE LAW

Utah Code Ann. §59-10-114 provides for certain additions to and subtractions from the federal taxable income of an individual when calculating that person’s Utah state taxable income. A subtraction for ½

of the net amount of income tax paid or payable to the United States is allowed in accordance with Subsection 59-10-114(2)(b), as follows:

(2) There shall be subtracted from federal taxable income of a resident or nonresident individual:

(b) (i) except as provided in Subsection (2)(b)(ii), 1/2 of the net amount of any income tax paid or payable to the United States after all allowable credits, as reported on the United States individual income tax return of the taxpayer for the same taxable year; and

(ii) notwithstanding Subsection (2)(b)(i), for taxable years beginning on or after January 1, 2001, the amount of a credit or an advance refund amount reported on a resident or nonresident individual's United States individual income tax return allowed as a result of the acceleration of the income tax rate bracket benefit for 2001 in accordance with Section 101, Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, may not be used in calculating the amount described in Subsection (2)(b)(i);

For the tax year at issue, UCA §59-10-131 allows a taxpayer to take a credit for research activities conducted in Utah. For a taxpayer who qualifies for the credit, Section 59-10-131(1)(b) provides, as follows:

If a taxpayer qualifying for a credit under Subsection (1)(a) seeks to claim the credit the taxpayer shall:

- (i) claim the credit or a portion of the credit for the taxable year immediately following the taxable year for which the taxpayer qualifies for the credit;
- (ii) carry the credit or a portion of the credit forward as provided in Subsection (4)(f); or
- (iii) claim a portion of the credit and carry forward a portion of the credit as provided in Subsections (1)(b)(i) and (ii).

The Utah Legislature has specifically provided that the taxpayer bears the burden of proof, with limited exceptions, in proceedings involving individual income tax before the Tax Commission. UCA §59-10-543 provides, as follows:

In any proceeding before the commission under this chapter, the burden of proof shall be upon the petitioner except for the following issues, as to which the burden of proof shall be upon the commission:

- (1) whether the petitioner has been guilty of fraud with intent to evade tax;
- (2) whether the petitioner is liable as the transferee of property of a taxpayer, but not to show that the taxpayer was liable for the tax; and
- (3) whether the petitioner is liable for any increase in a deficiency where such increase is

asserted initially after a notice of deficiency was mailed and a petition under Title 59, Chapter 1, Part 5 is filed, unless such increase in deficiency is the result of a change or correction of federal taxable income required to be reported, and of which change or correction the commission had no notice at the time it mailed the notice of deficiency.

In those situations where penalty and interest have been properly imposed, UCA §59-1-401(11) grants the Commission the authority to waive, reduce, or compromise penalties and interest upon a showing of reasonable cause.

DISCUSSION

The Division imposed additional Utah income tax upon the Petitioners for the 2001 tax year pursuant to three revisions it made to the Petitioner's amended 2001 Utah non-resident income tax return. The Petitioners do not contest the revision that increased the amount of adjusted gross income that they apportioned to Utah. Remaining at issue, however, is whether the Division properly decreased the federal tax deduction that the Petitioners claimed and properly disallowed the tax credit they claimed for research activities.

Federal Tax Deduction. Section 59-10-114(2)(b) provides that a taxpayer may subtract from Utah taxable income "1/2 of the net amount of any income tax paid or payable to the United States after all allowable credits . . ." The Petitioners subtracted \$\$\$\$ from their Utah taxable income pursuant to this deduction, which if correct, would mean that their federal tax liability for the 2001 tax year is \$\$\$\$\$. The Division claims that the Petitioners' original federal tax liability was reduced by \$\$\$\$ when they filed an IRS Form 1045 and requested a credit for this amount for the 2001 tax year. As a result, the Division claims that the IRS reduced the Petitioners' 2001 federal tax liability to \$\$\$\$\$ and that, as a result, the amount they may deduct from Utah taxable income is only \$\$\$\$\$, not \$\$\$\$\$ (a difference of \$\$\$\$\$).

The Petitioners confirm that they filed an IRS Form 1045 seeking a credit of \$\$\$\$ of their 2001 federal tax liability and that the IRS granted their request. The Petitioners also do not contest that their 2001 federal tax liability was \$\$\$\$\$ and that half of this amount would be \$\$\$\$\$, the amount of the Division's

revision. However, the Petitioners claim that the instructions that accompanied the 2001 Utah income tax return instructed them to derive the amount of the federal tax deduction by adding the tax shown on lines 50, 52, and 55 of IRS Form 1040. On line 50 of the IRS Form 1040, a taxpayer lists “other credits” and is provided space to write in the form number on which he or she claimed a credit and the amount of the credit received. The \$\$\$\$ credit that the taxpayer’s received pursuant to their filing IRS Form 1045 is not listed on line 50 of their amended 2001 federal tax return.

The Petitioners have not shown that their federal tax liability for the 2001 tax year was other than the \$\$\$\$ amount that the claims. Accordingly, the Commission finds that the amount of federal tax liability that the Petitioners may deduct for the 2001 tax year, pursuant to Utah law, is one-half of \$\$\$\$\$, or \$\$\$\$\$, which is consistent with the Division’s assessment. Even were the Commission’s instructions that accompanied the 2001 Utah tax return to be deemed incorrect, they would not grant the Petitioners the right to deduct from Utah taxable income an amount that greater than allowed by law. Furthermore, it appears that the instructions accompanying the 2001 Utah income tax return may, in fact, be correct, because line 50 of the Form 1040 provides space for the Petitioners to report a credit they receive from the IRS and the Petitioners did not disclose the \$\$\$\$ credit they received. For these reasons, the Commission sustains the Division’s assessment of additional tax relating to its reduction of the Petitioners’ federal tax liability subtraction.

Tax Credit for Research Activities. Section 59-10-131 provides that upon qualifying for a research activities tax credit, the taxpayer may claim the credit in the taxable year that immediately follows the taxable year in which he or she qualified for the credit. In the alternative, the Petitioner may carry the tax credit forward to a subsequent year as provided in law. Nowhere in the law, however, is the taxpayer allowed to claim the tax credit in the same taxable year for which he or she qualifies for the credit.

The parties agree that in the 2001 taxable year, the Petitioners qualified for a tax credit for research activities in the amount of \$\$\$\$\$. The parties also agree that the Petitioners applied this credit on their 2001 Utah tax return. The Division disallowed the credit, as Utah law does not permit the credit to be claimed in the same year during which one qualified for it. Although the Petitioners argue that disallowing the credit will require them to expend time and money to file amended returns for years subsequent to 2001, the Commission is not authorized to overturn a statute because of the inconvenience that it may cause a taxpayer. For these reasons, the Commission sustains the Division's action to disallow the Petitioners' tax credit for research activities that they claimed for their amended 2001 Utah tax return.

The Petitioners also assert that they claimed the credit on their 2001 Utah tax return upon the advice of a Tax Commission employee. However, in determining whether or not a tax is due, the Commission is not bound by the incorrect advice that a Tax Commission employee may have given a taxpayer. Had the Petitioners shown that their mistake was due to their reliance upon a Commission employee's error, the Commission would have considered a waiver of the interest that arose because of the erroneous advice. The Division states, however, that the telephone number the Petitioners called to elicit information concerning the tax credit is not a number that is associated with the Tax Commission. Based on the information available in the written record, the Commission does not find that the Petitioners relied on the erroneous advice of a Tax Commission employee and, accordingly, does not find sufficient cause to waive that interest associated with the tax credit.

DECISION AND ORDER

Based on the foregoing, the Commission sustains the Division's audit assessment in its entirety and denies the Petitioners' appeal. It is so ordered.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written

Appeal No. 05-1341

request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission
Appeals Division
210 North 1950 West
Salt Lake City, Utah 84134

Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this _____ day of _____, 2006.

Kerry R. Chapman
Administrative Law Judge

BY ORDER OF THE UTAH STATE TAX COMMISSION.

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this _____ day of _____, 2006.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

Marc B. Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

Notice: If a Formal Hearing is not requested as discussed above, failure to pay the balance resulting from this order within thirty (30) days from the date of this order may result in a late payment penalty.

KRC/05-1268.int