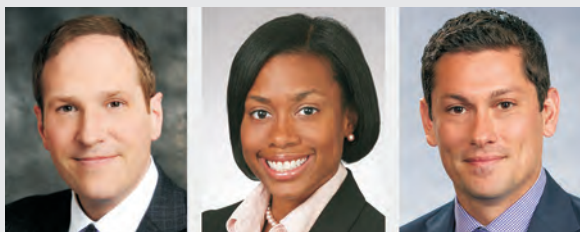


Opportunities for Interest Abatement in Maryland

by Stephen J. Blazick, Alexandra P. Sampson, and Jack Trachtenberg



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In this edition of *The Taxpayers' Advocate*, the authors discuss a topic important to the preservation of taxpayer rights: obtaining an abatement of interest assessments in Maryland.

It is reasonable for state tax authorities to assess interest when tax is lawfully due because interest is intended to represent to a taxpayer the price for the use of borrowed money. However, when the interest rate associated with a tax deficiency is unusually high or punitive, particularly as compared with prevailing market rates or the rate for interest paid to taxpayers, fairness dictates that taxpayers be given a reasonable opportunity to request an abatement of interest in appropriate circumstances.¹

It is no secret that Maryland's 13 percent interest rate on tax deficiencies is one of the highest in the country. However, many taxpayers are unaware that both the comptroller and the Maryland Tax Court have the authority to abate interest.² Although prior trends may make getting an abatement seem like an impossible task, taxpayers should be aware of recent Maryland case law, as well as guidance from other states, that may provide avenues to successfully seek an abatement of interest.

¹Unlike those of some states, Maryland's 13 percent interest rate is applicable to both assessments on unpaid taxes and refunds.

²See Md. Code Ann. Tax-Gen. section 13-606.

I. *Frey v. Comptroller*

The comptroller of Maryland has long held the power to waive interest. Md. Code Ann. Tax-Gen. section 13-606 provides that "for reasonable cause, a tax collector may waive interest on unpaid tax." Except in rare instances, the comptroller has generally declined to assert this power, arguing that such a waiver, and the grounds on which interest is waived, is subject to audit by the Maryland General Assembly for a showing of reasonable cause. While the potential for an audit by the legislature should encourage the comptroller to be judicious in the exercise of his interest abatement authority, it should not serve as a basis to deny relief when reasonable cause exists, as the law provides.

Although it may prove difficult for taxpayers to obtain an interest abatement from the comptroller, the 2011 Maryland Court of Appeals decision in *Frey v. Comptroller of the Treasury*, 29 A.3d 475 (Md. 2011), gives new hope to taxpayers seeking relief from the state's unusually high interest rate. In *Frey*, the court determined that nothing in Maryland's statutory scheme indicates that the General Assembly intended tax collectors to have sole authority over the waiver of interest. Instead, under Md. Code Ann. Tax-Gen. sections 3-103(a),³ 13-510(a)(1),⁴ and 13-528(a)(1)-(a)(2),⁵ the Maryland Tax Court may consider and order the abatement of interest assessed against parties appealing to it. The *Frey* decision further held that a reasonable cause or obvious error standard of review applies when the tax court considers a request to abate interest. That is, when the tax court considers appeals of a tax collector's refusal to abate an

³Md. Code Ann. Tax-Gen. section 3-103(a) grants the tax court jurisdiction over any "final decision, final determination, or final order" of "any . . . unit of State government or of a political subdivision of the State" authorized to make such a determination about any tax issue, including "the application for an abatement, reduction, or revision of any assessment or tax."

⁴Md. Code Ann. Tax-Gen. section 13-510(a)(1) provides that a party may appeal to the tax court "a final assessment of tax, interest, or penalty under this article."

⁵Md. Code Ann. Tax-Gen. section 13-528(a)(1) establishes that "the Tax Court shall have full power to hear, try, determine, or remand any matter before it." Md. Code Ann. Tax-Gen. section 13-528(a)(2) states that "in exercising these powers, the Tax Court may reassess or reclassify, abate, modify, change or alter any valuation, assessment, classification, tax or final order appealed to the Tax Court."

interest assessment, it looks at whether the party has demonstrated with affirmative evidence that reasonable cause exists or whether the tax collector's decision was an obvious error.

The *Frey* decision is important in that it places the tax court on equal footing with the comptroller regarding the abatement of interest. In contrast to states where a court cannot abate interest⁶ or where it may only review a tax agency's decision regarding interest to determine whether the agency acted reasonably,⁷ in Maryland, taxpayers who are unable to obtain a waiver of interest at the comptroller level get a second chance on appeal before the tax court, which may make an independent determination on whether to abate interest.

II. Grounds for Abatement

Since the *Frey* decision, a number of taxpayers have requested an interest abatement before the tax court. Some have been successful and others have not. The most common reason taxpayers have been unsuccessful is a failure to affirmatively state reasonable cause for the abatement. It is clear that Maryland's unduly high interest rate does not, standing alone, serve as reasonable cause,⁸ but it is less clear what constitutes reasonable cause that would warrant abatement. Below are options taxpayers might want to consider to demonstrate reasonable cause for an abatement of interest.

A. Reliance on Advice Given by Employees of the Comptroller

One instance in which reasonable cause for an abatement of interest may exist is when a taxpayer receives erroneous guidance from the comptroller's office regarding the tax treatment of a particular transaction.

In *Annapolis Accommodations v. Comptroller of the Treasury*,⁹ the taxpayer, a company in the business of renting residential homes to out-of-town guests, reached out to the comptroller's office on multiple occasions for advice regarding the tax treatment of weekly rentals. The taxpayer was told that no sales tax was due on its weekly rentals and then followed that advice. Later, however, the comptroller issued an assessment for unpaid sales tax on the rentals. The taxpayer contested the assessment, in part because of the guidance it had received from representatives within the comptroller's office. Although the tax court held that the

taxpayer was liable for the tax, it abated the interest and penalties. The court stated that the taxpayer did all it could reasonably do to determine whether any tax was owed.

Taxpayers that receive guidance from officials within the comptroller's office should document the advice provided, either by maintaining copies of any written advice or, if the guidance is obtained via a phone conversation, by keeping internal notes of the date, time, representative's name, and advice provided. In the latter situation, the taxpayer may also want to consider following up the phone conversation with a letter to the comptroller's office confirming the content of the discussion.

B. Unreasonable Delay by the Comptroller

Taxpayers may also be able to show reasonable cause when the comptroller's staff delays the resolution of a matter. An abatement of interest is warranted under those circumstances because the accrual of interest could be substantially reduced by a speedy resolution of the matter. Although Maryland has not ruled on the interest abatement in this context, a number of other courts have evaluated the abatement for unreasonable delay.

For example, the Michigan Court of Appeals has granted a partial abatement of interest in instances of an inordinate delay between the date when a decision should have been reached and the date when the Treasury Department rendered its decision.¹⁰ In those cases, the court determined that interest should not accrue during the period of delay and abated that portion.

It is important for taxpayers seeking an abatement of interest on grounds that the comptroller unreasonably delayed the issuance of an assessment or final determination to minimize or avoid grounds for the comptroller to make a similar argument regarding the taxpayer. Other courts evaluating the abatement of interest for unreasonable delay have generally declined to abate the interest when the cause for the delay was attributable, in whole or in part, to the taxpayer's actions.¹¹ Further, some courts have denied the

¹⁰See, e.g., *Master Craft Engineering Inc. v. Dep't of Treasury*, 366 N.W.2d 235 (Mich. App. 1985) (Michigan Court of Appeals abated interest for a 3.5 year period during which the Department of Treasury delayed rendering a decision); see also, *Holloway Sand & Gravel Co. Inc. v. Dep't of Treasury*, 393 N.W.2d 921 (Mich. App. 1986) (appeals court partially abated interest during a seven-year period of delay but excluded from the abatement the time when the delay was not attributable to the Department of Treasury); and *Monaghan v. Michigan Dep't of Treasury*, No. 329175 (Mich. Tax Trib. 2011) (Department of Treasury's hearing officer recommended the partial abatement of interest attributable to the department's delay in conducting an informal conference. On appeal, however, the tax tribunal determined that the taxpayer was not liable for the tax and, thus, never ruled on the request for waiver of interest).

¹¹See, e.g., *Skagit County Public Hospital District No. 1 v. Dep't of Revenue*, 242 P.3d 909 (Wash. Ct. App. 2010) (court of appeals declined to abate interest when the delay was for the taxpayer's convenience); *Dial Corp. v. Iowa Dep't of Revenue and Finance*, 634 N.W.2d

(Footnote continued on next page.)

⁶See, e.g., Conn. Gen. Stat. section 12-33a, which provides that "the court shall not waive statutory interest on any amount of tax for which any person is liable."

⁷See, e.g., *Comcast of South Jersey Inc. v. Director, Division of Taxation*, Docket No. 00153-2004 (N.J. Tax Ct. 2012).

⁸See *Ackers v. Comptroller of the Treasury*, No. 10-IN-OO-1370 (Md. Tax Ct. 2011) (tax court determined that the taxpayer was not entitled to an abatement of interest based on reasonable cause merely because he viewed the statutory rate as excessive).

⁹No. 10-SU-OO-0606 (Md. Tax Ct. 2012).

abatement of interest in circumstances where the delay was not attributable to the taxpayer but also was beyond the agency's control.¹²

C. Lack of Guidance or Change in Position

Taxpayers may also have an opportunity to prove reasonable cause when the dispute involves an issue for which there is no comptroller guidance and opinions may differ on the appropriate tax treatment of the issue. Similarly, reasonable cause may exist if the comptroller changes its position for an issue but does not provide guidance regarding the change.

In these instances, a taxpayer may argue that the comptroller is equitably estopped from assessing interest because of his failure to provide public guidance. Some state courts have held that equitable estoppel will not be applied to prevent the collection of taxes;¹³ however, it is still in question whether the doctrine might apply when a party seeks to have interest abated. Even in the absence of an equitable estoppel claim, courts generally disfavor the secret application of an agency's interpretation of tax statutes. For example, in *Meredith Corp. v. Tax Appeals Tribunal*,¹⁴ the New York Supreme Court, Appellate Division, rejected the state's attempt to retroactively apply a significant change in a long-standing policy upon which the taxpayer was relying. The appellate division determined that "retroactively applying a changed interpretation upon which a taxpayer was relying is 'arbitrary and capricious.'"¹⁵

D. Reliance on Prior Determinations or Audit Results

A taxpayer's reliance on a method or position applied in a prior audit or final determination may serve as reasonable cause for the abatement of interest in a subsequent audit involving the same set of facts and issues.

In *J&J Snack Food Sales Corp. v. Director, Division of Taxation*,¹⁶ the New Jersey Tax Court abated interest when the treatment of an issue in a 1993 audit determination was not followed when the same issue arose in a subsequent audit. In *J&J Snack Food*, the Division of Taxation audited the taxpayer in 2008 and determined that it was liable for use tax on its out-of-state purchases of parts that were shipped to the taxpayer in New Jersey and assembled. However, the taxpayer had been audited in 1992 on the same set

of facts and issues and, though based on an erroneous interpretation of applicable case law, the division determined that use tax was not due on the parts. The taxpayer appealed the assessment resulting from the 2008 audit to the New Jersey Tax Court. Although the court did not reverse the 2008 audit determination, it waived the interest and penalties imposed on the audit assessment. The court reasoned it would be inequitable for the division to impose the interest and penalties because had the taxpayer known of the correct interpretation of the case law applicable to its purchase, it may have made a business decision to pay the tax on its purchases and, thus, would not have accrued any interest. Instead, it was the taxpayer's reliance on the 1993 final determination that caused it to not pay use tax.

E. Additional Grounds to Establish Reasonable Cause May Exist

The aforementioned options for demonstrating reasonable cause are merely examples of the grounds that might be raised to support a request for interest abatement. However, depending on the facts and circumstances, other grounds for establishing reasonable cause might exist. For instance, taxpayers may consider whether other commonly asserted reasonable cause arguments used to obtain penalty relief, such as reasonable reliance on the advice of a tax professional, might also apply to interest abatement because the reasonable cause standard for penalty and interest abatements appears to be the same.

III. Caution: The Tax Court Does Not Have Unfettered Discretion

Although the Maryland Tax Court has the authority to make an independent determination regarding the abatement of interest, it does not have unfettered discretion in doing so. As with the comptroller, the tax court may only abate interest when a taxpayer shows that there is reasonable cause.

In *Jai Sik Shin v. Comptroller of the Treasury*,¹⁷ a case involving officer liability for unpaid sales tax, the tax court abated interest because it did not agree with the statute that imposes officer liability. The comptroller appealed this aspect of the court's ruling to the Circuit Court for Prince George's County. On appeal, the circuit court determined that the tax court may not abate interest on tax assessments for any reason it sees fit and that instead, it must require the taxpayer to present "affirmative evidence of reasonable cause" to abate the tax. The circuit court ordered the tax court to reinstate interest on the assessment.

643, 649 (Iowa 2001) (Iowa Supreme Court determined taxpayer was not entitled to an abatement of interest when the taxpayer contributed to the delays).

¹²See *In re City of Wichita*, 274 Kan. 915, 936 (Kan. 2002) (Kansas Supreme Court determined that an abatement of interest should be denied when the delay was caused by the unexpected medical retirement of the auditor originally assigned to the case, and the audit was completed in a timely manner once the second auditor was assigned).

¹³See, e.g., *Anonymous Taxpayers v. South Carolina Dep't of Rev.*, No. 01-ALJ-17-0446-CC (S.C. ALC 2002) (citing *Heyward v. South Carolina Tax Comm.*, 240 S.C. 347 (S.C. 1962)).

¹⁴102 A.D.3d 156 (N.Y. App. Div. 2012).

¹⁵*Id.* at 159.

¹⁶27 N.J. Tax 532 (N.J. Tax Ct. 2013).

¹⁷No. 11-SU-OO-0220 (Md. Tax Ct. 2012), *rev'd in part*, No. CAL 12-40630 (Md. Cir. Ct., Prince George's Cnty. 2013).

IV. Conclusion

Taxpayers seeking an abatement of interest should present affirmative evidence of reasonable cause for the abatement. While we are hopeful that the comptroller will begin to exercise his lawful duty to abate interest more frequently, taxpayers should be prepared to take their interest abatement request to the tax court. If reasonable cause can be shown, relief may be granted. And if enough taxpayers begin taking these cases to the tax court, the comptroller may begin to rethink his reluctance to provide relief to deserving taxpayers based solely on a fear of being audited by the General Assembly.

We would also encourage other states, especially those that do not provide for interest abatement or provide only limited rights to interest abatement, to follow Maryland's lead and permit both their tax authorities and courts to abate interest when reasonable cause exists to do so. Reasonableness is a proxy for fairness, and taxpayers should not be forced to pay interest, particularly at abnormally high rates, when it is unfair to require them to do so. ☆

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