

**BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO**

In the Matter of the Protest of )  
[Redacted], ) DOCKET NO. 25353  
Petitioner. ) DECISION  
\_\_\_\_\_ )

**BACKGROUND**

On August 16, 2012, the Audit Division (Audit) of the Idaho State Tax Commission (Commission) issued a Notice of Deficiency Determination (NODD) to [Redacted] (Petitioner), proposing a change in the sales factor of the 2008 taxable year. There was no change in income tax, penalty, or interest at the partnership level. The original return reported that the taxable income would be reported on the partner’s returns.

On October 17, 2012, the Petitioner’s accountant filed a timely protest. The file was transferred to Tax Policy on February 7, 2013, for resolution. The Commission sent a letter to the Petitioner and its representative dated February 28, 2013, explaining the options for resolving a protested audit.

**ISSUES**

1. Whether Audit was correct under Idaho Code section 63-3027(r)(2) to source sales to Idaho, based on a ratio in proportion to other taxable years, in the calculation of the Idaho sales factor for taxable year 2008.

**DISCUSSION**

When calculating the apportionment factor for taxable year 2008, the Petitioner reported zero sales for Idaho. Then, without explanation, the Petitioner recorded Idaho sales amounts for taxable years 2009 through 2010. The NODD was prepared using an Idaho sales amount for

taxable year 2008 that was in roughly the same proportion to the payroll as 2009 and 2010. Audit sent letters on May 22, 2012 and again on July 2, 2012, requesting an explanation for reporting zero sales to Idaho in 2008. After no reply from the Petitioner or its representative, Audit issued the NODD.

The Petitioner's representative protested the NODD. Audit sent the Petitioner a letter, dated November 13, 2012, requesting specific information supporting their position. No information was provided.

The Petitioner's accountant requested until November 30, 2012 to provide data. At November 30, the Petitioner requested until January 31, 2013 to provide information. The "Cost of Performance" argument was first raised by the Petitioner's representative in the protest letter, offering several court cases and explaining the statute and its application. There was still no information specific to the Petitioner or explanation of how the determination was made that in their case, the "Cost of Performance" principle of Idaho Code § 63-3027(r)(2) applies.

#### LAW AND ANALYSIS

The Idaho taxable income of corporations and partnerships that do business both within and without Idaho is calculated according to Idaho Code § 63-3027 and the related rules.

63-3027(i) (1) says in part " ... Idaho Code, all business income shall be apportioned to this state under subsection (j) of this section by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus two (2) times the sales factor, and the denominator of which is four (4)..."

Idaho Code section 63-3027(r)(2):

(r) Sales, other than sales of tangible property, are in this state, if:

...

(2) The income-producing activity is performed both in and outside this state and a greater proportion of the income-producing activity is performed in this state than in any other state, based on costs of performance. Underline added.

The Petitioner has not answered the primary question raised by Audit. They maintain that they are not able to provide the gross sales to Idaho customers. Among other things, Audit asked for a copy of the study and analysis that resulted in the conclusion that the sales are properly sourced to a state other than Idaho. Idaho law and tax administrative rules are very specific on documentation requirements.

A “Cost of Performance” analysis is a fact-intensive process. The purpose of our audit process is to review and verify, to the extent possible, the facts and conclusions presented by taxpayers. The starting point is the total Idaho sales and identifying the direct costs incurred in making those sales. The direct costs incurred within Idaho are then compared to the direct costs incurred elsewhere. The Petitioner’s representative insists that there is no way to track the Idaho sales and no direct costs are incurred within Idaho, therefore it doesn’t matter what the sales within Idaho are, the direct costs will always be greater elsewhere. All Idaho taxpayers are required to provide proper evidence to substantiate the position taken on their income tax returns. The general statement that the company’s headquarters are outside Idaho and direct costs will always be greater outside of Idaho is not sufficient to meet the standards of a Cost of Performance study.

Idaho Administrative and Enforcement Rule:

**201. EXAMINATION OF RECORDS: RECORDKEEPING AND PRODUCTION REQUIREMENTS** Sections 63-3042 and 63-3043, Idaho Code.

01. In General. a. A taxpayer shall maintain all records that are necessary to a determination of the correct tax liability. Required records must be made available on request by the Tax Commission or its authorized representatives. The time and place for production shall be reasonable and shall occur during regular business hours. When books and papers are requested they will be relevant and reasonable documentation for the issues under examination. The request for information is relevant if it is germane to or applicable to an audit issue.

Idaho Income Tax Administration Rule 450:

04. Verification of Factors. The taxpayer shall make available the fifty-one (51) state apportionment factor detail when requested by the Tax Commission. Failure to do so may justify the imposition of the negligence penalty provided by Section 63-3046(a), Idaho Code.

The 51 state apportionment factor detail is important to confirm that the total of property, payroll and sales in the apportionment denominators is not greater than the amounts used in the numerators.

Idaho Income Tax Administration Rule 550:

03. Costs of Performance. Costs of performance are the direct costs determined in a manner consistent with generally accepted accounting principles and according to accepted conditions or practices of the taxpayer's trade or business to perform the income producing activity that gives rise to the particular item of income. Included in the taxpayer's cost of performance are taxpayer's payments to an agent or independent contractor for the performance of personal services and utilization of tangible and intangible property that give rise to the particular item of income. Underline added.

#### CONCLUSION

A Notice of Deficiency Determination issued by the Idaho State Tax Commission is presumed to be accurate. Parsons v. Idaho State Tax Com'n, 110 Idaho 572 (Ct. App. 1986). The burden is on the taxpayer to show the deficiency is erroneous. Albertson's, Inc. v. State, Dept. of Revenue, 106 Idaho 810 (1984).

Having presented inadequate information in support of their position during the audit or redetermination process, the Petitioner has failed to meet its burden of proving error on the part of the deficiency determination. Absent information to the contrary, the Commission accepts Audit's calculation of the Idaho sales factor for the year 2008.

THEREFORE, the Notice of Deficiency Determination dated August 16, 2012, and directed to the Petitioner is hereby AFFIRMED.

| <u>YEAR</u> | <u>TAX</u> | <u>PENALTY</u> | <u>INTEREST</u> | <u>TOTAL</u> |
|-------------|------------|----------------|-----------------|--------------|
| 12/31/08    | \$ 0       | \$ 0           | \$ 0            | <u>\$ 0</u>  |

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

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

DATED this \_\_\_\_\_ day of \_\_\_\_\_ 2013.

IDAHO STATE TAX COMMISSION

\_\_\_\_\_  
COMMISSIONER

**CERTIFICATE OF SERVICE**

I hereby certify that on this \_\_\_\_\_ day of \_\_\_\_\_ 2013, 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.  
  
\_\_\_\_\_