

BEFORE THE ARIZONA DEPARTMENT OF REVENUE

In the Matter of)	DECISION OF
[REDACTED])	HEARING OFFICER
TID # [REDACTED])	Case No. 201300248-I
_____)	

A hearing was held on February 6, 2014 in the matter of the protest of [REDACTED] (Taxpayer) to an assessment of income tax and interest by the Individual Income Tax Audit Section (Section) of the Arizona Department of Revenue (Department) for tax year 2008. At the hearing leave to submit additional documentation was granted.

The parties have submitted their respective memoranda. This matter is now ready for ruling.

FINDINGS OF FACT

1. Taxpayer filed federal and Arizona income tax returns for tax year 2008.
2. The Section sent Taxpayer a letter dated November 19, 2012 that his federal Schedule A showed that Taxpayer took the standard deduction but claimed itemized deductions of \$[REDACTED] on his Arizona return. The letter requested Taxpayer to provide a copy of his federal Schedule A with documentation to verify each deduction.
3. Taxpayer did not respond and the Section issued a proposed assessment dated March 6, 2013 disallowing Taxpayer's itemized deductions and allowing a standard deduction of \$[REDACTED].
4. The proposed assessment calculated interest at the statutory rate. No penalties were imposed.

5. Taxpayer timely protested the assessment stating that he is a scientist involved in scientific research. As a part of his research Taxpayer travelled to the State of [REDACTED] and to [REDACTED] to collaborate with [REDACTED] scientists. Taxpayer's protest also stated that he had not received the Section's November 2012 letter.
6. Based on additional information provided by Taxpayer, the Section issued a modified proposed assessment dated January 29, 2014 allowing Taxpayer a portion of his itemized deductions, including medical expenses and some of his expenses associated with his trip to the state of [REDACTED].
7. With respect to the state of [REDACTED] trip, Taxpayer had claimed \$[REDACTED] consisting of:
 - a. Per diem of \$[REDACTED] (\$[REDACTED] per day for 105 days).
 - b. Per diem of \$[REDACTED] (\$[REDACTED] per day for 6 days travel).
 - c. Mileage of \$[REDACTED].
 - d. Hotels and ferry of \$[REDACTED].
 - e. [REDACTED] ([REDACTED]) housing and lab fees of \$[REDACTED].
That amount excluded \$[REDACTED] for dining hall fees for two dinners per week.
8. With respect to the [REDACTED] trip Taxpayer had claimed \$[REDACTED] consisting of:¹
 - a. Per diem of \$[REDACTED] (\$[REDACTED] per day for 38 days).
 - b. Airfare of \$[REDACTED].
9. The Section allowed the following unreimbursed expenses in its modified proposed assessment:

¹ Taxpayer's notes for the [REDACTED] trip expenses also included transportation expenses from and to the airport of \$[REDACTED]. Taxpayer however did not include that amount in his claimed itemized deduction. We will not therefore address the deductibility of the \$[REDACTED] transportation expense.

- a. [REDACTED] hotel and ferry expenses of \$[REDACTED].
 - b. [REDACTED] Housing and laboratory fees of \$[REDACTED], which included the \$[REDACTED] for dining hall fees for two dinners per week.
 - c. Mileage to and from [REDACTED] of \$[REDACTED].
10. The Section did not allow Taxpayer's claimed per diem for [REDACTED] because it allowed the actual dining hall fees and did not allow any [REDACTED] related expenses.
11. At the hearing the Section agreed to allow the airfare of \$[REDACTED] to [REDACTED].
12. Taxpayer testified at the hearing and provided in post-hearing memoranda that:
- a. During 2008, Taxpayer held a position of [REDACTED] in the [REDACTED].
 - b. Taxpayer is a research scientist and has had scientific papers published.
 - c. Taxpayer had applied for and had been awarded grants from the National Science Foundation to fund his research.
 - d. Taxpayer was the principal investigator on the grant but the funds were paid to [REDACTED] ([REDACTED]).
 - e. Taxpayer has to be employed by a [REDACTED] in order to submit grant applications.
 - f. Taxpayer's salary for his research was paid by [REDACTED] from the available grant funds.
 - g. Taxpayer does not receive a salary if there are no grant funds available. Taxpayer would again receive a salary if grant funds are awarded to the [REDACTED].
 - h. Taxpayer's grant from the National Science Foundation was exhausted in 2007 and no grant funds were available to pay Taxpayer a salary during 2008.

- i. Taxpayer continued his research using his own funds and continued to apply for grants during 2008.
 - j. Both before and during 2008 [REDACTED] provided Taxpayer with his personal laboratory space and an office.
 - k. [REDACTED] considered Taxpayer an employee both before 2008 and during 2008.
 - l. Taxpayer did not claim lodging expenses while in [REDACTED] because he stayed with his sister.
 - m. The per diem rate for meals and incidentals for [REDACTED] during September 2008 was \$[REDACTED].
13. The Section testified at the hearing that Taxpayer substantiated he was in [REDACTED] for research and agreed to allow his [REDACTED] airfare of \$[REDACTED].

CONCLUSIONS OF LAW

- 1. The burden is on the taxpayer to show he is entitled to a deduction or exemption from tax. *See Ebasco Servs., Inc. v. Ariz. State Tax Comm'n*, 105 Ariz. 94, 99, 459 P.2d 719, 724 (1969).
- 2. Taxpayer was an employee of [REDACTED] entitled to claim verified unreimbursed employee expenses.
- 3. A college professor may deduct research expenses undertaken in connection with the duties expected of him and without expectation of profit apart from salary. IRS Pub. 529 (2008) p.6.
- 4. A research professor may be considered an employee even if paid by the university from a grant and the means and methods of carrying on the project, as well as the hours during which the research services were performed, were left to the judgment of the professor. *See*, Rev. Rul. 55-583.

5. Taxpayer incurred his research related expenses during 2008 at least in part in an effort to secure additional grant funding for his research.
6. A taxpayer may use a standard meal allowance method, as an alternative to the actual cost method, to calculate the cost of daily meals and incidental expenses. IRS Pub 463 (2008) p. 5.
7. A taxpayer using the standard meal allowance (per diem) method does not have to keep records of actual costs. The taxpayer must still establish the time, place and business purpose of the travel. IRS Pub. 463 (2008), pg. 5.
8. A taxpayer is entitled to deduct only one-half of the per diem allowed for meals and incidental expenses. IRS Pub. 463 (2008) p. 6; IRS Pub. 17 (2008) p. 177.
9. Taxpayer was entitled to deduct one-half of his per diem meal and incidental expenses of \$[REDACTED], while he was in [REDACTED] collaborating with [REDACTED] scientists and \$[REDACTED] for his trip to [REDACTED].
10. Because Taxpayer is claiming a standard meal allowance, Taxpayer is not entitled to a deduction of the actual dining hall fee of \$[REDACTED].
11. 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.
12. The modified proposed assessment dated January 29, 2014 issued by the Section for tax year 2008 is upheld in part. The Section shall allow additional Schedule A miscellaneous itemized deductions, subject to the 2% limit, of \$[REDACTED] (one half of the per diem for [REDACTED] of \$[REDACTED], one half of the per diem for [REDACTED] of \$[REDACTED] and airfare of \$[REDACTED].)
13. The Section shall reduce the amount allowed for [REDACTED] Housing and lab fees from \$[REDACTED] to \$[REDACTED].

DISCUSSION

Taxpayer filed a 2008 resident Arizona individual income tax return claiming a Schedule A deduction for unreimbursed employee expenses of \$[REDACTED]. The Section reviewed Taxpayer's return and issued a proposed assessment disallowing the miscellaneous itemized deduction, allowing instead a standard deduction. Taxpayer protested stating that he is involved in scientific research and the claimed expenses were incurred in connection with his research activity working at [REDACTED]. Taxpayer's work is supported entirely by research grants and during 2008 he was between grants. Therefore Taxpayer did not receive a salary during 2008. Even though Taxpayer did not receive grant support for his research activity, he had to continue his research activity.

Taxpayer held a position of [REDACTED] in the [REDACTED] before and during 2008. [REDACTED] considered Taxpayer an employee, paid him a salary, provided benefits, withheld taxes and provided him with a laboratory and an office during years prior to 2008. Even though the grant was exhausted in 2007, [REDACTED] continued to provide Taxpayer laboratory and office space during 2008. The fact that grant funds were not available during 2008 and therefore Taxpayer was not paid a salary did not change his status as an employee. Taxpayer was entitled to deduct his verified unreimbursed research related expenses.

[REDACTED] Expenses:

The Section allowed a portion of Taxpayer's claimed expenses for his trip to [REDACTED]. However, instead of allowing Taxpayer a per diem meal allowance, the Section allowed Taxpayer his actual dining hall fee for two meals per week.

A taxpayer cannot claim both actual expenses and expenses based on a standard meal allowance. A taxpayer may choose either method. Here Taxpayer chose to use a standard meal allowance to calculate the cost of daily meals and incidental expenses. Meal expenses however, whether based on actual expenses or on a standard allowance, are limited to one-half of the allowable amount. Taxpayer is

therefore entitled to deduct one-half of his per diem meal allowance relating to his trip to [REDACTED].

[REDACTED] Expenses:

The Section has agreed to allow Taxpayer's air fare to [REDACTED] but has not allowed any other expenses. Taxpayer did not claim any lodging expenses (he stayed with family), but did claim a per diem allowance. The per diem allowance for [REDACTED] during September 2008 was \$[REDACTED]. Taxpayer's trip to [REDACTED] was in connection with his scientific research activity and Taxpayer was entitled to deduct one-half of his per diem meal allowance relating to his trip to [REDACTED].

The proposed assessment 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 abated unless the tax to which it relates is found not to be due.

Based on the foregoing, the Section's modified proposed assessment dated January 29, 2014 is upheld in part. The Section shall allow Taxpayer additional unreimbursed employee expenses consistent with Conclusions of Law Nos. 12 and 13.

DATED this 28th day of March, 2014.

ARIZONA DEPARTMENT OF REVENUE
HEARING OFFICE

[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