

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 14992
[Redacted],)	
)	DECISION
Petitioners.)	
_____)	

On August 2, 2000, the staff of the Income Tax Audit Bureau (Bureau) of the Idaho State Tax Commission issued a Notice of Deficiency Determination to [Redacted] (taxpayers), proposing additional income tax and interest for the taxable year 1998 in the total amount of \$596.

On August 16, 2000, the taxpayers' representative filed a timely appeal and petition for redetermination. The taxpayers' representative did not request a hearing but did provide their argument in writing. Therefore, the Tax Commission, having reviewed the file, hereby issues its decision.

The taxpayers were nonresidents of Idaho in 1998. [Redacted] was a shareholder in an Idaho limited partnership that sold its assets and liquidated in 1998. The taxpayers filed a return reporting the Idaho activity of this partnership and included a capital loss on the disposition of the partnership interest. The Bureau determined the loss attributable to the disposition of the partnership interest was reportable only to the state of the taxpayers' domicile and adjusted the taxpayers' Idaho taxable income accordingly.

The taxpayers appealed the Bureau's determination arguing that the loss on the Idaho partnership interest was attributable to Idaho rather than Washington. According to the taxpayers' representative,

This by the way is the same partnership that sold their property in 1998 and for which the taxpayers are reporting their proportionate share of the partnership gain. In fact the only asset of the partnership was a building

located in Idaho. To hold that the sale of the partnership asset is subject to Idaho taxation but the partnership interest itself is not, would result in the Idaho state taxable income being determined only by the method in which the property is sold. If the partnership were to liquidate before the sale of the property and each individual partner sells their proportionate undivided interest in the property then the Idaho State taxable income would be different than if the partnership sold the property and distributed the proceeds to the individual partners. This would clearly violate the aggregate theory of partnership taxation.

For the taxpayers if the partnership had liquidated before the sale of the property there would have been no taxable event on liquidation and the taxpayers would have had a basis of \$37,583 in the property received. Upon the sale of their proportionate part of the property the taxpayers would have received \$36,519 resulting in a loss of \$1,064 for federal and Idaho state taxation purposes. This is clearly the result that the taxpayers should have no matter how the transaction was structured.

The Tax Commission does not fully agree with this analysis. Under Idaho law, property located and sold in Idaho is reportable to Idaho. Therefore, the sale of the partnership asset, which was located in Idaho, was reportable to Idaho regardless of whether the asset was sold before or after liquidation of the partnership.

However, the issue at hand is whether the taxpayers were entitled to include the loss from the disposition of the partnership interest in the computation of their Idaho taxable income for 1998. A partnership interest is an intangible asset. Valentino v. Franchise Tax Bd., 105 Cal. Rptr. 2d 304, 312 (2001); In re Vannoy, 176 B.R. 758, 771 (Bankr. M.D.N.C., 1994). IDAPA 35.01.01.260.02, Income Tax Administrative Rules, provided in pertinent part:

02. Income From Intangible Property. Generally, gross income from intangible property is sourced to the state of the owner's domicile. There are three (3) exceptions to this rule.
 - a. If the intangible property is utilized in connection with the owner's trade, business or profession carried on within Idaho, any income derived from or related to the property, including gains from the sale thereof, constitutes income from Idaho sources. For example, if a nonresident pledges stocks, bonds, or other intangible personal property as security for the payment of indebtedness incurred in

connection with the nonresident's Idaho business operations, the intangible property has an Idaho situs and the income derived therefrom constitutes Idaho source income.

The gain or loss on the sale of an intangible asset is not subject to Idaho income tax unless the individual realizing the gain or loss is an Idaho resident at the time the gain or loss is recognized or has met one of the three exceptions. There is no evidence in the file to indicate that the partnership interest was, in any way, part of the taxpayers' trade or business. On the contrary, the nature of a limited partnership is for other than a trade or business. Therefore, the \$1,064 loss reported by the taxpayers on the 1998 Idaho Nonresident Income Tax Return is disallowed.

WHEREFORE, the Notice of Deficiency Determination dated August 2, 2000, is hereby APPROVED, AFFIRMED, AND MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that the taxpayers pay the following tax and interest:

<u>YEAR</u>	<u>TAX</u>	<u>INTEREST</u>	<u>TOTAL</u>
1998	\$537	\$97	\$634

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

An explanation of the taxpayers' right to appeal this decision is included 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][Redacted] [REDACTED]

ADMINISTRATIVE ASSISTANT 1