

STATE OF NORTH CAROLINA  
COUNTY OF WAKE

BEFORE THE  
SECRETARY OF REVENUE

IN THE MATTER OF:

The Proposed Assessment of Gift Tax )  
Penalties for the Taxable Year 2002 by the )  
Secretary of Revenue of North Carolina )  
vs. )  
Taxpayer )

**FINAL DECISION**  
Docket No. 2004-340

This matter was heard before the Assistant Secretary for Administrative Tax Hearings, Eugene J. Cella, in the city of Raleigh on September 2, 2004, upon an application for hearing by the accountant for taxpayer, hereinafter referred to as "Donor," wherein he protested on behalf of Donor the proposed assessment of gift tax penalties for the taxable year 2002. The hearing was held by the Assistant Secretary under the provisions of G.S. 105-260.1 and was attended by an Accountant, hereinafter referred to as "Accountant;" W. Edward Finch, Jr., Assistant Director of the Personal Taxes Division; and Patrick G. Penny, Administrative Officer in the Personal Taxes Division.

Pursuant to G.S. 105-241.1, an assessment proposing gift tax penalties for the tax year 2002 was mailed to Donor on December 5, 2003. A copy of the assessment notice was mailed to Accountant on the same day. On behalf of Donor, Accountant objected to the proposed assessment and requested an administrative tax hearing before the Secretary of Revenue.

**ISSUE**

The issues to be decided in this matter are as follows:

Is the assessment of penalties proposed against Donor for the taxable year 2002 lawful and proper?

Do special circumstances exist for waiving the twenty percent late filing penalty and the ten percent late payment penalty?

### **EVIDENCE**

The evidence presented by W. Edward Finch, Jr., Assistant Director of the Personal Taxes Division, consisted of the following:

1. Memorandum from E. Norris Tolson, Secretary of Revenue, to Eugene J. Cella, Assistant Secretary for Administrative Tax Hearings, dated May 16, 2001, a copy of which is designated as Exhibit PT-1.
2. Donor's North Carolina gift tax return for the taxable year 2002, a copy of which is designated as Exhibit PT-2.
3. Notice of Gift Tax Assessment for the taxable year 2002 dated December 5, 2003, a copy of which is designated as Exhibit PT-3.
4. Letter from Accountant to the Department of Revenue dated December 10, 2003, a copy of which is designated as Exhibit PT-4.
5. Letter from M. D. Wall, Revenue Tax Auditor, to Accountant dated January 5, 2004, a copy of which is designated as Exhibit PT-5.
6. Letter from Accountant to M.D. Wall dated January 29, 2004, a copy of which is designated as Exhibit PT-6.
7. Letter from M. D. Wall to Accountant dated March 2, 2004, a copy of which is designated as Exhibit PT-7.
8. Letter from Accountant to M.D. Wall dated April 15, 2004, a copy of which is designated as Exhibit PT-8.
9. Letter from Accountant to M.D. Wall dated June 23, 2004, a copy of which is designated as Exhibit PT-9.
10. Letter from Angela C. Quinn, Administrative Officer in the Personal Taxes Division, to Accountant dated July 1, 2004, a copy of which is designated as Exhibit PT-10.
11. Response from Accountant to Angela C. Quinn, a copy of which is designated as Exhibit PT-11.
12. Letter from Eugene J. Cella to Accountant dated July 27, 2004, a copy of which is designated as Exhibit PT-12.

Accountant presented the following evidence at the hearing:

1. Certificate of Assignment dated December 29, 1995, a copy of which is designated as Exhibit TP-1.
2. Certificate of Assignment dated December 29, 1995, a copy of which is designated as Exhibit TP-2.
3. Certificate of Assignment dated January 4, 1996, a copy of which is designated as Exhibit TP-3.
4. Certificate of Assignment dated January 4, 1996, a copy of which is designated as Exhibit TP-4.
5. Certificate of Assignment dated January 2, 1997, a copy of which is designated as Exhibit TP-5.
6. Certificate of Assignment dated January 2, 1997, a copy of which is designated as Exhibit TP-6.
7. Certificate of Assignment dated January 5, 1998, a copy of which is designated as Exhibit TP-7.
8. Certificate of Assignment dated January 5, 1998, a copy of which is designated as Exhibit TP-8.
9. Certificate of Assignment dated January 2, 1999, a copy of which is designated as Exhibit TP-9.
10. Certificate of Assignment dated January 2, 1999, a copy of which is designated as Exhibit TP-10.
11. Certificate of Assignment dated August 23, 2000, a copy of which is designated as Exhibit TP-11.
12. Certificate of Assignment dated August 23, 2000, a copy of which is designated as Exhibit TP-12.
13. Certificate of Assignment dated April 2, 2001, a copy of which is designated as Exhibit TP-13.
14. Certificate of Assignment dated April 2, 2001, a copy of which is designated as Exhibit TP-14.
15. Certificate of Assignment dated January 2, 2002, a copy of which is designated as Exhibit TP-15.

16. Certificate of Assignment dated January 2, 2002, a copy of which is designated as Exhibit TP-16.
17. Certificate of Assignment dated January 2, 2002, a copy of which is designated as Exhibit TP-17.
18. Certificate of Assignment dated January 2, 2002, a copy of which is designated as Exhibit TP-18.
19. Certificate of Assignment dated January 2, 2002, a copy of which is designated as Exhibit TP-19.
20. Certificate of Assignment dated January 2, 2003, a copy of which is designated as Exhibit TP-20.
21. Certificate of Assignment dated January 2, 2003, a copy of which is designated as Exhibit TP-21.
22. Certificate of Assignment dated January 2, 2003, a copy of which is designated as Exhibit TP-22.
23. Certificate of Assignment dated January 2, 2003, a copy of which is designated as Exhibit TP-23.
24. Certificate of Assignment dated January 2, 2003, a copy of which is designated as Exhibit TP-24.
25. Certificate of Assignment dated January 2, 2004, a copy of which is designated as Exhibit TP-25.
26. Certificate of Assignment dated January 2, 2004, a copy of which is designated as Exhibit TP-26.
27. Certificate of Assignment dated January 2, 2004, a copy of which is designated as Exhibit TP-27.
28. Certificate of Assignment dated January 2, 2004, a copy of which is designated as Exhibit TP-28
29. Certificate of Assignment dated January 2, 2004, a copy of which is designated as Exhibit TP-29.

## FINDINGS OF FACT

Based on the foregoing evidence of record, the Assistant Secretary makes the following findings of fact:

1. Donor has been a resident of North Carolina since 1999.
2. Donor made a series of gifts of units of a limited partnership on January 2, 2002. Donor has made similar gifts each year since 1995.
3. In each of the years 1997, 1998, 1999, 2000, and 2001, the amount of each gift did not exceed the annual exclusion amount; therefore, a federal gift tax return was not required to be filed for any of these years. Likewise, a North Carolina gift tax return was not required to be filed for 1999, 2000, and 2001.
4. Three of the gifts made on January 2, 2002, exceeded the annual exclusion amount, thereby requiring a 2002 federal gift tax return and a 2002 North Carolina gift tax return to be filed.
5. On behalf of Donor, Accountant timely filed federal Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return, reflecting a request for a gift tax return extension in addition to the individual income tax extension. The gift tax payment line on Form 4868 reflects *zero*. At the hearing, Accountant testified that it is his firm's practice to automatically request a federal gift tax extension when requesting a federal income tax extension, even when no known gifts have been made during the year because the gift tax extension request is included on the individual income tax extension request and can be obtained by simply checking the appropriate box. Accountant contends that the fact that Donor's federal income tax extension request included a request for a gift tax extension does not indicate that he or Donor was aware that taxable gifts had been made during 2002 at the time the federal extension request was filed.
6. On behalf of Donor, Accountant timely filed Form D-410, Application for Extension for Filing North Carolina Individual Income Tax Return. Accountant did not file Form D-410G, Application for Extension for Filing North Carolina Gift Tax Return, for calendar year 2002.
7. Donor filed her 2002 North Carolina gift tax return on August 15, 2003, without an approved extension of time for filing the return. The return reflected tax and interest of \$12,504.00, payment of which was included with the return.
8. Upon examination, the auditor asserted a late filing penalty of \$2,451.60 and a late payment penalty of \$1,225.80. A Notice of Gift Tax Assessment reflecting the penalties was mailed to Donor on December 5, 2003. A copy of the notice was mailed to Accountant on the same day.
9. Accountant objected to the proposed assessment of penalties and timely requested an administrative tax hearing before the Secretary of Revenue.

10. Accountant is the son-in-law of Donor. Accountant, his wife, and his children were recipients of gifts made by Donor in January 2002. Accountant and his family have received annual gifts from Donor since at least 1995.
11. In Accountant's letter of January 29, 2004, he stated that he was not aware of the substantial gifts Donor made in January 2002. At the hearing, Accountant clarified that he did not mean that he was unaware that Donor had made gifts; he was unaware that Donor had made taxable gifts requiring a return to be filed.
12. Donor is elderly and relied on Accountant to handle her tax matters. Accountant was aware that Donor made certain gifts each year and, since 1997, the gifts were designed not to exceed the annual exclusion amount, thereby avoiding any gift tax liability and requirement to file a gift tax return. Documentation provided by Accountant supports this gift-giving history of Donor. During 2002, Donor made her annual gifts, but three of the gifts exceeded the annual exclusion amount. Accountant assumed that Donor made her usual non-taxable gifts in 2002 and did not become aware that Donor had made taxable gifts until August 2003. Once Accountant became aware of the taxable gifts, he immediately prepared Donor's 2002 North Carolina gift tax return and calculated Donor's gift tax liability plus interest, which Donor paid when she filed the return on August 15, 2003.
13. Accountant agrees that penalties were properly assessed; however, Accountant contends that the facts set out in Findings of Fact #12 constitute special circumstances which support waiver of the penalties.

### **CONCLUSIONS OF LAW**

Based on the foregoing findings of fact, the Assistant Secretary makes the following conclusions of law:

1. A North Carolina gift tax return is required to be filed if a donor transfers property without receiving consideration equal to the fair market value of the property and the fair market value exceeds the consideration paid by the annual exclusion amount. The annual exclusion amount is equal to the federal inflation-adjusted exclusion amount provided in section 2503(b) of the Internal Revenue Code. For tax year 2002, the annual exclusion amount was \$11,000. Donor was required to file a 2002 North Carolina gift tax return since she made several gifts of property exceeding \$11,000 during 2002.
2. The North Carolina gift tax return for a given calendar year must be filed and the gift tax paid by April 15 of the following year. Donor's 2002 gift tax return was due to be filed on April 15, 2003. Donor's 2002 gift tax liability was due to be paid on April 15, 2003.
3. To receive an automatic six-month extension of time to file a North Carolina gift tax return, a donor must file Form D-410G, Application for Extension for Filing Gift Tax Return, by the original due date of the return. Donor did not file Form D-410G for tax year 2002.

4. A penalty is required for failure to file a gift tax return when due. The penalty is equal to five percent of the tax for each month, or fraction of a month, the return is late (minimum \$5.00, maximum twenty-five percent). A penalty is required for failure to pay gift tax when due. The penalty is equal to ten percent of the tax (minimum \$5.00). Because Donor did not file her 2002 gift tax return until August 15, 2003, a late filing penalty of \$2,451.60 and a late payment penalty of \$1,225.80 were properly imposed.
5. The Secretary of Revenue is authorized to waive or reduce any penalty. Such waiver or reduction is proper when a gift taxpayer establishes special circumstances.

### **DECISION**

Both the Department and Accountant agree that the late filing and late payment penalties were properly assessed as required by statute. The second issue to be decided is whether the facts and circumstances warrant waiver or reduction of the penalties proposed.

Based on the facts and evidence presented, the Assistant Secretary finds special circumstances for waiver of the late filing penalty of \$2,451.60 and the late payment penalty of \$1,225.80.

Made and entered this 19th day of November, 2004.

Signature\_\_\_\_\_

Eugene J. Cella

Assistant Secretary for Administrative Tax Hearings  
North Carolina Department of Revenue