

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 16223
[Redacted],)	
)	DECISION
Petitioners.)	
_____)	

[Redacted] (petitioners) protest the Notice of Deficiency Determination issued by the auditors for the Idaho State Tax Commission (Commission) dated November 13, 2001 asserting additional income taxes and interest in the total amounts of \$ 46 and \$1,144 for 1998 and 1999, respectively.

There are three issues to be addressed in this decision. The issues are as follows:

1. Whether the petitioners are entitled to deduct certain mortgage interest expenses which they claim to have paid in the amounts of \$12,637 for each of the years here in question.
2. Whether the petitioners are entitled to deduct employee business expenses in the amounts of \$1,224 and \$3,389 for 1998 and 1999, respectively.
3. Whether the petitioners are entitled to deduct irrigation taxes they deducted as itemized deductions in the amounts of \$138 and \$139 for 1998 and 1999, respectively.

In each of these issues, the petitioners are seeking deductions. In seeking such deductions, taxpayers have the burden of proof. The U. S. Supreme Court has stated:

Whether and to what extent deductions shall be allowed depends upon legislative grace; and only as there is clear provision therefor can any particular deduction be allowed.

* * *

Obviously, therefore, a taxpayer seeking a deduction must be able to point to an applicable statute and show that he comes within its terms.

New Colonial Ice Co. v. Helvering, 292 U.S. 435, 440, 54 S.Ct. 788, 790 (1934).

The first issue is whether the petitioners are entitled to deduct certain alleged payments as mortgage interest expenses. The auditor asked that the petitioners supply copies of canceled checks showing that the petitioners had paid the interest here in question. The petitioners failed to supply this documentation. While the petitioners have submitted some documentation regarding their alleged payments, the Commission finds that the petitioners have failed to carry their burden of proof regarding this claimed deduction.

The petitioners submitted a copy of a deed of trust securing the alleged debt from which the interest expense here in question allegedly arose. This deed of trust was secured by the petitioners' former residence which was sold on September 19, 1997. Therefore, this property was not a residence for the petitioners during the years here in question. Therefore, even if the alleged payments were made, based upon the record before us, we find that the interest expense would not be deductible.

The second issue is whether the petitioners are entitled to deductions for certain claimed employee business expenses. For 1998, the petitioners wish to increase the amount claimed on their original income tax return. They contend that they are entitled to the following deductions:

	<u>1998</u>	<u>1999</u>
Food (at 50%)	\$ 124.41	\$ 118.14
Seminar Registrations	375.00	
Vehicle Repairs	1,534.24	
Telephone	5.10	
Vehicle Fuel for Rental Cars	146.27	62.02
Other Vehicle Fuel		58.00
Lodging	1,173.02	1,472.29
Air Travel		1,566.50
Rental Vehicles		679.74
Skycap		3.00
Tolls		6.25
Additional Phone		250.72
Other Expenses	<u>282.15</u>	<u>809.80</u>
Petitioners' Totals	<u>\$3,640.19</u>	<u>\$5,026.46</u>

All of the employee business expenses deducted appear to be related to the business of [Redacted] (hereinafter [Redacted]), an S corporation in which the petitioners own an interest. The auditor disallowed some of the expenses because the claimed expenditures are unrelated to the business of [Redacted].

While there are deficiencies in the documentation and computations presented by the petitioners regarding the employee business expenses, it appears that the Commission need not consider them. The petitioners contend that they provided services and paid expenses on behalf of [Redacted]. They report no compensation having been paid to them by [Redacted]. An officer or employee who serves without compensation is not engaged in a trade or business. *Snarski v. Commissioner*, T. C. Memo 1981-328; *Low v. Nunan*, 154 F.2d 261 (2d Cir. 1946). Therefore, the expenses here in question cannot be deducted as trade or business expenses of the petitioners.

The last issue is whether the petitioners are entitled to a deduction for the irrigation tax that they allegedly paid. The Internal Revenue Service has addressed this deduction in Revenue Ruling 67-337 as follows:

The Internal Revenue Service has been asked whether an assessment imposed, under the circumstances described below, by an irrigation district against all farm property within the district is deductible as a tax under section 164 of the Internal Revenue Code of 1954.

The ABC irrigation district was organized as a political subdivision of the state in which it is located for the purpose of purchasing water from an irrigation project administered by the Department of the Interior of the United States Government and of reselling it to landowners within the district. Accordingly, it entered into an agreement with the Department of the Interior which provided, among other things, that the United States would construct a water distribution system within the district. The cost of the system is to be repaid to the United States over a period of X years in equal semiannual installments beginning with the year in which water deliveries are first made. Title to the distribution system is to be held by the United States until otherwise provided by Congress. The district, in order to finance its operation, imposes an annual ad valorem assessment against all farm property within the district on the basis of 10x dollars per \$100 of assessed land value. This assessment is allocated by the district as follows: operation and

maintenance, 2x dollars; administration, 1x dollars; water purchase cost, 3x dollars; and, repayment to the United States Government of the construction costs of the water distribution system, 4x dollars. Neither the district nor the taxpayers provided any further allocation. The district is not the type of special taxing district described in section 1.164-4(b)(2) of the Income Tax Regulations.

Section 164(a)(1) of the Code allows a deduction for state and local real property taxes.

Section 164(c) of the Code provides, in part, as follows:
No deduction shall be allowed for the following taxes:

(1) Taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not prevent the deduction of so much of such taxes as is properly allocable to maintenance or interest charges.

Section 1.164-4 of the regulations provides that:

(a) So-called taxes for local benefits *** more properly assessments, paid for local benefits such as street, sidewalks, and other like improvements, imposed because of and measured by some benefit inuring directly to the property against which the assessment is levied are not deductible as taxes. A tax is considered assessed against local benefits when the property subject to the tax is limited to property benefited. Special assessments are not deductible, even though an incidental benefit may inure to the public welfare. *** .

(b)(1) Insofar as assessments against local benefits are made for the purpose of maintenance or repair or for the purpose of meeting interest charges with respect to such benefits, they are deductible. In such cases, the burden is on the taxpayer to show the allocation of the amounts assessed to the different purposes. If the allocation cannot be made, none of the amounts so paid is deductible.

Since the assessments imposed by the ABC irrigation district are imposed because of, and measured by a benefit inuring directly to, the property against which the assessment is levied, they are deductible as taxes only to the extent they are properly allocable to maintenance or interest charges. However, the allocation provided by the district is not adequate in the instant case to carry the burden (referred to in section 1.164-4(b)(1) of the regulations) of showing the portion of the assessment which is attributable to maintenance or interest charges, and since neither the irrigation district nor the taxpayers are able to furnish any more detailed allocation, no part of the assessment is deductible as a tax under section 164 of the Code.

The amounts attributable to operation and maintenance, administration, and water purchase costs, however, are deductible under section 162 of the Code by the landowners in the district using the water in their trade or business. The amount attributable to the repayment to the United States Government of the cost of the

water distribution system is not deductible either as a business expense under section 162 of the Code or as a tax under section 164 of the Code. However, it may be treated as an adjustment under section 1016 of the Code to increase the basis of the property with respect to which the assessment is paid.

The petitioners have not claimed this deduction as a trade of business expense and have not shown a business connection for this expense. Therefore, the Commission finds that the petitioners are not entitled to this deduction.

WHEREFORE, the Notice of Deficiency Determination dated November 13, 2001 is hereby APPROVED, AFFIRMED, and MADE FINAL.

IT IS ORDERED and THIS DOES ORDER the petitioners to pay the following tax, penalty, and interest (calculated to July 15, 2002):

YEAR	TAX	INTEREST	TOTAL
1998	\$ 38	\$ 9	\$ 47
1999	977	171	<u>1,148</u>
			<u>\$1,195</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 _____, 2002.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this ____ day of _____, 2002, 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]

ADMINISTRATIVE ASSISTANT 1