

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)
)
 [Redacted] Petitioner.) DOCKET NO. 18357
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) DECISION
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 _____)

On July 23, 2004, the staff of the Income Tax Audit Bureau of the Idaho State Tax Commission issued a Notice of Deficiency Determination to [Redacted] (taxpayer), proposing income tax, penalty, and interest for the taxable years 2000 and 2001 in the total amount of \$16,376.

On September 20, 2004, the taxpayer filed a timely appeal and petition for redetermination. The taxpayer did not request a hearing but rather chose to provide additional information for the Tax Commission to consider. The Tax Commission, having reviewed the file, hereby issues its decision.

During a routine review of business returns filed with the Tax Commission, the Income Tax Audit Bureau (Bureau) found that the taxpayer, a partner of [Redacted] (Partnership), did not file Idaho individual income tax returns for the taxable years 2000 and 2001. The Partnership filed schedule K-1s for each of its three partners showing an income apportionment percentage to Idaho of 100 percent. The taxpayer did not share in the Partnership's profit, but he did receive a guaranteed payment for each year.

The Bureau contacted the taxpayer and asked about his requirement to file Idaho individual income tax returns. The taxpayer responded that he would discuss the matter with his accountant. The taxpayer's wife and accountant discussed the matter with the Bureau and both stated that returns would be prepared and submitted. A few months passed and the Bureau had

no returns from the taxpayer. Therefore, the Bureau prepared returns for the taxpayer based upon the information available and sent him a Notice of Deficiency Determination.

The taxpayer protested the Bureau's determination stating he was a resident of [Redacted], spent very little time in Idaho for the company, and had no knowledge or reason to believe he would be required to report any income to Idaho. The taxpayer further argued that a partner receiving a guaranteed payment is not someone who is properly classified as an employee, and in accordance with Idaho's taxation of nonresidents conducting business in Idaho using the three-factor apportionment method, he had no Idaho factors. Therefore, the taxpayer did not have a filing requirement with Idaho and owes no personal income tax to Idaho.

The matter was referred for administrative review and the Tax Commission sent the taxpayer a letter giving him the option of two methods for having the Notice of Deficiency Determination redetermined. The taxpayer chose to provide additional information in support of his position. The taxpayer did provide additional information in which he cited Income Tax Administrative Rules IDAPA 35.01.01.270.01 and .02. Those rules state that if an individual performs personal services as an employee, agent, independent contractor or otherwise both within and without Idaho, his Idaho source income is determined by using a compensation percentage. The compensation percentage is the number of Idaho work days divided by total work days.

The taxpayer maintained that the overwhelming majority of his time spent in service with the Partnership was in [Redacted]. He spent very little time in Idaho. The taxpayer stated that if Idaho is going to tax the guaranteed payments from the Partnership, the income sourced to Idaho should be governed by Income Tax Administrative Rule 270.

In 1999, the taxpayer, [Redacted], and [Redacted]. formed [Redacted]. For the taxable years 1999 through 2002, the Partnership transacted 100 percent of its business activities in Idaho. (Idaho apportionment factor reported on the Idaho Partnership returns.) Idaho Code section 63-3030(a)(9) states that returns with respect to taxes measured by income shall be made by every partnership which transacts business in Idaho. Income Tax Administrative Rule IDAPA 35.01.01.280 states that partnerships operating both within and without Idaho shall apply the principles of allocation and apportionment of income set forth in Idaho Code section 63-3027. However, since the partnership operated solely within Idaho, all income is allocated and apportioned to Idaho.

Partnerships are flow-through entities (Internal Revenue Code (IRC) section 701). In general, each partner accounts for his distributive share of the partnership's gains and losses, charitable contributions, taxes, and income or loss. (IRC section 702) In determining the income or loss of a partnership, guaranteed payments are treated as made to a person who is not a partner. However, for other tax purposes, guaranteed payments are treated as a partner's distributive share of ordinary income. (Treasury Regulation section 1.707-1(c)) Since guaranteed payments are a distributive share of ordinary income and the partnership allocated and apportioned 100 percent of its income to Idaho, the taxpayer was required to file and report the partnership income to Idaho.

The taxpayer argued if any of his income is reportable to Idaho it should be figured in accordance with Income Tax Administrative Rule 270. However, Rule 270 applies to individuals that perform personal services either as an employee, an agent, an independent contractor, or otherwise. As the taxpayer previously stated, a partner is not properly classified as an employee. Nor is a partner properly classified as an agent or an independent contractor. A

partner is a fractional owner with a vested interest in a partnership. Consequently, Rule 270 is not applicable in this case. The guaranteed payments are part of the taxpayer's distributive share of the Partnership's income or loss. On its partnership return, the Partnership determined the allocation and apportionment of its income. Idaho source income was determined at the partnership level. Therefore, no further division of income is needed on the individual return.

The taxpayer failed to show that the guaranteed payments from his partnership, solely transacting business in Idaho, should not be reported to Idaho. He did not meet his burden of proof. Albertson's, Inc. v. State, Dept. of Revenue, 106 Idaho 810, 814, 683 P.2d 846, 850 (1984). Therefore, for the reasons stated, the Tax Commission finds the Bureau properly reported the income to Idaho. However, the Bureau's returns showed the taxpayer as married filing joint with no exemptions or standard deduction. Absent any information from the taxpayer, the Tax Commission finds that the returns should reflect a filing status of married filing separate and allow the taxpayer his personal exemption and standard deduction for married filing separate. Therefore, the Tax Commission modified the returns to show a filing status of married filing separate and to allow one personal exemption and the standard deduction for married filing separate.

WHEREFORE, the Notice of Deficiency Determination dated July 23, 2004, is hereby MODIFIED, in accordance with the provisions of this decision and, as so modified, is APPROVED, AFFIRMED, and MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that the taxpayer pay the following tax, penalty, and interest:

<u>YEAR</u>	<u>TAX</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
2000	\$6,861	\$1,715	\$2,025	\$10,601
2001	3,970	993	868	<u>5,831</u>
			TOTAL DUE	<u>\$16,432</u>

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

An explanation of the taxpayer's right to appeal this decision is included with this decision.

DATED this ____ day of _____, 2005.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this ____ day of _____, 2005, 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]
[Redacted]
[Redacted]

Receipt No.

[Redacted]
