

6. The Department automatically processed the amended return and refunded to Taxpayer the tax that had been withheld of \$[REDACTED] plus interest of \$[REDACTED].
7. The Section sent Taxpayer a letter on February 1, 2013 asking Taxpayer to explain the difference between the amounts of Taxpayer's FAGI shown on his amended returns and the amounts reported to the Department by the Internal Revenue Service.
8. Taxpayer responded by letter dated February 27, 2013 that the difference was due to adjustments made under Internal Revenue Code (I.R.C.) § 1341(b)(1) relating to restoration of a substantial amount held under a claim of right.
9. Taxpayer did not specify why an adjustment under I.R.C. § 1341(b)(1) was proper.
10. Taxpayer presented no evidence that he was required to repay in a later tax year any of the income he received during 2008 or 2009.
11. On March 13, 2013 the Section issued Taxpayer proposed assessments for tax years 2008 and 2009 adding to Taxpayer's FAGI that amounts that he had subtracted in his amended returns.
12. The proposed assessments included interest but no penalties.
13. Taxpayer timely protested the assessments asserting that he was entitled to an adjustment for each year in accordance with I.R.C. § 1341.¹
14. Taxpayer requested a hearing by memoranda.
15. Taxpayer has presented no evidence that he did not receive the wages and other income included in the proposed assessments.

CONCLUSIONS OF LAW

¹ In prior correspondence to the Department Taxpayer also cited 31 U.S.C. § 3124 that a state cannot tax obligations of the United States and 12 U.S.C. § 411 that federal reserve notes are obligations of the United States and therefore Arizona cannot tax his wages which are or were paid in federal reserve notes.

1. The presumption is that an assessment of additional income tax is correct and the burden is on the taxpayer to overcome such presumption. *Arizona State Tax Commission v. Kieckhefer*, 67 Ariz. 102, 191 P.2d 729 (1948).
2. Once the presumption of correctness attaches, the taxpayer must present substantial credible and relevant evidence sufficient to establish that the assessment was erroneous. *U.S. v. McMullin*, 948 F.2d 1188 (10th Cir.,1991); *Anastasato v. C.I.R.*, 794 F.2d 884 (3rd Cir.,1986).
3. A general denial of liability is not sufficient to overcome the presumption that the assessment is correct. *Avco Delta Corp. Canada Ltd. v. U.S.*, 540 F.2d 258 (7th Cir., 1976).
4. Arizona Revised Statutes (A.R.S.) § 43-102(A)(1) provides that it is the intent of the Arizona legislature to adopt the provisions of the federal Internal Revenue Code relating to the measurement of adjusted gross income for individuals so that adjusted gross income reported to the Internal Revenue Service shall be the identical sum reported to Arizona, subject only to modifications set forth in Title 43 of the Arizona Revised Statutes.
5. The State of Arizona's power to tax is independent of the Constitution of the United States. *Department of Revenue v. Arthur*, 153 Ariz. 1, 734 P.2d 98 (App. 1986).
6. Article 9, § 12 of the Arizona Constitution extends to the Arizona Legislature the authority to levy and collect taxes, including income taxes. Pursuant to that authority, the Arizona Legislature enacted the Arizona Income Tax Act of 1978, effective as of January 1, 1979.
7. Under the claim of right doctrine in I.R.C. § 1341 and A.R.S. § 43-1029, a person who has to repay in a later year amounts he had received and held under a claim of right in previous years may deduct the repayment in the year in which it is made.

8. Taxpayer has not shown that he has repaid any of the wages he had received during tax years 2008 and 2009.
9. Taxpayer's argument that he properly filed the amended returns under I.R.C. § 1341 is without merit.
10. Taxpayer was and continues to be subject to Arizona income tax on the income he received during 2008 and 2009.
11. The Section's proposed assessments for tax years 2008 and 2009 are upheld.

DISCUSSION

Taxpayer filed an Arizona state income tax return for 2008 and paid the taxes due. Taxpayer did not file an original return for 2009 but Arizona state income taxes were withheld from his wages. Taxpayer thereafter filed amended Arizona returns for 2008 and 2009 subtracting income so that his computed tax liability was zero. The Department automatically processed Taxpayer's amended returns and issued refunds.

Because Taxpayer had reduced his Arizona income when he filed the amended returns, his Arizona income did not match his FAGI. The Section therefore sent Taxpayer a letter inquiring about the difference. Taxpayer responded that the amended returns were properly submitted pursuant to I.R.C. § 1341. The Section thereafter issued proposed assessments for the taxes that were properly due for tax years 2008 and 2009 based on the income Taxpayer had received. Taxpayer timely protested.

Taxpayer's primary assertion continues to be that he may exclude the income he received during 2008 and 2009 under I.R.C. § 1341. I.R.C. § 1341, and the corresponding Arizona provision, A.R.S. § 43-1029, allow a person who has to repay in a later year amounts he had received and held under a claim of right in previous years to deduct the repayment in the later year. The keys are that the person has to repay the amount he had received and reported as income in a prior year before he can claim a deduction in the later year. Without repayment in a later year there is no right to a deduction in the later year (not, as Taxpayer is attempting to do here, claim a deduction

in the year the income was received). There is no evidence that Taxpayer repaid any of the wages or other income he received during 2008 and 2009. I.R.C. § 1341 therefore does not support Taxpayer's amended returns.

Taxpayer had previously argued to the Department that under 31 U.S.C. § 3124 (a state cannot tax obligations of the United States) and 12 U.S.C. § 411 (federal reserve notes are obligations of the United States) Arizona cannot tax his wages and other income which are or were paid in federal reserve notes.² The contention that federal reserve notes are not subject to state income tax was previously rejected by the Maryland Special Court of Appeals in *Provenza v. Comptroller of Treasury*, 64 Md.App. 563, 497 A.2d 831 (1985). Taxpayer has cited no contrary authority.

Finally, Taxpayer questioned whether the Section's notice of proposed assessments adequately set out the basis of the assessments as provided in A.R.S. § 42-2076. The Section clearly informed Taxpayer that the amount of his income reported to the Section by the IRS was different than what Taxpayer had reported to the Section. Under the statutes cited in the proposed assessments, a Taxpayer's Arizona gross income is the same as his FAGI subject to adjustments provided by A.R.S. §§ 43-1021 and 43-1022. Taxpayer has not established an entitlement to any adjustment. The Section's proposed assessments therefore adequately informed Taxpayer of the basis of the assessments and they are upheld.³

The proposed assessments included interest. A.R.S. § 42-1123(C) provides that if the tax "or any portion of the tax is not paid" when due "the department shall collect, as a part of the tax, interest on the unpaid amount" until the tax has been paid. For Arizona purposes, therefore, interest is a part of the tax and generally may not be

² Even if Taxpayer's contention were valid, Taxpayer has presented no evidence that he was paid in federal reserve notes and not by check, direct deposit or some other mechanism.

³ Even if the notices were not adequate, the provisions of A.R.S. § 42-2076 are directory and not mandatory. See, 67 C.J.S. *Officers* § 238.

abated unless the tax to which it relates is found not to be due for whatever reason.
The tax was due in this case and the associated interest cannot be abated.

Based on the foregoing, the Section's proposed assessments for tax years 2008
and 2009 are upheld.

DATED this 20th day of May, 2014.

ARIZONA DEPARTMENT OF REVENUE
APPEALS SECTION

[REDACTED]
Hearing Officer

Original of the foregoing sent by
certified mail to:

[REDACTED]

Copy of the foregoing delivered to:

Arizona Department of Revenue
Individual Income Tax Audit Section