

RALPH J. DUFFIE TRUST FBO
JUSTIN C. DUFFIE, et al

vs.

COMPTROLLER OF THE TREASURY

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IN THE

MARYLAND TAX COURT

No. 11-IN-OO-1287
through 11-IN-OO-1294

MEMORANDUM AND ORDER

Petitioners are eight trusts (the "Duffie Trusts") created by Ralph J. Duffie and his son, Jonathan C. Duffie, for the benefit of Jonathan's children. Each of the Duffie Trusts opted for status under 26 U.S.C. §1361 as an "electing small business trust" (ESBT). ESBT status permits each trust to own stock of a subchapter S corporation, without disqualifying the corporation under the Internal Revenue Code. Each trust owns stock in RJ Duffie, Inc., a subchapter S corporation owned by the Duffie family.

Under the Internal Revenue Code, ESBTs are treated as two separate trusts and receive special tax treatment as a result of such bifurcated status. 26 U.S.C. §641(c); 26 C.F.R. §1.641(c)-1(a). Section 641(c) and applicable regulations provide that an ESBT's income from a subchapter S corporation is taxed at the highest rate imposed on estates and trusts. Fiduciaries reporting gross income of ESBTs make separate computations of the subchapter S income and other income of the ESBT. In tax years before 2013, this permitted a portion of an ESBT's income to receive favorable tax treatment under both federal and State income tax law. During the years 1999 through and including 2008, the Duffie Trusts filed timely Maryland fiduciary tax returns and paid the taxes shown due thereon.

The Petitioners in eight consolidated income tax cases have made claims for a refund of taxes paid for tax years ending December 31, 1999 through and including 2005.

The Duffie Trusts assert that they inadvertently and/or erroneously overpaid their State income taxes during the years 1999 through and including 2005 by including in Maryland adjusted income amounts that should have been excluded as a result of the federal ESBT income bifurcation calculation. The Comptroller issued refunds for the years 2006, 2007 and 2008 but asserts that the request for refunds prior to 2006 are barred by the three year statute of limitations in §13-1104 of the Tax-General Article of the Annotated Code of Maryland ("Tax Article").

The Petitioners assert that the Comptroller breached its affirmative statutory duty set forth in §2-103 of the Tax Article, to "adopt reasonable regulations to administer the provisions of the tax laws listed in §2-102 of this subtitle," which includes the Maryland income tax. By failing to provide public guidance of the Comptroller's position, taxpayers and tax preparers were confused and erroneously reported income. Petitioners contend that the Comptroller's lack of interpretation of the tax laws led to the non-intuitive and illogical result that income taxed at the federal level under the Internal Revenue Code would not be taxed at the state level without any statute, regulation or explanation.

As a result of the Comptroller's breach of its statutory duty to adopt reasonable regulations, taxpayers paid tax on income that was not subject to state income tax. Consequently, Comptroller should not be permitted to deny a claim for refund based on the statute of limitations, and allow the state to be unjustly enriched by tax on income the Comptroller has conceded should not be subject to tax.

The first question for the Court to decide is whether the Comptroller violated TG § 2-103 by failing to issue regulations clarifying 26 U.S.C. §641. TG §2-102 provides that the Comptroller “shall” promulgate regulations for all taxes under his administration. An interpretation of §2-103 as advanced by the Petitioners would require the Comptroller to issue a regulation interpreting the interaction of one Tax-General provision, TG §10-203, with 26 U.S.C. §641, one of several hundred Internal Revenue Code provisions. Given the breadth and context of TG §2-103, it is likely that the statute is intended to *authorize* the Comptroller to issue regulations as he deems necessary, rather than to *require* that he issue a regulation corresponding to each of the hundreds of provisions in the Tax-General article and the myriad possible interactions of such provisions with the Internal Revenue Code. The Court finds that the Comptroller was not required to issue clarifying regulations regarding 26 U.S.C. §641.

Even if the Court assumes a failure by the Comptroller of performing its statutory duty, Maryland follows the “voluntary payment rule” with respect to tax refunds. This rule holds that there is no common law right to sue for a tax refund. *See Halle Dev., Inc. v. Anne Arundel County*, 371 Md. 312, 322-28 (2002). To the extent such a right may exist, it must be found in statutory law. Title 13 of the Tax-General article provides the exclusive procedures to be used by a claimant seeking a tax refund from a Maryland taxing authority. Any claim for refund is required to “be filed within the time required under §13-1104”.

The Petitioners’ refund claims for the years 1999 through and including 2005 were filed on April 15, 2010. Applying the three-year look-back rule of 26 U.S.C. §6511(a), the last date on which the claims for 2005 (the latest of the years at issue here) could have

been filed was April 15, 2009. Therefore, the refund claims for tax year 2005 and all prior years at issue here are barred under TG §13-1104(c), as it incorporates the three-year look-back rule of 26 U.S.C. §6511(a). The Petitioners further suggest that some form of equitable tolling might be adopted and applied by the Court. In so doing, the trusts argue that the Supreme Court's refusal to apply equitable tolling to federal refund claims in *United States v. Brockamp*, 519 U.S. 347 (1997) is inapposite, because the Maryland tax refund scheme differs from the federal statutory arrangement. The Court disagrees. Maryland expressly incorporates the federal statute of limitations on tax refund claims and the Supreme Court stated in *Brockamp* that equitable tolling was not applicable to §6511.

Finally we agree with the Comptroller that Maryland law makes the same distinction between statutes of limitations and statutes of repose as does federal law. Tax refund suits did not exist at common law in Maryland but are created by statute TG § 13-901. By creating a "new" statute in derogation of the common law, the legislature also provided a limitations period. Thus, TG §13-1104(c)(1) operates as a statute of repose and a jurisdictional limitation. As such, it is not subject to equitable tolling.

For the forgoing reasons, it is the decision of the Maryland Tax Court, this
15th day of August, 2013, **AFFIRMS** the Comptroller's application of the three year statute of limitations and denies Petitioners' request for refunds.