

STATE OF ALABAMA,

V.

ALABAMA PLASTIC SURGERY, P.A.
1722 Pine Street
Montgomery, AL 36106,

Taxpayer.

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STATE OF ALABAMA

DEPARTMENT OF REVENUE

ADMINISTRATIVE LAW DIVISION

DOCKET NO. INC.85-128

ORDER

This case involves a disputed withholding tax preliminary assessment entered by the Revenue Department against Alabama Plastic Surgery, P.A. (hereinafter Taxpayer) for the period January 1, 1982 - December 31, 1982. A hearing was conducted under the provisions of the Administrative Procedure Act, Code of Alabama 1975, '41-22-1, et seq., on September 24, 1985. Representing the parties were Dr. David M. Connelly, M.D., for the Taxpayer, and Elizabeth Bookwalter, for the Department. Based on the evidence introduced at said hearing, the following findings of fact and conclusions of law are hereby made and entered.

FINDINGS OF FACT

The pertinent facts are undisputed. The Taxpayer is a professional association operating in Montgomery. On August 15, 1982, the Taxpayer received from Dr. David M. Connelly, an employee, a federal W-4 form (employees withholding allowance certificate) claiming exempt status for the year 1982. Dr. Connelly received wages from the Taxpayer on September 26, 1982. No federal or state income tax was withheld on said wage payment.

The Revenue Department audited the Taxpayer and determined that the Taxpayer had erroneously failed to withhold state taxes relative to the wages paid to

Dr. Connelly. The Department auditor, not knowing exactly when Dr. Connelly had received the wages, prorated the entire amount equally over the four quarters of the year. Withholding tax was computed on the income prorated for each quarter. Penalty and interest was then computed on the tax determined to be due. The Department subsequently found no tax due by Dr. Connelly for the year. Consequently, the preliminary assessment in issue shows only penalty and interest due on the tax that should have been withheld by the Taxpayer from Dr. Connelly's wages.

The Taxpayer admits that it should have withheld from Dr. Connelly's wages. The failure to withhold was based on the advice of counsel, and an incorrect interpretation of a Revenue Department instruction booklet. The Department agrees that the penalty included in the assessment should be waived. The only issue is the proper method for the computation of interest.

The Department argues that interest is due in at least the amount shown on the assessment. The Taxpayer argues that the Department's computation of interest is incorrect and that a lesser amount is due than set out in the assessment.

CONCLUSIONS OF LAW

Code of Alabama 1975, '40-1-44 provides in substance that interest on any unpaid taxes shall accrue from the due date of said taxes. The Taxpayer objects to the method of computation employed by the Department in computing interest on the assessment. As stated above, the Department auditor split Dr. Connelly's total 1982 income into equal quarterly portions. Withholding tax was then computed for each quarter, and Interest was computed on the tax determined to be due beginning on

each quarterly report due date.

The Taxpayer contends that its withholding tax liability arose only in the third quarter of 1982, when Dr. Connelly actually received the wages, and not before. The Department agrees. The splitting of Dr. Connelly's income into four quarterly installments was done only because the Department auditor did not know in which quarter the wages had actually been received. The Taxpayer further contends that interest should accrue from the due date of the third quarter report, which was October 31, 1982. Again the Department agrees. However, while it appears at first glance that the interest included in the assessment is excessive because tax and interest was computed on the first and second quarters, a comparison of the actual method of computation used to compute the tax and interest due thereon as opposed to the correct method set out herein, illustrates that the Taxpayer would owe more interest, not less, if the correct computation method were used. The reason is an increase in the withholding rate effective July 1, 1982.

Section 40-18-71, which specifies the withholding amounts, was amended effective July 1, 1982 to provide for a significant increase in the rate of withholding tax. Consequently, because Dr. Connelly's entire wages were received in September, 1982, after the increase took effect, the entire amount should have been subject to the increased rates. Under the method used by the Department, only one-half of the wages were subject to the increased rate, while the other half were taxed at the lower pre-July 1, 1982 rate. According to the Department's computations, the tax computed entirely under the higher rate would result in a much larger tax liability, and correspondingly, a greater basis on which to compute interest.

Interest due on the preliminary assessment as entered is \$625.76. The interest due if the tax and interest were correctly recomputed would be \$675.06. Thus, although the Taxpayer is correct in arguing that interest was computed incorrectly on the preliminary assessment, the corrected computation would result in a greater liability.

Based on the above, the Department is hereby directed to waive the penalty, as agreed by the Department, and there after make the assessment final based on the interest amount as originally computed, as argued by the Department.

Done this 2nd day of October 1985.

BILL THOMPSON
Chief Administrative Law Judge