



**MULTISTATE TAX COMMISSION**

*Maximizing the synergies of multi-state tax cooperation*

**To: MTC Uniformity Committee**

**From: Sheldon H. Laskin, Counsel**

**Date: March 3, 2017**

**Subject: Joint Request from COST, TEI, the ABA SALT Committee, and the AICPA State Tax Working Group to Update the MTC's Model Uniform Statute for Reporting Adjustments to Federal Taxable Income**

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The purpose of this memo is to provide the Committee with a comparison of the provisions of the State Tax Working Group's proposed Model Uniform Statute for Reporting Adjustments to Federal Taxable Income (hereafter, "Working Group Model") with the provisions of the Commission's Model Uniform Statute for Reporting Federal Tax Adjustments. Both models are attached.

The Working Group Model is generally consistent with the Commission's model, with the following significant differences.

### **1. Definition of Final Determination**

The Working Group Model provides a considerably more detailed definition of the term "final determination" than does the Commission's model.

The Commission model defines "final determination" as:

- (a) the allowance of a refund or credit under Section 6407 of the Internal Revenue Code of 1986; or
- (b) the official act of assessment under Section 6203 of the Internal Revenue Code of 1986, except assessments that result from the following shall not be considered final determinations:
  1. tax under a partial agreement,
  2. tax in jeopardy, and
  3. advance payments; or
- (c) a final denial of a refund claim where a state refund claim has been filed or any other final action by the Internal Revenue Service that increases or decreases the state tax liability of a taxpayer for any tax year.

The Working Group Model defines “final determination” as:

“Final determination” shall mean and be deemed to occur when the last of any of the following events has occurred with respect to a taxpayer’s federal taxable year, except for entities filing unitary or other types of combined or consolidated returns with the [State Agency], “final determination” shall be based upon the occurrence of the last of such events for all members of the group:

- (a) The taxpayer: (i) has final adjustments to its federal taxable income resulting from an examination by the IRS pursuant to Section 7601 of the IRC, including any requisite review by the Joint Committee on Taxation pursuant to Section 6405 of the IRC; and (ii) has not filed a petition for redetermination with the United States Tax Court pursuant to Sections 6213 or 6226 of the IRC or a claim for refund with a district court or the United States Court of Federal Claims pursuant to Sections 6226 or 7422 of the IRC, and the time for the taxpayer to timely file such a petition for redetermination or such a claim for refund has lapsed under the applicable statute;
- (b) The taxpayer and the IRS have executed the forms necessary for the relevant tax period so as to establish finality under Section 7121(b) the IRC;
- (c) The time for the IRS to make an assessment for the relevant tax period has expired pursuant to Section 6501 of the IRC; or
- (d) A judgment from a United States court, or any other court of original jurisdiction to which the United States has submitted to personal jurisdiction regarding a taxpayer’s tax issues, has become final under Section 2412(d)(2)(G) of Title 28 of the United States Code.

It is possible that the detailed definition of “final determination” in the Working Group Model may present either policy or technical issues for some states if those states define “final determination” somewhat differently.

## **2. De minimis adjustments**

The Commission model does not have a provision addressing *de minimis* federal adjustments.

Section B.(2) of the Working Group Model governs *de minimis* federal adjustments of less than \$250, excluding interest and penalties or *de minimis* refunds in the same amount. The taxpayer would have the option of reporting *de minimis* adjustments to the state on a form prescribed by the State, in lieu of filing a report of federal adjustments. This form is to be provided within 180 days following the date of the final determination. The notice shall contain information reasonably necessary to provide the State with an understanding of the federal changes and their impact on the taxpayer’s state tax liability.

If the taxpayer filed a *de minimis* adjustment notice, the state would have the right to request that the taxpayer file the report of federal adjustments instead. The state must do so within the later of 180 days following the date on which the taxpayer provided the *de minimis* notice or the expiration of the normal limitations period specified in the state statute. The taxpayer would then have 180 days of the date on which the state’s request is postmarked (*query*: would electronically conveyed requests count?) in which to file a report of federal adjustments.

The proposed model sets forth two alternatives regarding the treatment of the *de minimis* notice if the State does not request a report of federal adjustments. Option 1 is that the *de minimis* adjustments are deemed accepted by the State. Option 2 also provides that the *de minimis* adjustments are deemed to be accepted and the State may assess and bill the taxpayer the fixed sum of \$250 if the taxpayer reported that it would have owed the State a *de minimis* amount of tax.

Finally, where the taxpayer has filed a notice of *de minimis* adjustments that has been deemed accepted, the taxpayer shall not be subject to additional assessment, absent fraud, nor allowed to file a refund claim, provided that the statute of limitations for issuing an assessment has expired.

### **3. Time for Issuing Assessments of Additional Tax Arising From Adjustments to Federal Taxable Income**

Section C of the Working Group Model governs the time within which the State may assess additional tax, depending on whether or not the taxpayer has filed a timely report of federal adjustments. For the most part, these provisions track the provisions of the Commission's model set forth at Section A 3(a) and (b) of the Commission's model. However, Section C(2)(d) provides an additional outermost limitation on the time to issue an assessment if the taxpayer failed to timely file a report of federal adjustments. Absent fraud, the maximum period for issuing an assessment in such cases would be 6 years following the date of the final determination regarding the federal adjustments.

### **4. Estimated State Tax Payments During Federal Audit**

The Commission's model does not provide for estimated payment of state taxes. Section D of the Working Group Model allows taxpayers to make an estimated payment of state taxes that may be due as a result of an ongoing federal audit. Any estimated payments made would be credited against any final tax liability ultimately determined to be due to a State and would limit the accrual of further interest on the estimated amount paid. The taxpayer shall be entitled to a refund or credit of any excess state tax ultimately determined to be due as a result of any federal adjustments (or if there are no federal adjustments), provided the taxpayer has filed a report of federal adjustments or claim for refund within one year following the final determination date.

### **5. Scope of Adjustments**

Section F of the Working Group Model limits state tax adjustments made after the expiration of the State's normal statute of limitations for assessment and refund to changes to the taxpayer's state tax liability arising directly from adjustments to the taxpayer's federal taxable income. (NOTE: this provision would bar a state from offsetting any refund due as a result of the federal adjustments by any additional tax due for reasons other than the federal adjustments.). The Commission's model does not have an analogous provision.

## Supplemental Information

In response to a request from General Counsel Helen Hecht, I prepared the following answers to the indicated questions. In addition, I began a survey of the states to determine what the current state practices are in reference to the treatment of advance estimated state tax payments before proposed federal tax adjustments are finalized.

### **A. What event at the federal level requires the taxpayer to amend the state return or take some other action to report a related state tax liability/file a claim for refund?**

#### 1. The MTC Model

- (a) the allowance of a refund or credit under Section 6407 of the Internal Revenue Code of 1986; or
- (b) the official act of assessment under Section 6203 of the Internal Revenue Code of 1986, except assessments that result from the following shall not be considered final determinations:
  - 1. tax under a partial agreement,
  - 2. tax in jeopardy, and
  - 3. advance payments; or
- (c) a final denial of a refund claim where a state refund claim has been filed or any other final action by the Internal Revenue Service that increases or decreases the state tax liability of a taxpayer for any tax year.

#### 2. The COST model

When the last of any of the following events has occurred with respect to a taxpayer's federal taxable year, except for entities filing unitary or other types of combined or consolidated returns with the [State Agency], "final determination" shall be based upon the occurrence of the last of such events for all members of the group:

- (a) The taxpayer:
  - (i) has final adjustments to its federal taxable income resulting from an examination by the IRS pursuant to Section 7601 of the IRC, including any requisite review by the Joint Committee on Taxation pursuant to Section 6405 of the IRC; and
  - (ii) has not filed a petition for redetermination with the United States Tax Court pursuant to Sections 6213 or 6226 of the IRC or a claim for refund with a district court or the United States Court of Federal Claims pursuant to Sections 6226 or

7422 of the IRC, and the time for the taxpayer to timely file such a petition for redetermination or such a claim for refund has lapsed under the applicable statute;

- (b) The taxpayer and the IRS have executed the forms necessary for the relevant tax period so as to establish finality under Section 7121(b) the IRC;
- (c) The time for the IRS to make an assessment for the relevant tax period has expired pursuant to Section 6501 of the IRC; or
- (d) A judgment from a United States court, or any other court of original jurisdiction to which the United States has submitted to personal jurisdiction regarding a taxpayer's tax issues, has become final under Section 2412(d)(2)(G) of Title 28 of the United States Code.

**B. How long does the taxpayer have from the triggering events described in A., above, to file an amended return or take some other action ?**

Both the MTC and the COST model provide that the taxpayer must take action within 180 days of the final federal action.

**C. Does a state allow a taxpayer to make an estimated payment of tax to stop the accrual of interest?**

1. The MTC model has no such provision.

2. The COST model.

A taxpayer may make estimated payments to the [State Agency] of the [State] tax that it determines may ultimately be owed to [State] as a result of a pending IRS audit, prior to a final determination for a tax year, without filing a report of federal adjustments with the [State Agency]. The estimated [State] tax payments shall be credited against any tax liability ultimately found to be due to [State] ("final tax liability") and limit the accrual of further statutory interest on that amount. If the estimated [State] tax payments exceed the final [State] tax liability and statutory interest ultimately determined to be due on that amount, or the IRS ultimately does not make any adjustments to the taxpayer's federal taxable income, the taxpayer shall be entitled to a refund or credit for the excess, provided the taxpayer files a report of federal adjustments or claim for refund or credit of [State] tax pursuant to [citation to State statute setting forth claim for refund requirements] within one (1) year following the final determination date.

**D. Current state practices regarding advance payment of estimated state tax following reporting of federal adjustments.**

The MTC is conducting a survey of the states to see what their current practices are regarding the treatment of advanced tax payments of estimated state tax following reported federal tax adjustments. Only two states have answered to date, but the results are summarized here.

*Does your state allow taxpayers who have received a notice of a proposed federal tax adjustment (RAR report) to make an estimated advance payment of some or all of any state tax that may be due once the federal adjustment is final?*

CT: Yes

NJ: Yes

*If yes, please also answer these three questions:*

- 1. If the taxpayer ultimately does not owe any additional state tax as a result of the federal tax adjustment, does your state pay interest on any overpayment of state tax as a result of the estimated payment?*

CT: Very rarely do we encounter overpayments with respect to RAR adjustments. The population is stratified and they are run through a tax calc. Only those taxpayers that have a balance due are contacted with a notice of proposed amount due. Our refund interest provision only applies to situations where there is a claim for refund. Therefore, in the rare instance where the taxpayer has overpaid on an RAR adjustment, refund interest would not be paid.

NJ: No, NJ would only pay interest on any overpayment if the overpayment was not paid within 6 months of the claim for refund. The interest would only accrue from the date of claim not the date of payment.

- 2. If you pay interest on the overpayment, does your state abate the accrual of interest on an estimated advance partial payment of a state tax deficiency later determined to be due after the federal adjustment is final?*

CT: This situation would not be encountered with our current workflow.

NJ: Yes, the advance payment would stop the accrual of interest on that amount of eventual tax due.

3. *How does your state account for the estimated advance payment before the federal adjustment is final? For example, if the proposed federal adjustment is for multiple years, in what order would you assign the estimated advance payments?*

CT: The advance payment is posted to the taxpayers account and the payment will suspend until the matter is resolved. Audit staff will apply the payments to the appropriate tax years in accordance with the RAR adjustments.

NJ: Unless the taxpayer designated the amount for each year we would apply the payments against the earliest liability years first.