

DAVID J. NAGLE & JOSEPH X. DONOVAN

Mass. should conform to federal tax policies

Sometimes conformity is a good thing. It's easier to follow one set of rules than two, and fairer when all play by the same rules. Our legislature should keep this in mind this tax season.

For efficiency's sake, the legislature should align our tax rules to current federal rules wherever possible. Massachusetts' personal income tax laws conform generally to federal laws dating to 2005, subject to myriad exceptions. If we are conforming to federal rules, why conform to 11-year-old rules subject to unnecessary exceptions? Does Massachusetts really need its own rules for taxing transit-pass benefits, IRA contributions and gambling losses, or unique rules for businesses that receive dividends or claim depreciation expense?

Sometimes conformity is a matter of good tax policy. Under current law, donors who make charitable contributions may have less to give, because their charitable contributions are deductible federally but not in Massachusetts. Other times, it's only fair to have one set of rules. Commercial banks may charge compound interest on our loans, but pay simple interest at lower rates on deposits in our savings accounts.

There is no reason for our government to do the same. Yet the state Department of Revenue charges 5 percent interest on tax underpayments, compounded daily from the due date of a tax return, but pays simple interest at 3 percent on refunds from the date claimed. Anyone familiar with the miracle of compound interest can imagine how quickly underpayment interest outstrips refund interest.

The problem is actually worse, because the start dates for interest accrual differ. If an auditor concludes tomorrow that you deducted an expense in the wrong year, resulting in a \$10,000 underpayment in 2012 and an equal overpayment in 2013, she would charge three years of interest on the underpayment (about \$1,300) but pay no interest on your refund, even if it were claimed and paid tomorrow. For larger adjustments and longer terms, playing by such different rules is downright punitive.

Some failures to conform to federal law implicate both efficiency and fairness. If an IRS auditor makes an adjustment that increases your Massachusetts taxable income, then you must report and pay additional Massachusetts tax. If the adjustment decreases your income, however, DOR may or may not allow a refund, depending upon whether it agrees with how the federal rules apply in Massachusetts. Taxpayers get the worst of both worlds. Federal tax deficiencies yield Massachusetts deficiencies, but federal refunds do not necessarily yield Massachusetts refunds.

Federal tax rules and IRS conclusions are often good enough for Massachusetts purposes. Legislators should refrain from creating a parallel tax system wherever possible, especially if it operates solely to taxpayers' detriment, and they should require taxpayers and DOR to play by the same rules when computing interest. Such conformity would be good for us all.

David J. Nagle and Joseph X. Donovan are tax attorneys in the Boston office of Sullivan & Worcester LLP.