14-1635
TAX TYPE: CIRCUIT BREAKER TAX ABATEMENT
TAX YEAR: 2014
DATE SIGNED: 3-30-2015
COMMISSIONERS: J. VALENTINE, M. CRAGUN, R. PERO
EXCUSED: D. DIXON
GUIDING DECISION

BEFORE THE UTAH STATE TAX COMMISSION

| | |
|---|---|
| PETITIONER,<br><br>Petitioner,<br><br>vs.<br><br>COUNTY-1 COUNCIL/TAX ADMINISTRATION, UTAH,<br><br>Respondent. | **INITIAL HEARING ORDER**<br><br>Appeal No. 14-1635<br><br>Tax Type: Circuit Breaker Tax Abatement<br>Tax Year: 2014<br><br>Judge: Phan |

**Presiding:**
Jane Phan, Administrative Law Judge

**Appearances:**
For Petitioner: PETITIONER
REPRESENTATIVE FOR PETITIONER, Accountant
For Respondent: RESPONDENT, Tax Relief/Deferral Program Coordinator, COUNTY-1 Tax Administration

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission on February 2, 2015, for an Initial Hearing in accordance with Utah Code §59-1-502.5. Petitioner ("Property Owner") had filed an appeal of the denial by COUNTY-1 Tax Administration to allow Circuit Breaker Property Tax Relief.

APPLICABLE LAW

The Counties are authorized to provide Circuit Breaker Property Tax Relief at Utah Code Sec. 59-2-1208 as follows:

> (1)(a) Subject to Subjections (2) and (4), for calendar years beginning on or after January 1, 2007, a claimant may claim a homeowner's credit that does not exceed the following amounts . . .

The amount of the credit provided is based on "household income". "Household income" and "income" are defined at Utah Code Sec. 59-2-1202(5)&(6) as follows:

(5) "Household income" means all income received by all persons of a household in: (a) the calendar year preceding the calendar year in which property taxes are due . . .

(6)(a)

(i) "Income" means the sum of: (A) federal adjusted gross income as defined in Section 2, Internal Revenue Code; and (B) all nontaxable income as defined in Subsection (6)(b).

(ii) "Income" does not include: (A) aid, assistance, or contributions for a tax exempt nongovernmental source; (B) surplus foods; (C) relief in kind supplied by a public or private agency; or (D) relief provided under this part, Section 59-2-1108, or Section 59-2-1109.

(b) For purposes of Subsection (6)(a)(i), "nontaxable income" means amounts excluded from adjusted gross income under the Internal Revenue Code, including:

(i) capital gains; (ii) loss carry forwards claimed during the taxable year in which a claimant files for relief under this part, Section 59-2-1108, or Section 59-2-1109; (iii) depreciation claimed pursuant to the Internal Revenue Code by a claimant on the residence for which the claimant files for relief under this part, Section 59-2-1108, or Section 59-2-1109; (iv) support money received; (v) nontaxable strike benefits; (vi) cash public assistance or relief; (vii) the gross amount of a pension or annuity, including benefits under the Railroad Retirement Act of 1974, 45 U.S.C. Sec. 231 et seq., and veterans disability pensions; (viii) payments received under the Social Security Act; (ix) state unemployment insurance amounts; (x) nontaxable interest received from any source; (xi)workers' compensation; (xii) the gross amounts of "loss of time" insurance; and (xiii) voluntary contributions to a tax-deferred retirement plan.

## DISCUSSION

The Property Owner had timely filed an application to the COUNTY-1 Treasurer for the 2014 Circuit Breaker Property Tax Abatement and the request was denied on the basis that the Property Owner's 2013 household income was over the limit of $$$$$ set in the statute. She then appealed that denial to the COUNTY-1 Property Tax Committee which upheld the denial by the Treasurer's Office, on the basis that it had disallowed the deduction from her household income of business losses the Property Owner had incurred as a real estate agent. It was the disallowance of the deduction for these losses that put her income over the statutory threshold. However, the COUNTY-1 Property Tax Committee did recommend approval of Hardship Tax Relief, that recommendation was approved by the County Council and is not an issue herein. The Property Owner timely appealed the denial of the Circuit Breaker Property Tax Abatement to the Utah State Tax Commission and the matter proceeded to the Initial Hearing.

The Property Owner had provided a copy of her 2013 U.S. Individual Income Tax Return and the amount of federal adjusted gross income she had claimed on the return had been $$$$$. Her federal adjusted gross income was based on the $$$$$ in taxable pensions and annuities she had received during 2013. She had made a deduction on Line 12 for $$$$$ in business loss from the current year from Schedule C, and a deduction on Line 13 for $$$$$ in capital loss. These two different losses offset a portion of the $$$$$ income, leaving the Property Owner with only the $$$$$ in federal adjusted gross income.

It was the Schedule C business loss that is at issue in this hearing. The business loss was a result from the Property Owner's real estate business in the current year. The County argued that the Property owner had a loss on her real estate business for the last six years in a row and had concluded it was a hobby loss rather than a business loss. It was the County's position that as a hobby loss the Property Owner had improperly deducted the loss on her federal return, because she would not be qualified to take this loss under federal law. Therefore, the County concluded that the $$$$$ Schedule C business loss should be added back to the federal adjusted gross income that she claimed on her return.

That the Line 13 $$$$$ capital loss would be added to the federal adjusted gross income was not in dispute because this was a loss carry forward from prior years and is added to the federal adjusted gross income by operation of Utah Code Sec. 59-2-1202(6)(a)(i). The Property Owner had also received $$$$$ in nontaxable social security benefits in 2013. Like the loss carry forward, the nontaxable social security benefits are added to the federal adjusted gross income by operation of Utah Code Sec. 59-2-1202(6)(a)(i). The County concluded that the Property Owner's household income was $$$$$. This is calculated by taking the $$$$$ in federal adjusted gross income which she had claimed on her return, then adding to that the $$$$$ in claimed Schedule C business loss, the $$$$$ capital loss carry forward and the $$$$$ in nontaxable social security benefits.

It was the Property Owner's contention that the County should not have added back her Schedule C business loss. If this loss of $$$$$ had not been added back it would indicate a household income of $$$$$, below the household income cut off for Circuit Breaker Property Tax Abatement. The Property Owner states that her real estate business was, in fact, a business and not a hobby. The Property Owner had started the business about 16 years ago after her husband died and she needed to earn a living. The Property Owner's representative explained that she had made $$$$$ to $$$$$ per year in this business in the late 1990's and early 2000's. But with the market slump in 2008 her sales plummeted. She had no sales in 2008 and losses every year from 2008 forward. She had 1 sale in 2009, 0 sales in 2010, 1 sale in 2011, 1 sale in 2012 and none in

2013. The Property Owner is still working, listing properties showing properties and having to maintain her licensing which includes both annual fees and hours of training. She has to pay monthly broker fees and Multiple Listing fees. During 2013 she had three listings that she was trying to sell. Two were residential properties and one was a commercial property, but she had no sales that closed during that year. She said one of the residential properties she had thought she sold on two separate occasions but neither buyer was able to obtain financing. The Property Owner states that she is ##### years old and is working 800 to 1000 hours per year towards this business.

The Property Owner's representative also notes that she has claimed this as a Schedule C business loss on her Federal Individual Income Tax Returns for 2013 and prior years and the IRS has never questioned this deduction.

The representative for the County argues that due to the fact that there were six years of losses it appeared to the County that this was a Hobby Loss under IRS regulations and not a business loss. The County did not cite to any IRS regulations, but did provide in its Reply to the appeal that the County had reviewed information from the Internal Revenue Service Website regarding business and hobby loss and IRS FS-2007-18, dated April 2007, states, "The IRS presumes tha[t] any activity is carried on for profit if it makes a profit during at least three of the last five tax years, including the current year."[1] The County acknowledges that the Property Owner had claimed this as a business loss on her federal returns, therefore, it was not included in her adjusted gross income. This is not one of the items of "nontaxable income" that is added to federal adjusted gross income under Utah Code Sec. 59-2-1202 (6) for purposes of determining "household income." It was the County's contention under federal law the Property Owner did not qualify to deduct her claimed Schedule C business loss on her federal return and the reason that it had not been disallowed by the IRS was that the IRS had just not audited the Property Owner's returns.

The representative for the Property Owner pointed out that what the County was referring to was the IRS's presumption that if there was a profit in three of the last five years it would be considered a business activity carried on for profit, but that a taxpayer could still show the activity was a for profit business by looking at a number of other factors.

Deciding whether or not a business activity is carried on for profit under IRS regulations is more complicated than just determining whether there was a profit during at least three of the last five tax years. If there had been a profit during at least three of the last five years it would have fallen within the IRS's safe harbor provision. Although neither side provided the provision

[1] Respondent's County Tax Relief Appeal Reply, pg. 1.

nor any information in detail, the relevant section is IRC §183. Under that section it is necessary to determine if the taxpayer operates an activity with an actual and honest profit motive. To make this determination there are nine non-exclusive factors at Treas. Reg. §1.183 as follows:[2]

1. The manner in which the taxpayer carried on the activity,
2. The expertise of the taxpayer or his or her advisors,
3. The time and effort expended by the taxpayer in carrying on the activity,
4. The expectation that the assets used in the activity may appreciate in value,
5. The success of the taxpayer in carrying on other similar or dissimilar activities,
6. The taxpayer's history of income of loss with respect to the activity,
7. The amount of occasional profits, if any, which are earned,
8. The financial status of the taxpayer, and
9. Elements of personal pleasure or recreation.

For purposes of determining the Property Owner's "household income" under Utah Code Sec. 59-2-1209, the County is second guessing or overriding what the Property Owner had claimed on her federal tax return for the 2013 year. The County argues what the Property Owner claimed was improper, regardless that the return has never been questioned by the IRS. Further, in doing so, the County applies a determination based only on the safe harbor provision and not the other factors relevant to IRC §183. Considering the wording of the Utah statutes on the Circuit Breaker Property Tax Abatement provisions they do not expressly state that the County must go by the federal adjusted gross income as claimed by the property owner on his or her federal return. Utah Code Sec. 59-2-1202(5) provides that "household income" is all "income". "Income" is defined at Utah Code Sec. 59-2-1202(5) to be "the sum of . . . federal adjusted gross income as defined in Section 62, Internal Revenue Code . . . and . . . all nontaxable income as defined in Subsection (6)(b)." These provisions do provide a basis for the County to argue that regardless of what a property owner has claimed on his or her return, it is not federal adjusted gross income as defined in Section 62. However, if the County is going to make this inquiry, consideration should be given to the full provisions of the federal law, with some deference to how a person has filed his or return and whether or not the return has been questioned by the IRS.

In this matter, the Property Owner did meet many of the nine factors noted above, although the Tax Commission cannot say for certainty how the IRS would rule on this question if it were to review it. The manner in which the taxpayer carried on the activity seemed to be spending considerable hours at work and keeping up the extensive licensing requirements and other costs. This was her area of expertise, as it was her only career for 16 years. She did spend considerable time and effort. She had success in carrying on this business previously and there

[2] This is the list provided at www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/IRC-183-Activities.

was no indication that she had tried other business actives. Yes, recently she had had losses, but overall she had considerable income from this business. There had been profits in this business which were substantial compared to her other income. Regarding the financial status of the Property Owner, in the past when she made considerable money from the business, she may or may not have received retirement or social security at that time. Now she does have retirement and social security income. The amount of the losses she has claimed are just over %%%%% of the income she received from retirement and social security. The last factor is elements of personal pleasure or recreation. The Property Owner could be maintaining this business just for fun or to have something to do. It does seem like quite a bit of effort on her part due to the licensing requirements if that is the case.

Given the fact that the Property Owner claimed this deduction on her federal return, which she signed under penalty of perjury and if inaccurate could be subject to penalties or even criminal charges, the deduction has not been questioned by the IRS and she does have a basis meeting a reasonable amount of the nine factors set out at Treas. Reg. §1.183, the County should accept the federal adjusted gross income that the Property Owner had claimed on her return when the County calculates her household income. The County should start with the Property Owner's federal adjusted gross income of $$$$$, add the $$$$$ loss carry forward and the $$$$$ in social security income based on Utah Code Sec. 59-2-1202(6), which results in $$$$$ in "household income". The County should calculate the amount of the Circuit Breaker Property Tax Abatement on that basis.

Jane Phan
Administrative Law Judge

## DECISION AND ORDER

Based on the foregoing, the Commission finds that the Property Owner's Circuit Breaker Property Tax Abatement credit should be recalculated based on the "household income" of $$$$$. The COUNTY-1 Auditor is hereby ordered to adjust its records accordingly. 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, or emailed, 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

or emailed to:

taxappeals@utah.gov

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

DATED this _____day of _____, 2015.

John L. Valentine
Commission Chair

D'Arcy Dixon Pignanelli
Commissioner

Michael J. Cragun
Commissioner

Robert P. Pero
Commissioner