

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)
[Redacted],) DOCKET NO. 22852
)
)
Petitioners.) DECISION
)
_____)

[Redacted] (petitioners) protest the Notice of Deficiency Determination (NODD) issued by the auditor for the Idaho State Tax Commission (Commission) dated March 2, 2010, asserting additional liabilities for Idaho income tax, penalty, and interest in the total amounts of \$251 and \$44,135 for 2006 and 2007, respectively.

The petitioners were, during the relevant years, nonresidents of Idaho. They did not file Idaho income tax returns for these years. During these years, they held an interest in an S-Corporation which reported an Idaho apportionment factor of 100 percent for both years. The sole issue is whether the petitioners' share of a capital gain from the sale of stock by the S-Corporation is taxable by Idaho. The income in question was reported by the S corporation as business income.

After contacting the petitioners concerning their failure to file Idaho income tax returns, the auditor sent the NODD referred to above, and the petitioners filed this administrative appeal.

The auditor's position was that the income from the petitioners' distributive share of the S-Corporation's income should be reported as Idaho source income. The petitioners contend that they were not required to report the capital gain from the sale of stock by the S corporation due to the provisions of the Interstate Tax Compact. Article II of the Compact provides some

definitions. One of these is:

3. "Taxpayer" means any corporation, partnership, firm, association, governmental unit or agency or person acting as a business entity in more than one state.

The petitioners contend that they were acting as a "business entity" in Idaho through their interest in the S corporation.

Article III of the Compact states, in part:

ELEMENTS OF INCOME TAX LAWS

Taxpayer Option, State and Local Taxes

1. Any taxpayer subject to an income tax whose income is subject to apportionment and allocation for tax purposes pursuant to the laws of a party State or pursuant to the laws of subdivisions in two or more party States may elect to apportion and allocate his income in the manner provided by the laws of such State or by the laws of such States and subdivisions without reference to this compact, or may elect to apportion and allocate in accordance with Article IV.

Article IV 6(c) states, in part, that:

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.

The petitioners therefore contend that, since their domicile is in another state, the capital gains in question are not taxable by Idaho.

Article IV of the Compact also provides the following:

9. All business income shall be apportioned to this State by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three.

Administrative Rule 263.03 stated, in part:

Pass-Through Items. Whether a pass-through item of income or loss is business or nonbusiness income is determined at the pass-through entity level. Pass-through items of business income or loss may include:

* * *

g. Capital gain or loss;

There may be several reasons for the denial of the petitioners' position. Only one is needed. The portion of the Multistate Tax Compact relied upon by the petitioners (Article IV 6(c)) is for the allocation of nonbusiness capital gains, not for business income as is the case at hand.

The income in question was business income to the petitioners pursuant to Administrative Rule 263.03. Business income from the S-Corporation is taxable by Idaho whether one looks to Idaho Code § 63-3026A(3)(a)(i) or to the Multistate Tax Compact, Article IV.9. Idaho Code § 63-3026A 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:
 - (i) Any business, trade, profession or occupation conducted or carried on in this state, including the distributive share of partnership income and deductions, and the pro rata share of S corporation income and deductions;

Accordingly, the Commission finds that the income from the capital gain from the sale by the S -Corporation of the stock is taxable to the petitioners. The Commission finds it unnecessary to address the other deficiencies in the petitioners' arguments in this decision.

After the issuance of the NODD, the auditor determined that the amount of itemized deductions allowed in computing the liability was understated. Therefore, the NODD must be adjusted to reflect the higher amount of itemized deductions allowable.

WHEREFORE, the Notice of Deficiency Determination dated March 2, 2010, is hereby MODIFIED, and AS SO MODIFIED, is APPROVED, AFFIRMED, and MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that the petitioners pay the following tax, penalty, and interest (computed to May 31, 2011):

<u>YEAR</u>	<u>TAX</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
2006	\$ 174	\$ 44	\$ 41	\$ 259
2007	32,034	8,009	5,373	45,416
				<u>\$45,675</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.

DATED this _____ day of _____ 2011.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this _____ day of _____ 2011, 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.
