

09-0982
INCOME
TAX YEARS: 2005-2007
SIGNED: 1-13-2011
COMMISSIONERS: R. JOHNSON, D. DIXON, M. CRAGUN
DISSENT: M. JOHNSON

BEFORE THE UTAH STATE TAX COMMISSION

<p>PETITIONER 1 & PETITIONER 2, Petitioners, v. AUDITING DIVISION OF THE UTAH STATE TAX COMMISSION, Respondent.</p>	<p>FINDINGS OF FACT, CONCLUSIONS OF LAW AND FINAL DECISION</p> <p>Appeal No. 09-0982 Account No. ##### Audit Period: 2005-2007 Tax Type: Income</p> <p>Judge: Phan</p>
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Presiding:
Jane Phan, Administrative Law Judge

Appearances:
For Petitioner: PETITIONER 1
For Respondent: RESPONDENT REP. 1, Assistant Attorney General
RESPONDENT REP. 2, Manager, Income Tax Auditing

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for a Formal Hearing on September 15, 2010, pursuant to the provisions of Utah Code Secs. 59-1-501 and 63G-4-204 et al. The matter is before the Commission on Petitioners' appeal of an audit deficiency for the tax years 2005 through 2007. Based upon the evidence and testimony presented at the hearing the Tax Commission hereby makes its:

FINDINGS OF FACT

1. This matter is before the Commission on Petitioners' (the "Taxpayers") appeal of interest deficiencies assessed against him for tax years 2005 through 2007. The Statutory Notices of Deficiency and Audit Change had originally been issued on February 9, 2009.

2. On March 30, 2009, after the Audits had been issued, the Taxpayer filed an amended Utah return for tax year 2007. Respondent (the "Division") amended its audit for that year based on the Taxpayer's amended return. The Division issued an amended Notice of Deficiency and Audit Change on April 29, 2009 which

indicated a \$\$\$\$ balance or no deficiency. Therefore, there are no further issues with the 2007 audit.

3. The Taxpayer does not dispute the audit tax due as indicated on either the 2005 or the 2006 tax return. The Taxpayer's issue with the audit is the interest. The Taxpayer argues as a matter of fairness or equity some or all of the interest should be abated. The amount of the deficiency indicated in the Statutory Notices for these years is as follows:

Year	Tax	Penalty	Interest	Total ¹
2005	\$\$\$\$	\$\$\$\$	\$\$\$\$	\$\$\$\$
2006	\$\$\$\$	\$\$\$\$	\$\$\$\$	\$\$\$\$

4. The facts were not in dispute. The Taxpayer had filed 2005 and 2006 state and federal returns as they became due. In 2007 the Taxpayer had made some expenditures that qualified for the historic preservation tax credit under Utah Code Sec. 59-10-1006(1)(a). The amount of credit for which he qualified was \$\$\$\$\$. This credit is a nonrefundable credit, whatever portion of the credit that may not be claimed in the year incurred may be carried forward for five years. This credit may not be carried backward to previous years.

5. For the 2007 year the Taxpayer could use only \$\$\$\$\$ of the historic preservation credit. The Taxpayer claimed \$\$\$\$\$ of the credit on his 2008 Utah Individual Income Tax Return and \$\$\$\$\$ of the credit on his 2009 income tax return.

6. The Taxpayer testified that he knew he would be getting a refund of most or all of his state withholding for the 2007 year because of this credit, so he asked his employer to change the state withholding in 2007. However, his employer indicated that they could not change the state withholding differently from what they were doing for his federal withholding. So they continued to withhold and pay over to Utah about \$\$\$\$\$ in withholding per month in 2007, 2008 and 2009. When the Taxpayer filed his returns for each of these years he was claiming the credit he received back from Utah for all of this withholding.

7. Sometime prior to February 2009 the Internal Revenue Service audited the Taxpayer's federal tax returns for the years 2005 through 2007 and disallowed some itemized deductions. The Tax Commission then made the change that flowed from this to the Taxpayer's Utah returns for 2005 and 2007. This resulted in the tax deficiencies stated on the original audit Notices for these years. The Taxpayer did not contest the change with the state of Utah and paid the tax portion of the audit for the years 2005 and 2006. For 2007 he filed an amended Utah return claiming on that return more of the historical preservation credit to offset the additional tax amount, which resulted in a \$\$\$\$\$ balance for that year.

¹ Interest as calculated to the date of the Statutory Notices.

APPLICABLE LAW

Section 59-1-402 of the Utah Code governs the assessment of interest, as follows, in pertinent part:

(4) (a) Except as provided in Subsection (4)(c), if any overpayment of tax or fee administered by the commission is refunded within 90 days after the last date prescribed for filing the return of such tax or fee, no interest shall be allowed on the overpayment.

(b) Except as provided in Subsection (4)(c), if the return is filed after the last date prescribed for filing the return, no interest shall be allowed on the overpayment if the overpayment is refunded within 90 days after the date the return is filed.

...

(5) Interest on any underpayment, deficiency, or delinquency of any tax or fee administered by the commission shall be computed from the time the original return is due, excluding any filing or payment extensions, to the date the payment is received.

The Commission has been granted the discretion to waive penalties and interest. Section 59-1-401(13) of the Utah Code provides:

Upon making a record of its actions, and upon reasonable cause shown, the commission may waive, reduce, or compromise any of the penalties or interest imposed under this part.

The Commission has promulgated Administrative Rule R861-1A-42 to provide additional guidance on the waiver of penalties and interest, as follows in pertinent part:

(2) Reasonable Cause for Waiver of Interest. Grounds for waiving interest are more stringent than for penalty. To be granted a waiver of interest, the taxpayer must prove that the commission gave the taxpayer erroneous information or took inappropriate action that contributed to the error.

ANALYSIS

The Taxpayer's point was that although he did owe additional tax for 2005 and 2006, by 2007 the state had this large balance on his account in the form of the credit and in the form of withholding. He understood that there was no legal provision that required the state to pay him interest on this balance or credit, but pointed out that the balance was substantially higher than the additional tax amounts assessed with the audits. It was the Taxpayer's position that the Commission should look at the right thing or the fair thing to do and waive the interest because by 2007 the state had his money to use in excess, monies that were deficient were always with the Tax Commission after 2007.

It was the Division's position that it understood the Taxpayer's argument on an equity basis but there was, however, no relief available under Utah law. The Division pointed out that the historic preservation tax was a nonrefundable credit and also one that could only be carried forward. So the Taxpayer could not have obtained a refund of all the credit on his 2007 return, or have claimed the credit on his 2005 or 2006 returns. The Division pointed out that because this was a credit, no interest accrued. Further, the Division explained that Taxpayers are not entitled to interest payments on their over withholding. It was the representatives' assertion that if interest were to be paid, taxpayers would withhold more on purposes as an investment. The Division pointed out that there was nothing in state law that required an employer to use the same withholding factors for the state as they do the federal. It was the Division's assertion that the Taxpayer's employer had refused to do this because of its own internal policies.

The Division cited to Utah Admin. Rule R861-1A-42(2) as the basis for denial of the waiver of interest. The rule provides that interest would be waived if the taxpayer showed that a commission employee gave him erroneous information or took inappropriate actions that contributed to the error. There was no showing of this on the part of the Tax Commission. The Division also asserted that the basis relied on in the Commission's Initial Hearing decision had been erroneous and the Taxpayer did not disagree with this contention.

CONCLUSION OF LAW

1. The historic preservation credit that the Taxpayer had qualified for in 2007 was a non refundable credit and could not be carried back to tax years 2005 and 2006. See Utah Code Sec. 59-10-1006. The Taxpayers claimed a refund of the portion of the credits that they could obtain on their 2007 original return and received the refund sometime within 90 days of the April 15, 2008 filing of that return. After the audit had been issued, the Taxpayer filed an amended 2007 tax return on which he claimed additional credits to offset the additional tax liability that he had reported on the return. As noted by the parties, there was no refund associated with the Taxpayer's amended return. The Commission agrees with the Division that the Taxpayer was not entitled to interest on the credits or on his over withholding under Utah Code Sec. 59-1-402.

2. The Taxpayer argues that based on equity or fairness the interest should be abated. The applicable rule governing the waiver of interest does not provide for waiver based on equity. Utah Admin. Rule R861-1A-42(2) expressly limits cause for waiver of interest to Commission employee error. The rule distinguishes waiver of penalties from waiver of interest and provides a number of factors for which penalties may be waived including equitable considerations at Subsection 42(4). It is clear that these considerations only apply to penalties. Based on these express provisions the Commission may not consider equity or fairness in determining whether interest should be waived.

3. However, although there is no reasonable cause basis for waiver of interest under the factors in this

matter, there was an overpayment for a brief period of time² on the Taxpayers' account during which interest was charged. Utah Code Sec. 59-1-402(5) states, "Interest on any underpayment, deficiency, or delinquency of any tax or fee administered by the commission shall be computed from the time the original return is due, excluding any filing or payment extensions, to the date the payment is received." Clearly there was an underpayment from the time the 2005 and 2006 taxes were due up to when this overpayment occurred. The Taxpayer's position was that there were more than sufficient funds paid in to his account to cover the 2005 and 2006 deficiencies in 2007 because of withholding and the historic preservation tax credit. The Commission concludes, however, that withholding and the preservation credit are not payments to the Taxpayers' specific account until the Taxpayers filed and claimed these on their original 2007 income tax return, which was on or around April 15, 2008. Once that return was filed and until the refund that the Taxpayer had claimed on the return was issued, there was a \$\$\$\$ credit on the Taxpayer's account, which was far more than the \$\$\$\$ in combined tax deficiency that was the subject of the audits for 2005 and 2006. However, when the refund for the 2007 tax year claimed on the Taxpayer's original return was paid out to the Taxpayer, which was apparently within 90 days of the date the return was filed, there would no longer have been an overpayment on the Taxpayer's account. Interest should be waived for the period of overpayment, which occurred between the filing of the Taxpayers' 2007 original return and the date the refund was issued that was claimed on the return.

DECISION AND ORDER

Based on the foregoing, the Tax Commission abates the portion of the interest accruing for the 2005 and 2006 tax audits from the time the Taxpayer filed his 2007 original return on April 15, 2008, until the time the refund claimed on that return was issued to the Taxpayer. Interest that accrued prior to this period and the interest that accrued after this period until the audit deficiency was paid by the Taxpayer is sustained. The Division is to recalculate the amount of interest on this basis. It is so ordered.

DATED this ____ day of _____, 2011.

R. Bruce Johnson
Commission Chair

D'Arcy Dixon Pignanelli
Commissioner

Michael Cragun
Commissioner

DISSENT

I respectfully disagree with my colleagues' decision to waive the portion of interest that accrued from the

² See Tax Commission Order in Appeal No. 05-1164.

time the Taxpayers filed their 2007 return to when the 2007 refund was issued based on that return. Utah Code Sec. 59-1-402(5) provides that interest is assessed on a deficiency from the time the original return was due to the date payment is received. My colleagues' position would broadly interpret this provision to indicate that whenever there is an overpayment on an account, regardless of whether the overpayment was for other tax years, a deficiency would be considered paid. They cite to Tax Commission Appeal No. 05-1164 as precedence for this decision. I would note that the facts in Appeal No. 05-1164 were dissimilar, that case involved only one tax year, with the Taxpayer making a prepayment for the 2002 tax year by April 15, 2003, then not filing a return for 2002 until January 16, 2004. Based on the return the taxpayer received a refund on January 29, 2004. The 2002 year was later audited and the Taxpayer required to pay back a portion of the refund. In the audit the Division had assessed interest going back to April 15, 2003. In Appeal No. 05-1164 the Commission determined interest for the 2002 deficiency should have only been assessed back to January 29, 2004, because there had not been an underpayment prior to that date for the tax period 2002.

I find the Division's interpretation and application of Utah Code Sec. 59-1-402(5) reasonable in this case. The audit deficiency was not paid until a payment relating to that deficiency was received. Further, I would point out that this Commission adopted a rule that expressly limits when interest may be waived. There was no showing of error or inappropriate action on the part of the Tax Commission, which is the only basis for waiver of interest. Based on this rule the Commission may not waive interest for equitable considerations. *See* Utah Code Sec. R861-1A-42.

Marc B. Johnson
Commissioner

Notice: Failure to pay within thirty days the balance that results from this order may result in additional penalties and interest. You have twenty (20) days after the date of this order to file a Request for Reconsideration with the Tax Commission Appeals Unit pursuant to Utah Code Sec. 63G-4-302. A Request for Reconsideration must allege newly discovered evidence or a mistake of law or fact. If you do not file a Request for Reconsideration with the Commission, this order constitutes final agency action. You have thirty (30) days after the date of this order to pursue judicial review of this order in accordance with Utah Code Sec. 59-1-601 et seq. & 63G-4-401 et seq.