

JURISDICTION: OKLAHOMA TAX COMMISSION
CITE: 2010-11-30-05 / NON-PRECEDENTIAL
ID: P-10-037-H
DATE: NOVEMBER 30, 2010
DISPOSITION: DENIED
TAX TYPE: INCOME
APPEAL: NO APPEAL TAKEN

FINDINGS OF FACT AND CONCLUSIONS OF LAW

HUSBAND AND WIFE (“Protestants”) appear by and through CPA, FIRM, PLLC. The Case Management Section of the Account Maintenance Division (“Division”), Oklahoma Tax Commission, appears through OTC ATTORNEY, Assistant General Counsel, Office of General Counsel, Oklahoma Tax Commission.

PROCEDURAL HISTORY

On February 2, 2010, the protest file was received by the Office of Administrative Law Judges for further proceedings consistent with the *Uniform Tax Procedure Code*¹ and the *Rules of Practice and Procedure Before the Office of Administrative Law Judges*.² On February 4, 2010, a letter was mailed to the Protestants’ Representative stating this matter had been assigned to ALJ, Administrative Law Judge, and docketed as Case Number P-10-037-H. The letter also advised the Protestants that a Notice of Prehearing Conference would be sent by mail and enclosed a copy of the *Rules of Practice and Procedure Before the Office of Administrative Law Judges*.³ On February 5, 2010, OTC ATTORNEY filed an Entry of Appearance as Counsel of record for the Division.

On March 3, 2010, the Notice of Prehearing Conference was mailed to the last-known address of the Protestants’ Representative, setting the prehearing conference for March 31, 2010, at 10:30 a.m.⁴ On March 29, 2010, a letter was received by facsimile from CPA requesting a continuance of the prehearing conference until after tax season. There being no objection by the Division, a Notice of Prehearing Conference was mailed to the parties striking the prehearing conference from the March 31, 2010, docket and resetting the prehearing conference for April 26, 2010, at 9:30 a.m.

On April 26, 2010, at 9:30 a.m. the prehearing conference was held by telephone as scheduled. On April 26, 2010, a letter was mailed to the parties directing that on or before May 26, 2010, CPA was to submit the additional documentation discussed during the prehearing

¹ OKLA. STAT. ANN. tit. 68, § 201 et seq. (West 2001).

² OKLA. ADMIN. CODE §§ 710:1-5-20 through 710:1-5-47.

³ *Id.*

⁴ OKLA. STAT. ANN. tit. 68, § 208 (West Supp. 2010).

conference to the Division and the parties would submit a proposed scheduling order to submit this matter on stipulations and briefs.

On May 10, 2010, CPA filed the additional documentation with the Court Clerk.⁵ On May 26, 2010, the Proposal of Scheduling Order was filed with the Court Clerk.

On June 2, 2010, the Scheduling Order was issued with stipulations due on or before July 21, 2010, the Protestants' brief-in-chief due on or before August 4, 2010, the Division's response brief due on or before August 18, 2010, and the Protestants' reply brief due, if desired, on or before August 25, 2010.

On July 15, 2010, the Stipulation of Facts and Statement of Issue was filed with Exhibits 1 through 4 attached thereto.

On August 4, 2010, the Protestants' Brief-in-Chief was filed with the Court Clerk. On August 18, 2010, the Division's Brief was filed with the Court Clerk. On August 24, 2010, CPA advised the Court Clerk by telephone that a reply brief would not be filed. The record in this matter was closed and this case was submitted for decision on August 25, 2010.

STIPULATION OF FACTS

On July 15, 2010, the parties filed Stipulation of Facts and Statement of Issue,⁶ as follows, to-wit:

1. On September 29, 2009, Protestants filed their 2008 Oklahoma resident income tax return, with a copy of their 2008 Federal return attached. On Line 7 of the Schedule 511-C attached to the return, Protestants claimed a \$16,953.00 Miscellaneous Oklahoma deduction. On Statement 4 attached to the return, Protestants detailed the adjustments as fees attributable to BROKERAGE ACCOUNT municipal bond interest income 1099's, which themselves were attached to the 2008 Federal return. The return sought a refund of \$48,942.00. **(Exhibit 1.)**

2. By letter dated October 12, 2009, the Division notified Protestants that it had adjusted the 2008 returns [sic], disallowing the \$16,953.00 Miscellaneous Oklahoma deduction, thereby reducing and partially denying the refund claim by the amount of \$933.00. **(Exhibit 2.)**

3. On November 16, 2009 the Division received Protestants' representative's letter wherein they protested the partial refund claim denial, arguing that the \$16,953.00 should be allowed as an Oklahoma adjustment/deduction. **(Exhibit 3.)**

⁵ OKLA. ADMIN. CODE § 710:1-5-10(c)(2) (June 25, 1999).

⁶ The text of the stipulated facts is set out *in haec verba*. "*in haec vega*" (in heek v<<schwa>>r-b<<schwa>>). [Latin] In these same words; verbatim. BLACK'S LAW DICTIONARY (8TH ed. 2004), available at <http://westlaw.com> (Last visited October 18, 2006).

4. On May 10, 2010, Protestants' representative submitted pertinent portions of the BROKERAGE ACCOUNT statements substantiating the mathematical correctness of the \$16,953.00 dollar amount of the fees. **(Exhibit 4.)**

5. The \$16,953.00 in fees deducted were related to out-of-state municipal bond interest income reported as an Oklahoma addition to Oklahoma taxable income on Line 1 of the Schedule 511-B to the return. Of the \$16,953.00, \$911.00 represented purchased interest on the out-of-state municipal bonds, and the remainder of the \$16,953.00 represented tax preparation and investment fees allocable only to the out-of-state municipal bond interest.

6. The investment fees allocable to the entire portfolio income taxed at the Federal level totaled \$61,369.00. The amount of the two percent (2%) Federal itemized deduction limitation benchmark for Protestants' 2008 return was \$33,231.00. Therefore, all of the \$16,953.00 would have been deductible at the Federal level had the municipal bond interest been taxable at the Federal level.

ADDITIONAL FINDINGS OF FACT

Upon review of the file and records, including the record of the proceedings, the exhibits received into evidence, and the position letters, the undersigned finds:

7. On October 12, 2009, the Division adjusted the Protestants' Oklahoma return for the 2008 Tax Year⁷ as follows, to-wit:

FORM 511	REPORTED	ADJUSTED
LINE 08-TOTAL ADJUSTMENTS TO INCOME	17,353.00	400.00
LINE 09-INCOME AFTER ADJUSTMENTS	1,781,828.00	1,798,781.00
LINE 13-OKLAHOMA TAXABLE INCOME	1,593,843.00	1,610,796.00
LINE 14-OKLAHOMA INCOME TAX	87,231.00	88,164.00
LINE 19-BALANCE	87,231.00	88,164.00
LINE 31-OVERPAYMENT OF INCOME TAX	48,942.00	48,009.00
LINE 32-AMT OF REFUND TO EST TAX	48,942.00	48,009.00

8. The Protestants' "Miscellaneous Deductions"⁸ on the Federal return for the 2008 Tax Year were calculated as follows, to-wit:

Line 38 of Form 1040	adjusted gross income	1,661,572.00
	Times two percent (2%) limitation equals	33,231.00
Line 24 of Schedule A	"Miscellaneous Deductions"	61,369.00
	Minus two percent (2%) limitation	<u>33,231.00</u>
	Miscellaneous Deductions	28,138.00

⁷ Exhibit 2.

⁸ Exhibit 1. The Protestants' itemized deductions were further reduced on the Federal return (Line 29 of Schedule A) by \$15,016.00 from \$201,001.00 to \$185,985.00.

STATEMENT OF ISSUE

The issue to be decided is whether the \$16,953.00 in investment fees and purchased interest is allowable as an Oklahoma adjustment to Oklahoma taxable income under the terms of the Oklahoma Income Tax Act.

CONCLUSIONS OF LAW

1. The Oklahoma Tax Commission is vested with jurisdiction over the parties and subject matter of this proceeding.⁹
2. Tax exemption, deductions, and credits depend entirely on legislative grace and are strictly construed against the exemption, deduction or credit.¹⁰
3. In all proceedings before the Tax Commission, the taxpayer has the burden of proof.¹¹
4. A proposed assessment is presumed correct and the taxpayer bears the burden of showing that it is incorrect and in what respects.¹²

DISCUSSION

The Protestants' position is in pertinent part, "...[i]f this disallowance stems from a reliance on any limitations at the Federal level, it is important to note that given the level of the investment fees allocable to the entire portfolio taxed for U.S. income tax purposes the two percent (2%) Federal itemized deduction limitation benchmark for [Protestants'] 2008 return was

⁹ OKLA. STAT. tit. 68, § 221(D) (West Supp. 2010).

¹⁰ *TPQ Inv. Corp. v. Oklahoma Tax Com'n*, 1998 OK 13, 954 P.2d 139.

¹¹ OKLA. ADMIN. CODE § 710:1-5-47 (June 25, 1999):

In all administrative proceedings, unless otherwise provided by law, the burden of proof shall be upon the protestant to show in what respect the action or proposed action of the Tax Commission is incorrect. If, upon hearing, the protestant fails to prove a prima facie case, the Administrative Law Judge may recommend that the Commission deny the protest solely upon the grounds of failure to prove sufficient facts which would entitle the protestant to the requested relief.

OKLA. ADMIN. CODE § 710:1-5-77(b) (June 25, 1999), provides in pertinent part:

...“preponderance of the evidence” means the evidence which is of greater weight or more convincing than the evidence which is offered in opposition to it; evidence which as a whole shows that the fact sought to be proved is more probable than not.

¹² See *Enterprise Management Consultants, Inc. v. State ex rel Oklahoma Tax Com'n*, 1988 OK 91, 768 P.2d 359.

surpassed. Therefore, all of the investment fees in question would have been deductible at the Federal level had the municipal bond interest been taxable for U.S. income tax purposes.”¹³

The Division cites *TPQ Investment Corp. v. State, ex rel. Okla. Tax Com’n*, 1998 OK 13, 954 P.2d 139 as the controlling law on this issue. In *TPQ*, the taxpayer argued that because it had made a certain election available under the Internal Revenue Code, its investment in a wholly-owned subsidiary be treated as an asset purchase. The taxpayer argued its employment levels rather than those of the subsidiary should have been examined for purposes of qualifying for an Oklahoma investment credit. The Oklahoma Income Act (“Act”)¹⁴ did not contain any provision allowing the subsidiary to be treated as a new corporation for purposes of the credit. In *TPQ*,¹⁵ the Court stated:

Merely because the Internal Revenue Code allows TPQ to treat [the subsidiary] as a new corporation, for purposes of calculating a deduction for assets, does not mean that the federal code overrides the intent of the Oklahoma Legislature in providing tax credits to encourage the creation of new jobs in manufacturing or processing in this state.

Tax exemption, deductions, and credits depend entirely on legislative grace and are strictly construed against the exemption, deduction or credit.¹⁶

The last sentence of the Protestants’ position succinctly states the basic problem in this matter. The investment fees in question *were not deductible* at the Federal level because the municipal bond interest was *not taxable* for U.S. income tax purposes. The Protestants are trying to create a miscellaneous deduction at the state level to accomplish what they could not at the Federal level because of the two percent (2%) limitation. Unfortunately, the Protestants have failed to cite any Oklahoma statutory authority or case law to support their position that the deduction should be allowed on the Oklahoma return for the 2008 Tax Year.

DISPOSITION

It is the ORDER of the OKLAHOMA TAX COMMISSION, based upon the facts and circumstances of this case that the protest should be denied.

OKLAHOMA TAX COMMISSION

CAVEAT: This decision was NOT deemed precedential by the Commission. This means that the legal conclusions are generally applicable or are limited in time and/or effect. Non-

¹³ Protestants’ Position Letter at 1.

¹⁴ OKLA. STAT. ANN. tit. 68, § 2351 *et seq.* (West 2008).

¹⁵ See Note 10, *supra*.

¹⁶ *Id.* See *R.R. Tway, Inc. v. Okla. Tax Com’n*, 1995 OK 129, 910 P.2d 972, 978.

precedential decisions are not considered binding upon the Commission. Thus, similar issues may be determined on a case-by-case basis.

NOTE: The distinction between a Commission Order designated as “Precedential” or “Non-Precedential” has been blurred because all OTC Orders resulting from cases heard by the Office of Administrative Law Judges are now published, not just “Precedential” Orders. *See* OKLA. STAT. ANN. tit.68, § 221(G) (West Supp. 2009) and OKLA. STAT. ANN. tit. 75, § 302 (West 2002). *See also* OTC Orders 2009-06-23-02 and 2009-06-23-03 (June 23, 2009), which also conclude the language of the Statute is “clear and unambiguous.”