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April 12, 2011

Via Email

Senator Ben Brooks
Room 729
11 South Union Street
Montgomery, Alabama 36130

Representative Paul J. DeMarco
Room 516-F, State House
11 South Union Street
Montgomery, Alabama 36130

Re: **Support for HB 427/SB 232 – Establishment of Alabama Tax Appeals Commission**

Dear Senator Brooks and Representative DeMarco:

As president of Tax Executives Institute, I write to express the Institute's support for HB 427 and SB 232 (the "Legislation"), which would establish an Alabama Tax Appeals Commission to hear appeals of tax assessments and other matters administered by the Department of Revenue and certain taxes levied by or on behalf of counties and municipalities. TEI applauds the efforts to establish an independent tax tribunal in Alabama, which we agree will help build confidence and respect between taxpayer and tax collector, and contribute to overall sound tax administration.

Tax Executives Institute was founded in 1944 to serve the professional needs of in-house tax professionals. Today, the organization has 54 chapters in North America, Europe, and Asia. Our 7,000 members represent 3,000 of the largest companies in the world, many of which either are resident or do business in Alabama. As the preeminent association of business tax professionals worldwide, TEI has a significant interest in encouraging the uniform and equitable enforcement of the tax laws and reducing the cost and burden of administration and compliance to the benefit of taxpayers and government alike. The Institute is committed to maintaining a system that works — one that builds upon the principle of voluntary compliance and is consistent with sound tax policy. Along with federal, state, and local governments, TEI and its members have much at stake in crafting a tax system that is administrable and efficient.

General Comments in Support of the Legislation

In recent years, significant attention has been devoted to the need to establish uniform and balanced state tax administration procedures to make compliance efficient and reduce uncertainty for taxpayers. Governing procedures should be even-handed (as between similarly situated taxpayers as well as between taxpayers and the taxing authority) to vindicate basic principles of fairness and equity and maintain the integrity of the self-assessment tax system. Nearly two decades ago, Alabama enacted its existing procedures with the Alabama Taxpayers' Bill of Rights and Uniform Revenue Procedures Act of 1992 modeled on similar federal provisions then in effect. (TEI strongly supports the enactment of administrative or procedural "bills of rights" by the various states.)

Building on the positive foundations established by the Alabama Taxpayers' Bill of Rights, the Legislation would establish the Alabama Tax Appeals Commission as an independent tribunal within the executive branch having jurisdiction to hear tax appeals from the Department of Revenue, as well as from counties and municipalities. The Commission would be a prepayment forum, and taxpayers would not be required to pay the disputed tax or post a bond as a prerequisite to review. These features represent best practices and will provide taxpayers with a fair and independent pre-payment procedure to resolve disputes with the Department of Revenue and localities within Alabama.

Allowing the same state authority that seeks to impose or collect a tax to adjudicate a taxpayer's appeal is by definition unfair; it creates a conflict of interest that fosters the perception that the deck is stacked against taxpayers. Nearly half of all states avoid these conflicts by providing an independent forum to adjudicate tax appeals. In addition to minimizing conflicts of interest, funneling appeals of tax cases to an independent tribunal staffed with seasoned tax professionals helps ensure consistent and well-reasoned dispositions of cases.

Section 1 of the Legislation succinctly explains the benefits of the proposed Alabama Tax Appeals Commission, as follows:

By establishing an independent tax tribunal within the executive branch of government, this act shall provide taxpayers with a means of resolving controversies that ensures both the *appearance and the reality of due process and fundamental fairness*. (Emphasis added.)

TEI strongly supports the passage of the Legislation so that taxpayers may realize these benefits.

Concerns with New Substantial Understatement Penalty

While TEI supports the passage of the Legislation, we remain concerned about provisions that would establish a new "substantial understatement" penalty. Section 4 would impose a 20% penalty on "the amount of [any] understatement of tax that exceeds the greater of five thousand dollars (\$5,000) or 20 percent of the tax required to be shown on the return for the tax period."

Similar to the federal substantial understatement penalty, the Legislation provides that the penalty will not be assessed “if reasonable cause exists,” or where the position is disclosed on a return and “there is a reasonable basis for the tax treatment of such item.” Unlike the federal rules,¹ however, the Legislation contains no exclusion from the penalty for amounts attributable to tax positions not specifically disclosed on the return but supported by “substantial authority.”

TEI believes that failing to include an exclusion from the penalty for tax positions supported by substantial authority belies the complexity of the tax law and would undermine the fairness of Alabama’s tax penalty provisions. Where a statute is ambiguous, multiple interpretations of a rule are possible, or no single controlling authority exists on an unsettled issue, it will frequently be impossible — for either taxpayers or the tax authorities — to determine with certainty how a court would rule if the issue were litigated. Without some check on the ability to impose the substantial understatement penalty in these cases, taxpayers will be forced to disclose myriad everyday tax positions to avoid a penalty assessment or litigate cases where they would otherwise be disinclined to do so. That approach will burden both taxpayers and the tax authority (which will have to review the disclosures), lessening the efficiency and fairness advanced by the many positive provisions in the Legislation. TEI recommends that the Legislation be amended to conform to the federal penalty by including language stating that undisclosed tax positions supported by “substantial authority” are excluded from the new substantial understatement penalty.

If you have any questions about the Institute’s views or desire additional information regarding the comments contained in this letter, please do not hesitate to contact Linda Dickens, Chair of TEI’s State and Local Tax Committee, at 972.917.6912 (linda-dickens@ti.com) or Daniel B. De Jong of TEI’s legal staff at 202.638.5601 (ddejong@tei.org).

Respectfully submitted,
Tax Executives Institute, Inc.



Paul O’Connor
International President

¹ Section 6662(d) of the Internal Revenue Code imposes a 20% penalty on “[a]ny substantial understatement of income tax.” However, “[t]he amount of the understatement...shall be reduced by that portion of the understatement which is attributable to – (i) that tax treatment of any item by the taxpayer if there is or was substantial authority for such treatment.” IRC section 6662(d)(2)(B). *See also* Treas. Reg. § 1.6662-4(d)(2).