

10/11/93

STATE OF MINNESOTA
DEPARTMENT OF REVENUE

**In the Matter of the Proposed
Adoption Without a Public Hearing
of the Rule Governing Penalty for
Repeated Failures to Pay Taxes**

**STATEMENT OF NEED
AND REASONABLENESS**

This document has been prepared to establish the statutory authority, need for, and reasonableness of the proposed rule. It is submitted pursuant to Minnesota Statutes, section 14.23 and Minnesota Rules, part 2010.0700 requiring a statement of need and reasonableness.

Authority to Adopt Rules. The adoption of the rule is mandated by Laws 1993, Chapter 375, Article 10, Section 51, which requires the Department of Revenue to promulgate rules prescribing what constitutes repeated failures to pay taxes before the 25 percent penalty for such failures, enacted in the same article, can be imposed.

Small Business Considerations. The Department of Revenue believes that the rule will not have an impact on small business as contemplated by Minnesota Statutes, section 14.115. The rule does not impose any new filing requirements or additional taxes on small business. It merely impacts small businesses who repeatedly pay their taxes late, which presumably is a low percentage of the business population. Also, as explained in the discussion of subpart 1, item A, of the rule in this statement, the impact on small businesses is minimal in comparison to the impact on large businesses that repeatedly pay their taxes late.

Expenditure of Public Money by Local Public Bodies. The Department of Revenue estimates the total cost to public bodies to implement the rule for the two years following the adoption of the rule is less than \$100,000, and therefore Minnesota Statutes, section 14.11, subdivision 1, is not applicable. The rule has no provisions that require implementation by local public bodies. The statutes that the rule interprets impose a penalty for repeatedly paying taxes late, and the rule merely prescribes when the penalty is imposed.

Minnesota Rules, part 8175.0100. Subpart 1. Item A. This item describes the scope of the rule by listing the statutory references for all the tax types that have a 25 percent penalty for repeated failures to pay taxes. The statutes impose the penalty for both the late filing of returns and the late payment of taxes. The rule is confined, however, to late payment. This is because the penalty is always based upon the amount of tax paid late, and thus it is not reasonable or workable to include the late filing of returns in the formula for determining the penalty.

This item also prescribes the measuring period and the number of violations that constitute a pattern of repeated failures to pay taxes. The Department of Revenue chose the time period of 25 months, because it is reasonable to presume that two years is a sufficient amount of time in which to judge the tax payment history of both taxpayers who file on a monthly basis and those who file on a quarterly basis. With the additional month, the Department can review 25 reporting periods for the monthly filers and 9 reporting periods for the quarterly filers. The number of violations chosen was three, because it is reasonable to

presume that this number constitutes a pattern or is repetitious in common, everyday understanding. Also, the formula is applied to late payment violations for the same tax type. This is reasonable, because each tax type has its own filing and payment requirements, and the Department of Revenue and many taxpayers administer them separately.

The standard of three violations in 25 months places the highest exposure to the penalty on those taxpayers who are monthly filers. This is reasonable, because in the case of sales taxes, for example, the requirement to file yearly, quarterly or monthly is based upon the amount of the taxpayer's liability. The greater the liability, the more frequently the taxpayer is required to pay. The Legislature has emphasized the importance of having the larger taxpayers pay their taxes frequently and timely, not only with when the due dates of the payments occur, but also with the requirement to pay taxes by means of electronic funds transfers. These burdens are justified, because the larger taxpayers are generally more sophisticated in tax matters. Greater exposure to this penalty is therefore consistent with legislative intent in related areas.

Finally, this item states that if one or more of the violations is a late payment of estimated tax subject to an additional tax charge, the number of violations that constitutes a pattern increases to four. The charge referred to is assessed as an equivalent of interest. By not providing a more severe late payment penalty, the Legislature has declared that this type of violation is less serious. Therefore, it is reasonable to allow one extra violation to constitute a pattern.

Item B. This item lumps certain tax types together as one tax type for purposes of the rule, because they are taxes that are reported and paid at the same time and in the same manner. Examples are: (1) the cigarette tax and tobacco products tax imposed under Minnesota Statutes, chapter 297; and (2) the solid waste assessment that is included on the sales tax return. Example one is reasonable, because distributors in the cigarette and tobacco industry normally pay both taxes, and they are due at the same time and must be sent to the same office in the Department of Revenue. Example two is reasonable, because when the taxpayer files the return, the taxpayer submits one payment for both the sales tax and the solid waste assessment, not two separate payments.

Item C. This item states that late deposits of withholding tax are not included in the formula for determining the penalty, as long as the deposits are fully paid by the end of the quarterly reporting period. This is reasonable, because deposits can be due as frequently as every Wednesday and Friday, resulting in this group of taxpayers having a much greater exposure to the penalty than all other taxpayers affected by the rule. Furthermore, the applicability of other late payment penalties, coupled with the great frequency of these deposits, should encourage general compliance and impose a significant penalty burden on chronic late depositors.

Item D. This item clarifies that estimated payments, electronic funds transfer payments, and the June estimated payment (which is required for sales tax, cigarette and tobacco products taxes, and liquor taxes) are included in the formula for determining the penalty. This is needed so that all types of tax payments, not just payments due with returns, are covered by the rule. It is reasonable, because a late

payment should not be excluded from the scope of the penalty merely because it is a different type or manner of payment.

Item E. This item excludes from the formula late payments for which the taxpayer established reasonable cause for the lateness. Once a late payment penalty has been abated for a violation, it would be unjust and inequitable to still include that late payment in the formula for determining the chronic delinquency penalty.

Item F. This item is consistent with long-standing administrative practice and procedure regarding the imposition of late filing and late payment penalties. If a taxpayer has been granted an extension of time in which to file a return or pay a tax and the return is not filed or the tax is not paid by the extended due date, the Department of Revenue calculates the late filing and late payment penalties from the original due date. In other words, if the taxpayer does not comply with the terms of the extension, the extension is treated as if it had never been granted.

Subpart 2. The statutes cited in subpart 1, item A, all state that before the 25 percent penalty can be imposed, the Department of Revenue must give the taxpayer written notice. This subpart is necessary to clarify how many days notice is required, what information is in the notice, and how long the notice remains in effect. Ten days notice is a reasonable amount of time, since the taxpayer has incurred three late payment violations and has already received billing notices from the Department. The information required by the fourth sentence of this subpart is necessary for the taxpayer to understand the purpose of the notice, and to verify its correctness. Finally, the length of time the notice is effective is reasonable, because it requires the taxpayer to demonstrate timely payment of taxes until the taxpayer falls below the threshold criteria that gave rise to the notice in the first place. Having the notice ongoing instead of for a fixed time eliminates the administrative burden of having to issue periodic warning notices for behavior that the taxpayer already knows is a violation of law.

Subpart 3. The first sentence of this subpart is necessary to clarify that if the tax the taxpayer reports on a return and pays late is not the correct tax, the penalty is 25 percent of the amount of tax finally determined to be due. The second sentence is necessary to clarify that the 25 percent penalty is in addition to, not in lieu of, the standard late payment penalties and additional charges.

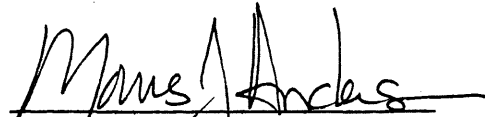
Subpart 4. The statutes cited in subpart 1, item A, all state that the 25 percent penalty can be abated under the authority of Minnesota Statutes, section 270.07, subdivisions 1, paragraph (e), and 6. This subpart is necessary to clarify that the basis of the taxpayer's abatement request can be twofold. First, if there is reasonable cause for abating the standard late payment penalty imposed upon the current late payment, then the 25 percent penalty is likewise abated. Second, the taxpayer can challenge the penalty on the ground that the notice warning the taxpayer a 25 percent penalty would be imposed on future late payment violations was incorrect. These provisions ensure that the taxpayer is afforded due process. However, the taxpayer cannot raise the issue of reasonable cause for those late payment violations in the notice for which the time to request a penalty abatement has expired. This is justified, because the purpose of the 25 percent penalty is to penalize taxpayers who are repeatedly delinquent, not to allow them an avenue to make late requests for penalty abatements. Finally, this subpart clarifies that the appeal procedures for this

penalty are governed by the same procedures and time limits that govern all other penalty abatements. This provision is needed for uniformity and consistency of the abatement process.

Subpart 5. This subpart is needed to clarify that the effective date of this rule coincides with the effective date of the statutes cited in subpart 1, item A. (See Laws 1993, chapter 375, article 10, section 52.)

Dated:

9-22-93


Morris J. Anderson
Commissioner of Revenue