

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 12928 & 15027
[Redacted],)	
)	DECISION
Petitioners.)	
_____)	

[Redacted] (petitioners) protested two Notices of Deficiency Determination issued by the Idaho State Tax Commission (Commission). The Notice dated June 22, 1998 asserts additional income tax and interest totaling \$11,373 for 1994. The Notice dated June 30, 2000 asserting additional income tax and interest totaling \$7,742, for 1995 and \$8,727 for 1996.

The auditor made the following adjustments to the petitioners' Idaho income tax returns:

1. Increased income from an interest the petitioners held in an S corporation due to audit adjustments to the returns filed by the S corporation;
2. Increased income by \$15,000 to reflect failures by the petitioners to document items on their 1994 return;
3. For 1996, increased by \$514 state income taxes which were allowed as an itemized deduction on the petitioners' federal income tax return but are not deductible on Idaho income tax returns;
4. Decreased the amount of taxes claimed on the petitioners' 1995 Schedule A by \$29;
5. Reduced the deductions claimed by the petitioners as charitable contributions for both 1995 and 1996 by \$2,045 and \$1,938, respectively;
6. Increased the deduction claimed by the petitioners on Schedule A as interest expense for 1996 by \$1,555;
7. Reduced the deduction claimed by the petitioners for medical expenses on Schedule A by \$2,458 for 1996; and

8. Adjusted the amounts of several deductions claimed on Schedule E with regard to the rental of a portion of petitioners' residence to the petitioners' employer, [Redacted], a wholly owned S corporation. The net effect of these adjustments increased the petitioners' Idaho taxable income by \$449 and \$1,649 for 1995 and 1996, respectively.

Adjustments 3, 4, and 6 are apparently not contested by the petitioners. Therefore, they will not be further addressed in this decision.

After the issuance of the Notice of Deficiency Determination, the petitioners contended that they were entitled to deductions for payments of self-employed health insurance for both 1995 and 1996.

ADJUSTMENT ISSUE 1

The petitioners were the sole owners of [Redacted], an S corporation. This corporation was audited. The adjustment to the income and deductions for the corporation are addressed in a decision issued concurrently with this decision.

ADJUSTMENT ISSUE 2

The auditor requested documentation to support the income and deductions on the Schedule E (Supplemental Income and Loss) and the Schedule A (Itemized Deductions) filed by the petitioners. The petitioners failed to provide the documentation; therefore, the auditor increased the Idaho taxable income of the petitioners for 1994 by \$15,000. The petitioners have still not provided the requested documentation. Therefore, the Commission must make their determination from the record.

The petitioners claimed itemized deductions in the total amount of \$14,282 reduced by state income taxes (which are not deductible in the computation of Idaho taxable income) in the amount of \$2,278. While the Commission can determine that some of the deductions were allowable, such

amounts would be less than the standard deduction for 1994, \$6,350. Therefore, the Commission finds that the petitioners should be allowed the standard deduction rather than the itemized deductions.

The petitioners reflected on their Schedule E income from the rental of a portion of their home in the amount of \$8,700. From this income, they deducted expenses in the total amount of \$5,158. Most of the deductions were not allowable due to the expenses being related to the rental of a portion of a structure which was used by the taxpayer during the taxable year as a residence.

Internal Revenue Code § 280A(c)(6). Internal Revenue Code § 280A stated, in part:

Disallowance of certain expenses in connection with business use of home, rental of vacation homes, etc. (a) General rule. Except as otherwise provided in this section, in the case of a taxpayer who is an individual or an S corporation, no deduction otherwise allowable under this chapter shall be allowed with respect to the use of a dwelling unit which is used by the taxpayer during the taxable year as a residence.

* * *

(c) Exceptions for certain business or rental use; limitation on deductions for such use.

(1) Certain business use. Subsection (a) shall not apply to any item to the extent such item is allocable to a portion of the dwelling unit which is exclusively used on a regular basis –

(A) [as] the principal place of business for any trade or business of the taxpayer.

(B) as a place of business which is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of his trade or business, or

(C) in the case of a separate structure which is not attached to the dwelling unit, in connection with the taxpayer's trade or business.

In the case of an employee, the preceding sentence shall apply only if the exclusive use referred to in the preceding sentence is for the convenience of his employer.

* * *

(3) Rental use. Subsection (a) shall not apply to any item which is attributable to the rental of the dwelling unit or portion thereof (determined after the application subsection (e)).

* * *

(6) Treatment of rental to employer. Paragraphs (1) and (3) shall not apply to any item which is attributable to the rental of the dwelling unit (or any portion thereof) by the taxpayer to his employer during any period in which the taxpayer uses the dwelling unit (or portion) in performing services as an employee of the employer.

Of the total of the Schedule E deductions, they reflected some items that, if documented, might have been allowed as itemized deductions. However, since the petitioners are being allowed only the standard deduction for 1994, such deductions are not allowable. Therefore, the income from Schedule E is to be increased by \$5,158 for 1994.

ADJUSTMENT ISSUE 5

The auditor reduced the deductions claimed by the petitioners as charitable contributions for both 1995 and 1996 by \$2,045 and \$1,938, respectively. After the notice of deficiency was issued, the petitioners submitted additional information regarding their claimed deduction for 1996. This eliminated the adjustments for both 1995 and 1996.

ADJUSTMENT ISSUE 7

The auditor eliminated the deduction claimed by the petitioners on their Schedule A as medical expense for 1996. This adjustment was in the amount of \$2,458. After the notice of deficiency was issued, the petitioners provided additional documentation which reduced the amount of the adjustment from \$2,458 to \$1,552.

ADJUSTMENT ISSUE 8

The adjustment made to the income reported for 1995 is affirmed. No contrary information was provided by the petitioners. The adjustments to the deductions made by the auditor are affirmed, not only because the petitioners failed to document the expenses, but also because Internal

Revenue Code § 280A(c)(6) specifically precludes the deductions. See the discussion of Adjustment Issue 2 above.

Upon examining the allowance of the deduction for self-employed health insurance, it was found that the deductions should be restricted. The allowable deduction for 1995 is \$379. The deduction for 1996 was claimed on the original return filed by the petitioners. Therefore, no additional deduction is allowable for 1996.

WHEREFORE, the Notices of Deficiency Determination dated June 22, 1998 and June 30, 2000, are hereby MODIFIED and, as so modified, are APPROVED, AFFIRMED, AND MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that petitioners pay the following tax and interest (calculated to December 15, 2001):

<u>YEAR</u>	<u>TAX</u>	<u>INTEREST</u>	<u>TOTAL</u>
1994	\$8,487	\$4,590	\$13,077
1995	2,391	1,085	3,476
1996	3,821	1,417	<u>5,238</u>
			<u>\$21,791</u>

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of the petitioners' right to appeal this decision is enclosed with this decision.

DATED this ____ day of _____, 2001.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this ____ day of _____, 2001, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to

[REDACTED]

Receipt No. [Redacted]

[REDACTED]

[Redacted]

[REDACTED]

ADMINISTRATIVE ASSISTANT 1