STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS

DIVISION OF TAXATION

ADMINISTRATIVE HEARING

FINAL DECISION AND ORDER

#2014-06

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DEPARTMENT OF REVENUE
DIVISION OF TAXATION
ONE CAPITOL HILL
PROVIDENCE, RHODE ISLAND 02908

IN THE MATTER OF:	:	**Personal Income Tax**
	:	**Case No.: 13-T-0040**
Taxpayers.	:	

DECISION

I. INTRODUCTION

The above-entitled matter came before the undersigned as the result of a Notice of Hearing and Appointment of Hearing Officer dated March 29, 2013 and issued to the above-captioned taxpayers ("Taxpayers") by the Division of Taxation ("Division") in response to a request for hearing filed with the Division. The parties agreed that this matter could be decided on stipulated facts and exhibits and briefs. The parties submitted a stipulation of facts and exhibits and filed timely briefs by January 9, 2014. The Division and Taxpayers both were represented.

II. JURISDICTION

The Division has jurisdiction over this matter pursuant to R.I. Gen. Laws § 44-30-1 *et seq.*, R.I. Gen. Laws § 44-1-1 *et seq.*, *Division of Taxation Administrative Hearing Procedures Regulation AHP 97-0,* and the *Division of Legal Services Regulation 1 Rules of Procedure for Administrative Hearings.*

III. ISSUE

Whether the Taxpayers[1] owe the personal income tax, interest, and penalties assessed by the Division?

IV. MATERIAL FACTS AND TESTIMONY

The parties agreed to the following facts:[2]

1. and (collectively "Taxpayers") are husband and wife, and residents of the State of .

2. ("Company") is a Corporation with an address in The Taxpayer is the sole officer and/or director of the Company and serves as Chief Executive Officer of the corporation. Division's Exhibit One (1).

3. At no time did Company register with the Rhode Island Secretary of State's Office to do business in the State of Rhode Island. Division's Exhibit Two (2).

4. ("Show") was a television drama that was produced by ("Network"), and all filming for this show took place within Rhode Island. Division's Exhibit Three (3).

5. As of April 4, 2007, Taxpayer entered into a contract with Network for his exclusive services on the Show. Taxpayer's Exhibit A.

6. In order to qualify for the Rhode Island Film and TV Motion Picture Production Tax Credit under R.I. Gen. Laws § 44-31.2 *et seq.*, the Network, the production company, was required to provide the Division with a list of all out-of-state vendors and loan-out companies used in the production of the Show.

7. In a letter dated April 6, 2009, Network provided the requisite documentation to the Division. Division's Exhibit Four (4).

8. Per the documentation provided by Network, Company had a hire date of July 28, 2008 and an end date of November, 21, 2008 for employee Taxpayer. Network paid Company a salary of for the services Taxpayer performed in the Show in 2008.

9. A Division revenue agent ("Auditor") was assigned the Show file for audit purposes. Auditor reviewed the internal documents and determined that as of October

[1] The taxpayers are a married couple who filed jointly. The income earned at issue in this matter was by the husband.

[2] The parties filed a stipulation of facts on which this summary is based.

2011, Taxpayer failed to file a 2008 Rhode Island Non-Resident Income Tax Return (Form RI 1040 NR). Division's Exhibit Five (5).

10. Pursuant to R.I. Gen. Laws § 44-30-83, the Auditor prepared an assessment by using Taxpayer's Rhode Island income as disclosed by the Network records and other documentation provided to the Division. Division's Exhibit Six (6).

11. The assessment resulted in tax due. In compliance with the Rhode Island General Laws, the Auditor imposed interest, late filing penalty, and late payment penalty. The Division mailed a Notice of Deficiency dated October 14, 2011 to Taxpayer. Division's Exhibit Six (6).

12. The Company had no record of filing or paying the requisite corporate tax to the Division. Therefore, the Division assessed the minimum corporate tax together with interest against Company for 2006, 2007, and 2008. Division's Exhibit Seven (7).

13. On December 11, 2011, the Division mailed an automatically-generated, updated Notice of Deficiency to the Taxpayer. Division's Exhibit Nine (9).

14. In 2012, the Company filed their 2008 RI-1120C and paid the appropriate corporate tax. Division's Exhibit Eight (8).

15. On or about January 11, 2012, the Taxpayer filed a [2008] RI-1040X amended return. Based on this amended return, the Taxpayer claimed the tax and late interest due to Rhode Island totaled a smaller amount than the Division's assessment. In his RI-1040X, the Taxpayer allocated the Rhode Island wages based on the number of days worked in Rhode Island. Division's Exhibit Ten (10).

16. On or about January 13, 2012, the Division contacted the Taxpayer's representative regarding the RI-1040X filed for tax year 2008. The Division requested more information and supporting documentation from Taxpayer. In particular, the Division requested the 2008 Federal 1120 return for the Company, the RI Corporate Return for the Company, and a "properly apportioned Schedule E." Division's Exhibit 11.

17. On or about January 31, 2012, the Division received a letter from the Taxpayer's representative. Division's Exhibit 12. Together with this letter, Taxpayer's representative provided the 2008 Federal 1120 return of the Company, the 2008 RI-1120C for the Company, and the W-2 form the Company issued to the Taxpayer in 2008. According to the W-2 provided, the Company paid the Taxpayer wages totaling in 2008. Division's Exhibits 13, 14, and 15.

18. On or about July 16, 2012, the Division contacted the Taxpayer advising him that the Division did not accept the allocation of Rhode Island wages as reflected in the RI-1040X filed by Taxpayers. Division's Exhibit 16. Specifically, the Division did not accept the allocation based on the number of days worked in Rhode Island.

19. Instead, the Auditor used the direct relationship between the payment for work done by Taxpayer in Rhode Island and the gross receipts of the Company to apportion the income and generate the assessment. The income was allocated as follows:

A. The Auditor began with the figure disclosed by Network as compensation to Company for the services of Taxpayer in Rhode Island on the Show for the period of July 28, 2008 through November 21, 2008.
B. She reviewed the RI-1120C submitted by Taxpayer, the Company and confirmed this figure was the amount listed as RI income in the Taxpayer's 2008 RI-1120C. Division's Exhibit 8, page 2, column A.
C. She reviewed and accepted the roughly 75% apportionment allocation asserted by the Taxpayer's on their RI-1120C.
D. She reviewed and accepted the statement that Taxpayer received from the Company only in the form of officer compensation in 2008. This figure was also adopted by the Taxpayers on their Federal 1120 return. Division's Exhibit 13, line 12.
E. The Auditor used the 75% apportionment allocation adopted by the Taxpayer and applied that figure to the of officer compensation Taxpayer received from the Company for 2008.
F. The result was a determination that the Taxpayer received of Rhode Island source income for the services he performed in Rhode Island on the Show.
G. The Auditor adjusted Taxpayer's RI-1040X return and revised the Notice of Deficiency accordingly.

21. With its July 16, 2012 letter, the Division provided the audited return, a revised Notice of Deficiency dated July 16, 2012, an interest and penalty calculation, and supporting documentation for the Division's apportionment allocation. Division's Exhibit 16.

22. On July 30, 2012, the Taxpayer's representative sent a letter to the Division enclosing the RI-1120C and Schedule F requesting the Division to adjust its records. Division's Exhibit 17.

23. In early August 2012, via phone conversation, the Auditor advised Taxpayer to request a hearing because the Division did not accept his apportionment allocation based on the number of days worked in Rhode Island. On August 6, 2012, the Taxpayer's representative sent a letter on behalf of Taxpayer disputing the July 16, 2012 Notice of Deficiency and requesting an administrative hearing. Division's Exhibit 18.

24. On August 21, 2012, the Division mailed an automatically-generated, updated Notice of Deficiency to Taxpayer. Division's Exhibit 19.

25. On or about March 11, 2013, a preliminary conference was held on this matter via telephone. The parties were unable to settle the matter at the preliminary conference and this matter went to administrative hearing. Division's Exhibit 20.

V. DISCUSSION

A. Legislative Intent

The Rhode Island Supreme Court has consistently held that it effectuates legislative intent by examining a statute in its entirety and giving words their plain and ordinary meaning. *In re Falstaff Brewing Corp.*, 637 A.2d 1047 (R.I. 1994). See *Parkway Towers Associates v. Godfrey*, 688 A.2d 1289 (R.I. 1997). If a statute is clear and unambiguous, "the Court must interpret the statute literally and must give the words of the statute their plain and ordinary meanings." *Oliveira v. Lombardi*, 794 A.2d 453 (R.I. 2002) (citation omitted). The Supreme Court has also established that it will not interpret legislative enactments in a manner that renders them nugatory or that would produce an unreasonable result. See *Defenders of Animals v. Dept. of Environmental Management,* 553 A.2d 541 (R.I. 1989) (citation omitted). In cases where a statute may contain ambiguous language, the Rhode Island Supreme Court has consistently held that the legislative intent must be considered. *Providence Journal Co. v. Rodgers*, 711 A.2d 1131 (R.I. 1998). The statutory provisions must be examined in their entirety and the meaning most consistent with the policies and purposes of the legislature must be effectuated. *Id.*

B. Relevant Statutes and Regulation

R.I. Gen. Laws § 44-30-1 provides that Rhode Island income is subject to tax. R.I. Gen. Laws § 44-30-1(e)(3) includes as Rhode Island taxable income, income of non-resident individuals as defined in R.I. Gen. Laws § 44-30-32. R.I. Gen. Laws § 44-30-32 delineates what is Rhode Island source income of non-residents. Such income includes "income derived from or connected with Rhode Island sources." R.I. Gen. Laws § 44-30-32(a)(1). The Taxpayer did not dispute that he is a non-resident of Rhode Island who

earned Rhode Island source income. What is at dispute is how this Rhode Island source income should be taxed.

The Taxpayers argue that the Division should use Regulation PIT 97-21 *Taxation of Nonresident Professional Athletes* ("PIT 97-21") in determining the tax owed by the Taxpayer. That regulation provides in part as follows:

> For taxable years beginning on or after January 1, 1997, the Rhode Island source income of nonresident members of professional athletic teams includes their total compensation for services rendered as team members during the taxable year, multiplied by a fraction, the numerator of which is the number of "duty days" spent within Rhode Island rendering services for the team in any manner during the taxable year, and the denominator of which is the total number of duty days spent both within and without Rhode Island during the taxable year.
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> The term "professional athletic team" includes, but is not limited to, any professional baseball, basketball, football, soccer or hockey team.
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> "Duty days:" "Duty days" include:
>
> 1. all days during the taxable year from the beginning of the professional athletic team's official pre-season training period through the last game in which the team competes or is scheduled to compete;
> 2. days that do not fall within (1), above, on which the team member renders services for a team (e.g., participation in instructional leagues, the "Pro Bowl" or promotional "caravans"). "Renders services" includes conducting training and rehabilitation activities, but only if conducted at the facilities of the team; and
> 3. game days, practice days, days spent at team meetings, promotional caravans and preseason training camps, and days served with the team through all post-season games in which the team competes or is scheduled to compete.
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> "Member of a professional athletic team" defined: A member of a professional athletic team includes employees who are active players, players on the disabled list and any other persons required to travel and who travel with and perform services on behalf of the team on a regular basis (e.g., coaches, managers, trainers, etc.).

The Division argues that PIT 97-21 is inapplicable to the Taxpayer since he is not a professional athlete and the Division's deficiency should be upheld. Since the Taxpayer did not file a 2008 non-resident Rhode Island return, the Division, pursuant to

R.I. Gen. Laws § 44-30-83, prepared an assessment of the Taxpayer's Rhode Island income. This assessment imposed interest and penalties. See Exhibit Six (6). The Taxpayer then filed a non-resident Rhode Island return for 2008 allocating his Rhode Island income based on the number of days worked in Rhode Island. Division's Exhibit Ten (10). The Division rejected the Taxpayer's use of number of days worked in Rhode Island calculations for his 2008 return. Instead, the Division revised its assessment by using the relationship between the payment for work done by Taxpayer in Rhode Island and the Company receipts by apportioning[3] the income. The revised assessment included interest and penalties. Division's Exhibit 16. The Division imposed late payment interest,[4] a late filing penalty,[5] and a late payment penalty.[6] The Taxpayers did not dispute the imposition of interest or either penalty.

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[3] R.I. Gen. Laws § 44-30-33 states as follows:

> Apportionment. – (a) The federal tax liability of a nonresident individual which is attributable to Rhode Island income shall be that proportion which Rhode Island income bears to federal adjusted gross income after the modifications in subsection (b) or (c) in § 44-30-12. For the purpose of this apportionment, a nonresident individual may elect to treat his or her federal adjusted gross income as his or her Rhode Island income unless the amount of the modifications increasing federal adjusted gross income under § 44-30-12 would exceed one hundred dollars ($100).
>
> (b) For tax years beginning on or after January 1, 2001, the Rhode Island income tax liability of a nonresident individual which is attributable to Rhode Island income shall be that proportion which Rhode Island income bears to federal adjusted gross income after the modifications in § 44-30-12(b) or (c). For the purpose of this apportionment, a nonresident individual may elect to treat his or her federal adjusted gross income as his or her Rhode Island income unless the amount of the modifications increasing federal adjusted gross income under § 44-30-12 would exceed one hundred dollars ($100).

[4] R.I. Gen. Laws § 44-30-84 states in part as follows:

> Interest on underpayment.
>
> (a) General.
>
> (1) If any amount of Rhode Island personal income tax, including any amount of the tax withheld by an employer, is not paid on or before the due date, interest on the amount at the annual rate provided by § 44-1-7 shall be paid for the period from the due date to the date paid, whether or not any extension of time for payment was granted. The interest shall not be paid if its amount is less than two dollars ($2.00).

[5] R.I. Gen. Laws § 44-30-85 states in part as follows:

> Additions to tax and civil penalties.
>
> (a) Failure to file tax returns or to pay tax. In the case of failure:

C. Whether the Taxpayers Owe the Deficiency

The Taxpayer is not a professional athlete and is not a member of professional athletic team that played in Rhode Island in 2008. He is an actor who earned his Rhode Island income in 2008 by acting in a Show for the Network. He does not fall under any of the definitions of PIT 97-21. Said regulation is inapplicable to the Taxpayer.

The Taxpayers argued that the Tax Administrator in his discretion can expand said regulation to include other classes of taxpayers. There is no statutory or regulatory basis for the Tax Administrator to expand a promulgated regulation covering professional athletes to also include professional actors without promulgating a new regulation. Any change in regulations would be subject to the regulatory process. See R.I. Gen. Laws § 44-30-95 and R.I. Gen. Laws § 42-35-1 *et seq.* While agencies are deferred to regarding the administration and enforcement of law, agencies are bound by their own regulations and must act consistently with their regulations. *Ratcliffe v. Coastal Resources Management Council*, 584 A.2d 1107 (R.I. 1991).

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(1) To file the Rhode Island personal income tax return or the employer's withheld tax return on or before the prescribed date, unless it is shown that the failure is due to reasonable cause and not due to willful neglect, an addition to tax shall be made equal to five percent (5%) of the tax required to be reported if the failure is for not more than one month, with an additional five percent (5%) for each additional month or fraction thereof during which the failure continues, not exceeding twenty-five percent (25%) in the aggregate. For this purpose, the amount of tax required to be reported shall be reduced by an amount of the tax paid on or before the date prescribed for payment and by the amount of any credit against the tax which may properly be claimed upon the return.

[6] R.I. Gen. Laws § 44-30-85 states in part as follows:

Additions to tax and civil penalties.

(a) Failure to file tax returns or to pay tax. In the case of failure:

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(2) To pay the amount shown as tax on the personal income tax return or the employer's withheld tax return on or before the prescribed date for payment of the tax (determined with regard to any extension of time for payment) unless it is shown that the failure is due to reasonable cause and not due to willful neglect, there shall be added to the amount shown as tax on the return five-tenths percent (0.5%) of the amount of the tax if the failure is for not more than one month, with an additional five-tenths percent (0.5%) for each additional month or fraction thereof during which the failure continues, not exceeding twenty-five percent (25%) in the aggregate.

The Taxpayers also argued that PIT 97-21 provides for a fair and equitable determination of tax due to the State based on services rendered on "duty days" and that PIT 97-21 should not be exclusive to professional athletes. The Division argued that policy behind PIT 97-21 would not be served by extending its alternative method of income allocation to individuals other than professional athletes. The Division would disagree that it would be fair and equitable to extend said regulation to professional actors. Nonetheless, equitable principles are not applicable to administrative proceedings. See *Nickerson v. Reitsma*, 853 A.2d 1202 (R.I. 2004) (Supreme Court vacated a Superior Court order that vacated an agency sanction on equitable grounds). There are no grounds to argue that professional actors should be treated like members of professional athletic teams that play in Rhode Island.

D. Conclusion

PIT 97-21 is not applicable to the Taxpayer. Thus, the Taxpayers owe the Division's revised Notice of Deficiency (Division's Exhibits 16 and 19) of tax owed, interest owed, and penalties owed.

VI. FINDINGS OF FACT

1. On or about March 29, 2013, the Division issued a Notice of Hearing and an Appointment of Hearing Officer to the Taxpayers. The parties filed an agreed to facts and exhibits and relied on briefs that were timely filed by January 9, 2014.

2. The facts contained in Section IV and V are reincorporated by reference herein.

VII. CONCLUSIONS OF LAW

Based on the testimony and facts presented:

1. The Division has jurisdiction over this matter pursuant to R.I. Gen. Laws § 44-1-1 *et seq.* and R.I. Gen. Laws § 44-30-1 *et seq.*

2. Pursuant to R.I. Gen. Laws § 44-1-1 *et seq.*, R.I. Gen. Laws § 44-30-1 *et seq.*, R.I. Gen. Laws § 44-30-33, R.I. Gen. Laws § 44-30-84, and R.I. Gen. Laws § 44-30-85, the Division properly assessed the income tax owed, interest owed, and penalties owed by Taxpayers.

VIII. RECOMMENDATION

Based on the above analysis, the Hearing Officer recommends as follows:

Pursuant to R.I. Gen. Laws § 44-1-1 *et seq.*, R.I. Gen. Laws § 44-30-1 *et seq.*, R.I. Gen. Laws § 44-30-33, R.I. Gen. Laws § 44-30-84, and R.I. Gen. Laws § 44-30-85, the Division properly assessed the income tax owed, interest owed,[7] and penalties owed by Taxpayers.

Date: January 31, 2014

Catherine R. Warren
Hearing Officer

ORDER

I have read the Hearing Officer's Decision and Recommendation in this matter, and I hereby take the following action with regard to the Decision and Recommendation:

X ADOPT
_____ REJECT
_____ MODIFY

Dated: FEB 11, 2014

David Sullivan
Tax Administrator

[7] The amount of interest owed increased between the July 16, 2012 Notice of Deficiency and the August 21, 2012 Notice of Deficiency. See Division's Exhibits 16 and 19. The Division will issue a revised Notice of Deficiency current with this decision.

NOTICE OF APPELLATE RIGHTS

THIS DECISION CONSTITUTES A FINAL ORDER OF THE DIVISION. THIS ORDER MAY BE APPEALED TO THE SIXTH DIVISION DISTRICT COURT PURSUANT TO R.I. Gen. Laws § 44-30-90 WHICH STATES AS FOLLOWS:

§ 44-30-90 Review of tax administrator's decision.

(a) General. Any taxpayer aggrieved by the decision of the tax administrator or his or her designated hearing officer as to his or her Rhode Island personal income tax may within thirty (30) days after notice of the decision is sent to the taxpayer by certified or registered mail, directed to his or her last known address, petition the sixth division of the district court pursuant to chapter 8 of title 8 setting forth the reasons why the decision is alleged to be erroneous and praying relief therefrom. Upon the filing of any complaint, the clerk of the court shall issue a citation, substantially in the form provided in § 44-5-26 to summon the tax administrator to answer the complaint, and the court shall proceed to hear the complaint and to determine the correct amount of the liability as in any other action for money, but the burden of proof shall be as specified in § 8-8-28.

(b) Judicial review sole remedy of taxpayer. The review of a decision of the tax administrator provided by this section shall be the exclusive remedy available to any taxpayer for the judicial determination of the liability of the taxpayer for Rhode Island personal income tax.

(c) Date of finality of tax administrator's decision. A decision of the tax administrator shall become final upon the expiration of the time allowed for petitioning the district court if no timely petition is filed, or upon the final expiration of the time for further judicial review of the case.

CERTIFICATION

I hereby certify that on the 14th day of February, 2014, a copy of the above Decision and Notice of Appellate Rights were sent by first class mail, postage prepaid to the Taxpayers' representative's address on file with the Division of Taxation and by hand delivery to Meaghan Kelly, Esquire, Department of Revenue, One Capitol Hill, Providence, Rhode Island, 02908.

Gail Belanco