

BEFORE THE STATE BOARD OF TAX APPEALS
STATE OF ARIZONA
100 North 15th Avenue - Suite 140
Phoenix, Arizona 85007
602.364.1102

VERNA POPE,

Appellant,

vs.

ARIZONA DEPARTMENT OF REVENUE,

Appellee.

Docket No. 1952-06-1

NOTICE OF DECISION
FINDINGS OF FACT AND
CONCLUSIONS OF LAW

The State Board of Tax Appeals, having considered all evidence and arguments presented, and having taken the matter under advisement, finds and concludes as follows:

FINDINGS OF FACT

Based on information obtained through an exchange of information agreement with the Internal Revenue Service, the Arizona Department of Revenue ("Department") audited the 2000 Arizona individual income tax return of Verna Pope ("Appellant"). The Department disallowed Appellant's subtraction of federal retirement contributions, medical expenses, moving expenses and investment interest expenses and issued an assessment of additional tax, negligence and late payment penalties and interest. Appellant provided additional information and the Department twice modified the original assessment: first, to allow the medical expenses and abate the negligence penalties; second, to allow \$397.00 of investment income and \$10,194.45 of moving expenses. Appellant protested the final modified assessment to the Department's hearing officer who abated the late payment penalty but otherwise upheld the assessment. Appellant now timely appeals to this Board.

DISCUSSION

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2 The issue before the Board is whether the Department properly disallowed the federal retirement
3 contributions, the remaining moving expenses, and the remaining investment interest expenses.

4 Appellant claimed a subtraction in the amount of \$5,483 for federal retirement contributions on
5 line 15 of her 2000 Arizona income tax return. The Department had included this line on the 2000 tax
6 returns as the result of litigation that was pending at that time challenging the constitutionality of Arizona
7 tax on federal retirement contributions. In February 2004, the Arizona Supreme Court held, in the final
8 decision in this case, that Arizona could tax federal retirement contributions for tax years after 1990. *Kerr*
9 *v. Killian*, 207 Ariz. 181, 84 P.3d 446 (2004). Therefore, the Department properly denied this subtraction.

10 Appellant claimed \$13,380 for moving expenses on her 2000 federal income tax return. Certain
11 moving expenses paid or incurred during the taxable year in connection with the commencement of work
12 by a taxpayer as a self-employed individual or as an employee at a new principal place of work are
13 deductible on the federal return as an adjustment to gross income under the Internal Revenue Code (IRC),
14 IRC § 217. Appellant provided documentation to the Department verifying less than \$6,000 of deductible
15 moving expenses. However, Appellant elected to take a per diem rate through her employer, who paid
16 \$10,194.45 for moving expenses as confirmed by Appellant's W-2 form, and the Department eventually
17 allowed the reimbursement from the employer as if the entire amount qualified as deductible moving
18 expenses. Appellant has not shown that she is entitled to any additional moving expenses.

19 Appellant claimed an investment interest expense deduction in the amount of \$5,016 on her 2000
20 Arizona tax return. The Department disallowed all but \$397 of the deduction. Arizona law generally allows
21 the same itemized deductions allowed at the federal level under the IRC. A.R.S. § 43-1042(A). The IRC
22 allows taxpayers to deduct interest paid or accrued within the taxable year on investment indebtedness.
23 IRC § 163(a). For individual taxpayers, this deduction is limited to the amount of the taxpayer's net
24 investment income for the taxable year. IRC § 163(d)(1). The IRC defines "net investment income" to
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1 mean the excess of the investment income over investment expenses. IRC § 163(d)(4)(A). It defines
2 "investment income" to include the net gain attributable to the disposition of investment property and the
3 net capital gain determined by taking into accounts gains and losses from dispositions of property held for
4 investment. IRC § 163(d)(4)(B). The use of the term "net" in the definition indicates that a taxpayer must
5 take into account capital loss carryovers from prior years. Since 2005, the federal tax instruction booklet
6 has explicitly instructed taxpayers to "include capital gain distributions from mutual funds and capital loss
7 carryovers" when figuring the amount of net gain from the disposition of property held for investment. The
8 fact that there was no change to the IRC between 2000 and 2005 is evidence that the language added to
9 the 2005 instruction booklet is the IRS's interpretation of the relevant statutory language for prior years,
10 including 2000, as well.

11 The Department allowed Appellant's \$397 deduction for gross income from property held for
12 investment (excluding any net gain from disposition of property held for investment). This includes the
13 \$323 in interest income and \$74 in dividend income that Appellant reported on her 2000 federal income
14 tax return. Appellant claims, however, that she had net gain from the disposition of property held for
15 investment in the amount of \$7,633. Appellant actually had a long-term loss carryover of \$16,406 from
16 prior years, resulting in a net long-term loss of \$13,295 for 2000. Thus, the net capital gain from the
17 disposition of property held for investment should have been zero. Because Appellant only had \$397 in
18 net investment income for 2000, the Department limited her investment interest expense deduction to that
19 amount.

20 At the hearing before the Board, Appellant proved that she is entitled to an additional deduction of
21 \$336. The Department disallowed \$336 in interest and fees from Bank of America on a \$7,000 loan
22 advance because Appellant did not provide sufficient documentation. Appellant testified before the Board
23 under oath that the loan advance was used for a margin call to pay-off debt incurred to buy stocks allowing
24 Appellant to avoid having to sell stocks at a loss. The Board finds that Appellant is entitled to this \$336
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1 deduction. Appellant has not shown that she is entitled to any further deduction for investment interest
2 expenses.

3 Finally, Appellant asserts that the Department should waive interest because it did not conduct
4 the audit until a few months before the expiration of the statute of limitations. The evidence shows that the
5 Department did issue the proposed assessment within the four-year statute of limitations established in
6 A.R.S. § 42-1104. A.R.S. § 42-1123(C) provides that if the tax "or any portion of the tax is not paid" when
7 due, "the department shall collect, as a part of the tax, interest on the unpaid amount" until the tax has
8 been paid. Therefore, Appellant is liable for the interest assessed for the time period between when she
9 should have paid the tax and when she actually paid the tax.

10 CONCLUSIONS OF LAW

11 1. The Department properly denied the subtraction for federal retirement contributions. See
12 *Kerr v. Killian*, 207 Ariz. 181, 84 P.3d 448 (2004).

13 2. Appellant has not shown that she is entitled to any additional moving expenses. See IRC §
14 217.

15 3. Appellant is entitled to an additional \$336 deduction as an investment interest expense. IRC
16 See § 163(a).

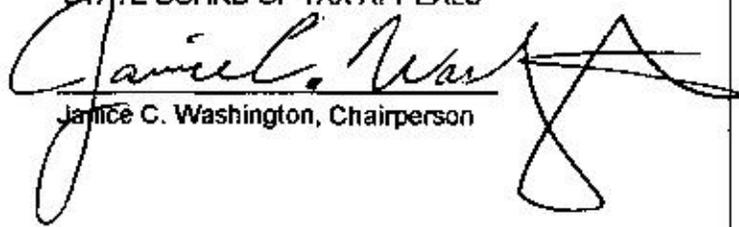
17 4. Appellant is liable for the interest assessed for the time period between when she should
18 have paid the tax and when she actually paid the tax. AR.S. §§ 42-1104, 42-1123(C)

19 ORDER

20 THEREFORE, IT IS HEREBY ORDERED that the appeal is denied in part and upheld in part and
21 the final order of the Department is modified.

1 This decision becomes final upon the expiration of thirty (30) days from receipt by the taxpayer
2 unless either the State or taxpayer brings an action in superior court as provided in A.R.S. § 42-1254.

3 DATED this 1st day of May, 2007.

4 STATE BOARD OF TAX APPEALS
5 
6 Janice C. Washington, Chairperson

8 JCW:ALW

9 CERTIFIED

10 Copies of the foregoing
11 Mailed or delivered to:

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