

**BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO**

In the Matter of the Protest of )  
[Redacted], ) DOCKET NO. 25064  
Petitioner. )  
DECISION  
\_\_\_\_\_ )

On May 1, 2012, the Idaho State Tax Commission’s (Commission) Income Tax Audit Bureau (ITA) issued a Notice of Deficiency Determination (NODD) to [Redacted] (Petitioner) disallowing the petitioner’s refund claim for taxable year 2007 in the amount of \$2,574. Petitioner filed a timely petition for redetermination. Petitioner was informed of his appeal rights. The Commission, having reviewed the file, hereby denies Petitioner’s refund claim.

This docket raises a number of issues including 1) what is the status of a refund claim where an amended return was not accepted by Commission staff, 2) does the [Redacted] ([Redacted] have to respond to the [Redacted] amended return before the Commission can resolve an Idaho refund claim, 3) should the Commission follow a [Redacted] Tax Court decision that conflicts with the [Redacted]apparent position or 4) where the [Redacted] tax court apparently issued conflicting decisions, how should the Commission find.

However, the Commission need not address any of these issues since Idaho Income Tax Administrative Rule 880.05 governs the outcome of this case and requires that the Commission deny Petitioner’s refund claim, as set forth below.

**BACKGROUND**

On Petitioner’s 2007 income tax return, Petitioner claimed federal Schedule A Itemized Deductions totaling \$76,520. The \$76,520 consisted of the following items:

- \$60,494 of net medical and dental expenses (\$64,551 total medical and dental less \$4,057 (7.5% of [Redacted] adjusted gross income)),
- \$10,733 of home interest expense,
- \$4,953 of taxes, and
- \$340 of charitable contributions.

Petitioner's 2007 [Redacted] income tax return was audited by the [Redacted]. As a result of that audit, in 2009, the [Redacted] disallowed the \$64,551 of medical expenses.<sup>1</sup> The reason provided in the [Redacted] audit report was “[w]e considered your documentation but we did not change our previous determination. We are still disallowing your Medical and Dental expenses because you did not verify your part of the expense paid by your health insurance”.<sup>2</sup> The [Redacted] had previously stated that “[w]e are proposing to disallow this “Schedule A” issue, pending verification and documentation to substantiate the deduction claimed.”<sup>3</sup> In September 2009, Petitioner paid the \$5,037 of [Redacted] tax and interest of \$377 for a total payment of \$5,414.

Petitioner did not file an Idaho amended income tax return to report the [Redacted] audit adjustments. However the ITA, based upon information obtained from the [Redacted], issued a Notice of Deficiency Determination on April 15, 2010, seeking an additional payment of tax, penalty, and interest totaling \$3,022. In the April 15, 2010, notice, the ITA provided an explanation of the [Redacted] adjustments that impacted Petitioner's Idaho taxable income

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<sup>1</sup> Federal Form 4549 Income Tax Examination Changes, dated August 8, 2009; which was provided to the Commission by Petitioner.

<sup>2</sup> Federal Form 886-A, Explanation of Items, attached to Federal Form 4549 (emphasis added).

<sup>3</sup> Federal Form 886-A, Explanation of Items, attached to Federal Form 4549.

including the disallowance of \$60,494 in medical and dental expenses.<sup>4</sup> Petitioner did not file a protest and instead simply paid the \$3,022 Idaho assessment in April 2010.

In December 2010, the United States Tax Court issued a decision, known as the Lang decision, in which the Tax Court found that a daughter could deduct, as itemized deductions, the medical expenses that her mother had paid directly to the daughter's medical providers.<sup>5</sup> In Lang, the daughter was not a minor and the mother was not legally obligated to pay the daughter's medical expenses. The [Redacted] argued that the daughter was not entitled to the deduction because the payments were made by someone else. The court disagreed and allowed the daughter the deductions by applying substance over form. The court stated:

Section 213(a) [IRC] allows a deduction for unreimbursed expenses paid during the taxable year for medical care of the taxpayer or a dependent.

Respondent [IRS] does not assert that Mrs. [Redacted] [mother] claimed the medical expense deduction for the amounts paid for her daughter, only that Mrs. [Redacted] paid the expenses and therefore petitioner [daughter] is not entitled to the deduction.

There is precedent for State law controlling whether a gift at the time of payment affects who is the payor. See, e.g., Ruch v. Commissioner, T.C. Memo.1982-493, revd. on another issue 718 F.2d 719 (5th Cir.1983). Mrs. [Redacted] made the medical expense payments for her daughter with donative intent. Although Mrs. [Redacted] and petitioner would not be subject to the gift tax,<sup>2</sup> the income tax treatment in this context is not controlled by the gift tax consequence. See Pierre v. Commissioner, 133 T.C. 24, 35 (2009). Applying substance over form, we treat petitioner as having received from her mother a gift of \$24,559 with which petitioner paid her own medical expenses. Petitioner should be credited with having made the payments for purposes of the income tax deduction in question.<sup>6</sup>

The Tax Court's 2010 decision in Lang is contrary to a Tax Court 2009 decision known as the McGrath decision.<sup>7</sup> However, in McGrath the taxpayer lost, in large part, because the

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<sup>4</sup> Notice of Deficiency Determination dated April 15, 2010, page 2, Explanation of Items.

<sup>5</sup> Lang v. C.I.R., T.C. Memo. 2010-286, 100 T.C.M. (CCH) 603 (2010).

<sup>6</sup> *Id.*

<sup>7</sup> McGrath v. C.I.R., T.C. Memo. 2009-126, 97 T.C.M. (CCH) (2009) (daughter and husband not entitled to deduct medical expenses paid by daughter's father).

taxpayer's position could not be determined, since the taxpayer failed to file a pretrial memorandum or brief as ordered by the Tax Court.<sup>8</sup>

On April 4, 2011, the Commission received an Idaho amended income tax return for taxable year 2007 in which Petitioner claimed a refund of tax in the amount of \$2,574. The amended return was filed a few days prior to the expiration of the statute-of-limitations for the filing of a refund claim, as set forth in Idaho Code section 63-3027(b). In addition, Petitioner filed an amended [Redacted] income tax return in April 2011.

In both the [Redacted] and Idaho amended return, Petitioner relied upon the Lang decision to reassert his right to claim the medical expenses. Petitioner attached the following explanation with the filing of the [Redacted] and Idaho amended returns:

The taxpayer is filing an amended return as a protective refund claim.

The taxpayer's originally filed 2007 income tax return claimed a deduction for medical expenses of \$64,551, including \$61,340 paid directly to the medical care providers by the taxpayer's father. The medical expenses were treated by the taxpayer and the taxpayer's father as a gift to the taxpayer. The medical expenses paid by the taxpayer's father were not deducted by the taxpayer's father. Upon examination the [Redacted] disallowed the deduction as the expenses were not paid by the taxpayer.

The U.S. Tax Court recently heard a case involving an identical fact pattern. See *Judith F. Lang v. Commissioner*. In Tax Court Memorandum 2010-286, the court ruled in favor of the taxpayer and allowed the deduction. Based on the recent Tax Court Memorandum the taxpayer is filing an amended return to claim the medical expenses disallowed by the [Redacted] upon examination.<sup>9</sup>

The ITA reviewed Petitioner's Idaho amended return and issued the NODD on May 1, 2012, and denied Petitioner's Idaho refund claim for the following reasons:

You filed an amended Idaho and [Redacted] income tax return for the tax year 2007 revising the adjustments previously made by the [Redacted]. The amended 2007 tax year return as filed cannot be accepted at this time for the following reason.

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<sup>8</sup> *Id.*

<sup>9</sup> Petitioner's Amended Idaho Individual Income Tax Return 2007, Statement 1, Explanation of Changes (emphasis added).

- When amended returns are being filed that are the direct result of a [Redacted] audit, the taxpayer is required to also submit copies of all schedules and written explanations provided by the [Redacted]. The required copies were not attached to the amended return as filed.

Our review of the on-line [Redacted] information indicates that the [Redacted] has not yet made any adjustments to their original audit of the above referenced tax year. All adjustments made to your 2007 Idaho Individual Income tax return were predicated on the same adjustments made by the [Redacted] to your 2007 [Redacted] income tax return.<sup>10</sup>

Petitioner's representative responded to the NODD on June 26, 2012, in part, as follows:

In 2007 [Petitioner] deducted medical expenses paid on his behalf by his father. The [Redacted] challenged the deductions. The position taken by the [Redacted] was the medical expenses were not deductible by [Petitioner] since they were paid by someone else. As a result of the changes to [Petitioner's] [Redacted] return additional taxes were also assessed by Idaho. Recently the US Tax Court has ruled that such expenses were deductible (Judith F. Lang v. Commissioner). As a result of the court's ruling [Petitioner] filed amended [Redacted] and Idaho returns.

Based on the notice it appears that the refund claim is being denied as the [Redacted] has yet to make an adjustment to [Petitioner's] 2007 account. Can you give us a better understanding of what must be done in order for [Petitioner] to receive his refund? Will [Petitioner] need to wait until his amended [Redacted] return is processed and approved? If so, how should [Petitioner] proceed once the adjustment has been made by the [Redacted]? . . .<sup>11</sup>

On June 27, 2012, the ITA treated the June 26, 2012 response as a timely filed protest and sent Petitioner's representative a letter which included a request that the representative provide the ITA with documentation showing the [Redacted] accepted the amended [Redacted] return.

After the exchange of a couple of e-mails showing that no movement had been made at the [Redacted] level with respect to the amended [Redacted] income tax return, the ITA placed the petition into the Commission's internal appeals process and the Petitioner's appeal was forwarded in September 2012 to Tax Policy (Appeals) for resolution.

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<sup>10</sup> NODD, May 1, 2012, Explanation of Items, page 2.

<sup>11</sup> E-mail correspondence dated June 26, 2016, from Petitioner's representative to the ITA (emphasis added).

In its protest summary, the ITA argues that:

The originally filed return claimed a deduction for medical expenses directly paid to the medical care provider by the taxpayer's father and were treated as a gift. The [Redacted] disallowed the deduction as the expenses were not paid by the taxpayer. .

..

Presumption is that the adjustments reported in the NODD which are based upon the adjustments reported in the final [Redacted] determination received from the [Redacted] per Idaho Code sections 63-3002, 63-3069, are correct.<sup>12</sup>

Appeals notified Petitioner of his right to appeal in a November 2012 letter and since that time, the appeal has been in a holding pattern waiting to see how the [Redacted] resolved Petitioner's [Redacted] amended return claim. During the Idaho appeals period, Petitioner's representative has provided a copy of the original [Redacted] audit report and responded to an occasional e-mail seeking an update as to the status of the [Redacted] amended return claim. The response has primarily been that the [Redacted] has taken no action on Petitioner's [Redacted] amended return claim which Appeals was able to verify through the Commission's exchange agreement with the [Redacted]. For example, in November 2014, Appeals asked the Commission's [Redacted] liaison officer to 1) contact the [Redacted] and obtain a copy of the [Redacted] amended return, 2) acquire any correspondence relating to that amended return, and 3) if no correspondence, any explanation as to the status of the [Redacted] amended return. Furthermore, on February 23, 2015, Appeals received notification from the Commission's [Redacted] liaison officer that the [Redacted] had notified her that in addition to the [Redacted] amended return claim, no letters or correspondence were in Petitioner's [Redacted] file. No explanation was provided by the [Redacted] as to the status of the [Redacted] amended return.

In an e-mail dated April 21, 2015, Petitioner's representative informed Appeals that, due to a cost/benefit analysis, Petitioner abandoned any further attempts to pursue the [Redacted] claim.

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<sup>12</sup> ITA Protest Summary (a document prepared by ITA in response to Petitioner's petition).

## ANALYSIS

Idaho Income Tax Administrative Rule 880 (Rule 880) provides the answer to resolving this docket. Subsection 05 of Rule 880 states:

05. Closed Issues. The Tax Commission will deny a credit or refund claim for a taxable year for which the Tax Commission has issued a Notice of Deficiency, unless the taxpayer shows that the changes on the amended return are unrelated to the adjustments in the Notice of Deficiency or that the changes result from a final federal determination.<sup>13</sup>

Petitioner acknowledged, in the statement attached to the amended return and in the petition, that the [Redacted] had originally disallowed the medical expenses because they were not paid by Petitioner and instead were paid by his father. In the Notice of Deficiency Determination, issued on April 1, 2010, the Commission had followed the [Redacted] disallowance of the medical expenses.

Thus, pursuant to Rule 880.05, the Commission denies Petitioner's refund claim filed in April 2011, since the adjustments in the 2011 amended return claim relate to the adjustments in the April 1, 2010, Notice of Deficiency; a notice that was not protested by Petitioner. If the [Redacted] responds to Petitioner's [Redacted] amended return by allowing the medical deductions as part of a [Redacted] final determination, then Idaho Code section 63-3072(d) contains a special provision that allows the petitioner to file an Idaho refund claim within one year of the final [Redacted] determination.

THEREFORE, for the reasons set forth within this Decision, the Notice of Deficiency Determination dated May 1, 2012, denying Petitioner's refund claim is hereby **AFFIRMED** and **MADE FINAL**.

An explanation of the Petitioner's right to appeal this decision is enclosed.

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<sup>13</sup> IDAPA 35.01.01.880.05. A minor wording change, having no impact on the current issue, was made to Rule 880.05 effective in 2014; otherwise, the language in Rule 880.05 has remained the same from 1997 to the present.

DATED this \_\_\_\_\_ day of \_\_\_\_\_ 2015.

IDAHO STATE TAX COMMISSION

\_\_\_\_\_  
COMMISSIONER

**CERTIFICATE OF SERVICE**

I hereby certify that on this \_\_\_\_\_ day of \_\_\_\_\_ 2015, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[Redacted]

Receipt No.

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