

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 21819 & 21820
[Redacted])	
Petitioners.)	DECISION
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The petitioners, [Redacted], a limited partnership, protest the Notices of Deficiency Determination issued by the auditor for the Idaho State Tax Commission (Commission) dated January 12, 2009, asserting additional liabilities for Idaho income tax, penalty, and interest for the [Redacted] in the total amount of \$72,342 for 2005.

The [Redacted], at all times relevant to this matter, were nonresidents of Idaho. They held a large portion of [Redacted] (the partnership) which owned real property in Idaho. During 2005, the partnership sold real property located in Idaho. Either the partnership or the [Redacted] owned stock in [Redacted], a C corporation ([Redacted]), which had operations in Idaho. The partnership held a note payable by [Redacted].

There are two issues to be resolved in these dockets. They are as follows:

1. Should the [Redacted]' portion of a bad debt incurred in 2004 by the partnership be allowed to be carried forward as an Idaho source capital loss?
2. Should the [Redacted] portion of a loss from worthless stock incurred in 2004 be allowed to be carried forward as an Idaho source capital loss?

The partnership owned real property in Idaho, but for 2002, 2003, and 2004, the Idaho income tax returns filed by the partnership did not reflect any business income or loss apportioned to Idaho or any nonbusiness income or loss allocated to Idaho. These income tax returns also did not reflect the Idaho real property in the property factor. The Idaho partnership income tax return

filed for 2005 reflected an Idaho apportionment factor of 99.8778 percent. The auditor adjusted the Idaho apportionment factor to zero to reflect the removal of the sale of Idaho real property from the apportionment factor of the partnership.

Issue 1. In 2004, [Redacted], a C corporation in which either the [Redacted] or the partnership held an interest, ceased operations. The ownership of the corporation is somewhat in question. The final (2004) income tax return for [Redacted] indicates that [Redacted] owned 100 percent of the stock. In a CONSENT TO ACTION OF SOLE SHAREHOLDER AND DIRECTOR (of the C corporation) dated December 16, 2004, [Redacted] signed as the sole shareholder of the C corporation. However, the representatives of the petitioners contend that the partnership was the 100 percent owner of the [Redacted] stock. In any case, there was a loss by the partnership from a bad debt from loans to the C corporation. The [Redacted] claimed their portion of this loss as a carryforward to their 2005 Idaho income tax return. The auditor denied the deduction stating that the loss was not properly attributable to Idaho.

The loan was originally a loan from Mr. [Redacted] to [Redacted]. The loan was subsequently transferred to the partnership.

The 2004 partnership return reflected an Idaho apportionment factor of zero (no Idaho business income or loss) and reflected no nonbusiness income or loss attributable to Idaho. According to the amounts claimed in the 2004 Idaho partnership return, no loss is available to be carried forward. The question is, therefore, whether the partnership return was incorrect and whether the loss from the loans to the Idaho C corporation should have been deemed to have been an Idaho source loss.

Idaho Income Tax Administrative Rule 370 prescribed the authority to govern the attribution of nonbusiness income:

APPLICATION OF SECTION 63-3027 -- ALLOCATION (RULE 370).

Section 63-3027, Idaho Code. A taxpayer subject to the taxing jurisdiction of Idaho shall allocate all of its nonbusiness income or loss within or without Idaho pursuant to Section 63-3027, Idaho Code.

Idaho Code § 63-3027(f)(3) stated:

Capital gains and losses from sales of intangible personal property are allocable to this state if the taxpayer's commercial domicile is in this state, unless such gains and losses constitute business income as defined in this section.

It appears that the commercial domicile of the partnership is in [Redacted]. The tax returns for the partnership were filed from an address in [Redacted]. Over 96 percent of the ownership is attributable to taxpayers with [Redacted] addresses. The “General partner or LLC member-manager” of the partnership was located in [Redacted]. Accordingly, the Commission finds that the loss is not properly attributed to Idaho. Therefore, this adjustment made by the auditor is affirmed.

Issue 2. The assets of [Redacted] were liquidated in 2004. As discussed above, it is not entirely clear who owned the stock of the corporation at the end of 2004. In either case, the Commission finds that the conclusion is the same, namely that the [Redacted] are not allowed to deduct a loss from the liquidation of [Redacted] in computing their Idaho taxable income.

If the stock of [Redacted] was owned by the partnership, then the analysis of the attribution of the loss would be the same as for the bad debt loss involved in Issue 1 above. It would be attributed to the commercial domicile of the partnership, and not to Idaho.

If the stock of [Redacted] was owned by [Redacted] then Idaho Code § 63-3026A is the controlling authority. It stated, in part:

Computing Idaho taxable income of part-year or nonresident individuals, trusts and estates. -- (1) For nonresident individuals, trusts, or estates the term "Idaho taxable income" includes only those components of Idaho taxable income as computed for a

resident which are derived from or related to sources within Idaho. This is to be computed without the deductions for either the standard deduction or itemized deductions or personal exemptions except as provided in subsection (4) of this section.

* * *

- (3) For the purposes of subsections (1) and (2) of this section:
(a) Income shall be considered derived from or relating to sources within Idaho when such income is attributable to or resulting from:

* * *

(iii) The ownership or disposition of any interest in intangible personal property only to the extent that such property is employed in a business, trade, profession or occupation conducted or carried on in this state. Provided however, that interest income from an installment sale of real or tangible personal property shall constitute income from sources within this state to the extent that the property sold was located within this state. Provided further, that interest income received by a partner or shareholder of a partnership or S corporation from such partnership or S corporation shall constitute income from sources within this state to the extent that the partnership or S corporation is transacting business within this state;

The “property” here in question is stock. The petitioners have failed to show that the stock was used in a “business, trade, profession or occupation conducted or carried on in this state.”

As we have previously stated,¹ the statutory language set out in Idaho Code § 63-3026A(3)(a)(iii) is a codification of the common law doctrine of *mobilia sequuntur personam*. *Mobilia sequuntur personam* is a Latin term meaning “movables follow the person.” This common law doctrine is a legal fiction that has its roots in ancient Roman law. Under the *mobilia* doctrine, movable property is said to have its situs in the place where its owner is domiciled. United Gas Corporation v. Fontenot, 129 So.2d 748, 752-755 (La. 1961). Although originally applicable only for purposes of establishing a situs for tangible property, the doctrine has for many years been applied to intangible property as well. *Id.*

Applying the concept of *mobilia sequuntur personam* to state taxation, courts have stated that intangible property is normally subject to taxation only by the state where the owner resides

¹ See the Commission’s decision for Docket No. 16349 (2003).

since that is where the property is deemed to have its situs. While the property is subject to taxation only by the state in which the property has its situs (i.e. where the property is deemed to be located), the income derived from the intangible property is not necessarily clothed with this same immunity. New York ex rel. Cohn v. Graves, 300 U.S. 308, 313, 57 S.Ct. 466, 468 (1937).

Because of the formalistic and arbitrary nature of the *mobilia* doctrine, it did not take long for courts to formulate an exception that permitted a state other than the state of the owner's domicile to impose a tax on the intangible property. United Gas Corporation, *supra*. This exception, commonly referred to as the "business situs exception to the *mobilia* doctrine," is premised on the theory that intangible property could be utilized in a state other than the state of the owner's domicile in such a way as to render that property constitutionally susceptible to taxation in that other state. In other words, a state other than the state of the owner's domicile may, consistent with the Due Process Clause of the United States Constitution, tax the intangible property if that property is used in such a way as to create a "business situs" in that foreign state.

If [Redacted] was the owner of the stock, we find that the deduction would not be properly attributable to Idaho since he has not established that the stock had a business situs in Idaho.

WHEREFORE, the Notices of Deficiency Determination dated January 12, 2009, 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 December 31, 2009):

<u>YEAR</u>	<u>TAX</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
2005	\$55,954	\$5,595	\$13,004	\$74,553

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.

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]
[Redacted]
[Redacted]

Receipt No.

Receipt No.