BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of	)	
	)	DOCKET NO. 23807
[Redacted],	)	
	)	
Petitioners.	)	DECISION
	)	

[Redacted] (Petitioners) protested the Notice of Deficiency Determination dated February 17, 2011, asserting income tax, penalty, and interest in the total amount of $24,050 for taxable year 2006. Petitioners disagreed with the computation of the gain on the sale of their Idaho property. The Tax Commission, having reviewed the file, hereby issues its decision.

BACKGROUND

Petitioners are residents of the state [Redacted]. In 2006, Petitioners sold real property located in Idaho. The Income Tax Audit Bureau (Bureau) researched the Tax Commission's records and found Petitioners did not file an Idaho individual income tax return for that year. The Bureau sent Petitioners letters asking about the sale of their Idaho property and their requirement to file an Idaho income tax return. Petitioners did not respond to the Bureau’s letters, so the Bureau reviewed the information available, determined Petitioners were required to file an Idaho income tax return, prepared a return for Petitioners, and sent them a Notice of Deficiency Determination.

Petitioners protested the Bureau’s determination stating the gross proceeds were overstated and the sale of the property was incorrectly categorized as a long-term capital gain. Petitioners offered to settle the matter for the sum of $400, but because the Bureau had very little information on the property sold, the offer was not even considered. The Bureau and Petitioners continued to correspond via e-mail and additional information was obtained. The Bureau modified its audit report based upon the information provided, but still Petitioners continued to disagree with the tax deficiency. Petitioners believe that as non-residents they are not being treated fairly and that the audit process was more difficult than it need be and was overly complicated to maximize Idaho tax revenue.

The Bureau acknowledged Petitioners' protest and referred the matter for administrative review. The Tax Commission reviewed the matter and sent Petitioners a letter that discussed the methods available for redetermining a protested Notice of Deficiency Determination. Petitioners stated they wanted a hearing before the Tax Commission. Petitioners stated they needed to obtain legal counsel and an Idaho tax professional before they could schedule a date for the hearing. The Tax Commission continued corresponding with Petitioners and allowed them sufficient time to obtain legal counsel and seek professional advice. In one correspondence, Petitioners stated they had representation and that their representative would contact the Tax Commission. No contact was made by Petitioners' representative, and Petitioners stopped corresponding with the Tax Commission. Seeing that Petitioners have had ample time to seek professional advice and to provide whatever additional information they wanted the Tax Commission to consider but have failed to do so, the Tax Commission hereby decides the matter based upon the information available.

LAW AND ANALYSIS

Idaho Code section 63-3026A(3)(ii) states that income shall be considered derived from or relating to sources within Idaho when such income is attributable to or resulting from the ownership or disposition of any interest in real or tangible personal property located in Idaho. In 2006, Petitioners sold property in Idaho with a sales price of $225,000. This information was provided via a 1099S informational return and confirmed by Petitioners.

Idaho Code section 63-3030 sets forth the filing requirements for nonresidents that have income from Idaho sources. For taxable year 2006, the threshold amount for filing a nonresident return was $2,500. Therefore, if Petitioners realized income on the sale of the Idaho property in excess of $2,500, they were required to file an Idaho income tax return.

Since Petitioners failed to respond to the Bureau's inquiries, the Bureau determined Petitioners' Idaho taxable income solely upon the sales price of the property sold. Petitioners argued this was an overstatement of the proceeds they received on the sale of the property. Petitioners provided the Bureau with a copy of their 2006 [Redacted] income tax return to show how the sale was reported for [Redacted] income tax purposes. The Bureau used that information and modified its original determination and presented it to Petitioners. Petitioners did not agree with the modified determination because the Bureau included depreciation in the computation of the gain on the sale when no depreciation was ever claimed in Idaho, and Petitioners disagreed that the Idaho capital gains deduction should be tied to capital gains reported on their federal income tax return.

Idaho Code section 63-3002 states:

> It is the intent of the legislature by the adoption of this act, insofar as possible to make the provisions of the Idaho act identical to the provisions of the Federal Internal Revenue Code relating to the measurement of taxable income, to the end that the taxable income reported each taxable year by a taxpayer to the internal revenue service shall be the identical sum reported to this state, subject only to modifications contained in the Idaho law; to achieve this result by the application of the various provisions of the Federal Internal Revenue Code relating to the definition of income, exceptions therefrom, deductions (personal and otherwise), accounting methods, taxation of trusts, estates, partnerships and corporations, basis and other pertinent provisions to gross income as defined therein, resulting in an amount called "taxable income" in the Internal Revenue Code, and then to impose the provisions of this act thereon to derive a sum called "Idaho taxable income"; to impose a tax on residents of this state measured by Idaho taxable income wherever derived and on the Idaho taxable income of nonresidents which is the result of activity within or derived from sources within this state. All of the foregoing is subject to modifications in Idaho law including, without limitation, modifications applicable to

> unitary groups of corporations, which include corporations incorporated outside the United States.

In the determination of income as defined in the Internal Revenue Code (IRC), the gain on the sale of a capital asset is determined by subtracting from basis the depreciation allowed or allowable. (*See* IRC section 1016.) Since Idaho follows the IRC in the determination of taxable income and there is no provision (modification) in the Idaho Code to add to basis, in the computation of adjusted basis on the sale of a capital asset, depreciation claimed, the adjusted basis determined for federal purposes is the adjusted basis for Idaho purposes. <u>State Tax Commission v. Stang</u>, 135 Idaho 800, 25 P.3d 113, (2001). Therefore, the gain on the sale of the Idaho property reported on Petitioners' federal income tax return is the gain that should be reported to Idaho.

Idaho Code section 63-3022H states in pertinent part:

> (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.

Idaho Code section 63-3022H provides that if an individual has reported in taxable income capital gain net income, 60% of the capital gain net income from the sale of qualifying property shall be a deduction in determining taxable income. Taxable income is defined in Idaho Code section 63-3011B as federal taxable income as determined in the IRC. IRC section 1222(9) defines capital gain net income as the excess of the gains from sales or exchanges of capital assets over the losses from such sales or exchanges.

Petitioners' 2006 federal income tax return reported a net capital loss. Petitioners did not have capital gain net income included in their taxable income. The Idaho Code allows a capital gain deduction if capital gain net income is included in taxable income. (Idaho Code section 63-3022H(1).) Since Petitioners had a net capital loss in determining taxable income, the Idaho capital gains deduction is not available to them. Furthermore, the Idaho Code limits the amount of the capital gains deduction in subsection (2) of section 63-3022H to the amount of capital gain net income from all property included in federal taxable income. Petitioners did not have capital gain net income in taxable year 2006. Therefore, according to Idaho Code section 63-3022H(2), Petitioners' capital gains deduction is limited to zero.

Petitioners failed to provide anything to support their position regarding the computation of the gain on the sale of their Idaho property or that the Idaho capital gains deduction should not be limited. In Idaho, a State Tax Commission deficiency determination is presumed to be correct, and the burden is on the taxpayer to show that the deficiency is erroneous. Parsons v. Idaho State Tax Commission, 110 Idaho 572, 574-575 n.2, 716 P.2d 1344, 1346-1347 n.2 (Ct. App. 1986). Petitioners did not meet their burden. However, Petitioners did provide information that established their basis in the property sold. The Bureau modified its determination to include that information. The Tax Commission reviewed the Bureau's modified determination and found it is an accurate representation of Petitioners' Idaho taxable income for taxable year 2006.

CONCLUSION

In 2006, Petitioners sold Idaho property thereby producing income from an Idaho source. Petitioners provided information that established their basis in the property which reduced the gain determined by the Bureau. Petitioners' gain exceeded the threshold for filing an Idaho income tax return for 2006; therefore, Petitioners were required to file a 2006 Idaho income tax return.

Petitioners' 2006 [Redacted] income tax return did not report net capital gain income. The Idaho capital gains deduction is limited to the amount of net capital gain income from all property included in taxable income. Since Petitioners did not have net capital gain income from the property they disposed of in 2006, no Idaho capital gains deduction is available to them.

The Bureau modified its original determination to account for Petitioners' basis in the property sold. The Bureau also added interest and penalty to Petitioners' Idaho tax liability. The Tax Commission reviewed the Bureau's modified determination and found it to be an accurate depiction of Petitioners' Idaho taxable income. Therefore, the Tax Commission upholds the Bureau's modified determination.

THEREFORE, the Notice of Deficiency Determination dated February 17, 2011, and directed to [Redacted] is AFFIRMED AS MODIFIED.

IT IS ORDERED that Petitioners pay the following tax, penalty, and interest:

YEAR	TAX	PENALTY	INTEREST	TOTAL
2006	$6,492	$1,626	$1,871	$9,989

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

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

DATED this ________ day of ____________________ 2012.

IDAHO STATE TAX COMMISSION

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COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this ________ day of __________________ 2012, 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.

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