

2004
Tax Forum
between
North Carolina Department of Revenue
and
North Carolina Society of Accountants



Point of Contact:

Ronald D. Powell (336) 625-1427

- 1. Erroneous Refund.** Married Filing Separately Tax returns were prepared for a couple. The wife owed the NC Department of Revenue \$75.00. A check signed by the husband but with the wife's social security number on it was sent with the wife's return and mailed. The husband receives a check at the end of April from the NC Department of Revenue for \$75.00 for refund of overpayment of his tax return. On July 6, 2004 we receive a letter from the NC Department of Revenue saying the wife owes \$75.00 in taxes plus penalty and interest. We made copies of the cancelled check and the check from the NC Department of Revenue. We write a letter back sending copies of the former correspondences along with copies of all the checks and another check for \$75.00. In August we get a bill for interest from the NC Department of Revenue, when in fact it was their fault in the beginning. The practitioner paid the nominal amount to resolve the issue.

Questions: What can be done to prevent this from happening again?

Answer: Unfortunately the Department of Revenue made a mistake on this account. Not as an excuse but for information only, the Department received 8.2 million pieces of mail during fiscal year 2002-2003. Of that mail, there were over 5.7 million payments received and processed. From the example stated above, the tax professional did everything she or he should have done to ensure that the payment was processed to the correct account.

- 2. Deductibility of Payment for Fellowship Obligation.** Individual graduates from college and receives a teaching fellowship requiring them to teach in NC for four years. Each year they are paid \$6500. Parents are asked to sign as responsible party if individual does not fulfill the requirement and are held liable.

Question: If parents are required to repay, is there a deduction to be taken on an individual tax return? Typically this would occur when the dependent is no longer claimed on the taxpayer's return.

Answer: North Carolina law does not provide for such a deduction.

- 3. Practitioners Priority Service.** The IRS established a direct line for practitioners a few years ago and this has been a great resource to our work.

Question: Is there a Practitioner Priority Line for DOR similar to what the IRS has setup for us to directly resolve issues?

Answer: The Department will be piloting a tax practitioner phone line near the end of 2004 or early 2005 to determine if it will work. It will initially be for individual income tax issues only, but the plan is to offer it for the other tax schedules later. Our Taxpayer Assistance Division will staff the phone line. You will be contacted directly once the phone line is implemented. It will be important, however, to retain this telephone number only for tax practitioners. If the number is given to taxpayers, it will defeat the purpose of the direct line.

- 4. Electronic Reconciliation.** W-2 forms and an annual reconciliation are sent each year. Many of us electronically file this information directly to the Social Security Administration. We are now forced to print hard copies to send to DOR.

Question: Can the information be obtained from SSA vice us sending a printed copy or is there a way the data file we send to SSA can also be sent to DOR?

Answer: This is certainly an idea the Department may try to pursue, but for now there is no coordination of this information between the SSA (federal) and the state.

5. Electronic Amended Returns. Despite best efforts, a tax return may have to be amended. Currently all amended returns must be filed on paper.

Question: Are there efforts to allow the amended return to be electronically filed?

Answer: Functionality for filing amended returns electronically is on the Department's priority list, but it is unlikely that it will be implemented in the near future. There are other applications that have a greater need. However, if your association believes that this functionality deserves the highest priority, the Department would be interested in getting your input.

6. eServices. The IRS began an eServices web-based program last year, which has helped tremendously to obtain information on tax matters and to resolve issues. We feel a similar program would be beneficial for NCDOR and the tax practitioners of North Carolina. Items we would propose to include:

Recommendation: A function similar to the IRS web-based 2003 Advance Child Credit inquiry or provide an eServices function where the practitioner can access individual estimated tax payments prior to completing the return. Most taxpayers who are making these payments utilize a professional to complete their tax returns. By adding this feature we feel we can eliminate most of the discrepancy notices issued relating to estimated tax payments.

Answer: Before the Department can provide some of the services you have requested, it must first develop a system that is secure to protect the confidentiality of taxpayer information much like the IRS. We expect to have this functionality completed in 2005, and once we have developed this functionality, we will be able to provide the types of things you are requesting.

Recommendation: A function to submit POAs. This would speed up the process of reconciling issues generated by notices.

Answer: The Department has always worked with tax practitioners concerning their clients for the most part without the need of a POA. If our employee has sufficient reason to believe you are representing the taxpayer, we do not require a POA unless the tax issue involves IRS information. It is our understanding that some of our employees have been requiring POAs, and we will resolve that issue internally. If you are requested to provide a POA for a tax issue not involving IRS information, we ask when you call the Department that you ask to speak to a level 2 or level 3 employee who will know when a POA is required.

Recommendation: A function to receive information on the status of an individual tax return or amended tax return.

Answer: Currently the Department has an automated refund inquiry line and plans to have a similar application on our website beginning in 2005. However, this is for checking on the status of a current return only. Since the Department now makes images of its tax returns, it is much easier to determine if an amended return has been received, and oftentimes we can assist on the status of amended through our taxpayer assistance telephone line. Plans are also underway to try to speed the processing of amended returns which have traditionally been processed primarily in the fall of the year. More of this information will be posted on our website in 2005.

Recommendation: A function to submit a response to a notice if the practitioner has a valid POA on file.

Recommendation: Need to have an DOR database for business entities similar to what the NC Secretary of State offers for Corporations from their website. Information recommended to be included:

- ü Corporate filings, tax payments etc.
- ü Partnership filings, etc.
- ü Payroll Withholding Filings; NC-3, NC-5, etc.

Answer: Once the system to protect confidentiality of tax information has been developed (detailed above), many of these functions listed should be made available as they can be developed.

7. **eFile Limitations.** Last year we began sending the Form 1099 for retirements exempt from taxation due to Bailey/Emory/Patton when filing electronically along with NC-RA. Presume this is to justify the deduction and the information is not available to you from IRS. This is defeating the purpose of electronically filing the return when we have to send the NC-RA and Form 1099 to you.

Questions: We know the IRS shares information on the tax returns, why can't they also share this information?

Answer: Your presumption is correct. The IRS did not make this information available to our Department. For tax year 2004 the NC-RA is no longer required. Therefore, the taxpayer and tax practitioner can retain the 1099 "Bailey" information, but the Department retains the right to request the information from the taxpayer.

Many of the Form 1099 come from North Carolina government agencies, why can't you get the information from them?

Answer: North Carolina no longer requires Form 1099 to be sent to us.

Why can't the electronic file information you require be modified to accept the W-2 / Form 1099 information? It is already present in our systems to include company address, FEIN, etc.

Answer: This is a suggestion that the Department will investigate for future years.

Recommendation: DOR develop a way to accept the W-2 and Form 1099 electronic data files that we submit to SSA and IRS.

- 8. Request for Zero Taxable Return.** Client received a notice to file a tax return for 2000. Their retirement was exempt from taxation due to Bailey/Emory/Patton decision (retirement from NC government agency) resulting in negative taxable income. There was no need to file a return. A copy of the return was created and sent along with the notice.

Questions: Why did it take three years to request the return?

Answer: This taxpayer was probably identified as a nonfiler on our federal income matching program. It takes time to receive the information from the IRS and match it against North Carolina's data base. However, this process is being improved and should not take as long in the future.

Is this a situation where we need to submit the return anyway?

Answer: A taxpayer who receives Bailey benefits and ends up with no North Carolina Taxable Income because of the Bailey deduction still has to file a North Carolina return if he or she meets the minimum gross filing requirements. In that case, a return must be filed to show the deduction from Federal Taxable Income.

- 9. Farm Exemption Number.** Recently clients with farms have been contacting us about obtaining a certificate. The information we have is they must obtain a new number for use by January 1, 2005 using E-595EA. After checking with your web-site, recent emails from your information service, I was able to obtain information from NC Department of Agriculture.

Question: Can you provide us more information on why this is being done?

Answer: Effective October 1, 2002, the General Assembly enacted G.S. 105-164.29A which authorizes the Department to issue an exemption certificate to persons exempt from tax or subject to the preferential rate of tax on certain purchases of tangible personal property. Since this provision was passed, the Department has developed a plan to assign exemption numbers to eligible entities such as farmers and commercial fishermen. Our Department and retailers have experienced problems over the years with purchases of property by purchasers not entitled to the exemption, and this policy will reduce ineligible purchases and also provide retailers with better assurance that a purchaser is eligible for the exemption.

North Carolina has been participating in the national Streamlined Sales Tax Project for several years, and one of the items developed by the Project is a uniform exemption certificate that all member states are required to adopt once the Streamlined agreement is effective. Although the agreement will most likely not go into effect until mid or late 2005, the Department decided to issue the new exemption form in conjunction with the new exemption number process. We anticipate that retailers will benefit by having to use only one type of exemption form rather than the several currently in use

Question: Why is there no new bulletin on your web-site and why hasn't there been a notice to practitioners?

Answer: Sales and Use Tax directive SD-04-01 was placed on the Department's website on June 17, 2004, and explains the new exemption procedures. Also posted on that day were copies of the exemption certificate and the application for an exemption

number. The Department also placed "Important Notice – June 2004" on the website to address some immediate issues and included a reference to this notice in the Directive. On June 21, 2004, an e-mail link to these documents was sent to subscribers to E-Alerts, the Department's Tax Updates Mailing List. Between June 10 and June 18, the Directive, Important Notice, and a Form E-595E were sent to all registered sales and use tax taxpayers and to those tax professionals and organizations on our mailing list.

10. Pseudo State Agents. The new law allowed for electing to make contributions to the judicial campaign fund on the 2003 D-400. We were sent information on this and contacted by individuals representing DOR.

Question: Why are we the new enforcers of new fund deductions? It seems as though we are being forced to be agents of the state.

Answer: Because of possible confusion about this campaign fund, the Department did ask for tax professionals to assist in ensuring that taxpayers understood the contribution election.

11. Postage Subject to Sales Tax. A client completed a state audit and was penalized for not taxing postage. A recent e-mail (4 pages) from the NC DOR that contained an item that said if postage is stated separately on the invoice it is not taxable.

Question: Can you clarify which is correct? Is this new, when is it effective?

Answer: Charges for postage made by a retailer in connection with the retail sale of tangible personal property constitute delivery charges. Effective January 1, 2002, all delivery charges made in connection with such sales constitute part of the sales price on which tax is due. Prior to January 1, 2002, separately stated delivery charges were taxable except for a sale originating in North Carolina when title to the property passed to the purchaser at the point of origin. A new exemption went into effect October 1, 2004, for delivery charges on direct mail that are separately stated. Direct mail constitutes printed material delivered or distributed by the United States Postal Service or other delivery service to a mass audience or to addresses on a mailing list provided by the purchaser or at the direction of the purchaser when the cost of the items is not billed to the recipients. Direct mail does not include multiple items of printed matter delivered to a single address.

12. Update forms on Web-Site. Completed Form E-585 (12-01) in August 2004 for a client downloaded from the DOR web site and mailed it in. The form was rejected, returned, and a new version of the form (12-03) was sent to us. This form has been updated as of September 2004.

Question: Why did it take so long for the updated form to be available on the web-site?

Answer: Since December 2002, there have been two versions of Form E-585 available for use to reflect the inclusion of the Mecklenburg County Public Transportation Tax on the general sales and use tax return, Form E-500. The refund forms have to complement the sales and use tax returns. For periods prior to July 1, 2002, a separate refund form was needed for the Mecklenburg County Public transportation Tax since a

North Carolina Department of Revenue Tax Forum - 2004

separate return was required to report this tax. Returns and refund forms usually have to be updated each year to address law changes.