

13-2245
TAX TYPE: INCOME TAX
TAX YEAR: 2010
DATE SIGNED: 11-17-2014
COMMISSIONERS: J. VALENTINE, M. CRAGUN, R. PERO
EXCUSED: D. DIXON

BEFORE THE UTAH STATE TAX COMMISSION

TAXPAYER-1 AND TAXPAYER-2, Petitioners, vs. AUDITING DIVISION OF THE UTAH STATE TAX COMMISSION, Respondent.	INITIAL HEARING ORDER Appeal No. 13-2245 Account No. ##### Tax Type: Income Tax Tax Year: 2010 Judge: Marshall
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Presiding:

Jan Marshall, Administrative Law Judge

Appearances:

For Petitioner: TAXPAYER-1, *Pro Se*
TAXPAYER-2, *Pro Se*
For Respondent: REPRESENTATIVE FOR RESPONDENT, Assistant Attorney
General
RESPONDENT, Income Tax Audit Manager

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission on July 2, 2014 for an Initial Hearing in accordance with Utah Code Ann. §59-1-502.5. The Petitioners (“Taxpayers”) are appealing an audit assessment by the Respondent (“Division”). The Division assessed tax in the amount of \$\$\$\$\$, and interest in the amount of \$\$\$\$\$ through November 16, 2013. Interest continues to accrue on any unpaid balance.

APPLICABLE LAW

State taxable income is defined in Utah Code Ann. §59-10-103(1)(w)¹ as follows:

- (i) subject to section 59-10-1404.5, for a resident individual, means the resident individual’s adjusted gross income after making the:

¹ The Utah Individual Income Tax Act has been revised and provisions renumbered subsequent to the audit period. The Commission cites to and applies the provisions that were in effect during the audit period on substantive legal issues.

- (A) additions and subtractions required by Section 59-10-114; and
- (B) adjustments required by Section 59-10-115...

Utah Code Ann. §59-10-115 allows for an equitable adjustment as set forth below:

- (1) The commission shall allow an adjustment to adjusted gross income of a resident or nonresident individual if the resident or nonresident individual would otherwise:
 - (a) receive a double tax benefit under this part; or
 - (b) suffer a double tax detriment under this part...

The Internal Revenue Code sets forth provisions for the repayment of a “claim of right” in 26 U.S.C §1341(a), as follows in pertinent part:

If –

- (1) an item was included in gross income for a prior taxable year (or years) because it appeared that the taxpayer had an unrestricted right to such item;
- (2) a deduction is allowable for the taxable year because it was established after the close of such prior taxable year (or years) that the taxpayer did not have an unrestricted right to such item or to a portion of such item; and
- (3) the amount of such deduction exceeds \$3,000, then the tax imposed by this chapter for the taxable year shall be the lesser of the following:
 - (4) the tax for the taxable year computed with such a deduction; or
 - (5) an amount equal to –
 - (A) the tax for the taxable year computed without such deduction, minus
 - (B) the decrease in tax under this chapter (or the corresponding provisions of prior revenue laws) for the prior taxable year (or years) which would result solely from the exclusion of such item (or portion thereof) from gross income for such prior taxable year (or years).

The burden of proof is placed upon the taxpayer, in accordance with Utah Code Ann. §59-1-1417, as follows in relevant part:

In a proceeding before the commission, the burden of proof is on the petitioner...

DISCUSSION

The Division issued a Notice of Deficiency and Audit Change on October 17, 2013 on the Taxpayer’s 2010 individual income tax return. The audit disallowed an equitable adjustment taken by the Taxpayer in the amount of \$\$\$\$\$, which resulted in an increase in tax liability by \$\$\$\$\$.

The Taxpayer’s wife received social security benefits in 2009 in the amount of \$\$\$\$\$. The Taxpayer maintains they repaid the amount to the Social Security in 2009; however, the amount was not credited as a repayment until 2010. The Taxpayer’s originally filed their 2009 return to exclude the Social Security income; however, when instructed by the IRS that the income must be included, the Taxpayer filed an amended state return to match the federal changes. The Taxpayer’s original 1099 from Social Security for the 2010 tax year did not include

the repayment, and the Taxpayer filed state and federal returns based on that 1099. The Taxpayer later received a corrected 1099 from Social Security reflecting the repayment, and filed amended state and federal returns. On their federal return, the Taxpayer took a refundable credit to account for the repayment. On their state return, the Taxpayer took an “equitable adjustment” to account for the repayment.

The Taxpayer stated that they got “squeezed” between the Social Security Administration and the IRS. He stated that they filed the amended tax return to the best of their knowledge. He stated that they tried to treat the amended returns for the 2010 tax year equally between the Federal and the State. He stated that the equitable adjustment amount was exactly the same as the amount that was added on their 2009 amended return, so the two years should be a wash. The Taxpayer believes fairness and equity are on their side.

The Taxpayer noted that the Division had included in their information a prior Tax Commission case, Appeal No. 09-2968. The Taxpayer argued that their case is different; he noted that they only received money in 2009 and repaid it the same year. He argued they did not have the income and should not have been assessed tax on it. He noted that the IRS has not made any adjustments to their 2010 amended return, whereas they did in the prior Tax Commission decision. He argues that they are being charged state income tax on income that they never received.

The Division’s representative explained that the Division disallowed the equitable adjustment. She noted that there is not a dispute as to the facts of the case, only as to whether the equitable adjustment was appropriate. She stated that the Social Security benefits were included only once, for the 2009 tax year. They were not included on the 2010 tax year, thus the Taxpayer is not being taxed twice on the same income. The Division’s representative explained that had the Taxpayers treated the repayment as an itemized deduction, rather than taking it as a credit on their federal return, the reduction in income would have flowed through on the State return. She noted that Tax Commission Appeal No. 09-2968 is similar, and upholds the Division’s position that the equitable adjustment should be disallowed. She noted that there is no statutory provision that would allow for the Taxpayer to take an equitable adjustment in this circumstance.

The Utah Code does not have a provision that specifically addresses a “claim of right”. Thus, in order for a taxpayer to receive a reduction in their Utah “taxable income” in the year of repayment, the taxpayer must elect to take either a deduction under Internal Revenue Code §1341(a)(4) or a credit under Internal Revenue Code §1341(a)(5).

The Taxpayer argues it is not equitable to tax them on the funds they had to repay. However, this is not a situation where the Social Security income is being taxed twice for state

income tax purposes. The income was included only once in the Taxpayer's federal adjusted gross income, in 2009. It was not included again in the Taxpayer's 2010 federal adjusted gross income. The Taxpayers took the tax credit under Internal Revenue Code §1341(a)(5), presumably because it was more advantageous on their federal tax return. Had the Taxpayers taken the repayment as an itemized deduction on their 2010 federal return, the lower federal adjusted gross income would have flowed through onto their state return. The audit assessment should be sustained.

Jan Marshall
Administrative Law Judge

DECISION AND ORDER

Based on the foregoing, the Commission sustains the audit assessment of tax and interest on the Taxpayer's individual income tax return for the 2010 tax year. 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 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 _____, 2014.

John L. Valentine
Commission Chair

D'Arcy Dixon Pignanelli
Commissioner

Michael J. Cragun
Commissioner

Robert P. Pero
Commissioner

Notice of Payment Requirement: Any balance due as a result of this order must be paid within thirty (30) days of the date of this order, or a late payment penalty could be applied.