

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 25638
[REDACTED],)	
)	
Petitioners.)	DECISION
<hr style="width: 45%; margin-left: 0;"/>		

BACKGROUND

On March 29, 2013, the Audit Division (Audit) of the Idaho State Tax Commission (Commission) issued a Notice of Deficiency Determination (NODD) to [Redacted] (Petitioners) proposing adjustments to the Idaho taxable income for the taxable years 2008 and 2009. The majority of the adjustments came from their wholly owned corporation, [Redacted]. See Docket No. 25639. [Redacted] is a Subchapter S corporation¹ (S corp.). The changes to taxable income made on the S corp.'s return are passed through to the owners and reflected herein.

On May 29, 2013, the Petitioners attorney-in-fact, under authority of an Idaho Power of Attorney (POA), filed a timely protest. On September 12, 2013, the file was transferred to the Legal/Tax Policy Division for resolution. A letter was sent on October 17, 2013, explaining the options for resolving an appeal. The POA was replaced a couple of times during the audit process. After working with the fourth POA on trying to reach a resolution, the owner replaced that POA and we started over. After reviewing the information provided, the Commission makes this decision with the information available.

¹ Under federal law, S corporations permit shareholders to elect a pass-through taxation system under which income is subjected to only one level of taxation; the corporation's profits pass through directly to its shareholders on a pro rata basis and are reported on the shareholders' individual tax returns. Internal Revenue Code, subchapter S.

ISSUES

1. Whether the adjustments made in the S corp. are correct. *See* Docket No. 25639 for details.
2. Whether the adjustments Audit made to the Petitioners' Schedule C are correct.
3. Whether the adjustments Audit made to the Petitioners' stock basis calculation are correct.
4. Whether the adjustments Audit made to the Schedule E rents and property taxes are correct.
5. Whether the adjustments Audit made to the Schedule A amounts are correct.
6. Whether the reduction in the Petitioners' grocery credit is correct.
7. Whether the Petitioner is required to recapture the Investment Tax Credit (ITC) claimed on the 2009 Idaho income tax return.
8. Whether the penalties are properly assessed on the NODD.

DISCUSSION

The disallowances of expenses claimed on the tax return were primarily for lack of or inadequate documentation and support. Audit cites Internal Revenue Code (IRC) section 6001 and Treasury Regulation 1.6001-1 as the requirement to maintain records necessary to substantiate income and deductions reported on a tax return. Idaho law also requires keeping adequate records. Idaho Code section 63-3075 and Tax Commission Administration and Enforcement Rule 410 both provide for penalties for not providing adequate records.

A Notice of Deficiency Determination issued by the Idaho State Tax Commission is presumed to be accurate. Parsons v. Idaho State Tax Commission, 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).

Issue 1.

See Docket No. 25639 for details of the adjustments to the S corp.

Issue 2.

Whether the adjustments Audit made to the Petitioners' Schedule C are correct. On the original NODD, auto, truck and meal expenses were disallowed. Depreciation expense was allowed for the [Redacted] Equipment owned by [Redacted]. [Redacted] opened for business in March 2008. The Petitioners were allowed the mid-year convention under MACRS or one half of the straight line depreciation in the first year.

The documentation provided did not distinguish the corporate meals and miles from the Schedule C meals and miles. The Commission made no changes to the adjustment for meals and miles, on the individual NODD. Some meals and mileage expenses were allowed in the corporation.

Issue 3.

Whether the adjustments Audit made to the Petitioners' stock basis calculation are correct.

Audit recalculated the installment sale of the S corp. reported on the Petitioners' original Idaho income tax return. The Petitioners filed an amended return, received by the Commission on August 19, 2013, after the NODD was issued and protested. Tax Commission Administration and Enforcement Rule 325.07 restricts the filing of an amended return for a year which has a pending protest. The amended return was not accepted or processed. It was included with the information to be reviewed in appeal. The documentation provided by the Petitioners as support for their amended return claiming additional basis was a printout of a QuickBooks check

register. There were expenses that were clearly personal. Most of the payments went to personal credit cards. There was no clear evidence that there were any business expenses that were not already being considered as deductions. The payments to personal credit cards should have been tracked as distributions to the extent that any personal items were purchased with those credit cards. The Commission upholds the audit adjustment and does not accept any changes reported on the amended return.

Issue 4.

Whether the adjustments Audit made to the Schedule E rents and property taxes are correct. The NODD adjusted rents, insurance and property taxes. The items that were documented were allowed in the review of the Corporate NODD. Those adjustments flow through to this decision and are reflected in the remaining tax liability.

Issue 5.

Whether the adjustments Audit made to the Schedule A amounts are correct. Medical expenses were limited to the amount over 7.5 percent of the petitioners' adjusted gross income (AGI). The increase in the AGI made the limit greater than the amounts claimed. The Commission upholds these adjustments.

Issue 6.

Whether the reduction in the Petitioners' grocery credit is correct. The Idaho Grocery Credit is \$50 per person when the Idaho taxable income is \$1,000 or less. The credit is reduced to \$30 per person when the Idaho taxable income is over \$1,000. The adjustments in this NODD result in taxable income over \$1,000 in the 2008 taxable year. The Commission upholds the NODD on this issue.

Issue 7.

Whether the Petitioner is required to recapture the Investment Tax Credit (ITC) claimed on the 2009 Idaho income tax return. The NODD said that the equipment was not in service for longer than a year and therefore recapture was owed. The Commission upholds the NODD on this issue.

Issue 8.

Whether the penalties are properly assessed on the NODD. There were three separate penalties assessed on the NODD:

Idaho Code section 63-3046. PENALTIES AND ADDITIONS TO THE TAX IN CASE OF DEFICIENCY.

(a) If any part of any deficiency is due to negligence or disregard of rules but without intent to defraud, five percent (5%) of the total amount of the deficiency (in addition to such deficiency) shall be assessed, collected and paid in the same manner as if it were a deficiency.

(b) If any part of any deficiency is due to fraud with intent to evade tax, then fifty percent (50%) of the total amount of the deficiency (in addition to such deficiency) shall be so assessed, collected and paid.

(c) (1) In the event the return required by this chapter is not filed on or before the due date (including extensions) of the return, there may be collected a penalty of five percent (5%) of the tax due on such returns for each month elapsing after the due date (including extensions) of such returns until the return is filed.

(d) (1) If there is a substantial understatement of tax for any taxable year, there shall be added to the tax an amount equal to ten percent (10%) of the amount of any underpayment attributable to such understatement.

....

(g) Total penalties imposed under subsections (a), (c) and (d) of this section and under section 63-3033, Idaho Code, shall not exceed twenty-five percent (25%) of the tax due on the return.

First, there is the late filing penalty for the 2009 return only. This is according to Idaho Code section 63-3046(c), five percent (5%), per month not to exceed twenty-five percent (25%) of the tax due on the return. The Petitioners' 2009 individual income tax return was filed on June 22, 2011, more than 5 months later than the latest extension that is available; the maximum of 25 percent was imposed. The Commission upholds the penalty on this issue. There is no need to discuss the negligence and substantial understatement penalties as the late filing penalty was

equal to the maximum allowed.

THEREFORE, the NODD dated March 29, 2013, and directed to [Redacted][Redacted] is hereby AFFIRMED as MODIFIED:

<u>YEAR</u>	<u>TAX</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
12/31/08	\$6,387			\$6,387
12/31/09	11,850	2,863	2,793	17,506
				<u>23,893</u>
			Less Payment 4-12-12	<u>(6,784)</u>
			TOTAL DUE	<u>\$17,109</u>

Interest is calculated through March 31, 2016, and will continue to accrue at the rate set forth in Idaho Code section 63-3045.

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 _____ 2016.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this _____ day of _____ 2016, 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.
