

# Bill as Introduced

HB 557-FN-A - AS INTRODUCED

2011 SESSION

11-0160

09/04

HOUSE BILL

***557-FN-A***

AN ACT

relative to the standards and burden of proof with respect to the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships.

SPONSORS:

Rep. Sapareto, Rock 5; Rep. Weyler, Rock 8; Rep. Major, Rock 8; Rep. Chandler, Carr 1; Rep. Mirski, Graf 10; Sen. Gallus, Dist 1; Sen. Barnes, Jr., Dist 17

COMMITTEE:

Ways and Means

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ANALYSIS

This bill modifies the standards and burden of proof with respect to the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships.

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Explanation:

Matter added to current law appears in ***bold italics***.

Matter removed from current law appears [~~in brackets and struckthrough.~~]

Matter which is either (a) all new or (b) repealed and reenacted appears in regular type.

STATE OF NEW HAMPSHIRE

*In the Year of Our Lord Two Thousand Eleven*

AN ACT                   relative to the standards and burden of proof with respect to the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships.

*Be it Enacted by the Senate and House of Representatives in General Court convened:*

1           1 Purpose. The legislature finds that:

2           I. Small businesses are the lifeblood of the New Hampshire economy and are the most  
3 important source of jobs for residents of New Hampshire.

4           II. Recent increases in audits of small businesses in which small business owners are not  
5 allowed to deduct the full and fair value of their services to their small business in determining the  
6 business profits tax liability of the business have undermined New Hampshire's ability to provide a  
7 sound and encouraging environment for small business growth.

8           III. Good tax policy requires tax rules that provide taxpayers with clear guidance, encourage  
9 compliance, and enhance the competitiveness of our economy.

10           IV. This act clarifies important business profits tax rules that apply to small businesses,  
11 eliminate costly and inefficient audits, and restore New Hampshire's ability to encourage small  
12 business growth and the good jobs these businesses create.

13           2 Clarification of Reasonable Compensation Deduction. RSA 77-A:4, III is repealed and  
14 reenacted as follows:

15           III.(a) In the case of a proprietorship, partnership, or limited liability company filing a  
16 business profits tax return as a proprietorship or a partnership, a deduction equal to a fair and  
17 reasonable compensation for the personal services of a natural person who is a proprietor, partner, or  
18 member provided to the business organization, provided, under this chapter however, that the  
19 amount of such deduction shall not reduce such business organization's tax to less than zero. The  
20 purpose of this paragraph is to permit a deduction from gross business profits of such a  
21 proprietorship, partnership, or limited liability company of all amounts that are fairly attributable to  
22 the personal services of the proprietor, partner, or member. Such amounts shall generally include all  
23 amounts reported as earned income on federal tax returns, but shall also include amounts  
24 attributable to personal services provided in connection with the operation and rental of real  
25 property, the sale of property and services, and other amounts due to services rendered.

26           (b) A taxpayer claiming a deduction under this paragraph shall bear the burden of  
27 proving that at least one or more proprietors, partners, or members provided actual services to the  
28 business organization at any time during the taxable period. Once a taxpayer has satisfied this  
29 burden of proof, the amount claimed as a deduction shall be presumed to be reasonable, unless the

**HB 557-FN-A - AS INTRODUCED**

**- Page 2 -**

1 commissioner proves by a preponderance of the evidence that the deduction claimed by the taxpayer  
2 is grossly excessive.

3 3 Applicability. Sections 1-2 of this act shall apply with respect to taxable periods ending after  
4 June 30, 2011.

5 4 Effective Date. This act shall take effect July 1, 2012.

LBAO  
11-0160  
12/20/10

**HB 557-FN-A - FISCAL NOTE**

**AN ACT** relative to the standards and burden of proof with respect to the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships.

**FISCAL IMPACT:**

The Department of Revenue Administration states this bill will decrease state revenue by \$49,430,000 in FY 2012 and each year thereafter. There will be no fiscal impact on county and local revenue or state, county, and local expenditures.

**METHODOLOGY:**

The Department of Revenue Administration states this bill would transfer the burden of proof for the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships to the Department. The Department states this bill would make it responsible for proving whether a deduction taken for reasonable compensation is grossly excessive. The Department states this bill will make it difficult for it to dispute a taxpayer's compensation deduction because the Department does not have any information about the services rendered by the partnership or proprietorship. The Department states as a result, it would be ineffective to conduct an audit of a partnership or proprietorship to ensure compliance with the law.

The Department of Revenue Administration states partnerships and proprietorships paid \$49,430,000 in business profits taxes during tax year 2008. The Department assumes the bill would result in no partnerships or proprietorships being liable to pay the business profits tax and would result in a decrease in revenue by the same amount. The Department further states it can administer the law without any additional direct costs.

# Amendments

"NOT ADOPTED"

Rep. Sapareto, Rock. 5  
February 25, 2011  
2011-0534h  
09/10

Amendment to HB 557-FN-A

1 Amend RSA 77-A:4, III as inserted by section 2 of the bill by replacing it with the following:

2  
3 III.(a) In the case of a proprietorship, partnership, or limited liability company filing a  
4 business profits tax return as a proprietorship or a partnership, a deduction equal to a fair and  
5 reasonable compensation for the personal services of a natural person who is a proprietor, partner,  
6 or member provided to the business organization, provided, under this chapter however, that the  
7 amount of such deduction shall not reduce such business organization's tax to less than zero. The  
8 purpose of this paragraph is to permit a deduction from gross business profits of such a  
9 proprietorship, partnership, or limited liability company of all amounts that are fairly attributable to  
10 the personal services of the proprietor, partner, or member. Such amounts shall generally include  
11 all amounts reported as earned income on federal tax returns, but shall also include amounts  
12 attributable to personal services provided in connection with the operation and rental of real  
13 property, the sale of property and services, and other amounts due to services rendered.

14 (b) Subject to the provisions of subparagraph (c) which establishes a record-keeping safe  
15 harbor, the amount of the deduction allowed under this paragraph shall be determined using the  
16 standards set forth in section 162(a)(1) of the United States Internal Revenue Code, as it may be  
17 amended from time to time, and the Treasury Regulations, administrative rulings, and judicial cases  
18 issued thereunder.

19 (c) In lieu of substantiating the value of the personal services of proprietors, partners, or  
20 members, a business organization or group of related business organizations may elect, as a record-  
21 keeping safe-harbor, to deduct up to \$50,000 as total compensation for the tax year;

22 (d)(1) In this paragraph, "record-keeping safe harbor" means that amount of  
23 compensation for personal services claimed by a business organization which does not need to be  
24 substantiated by any evidence, records, or legal or regulatory authority, except as provided in  
25 subparagraph (e).

26 (2) Notwithstanding subparagraph III(d)(1), the record-keeping safe harbor shall not  
27 be relevant or admissible for any purpose in determining whether a compensation deduction claimed  
28 in an amount in excess of any such record-keeping safe harbor is fair and reasonable.

29 (e) A business organization or group of related business organizations may elect the  
30 record-keeping safe-harbor option in subparagraph III(c) without a redetermination of the  
31 reasonableness of the deduction by the commissioner. Any such deduction claimed by the business  
32 organization or group of related business organizations shall not be subject to challenge; provided,



1 that upon request, the business organization or group of related business organizations shall be  
2 required to substantiate that the proprietor or at least one partner or member performed personal  
3 services for the business organization or group of related business organizations.

4 (f) Related business organizations electing not to substantiate the extent of the personal  
5 services of their proprietors, partners, and members, shall be limited to the safe harbor deduction,  
6 less any owners' compensation taken on the federal tax returns of corporate members of the group,  
7 allocated among the related business organizations. For the purposes of RSA 77-A:4, III, "related  
8 business organizations" are unitary business organizations and business organizations that would  
9 qualify as unitary but for the fact that they conduct business only within the state.

10  
11 Amend the bill by inserting after section 2 the following and renumbering the original sections 3-4 to  
12 read as 5-6, respectively:

13  
14 3 New Paragraph; Appeal for Redetermination or Reconsideration; Procedure. Amend RSA 21-  
15 J:28-b by inserting after paragraph VII the following new paragraph:

16 VIII. The department shall bear the burden of proof on any change to any compensation  
17 deduction under RSA 77-A finally determined to be due after January 1, 2011.

18 4 New Section; Interest and Dividends Tax; Excess Compensation. Amend RSA 77 by inserting  
19 after section 4-f the following new section:

20 77:4-g Dividend. Excess compensation determined by audit of the department shall not be  
21 considered a dividend under this chapter unless such determination is accepted by the Internal  
22 Revenue Service.



Amendment to HB 557-FN-A

1 Amend RSA 77-A:4, III as inserted by section 2 of the bill by replacing it with the following:

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3 III.(a) In the case of a proprietorship, partnership, or limited liability company filing a  
4 business profits tax return as a proprietorship or a partnership, a deduction equal to a fair and  
5 reasonable compensation for the personal services of a natural person who is a proprietor, partner,  
6 or member provided to the business organization, provided, under this chapter however, that the  
7 amount of such deduction shall not reduce such business organization's tax to less than zero. The  
8 purpose of this paragraph is to permit a deduction from gross business profits of such a  
9 proprietorship, partnership, or limited liability company of all amounts that are fairly attributable to  
10 the personal services of the proprietor, partner, or member. Such amounts shall generally include  
11 all amounts reported as earned income on federal tax returns, but shall also include amounts  
12 attributable to personal services provided in connection with the operation and rental of real  
13 property, the sale of property and services, and other amounts due to services rendered.

14 (b) Subject to the provisions of subparagraph (c) which establishes a record-keeping safe  
15 harbor, one method of determining the amount of the deduction allowed under this paragraph shall  
16 be by using the standards set forth in section 162(a)(1) of the United States Internal Revenue Code,  
17 as it may be amended from time to time, and the Treasury Regulations, administrative rulings, and  
18 judicial cases issued thereunder.

19 (c) In lieu of substantiating the value of the personal services of proprietors, partners, or  
20 members, a business organization or group of related business organizations may elect, as a record-  
21 keeping safe-harbor, to deduct up to \$50,000 as total compensation for the tax year;

22 (d)(1) In this paragraph, "record-keeping safe harbor" means that amount of  
23 compensation for personal services claimed by a business organization which does not need to be  
24 substantiated by any evidence, records, or legal or regulatory authority, except as provided in  
25 subparagraph (e).

26 (2) Notwithstanding subparagraph III(d)(1), the record-keeping safe harbor shall not  
27 be relevant or admissible for any purpose in determining whether a compensation deduction claimed  
28 in an amount in excess of any such record-keeping safe harbor is fair and reasonable.

29 (e) A business organization or group of related business organizations may elect the  
30 record-keeping safe-harbor option in subparagraph III(c) without a redetermination of the  
31 reasonableness of the deduction by the commissioner. Any such deduction claimed by the business  
32 organization or group of related business organizations shall not be subject to challenge; provided,

Amendment to HB 557-FN-A

- Page 2 -

1 that upon request, the business organization or group of related business organizations shall be  
2 required to substantiate that the proprietor or at least one partner or member performed personal  
3 services for the business organization or group of related business organizations.

4 (f) Related business organizations electing not to substantiate the extent of the personal  
5 services of their proprietors, partners, and members, shall be limited to the safe harbor deduction,  
6 less any owners' compensation taken on the federal tax returns of corporate members of the group,  
7 allocated among the related business organizations. For the purposes of RSA 77-A:4, III, "related  
8 business organizations" are unitary business organizations and business organizations that would  
9 qualify as unitary but for the fact that they conduct business only within the state.

10 (g) A taxpayer claiming a deduction under this paragraph shall bear the burden of  
11 proving that at least one or more proprietors, partners, or members provided actual services to the  
12 business organization at any time during the taxable period. Once a taxpayer has satisfied this  
13 burden of proof, the amount claimed as a deduction shall be presumed to be reasonable, unless the  
14 commissioner proves by a preponderance of the evidence that the deduction claimed by the taxpayer  
15 is grossly excessive.

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25 after section 4-f the following new section:

26 77:4-g Dividend. Excess compensation determined by audit of the department shall not be  
27 considered a dividend under this chapter unless such determination is accepted by the Internal  
28 Revenue Service.

# Speakers



# Hearing Minutes

HOUSE COMMITTEE ON WAYS AND MEANS

PUBLIC HEARING ON HB 557-FN-A

**BILL TITLE:** relative to the standards and burden of proof with respect to the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships.

**DATE:** February 22, 2011

**LOB ROOM:** 202      **Time Public Hearing Called to Order:** 2:07 PM

**Time Adjourned:** 2:52 PM

(please circle if present)

**Committee Members:** Reps. Stepanek, Major, Griffin, Hess, Sapareto, Ulery, Osgood, Ober, Abrami, Azarian, Daugherty, McDonnell, Murphy, Ohm, Sanborn, Shuler, Almy, Hamm, Butynski, Hatch and Cooney.

**Bill Sponsors:** Reps. Sapareto, Rock 5; Weyler, Rock 8; Major, Rock 8; Chandler, Carr 1; Mirski, Graf 10; Sens. Gallus, Dist 1; Barnes, Jr., Dist 17

TESTIMONY

\* Use asterisk if written testimony and/or amendments are submitted.

**Representative Sapareto, prime sponsor – supports.** Places the burden on DRA to prove gross excess compensation.

Questions:

Representative Hatch – asks whether this is really like the laws from 20 years ago? Answer: Yes, very similar.

Representative Almy – what is a small business? Answer: Less than \$200,000 gross.

**Patrick Jeffery, North Hampton, NH – supports.** He is a small business owner and is worried about the existing reasonable compensation “safe harbor.” Wants “safe harbor” increased to \$100,000 from \$50,000. Most of the testimony had to do with safe harbors.

**Dave Juvet, BIS – supports.** Many businesses support this bill. He would also like “safe harbor” amendment - \$100,000 would be good.

**John Lighthall & Kathy Surer, DRA – no position.** Gave a history of “grossly excessive compensation.” They were asked to describe how an audit is done.

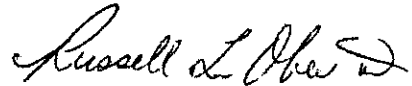
Page 2  
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Question:

Representative Hatch -- are there many audits by the DRA? Answer: We really haven't increased all that much.

Held a long discussion about how many auditors they have and what they do.

Respectfully submitted,

A handwritten signature in cursive script that reads "Russell L. Ober". The signature is written in black ink and is positioned above the printed name.

Representative Russell Ober, Clerk

HOUSE COMMITTEE ON WAYS AND MEANS

PUBLIC HEARING ON HB 557-FN-A

BILL TITLE: relative to the standards and burden of proof with respect to the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships.

DATE: 2/22/2011

LOB ROOM: 202 Time Public Hearing Called to Order: 2:07 pm

Time Adjourned: 2:52 pm

(please circle if present)

Committee Members: Reps. Stepanek, Major, Griffin, Hess, Sapareto, Ulery, Osgood, Ober, Abrami, Azarian, Daugherty, McDonnell, Murphy, Ohm, Sanborn, Shuler, Almy, Hamm, Butynski, Hatch and Cooney

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TESTIMONY

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Rep Sapareto - prime sponsor -

places the burden on DRA to prove gross excess compensation

Question - Rep Hatch - asks whether this is really like the laws from 20 yrs ago

an - yes, very similar

Rep Almy - what is a small business?

Patrick Jeffrey (an) - less than \$200,000 gross

small business owner

supports bill

worried about the existing reasonable compensation "safe harbor"

wants "safe harbor" increased to \$100,000 from \$50,000

most of testimony had to do with safe harbors

Dave Juret - BIA -

supports bill

many businesses support this bill

would also like "safe harbor" amendment - \$100,000 would be good

DRA has no position on bill

Kathy Siner

John Bightwell

gave history of "grossly excessive compensation"

they were asked to describe how an audit is done



Question Rep Hatch - are there many audits by DRA?

Ans - misconception we really haven't involved  
all that much.

Went through a long discussion about how many auditors they have  
and what they do.

# Voting Sheets

HOUSE COMMITTEE ON WAYS AND MEANS

EXECUTIVE SESSION on HB 557-FN-A

**BILL TITLE:** relative to the standards and burden of proof with respect to the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships.

**DATE:** March 9, 2011

**LOB ROOM:** 202

**Amendments:**

Sponsor: Rep. Sapareto OLS Document #: 2011 0534h

Sponsor: Rep. Sapareto OLS Document #: 2011 0757h

Sponsor: Rep. OLS Document #:

**Motions:** OTP OTP/A, ITL, Interim Study (Please circle one.) **AMENDMENT 0534h**

Moved by Rep. Sapareto

Seconded by Rep. Azarian

Vote: 20-0 VOICE VOTE – MOTION NOT ADOPTED (Please attach record of roll call vote.)

**Motions:** OTP OTP/A, ITL, Interim Study (Please circle one.) **AMENDMENT 0757h**

Moved by Rep. Sapareto

Seconded by Rep. Azarian

Vote: 16-4 VOICE VOTE – MOTION ADOPTED (please attach record of roll call vote.)

**Motions:** OTP OTP/A, ITL, Interim Study (Please circle one.) **AMENDMENT 0757h**

Moved by Rep. Sapareto

Seconded by Rep. Azarian

Vote: 16-4 (Please attach record of roll call vote.)

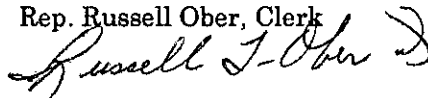
**CONSENT CALENDAR VOTE:**

(Vote to place on Consent Calendar must be unanimous.)

**Statement of Intent:** Refer to Committee Report

Respectfully submitted,

Rep. Russell Ober, Clerk



HOUSE COMMITTEE ON WAYS AND MEANS

EXECUTIVE SESSION on HB 557-FN-A

**BILL TITLE:** relative to the standards and burden of proof with respect to the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships.

**DATE:** 3/9/11

**LOB ROOM:** 202

Amendments:

Sponsor: Rep. Sapareto

OLS Document #: 2011-<sup>0534</sup>~~0757~~h

Sponsor: Rep. Sapareto

OLS Document #: 2011 0757h

Sponsor: Rep.

OLS Document #:

Motions: OTP, OTP/A, ITL, Interim Study (Please circle one.) <sup>1st 2011-0534h</sup> <sup>2nd</sup>

Moved by Rep. Sapareto

~~Sapareto~~ Sapareto

2011-0757h

Seconded by Rep. AZARIAN <sup>VOICE</sup>

AZARIAN

Vote: 20-0 (Please attach record of roll call vote.)

16-4 VOICE OTP

Motions: OTP, OTP/A, ITL, Interim Study (Please circle one.)

Moved by Rep. SAPARETO

Seconded by Rep. AZARIAN

Vote: 16-4 (Please attach record of roll call vote.)

CONSENT CALENDAR VOTE:

(Vote to place on Consent Calendar must be unanimous.)

Statement of Intent: Refer to Committee Report

Respectfully submitted,

Rep. Russell Ober, Clerk



# Committee Report

**REGULAR CALENDAR**

**March 16, 2011**

**HOUSE OF REPRESENTATIVES**

**REPORT OF COMMITTEE**

**The Majority of the Committee on WAYS AND MEANS  
to which was referred HB557-FN-A,**

**AN ACT relative to the standards and burden of proof  
with respect to the business profits tax deduction for  
reasonable compensation attributable to owners of  
partnerships, limited liability companies, and sole  
proprietorships. Having considered the same, report  
the same with the following amendment, and the  
recommendation that the bill OUGHT TO PASS WITH  
AMENDMENT.**

**Rep. Frank V Sapareto**

**FOR THE MAJORITY OF THE COMMITTEE**

**MAJORITY  
COMMITTEE REPORT**

Committee: **WAYS AND MEANS**  
Bill Number: **HB557-FN-A**  
Title: **relative to the standards and burden of proof  
with respect to the business profits tax  
deduction for reasonable compensation  
attributable to owners of partnerships, limited  
liability companies, and sole proprietorships.**  
Date: **March 9, 2011**  
Consent Calendar: **NO**  
Recommendation: **OUGHT TO PASS WITH AMENDMENT**

**STATEMENT OF INTENT**

This bill leaves a \$50,000 safe-harbor deduction as reasonable compensation just as in current law. It also moves the burden of proof from the Dept. of Revenue Administration for determining what is reasonable compensation, from the taxpayer to the department. It provides for definite proof of the amount deducted under IRS Code 162A and allows the commissioner to disallow the deduction only under the terms of excessive gross distributions. This definition of what is reasonable is the same as what existed in the state from 1973 to 1993. Overall this bill brings us back to the business friendly and fair application of the reasonable compensation deduction on the LLC tax.

Vote 16-4

Rep. Frank V Sapareto  
FOR THE MAJORITY

Original: House Clerk  
Cc: Committee Bill File



## REGULAR CALENDAR

### WAYS AND MEANS

**HB557-FN-A**, relative to the standards and burden of proof with respect to the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships. **OUGHT TO PASS WITH AMENDMENT.**

Rep. Frank V Sapareto for the **Majority** of WAYS AND MEANS. This bill leaves a \$50,000 safe-harbor deduction as reasonable compensation just as in current law. It also moves the burden of proof from the Dept. of Revenue Administration for determining what is reasonable compensation, from the taxpayer to the department. It provides for definite proof of the amount deducted under IRS Code 162A and allows the commissioner to disallow the deduction only under the terms of excessive gross distributions. This definition of what is reasonable is the same as what existed in the state from 1973 to 1993. Overall this bill brings us back to the business friendly and fair application of the reasonable compensation deduction on the LLC tax.

**Vote 16-4.**

Original: House Clerk  
Cc: Committee Bill File

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Handwritten initials "SJS" inside a circle.

HB 557-FN-A

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OK SBS

## HB 557-FN-A

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**REGULAR CALENDAR**

**March 16, 2011**

**HOUSE OF REPRESENTATIVES**

**REPORT OF COMMITTEE**

**The Minority of the Committee on WAYS AND MEANS  
to which was referred HB557-FN-A,**

**AN ACT relative to the standards and burden of proof  
with respect to the business profits tax deduction for  
reasonable compensation attributable to owners of  
partnerships, limited liability companies, and sole  
proprietorships. Having considered the same, and  
being unable to agree with the Majority, report with the  
following Resolution: RESOLVED, That it is  
INEXPEDIENT TO LEGISLATE.**

**Rep. William A Hatch**

**FOR THE MINORITY OF THE COMMITTEE**

## MINORITY COMMITTEE REPORT

Committee: **WAYS AND MEANS**  
Bill Number: **HB557-FN-A**  
Title: **relative to the standards and burden of proof  
with respect to the business profits tax  
deduction for reasonable compensation  
attributable to owners of partnerships, limited  
liability companies, and sole proprietorships.**  
Date: **March 9, 2011**  
Consent Calendar: **NO**  
Recommendation: **INEXPEDIENT TO LEGISLATE**

### STATEMENT OF INTENT

This bill as amended changes the standards and burden of proof for the business profits tax deduction for reasonable compensation for owners of partnerships, LLC's and sole proprietorships. HB557 states a taxpayer claiming a deduction for an owners compensation need only to show one or more proprietors, partners or members provided actual services to the business organization at any time during the taxable period. Once a taxpayer has satisfied this burden of proof, the amount claimed as a deduction shall be presumed to be reasonable, unless the commissioner proves by a preponderance of the evidence that the deduction claimed by the taxpayer is grossly excessive. This bill shifts the burden of proof for compensation deductions from the taxpayer to the DRA from the onset.

The majority states this is necessary to stop excessive auditing by the DRA over this issue. The majority also believes that in recent audits business owners are not allowed to deduct the full and fair value of their services to their small business to determine the business profits tax. The majority good tax policy requires tax rules that provide taxpayers with clear guidance that encourages compliance. Based on 2008 tax returns the fiscal note indicates the revenue was \$49 million for this tax which equals the maximum loss exposure. The DRA states in reality the revenue loss would be somewhere in the middle which would equate to the neighborhood of 25 million. The majority did not express any concern over the revenue loss.

The minority believes this change is not good tax policy and should not go forward. The minority is very concerned with the burden of proof issue and believes this alone will effectively eliminate the business profit tax paid by these businesses. In any other area of tax law the burden of proof belongs with the tax payer until there is adjudication and for good reason. The DRA does not have the company records that would give them the necessary information to contest a compensation deduction on file, there for take away any bases except by subpoena. The minority

Original: House Clerk  
Cc: Committee Bill File

is also concerned this may bring our business tax structure back into the courts because it will create a disproportionate business tax structure for our larger corporations.

The minority is also very concerned with the revenue loss this bill creates. Though it is impossible to determine the exact loss it is agreed the loss will be several millions which again limits the state's ability to provide the necessary services, an ability that the minority believes is at the breaking point.

Rep. William A Hatch  
FOR THE MINORITY

Original: House Clerk  
Cc: Committee Bill File



## REGULAR CALENDAR

### WAYS AND MEANS

**HB557-FN-A**, relative to the standards and burden of proof with respect to the business profits tax deduction for reasonable compensation attributable to owners of partnerships, limited liability companies, and sole proprietorships. **INEXPEDIENT TO LEGISLATE.**

Rep. William A Hatch for the **Minority** of WAYS AND MEANS. This bill as amended changes the standards and burden of proof for the business profits tax deduction for reasonable compensation for owners of partnerships, LLC's and sole proprietorships. HB557 states a taxpayer claiming a deduction for an owners compensation need only to show one or more proprietors, partners or members provided actual services to the business organization at any time during the taxable period. Once a taxpayer has satisfied this burden of proof, the amount claimed as a deduction shall be presumed to be reasonable, unless the commissioner proves by a preponderance of the evidence that the deduction claimed by the taxpayer is grossly excessive. This bill shifts the burden of proof for compensation deductions from the taxpayer to the DRA from the onset.

The majority states this is necessary to stop excessive auditing by the DRA over this issue. The majority also believes that in recent audits business owners are not allowed to deduct the full and fair value of their services to their small business to determine the business profits tax. The majority good tax policy requires tax rules that provide taxpayers with clear guidance that encourages compliance. Based on 2008 tax returns the fiscal note indicates the revenue was \$49 million for this tax which equals the maximum loss exposure. The DRA states in reality the revenue loss would be somewhere in the middle which would equate to the neighborhood of 25 million. The majority did not express any concern over the revenue loss.

The minority believes this change is not good tax policy and should not go forward. The minority is very concerned with the burden of proof issue and believes this alone will effectively eliminate the business profit tax paid by these businesses. In any other area of tax law the burden of proof belongs with the tax payer until there is adjudication and for good reason. The DRA does not have the company records that would give them the necessary information to contest a compensation deduction on file, there for take away any bases except by subpoena. The minority is also concerned this may bring our business tax structure back into the courts because it will create a disproportionate business tax structure for our larger corporations.

The minority is also very concerned with the revenue loss this bill creates. Though it is impossible to determine the exact loss it is agreed the loss will be several millions which again limits the state's ability to provide the necessary services, an ability that the minority believes is at the breaking point.

Original: House Clerk  
Cc: Committee Bill File

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OK  
SSJ

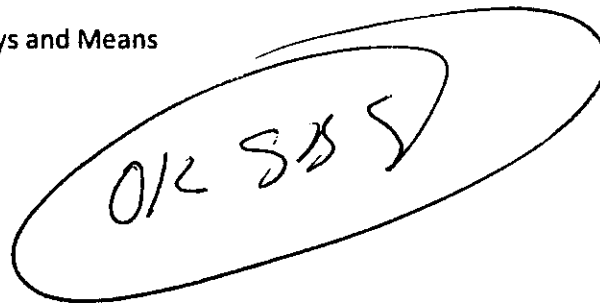
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Representative William A. Hatch, Ways and Means

A handwritten signature consisting of the letters 'O/K' followed by 'SSS' in a stylized, cursive font. The signature is enclosed within a hand-drawn, irregular black oval.

MINORITY REPORT

COMMITTEE: Waiver-Misc

BILL NUMBER: HB 557

TITLE: relative to the standards

DATE: 3/9/11 CONSENT CALENDAR: YES  NO

- OUGHT TO PASS
  - OUGHT TO PASS W/ AMENDMENT
  - INEXPEDIENT TO LEGISLATE
  - INTERIM STUDY (Available only 2<sup>nd</sup> year of biennium)
- Amendment No.  
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STATEMENT OF INTENT:

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COMMITTEE VOTE: 10-4

• Copy to Committee Bill File

RESPECTFULLY SUBMITTED,  
Rep. Walter H. Stoltz  
For the Minority