

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 21357
[Redacted])	
)	DECISION
Petitioners.)	
_____)	

[Redacted] (petitioners) protest the Notice of Deficiency Determination issued by the auditor for the Idaho State Tax Commission (Commission) dated June 12, 2008. The Notice of Deficiency Determination asserted additional Idaho income tax and interest in the total amount of \$21,425 for 2005.

The petitioners were residents of Idaho at all times relevant to this matter. The petitioners operated [Redacted] in a storefront until 2005. At that point, the petitioners sold the [Redacted] equipment which resulted in a taxable gain.

The question to be resolved is whether the petitioners are eligible for the Idaho capital gains deduction. The details of the sale reflect an original cost of the property for \$63,322, which was fully depreciated, and a sales price of \$87,000. The net result was a gain in the amount of \$87,000.

Idaho Code § 63-3022H sets out the authority for the Idaho capital gains deduction. It stated, in part:

Deduction of capital gains. -- (1) If an individual taxpayer reports capital gain net income in determining taxable income, eighty percent (80%) in taxable year 2001 and sixty percent (60%) in taxable years thereafter of the capital gain net income from the sale or exchange of qualified property shall be a deduction in determining Idaho taxable income.

(2) The deduction provided in this section is limited to the amount of the capital gain net income from all property included in taxable income. Gains treated as ordinary income by the Internal Revenue Code do not qualify for the deduction allowed in this section. The deduction otherwise allowable under this

section shall be reduced by the amount of any federal capital gains deduction relating to such property, but not below zero.

(3) As used in this section "qualified property" means the following property having an Idaho situs at the time of sale:

* * *

(b) Tangible personal property used in Idaho for at least twelve (12) months by a revenue-producing enterprise;

* * *

(7) As used in this section "revenue-producing enterprise" means:

(a) The production, assembly, fabrication, manufacture, or processing of any agricultural, mineral or manufactured product;

(b) The storage, warehousing, distribution, or sale at wholesale of any products of agriculture, mining or manufacturing;

(c) The feeding of livestock at a feedlot;

(d) The operation of laboratories or other facilities for scientific, agricultural, animal husbandry, or industrial research, development, or testing. (Emphasis added.)

Income Tax Administrative Rule 172 stated:

IDAHO CAPITAL GAINS DEDUCTION -- REVENUE-PRODUCING ENTERPRISE (RULE 172).

Section 63-3022H, Idaho Code.

(3-20-97)

01. In General. Only the activities listed in Section 63-3022H(7), Idaho Code, qualify as a revenue-producing enterprise. A revenue-producing enterprise does not include retail sales, professional, managerial, or repair services.(3-20-97)

02. Multiple Activities. If a business is engaged in both revenue-producing and nonrevenue-producing activities, tangible personal property must be used in the revenue-producing activity to qualify for the Idaho capital gains deduction.

(3-20-97)

The auditor asserted that the property in question had not been used by a "revenue producing enterprise." He therefore denied the Idaho capital gains deduction claimed by the petitioners with regard to this property. The petitioners disagree with the auditor's position.

This is the sole issue to be decided.

The petitioners' argument is:

[Redacted]

Rule 172.01 (above) makes it clear that gains from the sales of property used in retail sales do not qualify for this deduction. It appears from the advertisements for the business that much or all of the sales were retail sales. Although the staff of the Commission inquired of the petitioners as to how they would like to proceed with their administrative appeal, they failed to respond. Therefore, there is no explanation of why their sales should not be considered to have been at retail. Accordingly, we find that the petitioners have failed to carry their burden of proof that their sales were of qualifying property.

In addition, Idaho Code § 63-3022H stated, in part: "Gains treated as ordinary income by the Internal Revenue Code do not qualify for the deduction allowed in this section." Of the reported gain of \$87,000, \$63,322 was from the recapture of depreciation pursuant to Internal Revenue Code § 1245. Internal Revenue Code § 1245 stated, in part:

§ 1245 Gain from dispositions of certain depreciable property.

(a) General rule.

(1) Ordinary income.

Except as otherwise provided in this section, if section 1245 property is disposed of the amount by which the lower of—

(A) the recomputed basis¹ of the property, or

(B)

(i) in the case of a sale, exchange, or involuntary conversion, the amount realized, or

(ii) in the case of any other disposition, the fair market value of such property, exceeds the adjusted basis of such property shall be treated as ordinary income. Such gain shall be recognized notwithstanding any other provision of this subtitle.

Since most of the gain is attributable to the recapture of Internal Revenue Code § 1245 depreciation, it is ordinary income and is not eligible for the Idaho capital gains deduction.

¹The term "recomputed basis" means, with respect to any property, its adjusted basis recomputed by adding thereto all adjustments reflected in such adjusted basis on account of deductions (whether in respect of the same or other property) allowed or allowable to the taxpayer or to any other person for depreciation or amortization. Internal Revenue Code § 1245(a)(2)(A).

Therefore, it appears that a reasonable argument might be mounted only for the remaining \$23,678.

There may be a stronger argument to be made for the deduction sought by the petitioners than has been presented. However, as it stands, the Commission finds that the petitioners have failed to present a compelling argument for their position. In addressing the allowance of deductions, the Idaho Supreme Court stated:

When construing the provisions of the Idaho Income Tax Code, however, we must enforce the law as written. Potlatch Corp. v. Idaho State Tax Comm'n, 128 Idaho 387, 913 P.2d 1157 (1996). If there is any ambiguity in the law concerning tax deductions, the law is to be construed strongly against the taxpayer. *Id.* This Court has no authority to rewrite the tax code. Bogner v. State Dep't of Revenue and Taxation, 107 Idaho 854, 693 P.2d 1056 (1984). Any exemption from taxation must be created or conferred in clear and plain language and cannot be made out by inference or implication. Herndon v. West, 87 Idaho 335, 393 P.2d 35 (1964). This Court does not have the authority to create deductions, exemptions, or tax credits. If the provisions of the tax code are socially or economically unsound, the power to correct it is legislative, not judicial. *Id.*

Idaho State Tax Commission v. Stang, 135 Idaho 800, 802-803, 25 P.3d 113, 115-116 (2001).

WHEREFORE, the Notice of Deficiency Determination dated June 12, 2008, is hereby APPROVED, AFFIRMED, AND MADE FINAL.

The petitioners have paid the amount asserted in the Notice of Deficiency Determination. Therefore, no further demand is made.

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

DATED this _____ day of _____, 2009.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this _____ day of _____, 2009, 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.
