

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

In the Matter of the Protest of )  
[Redacted] ) DOCKET NO. 0-704-071-680  
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Petitioner. ) DECISION  
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\_\_\_\_\_ )

On August 22, 2017, the staff of the Tax Discovery Bureau (Bureau) of the Idaho State Tax Commission (Commission) issued a Notice of Deficiency Determination (Notice) to [Redacted] (Petitioner) proposing corporate income tax, penalty, and interest in the total amount of \$415. Petitioner filed a timely petition for redetermination (Petition).

Having reviewed the Bureau’s audit file, the Petition, and the Bureau’s response to the Petition (Protest Summary), the Commission hereby upholds the Notice.

**I. ISSUE(S)**

Is Petitioner, incorporated outside of Idaho, required to file Idaho corporate income tax returns for 2014 and 2015? The Commission finds that Petitioner was required to file Idaho corporate income tax returns for 2014 and 2015.

**II. GENERAL STATEMENT OF LAW**

Every corporation which is transacting business in this state, authorized to transact business in this state or having income attributable to this state, unless exempt from the tax imposed in this chapter, is required to file an Idaho income tax return.<sup>1</sup> Subject only to the limitations of the constitutions of the United States and of the state of Idaho, the term “transacting business” shall include owning or leasing, whether as lessor or lessee, of any property, including real and personal

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<sup>1</sup> Idaho Code § 63-3030(a)(3).

property, located in this state, or engaging in or the transacting of any activity in this state, for the purpose of, or resulting in, economic or pecuniary gain or profit.<sup>2</sup>

### **III. BACKGROUND AND AUDIT FINDINGS**

On July 18, 2017, the Bureau sent a letter notifying Petitioner that they may have an Idaho filing requirement for tax years 2010 through 2015 due to the reporting of Idaho wages for these years. In its letter, the Bureau noted, “having an employee acting on your behalf in Idaho constitutes transacting business.” The Bureau further requested that Petitioner file Idaho corporate income tax returns or if it filed Idaho returns, reply with the name and employer identification number used on the Idaho return.

During the next several days, the Bureau and Petitioner exchanged several e-mails. Petitioner sought further explanations from the Bureau regarding Idaho income tax filing requirements and to express frustration over the time it took the Commission to notify Petitioner that it had an Idaho filing requirement. For example, Petitioner states:<sup>3</sup>

[sic] I don't think it is fair to pay the Interest or the principle so far back when there is not reasonable way to even know about the tax. After all it is called an income tax and Idaho is making something up out of thin air that isn't even based on income in your State. It seems to me that it is the Idaho's responsibility to inform [Petitioner] in a timely manner. Idaho does have payroll records from 2011 after all, why would it take 6 years to become informed? We have no other ties in your State other than our one single employee and I just can't think of how we would have ever found out without the State of Idaho making it known to [Petitioner].

On July 24, 2017, the Bureau sent the taxpayer a letter requesting that Petitioner file Idaho corporate income tax returns for tax years 2011 through 2015 by August 31, 2017. The Bureau cited Idaho Code §§ 63-3023, 63-3027, and 63-3030, as support concluding that:

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<sup>2</sup> Idaho Code § 63-3023.

<sup>3</sup> Petitioner's e-mail dated July 25, 2017.

An out-of-state business is, or is deemed to be physically present in the taxing state for application of that state's corporate income tax requirements if they engage in activities which constitute a physical connection with the taxing state, including without limitation, the performance of services in the taxing state.

The Tax Commission finds that though its employee in Idaho, [Petitioner] is transacting business in Idaho.

*Id*

On August 10, 2017, Petitioner provided the Bureau with an analysis prepared by a certified public accounting firm (CPA) in which the CPA disagreed with the Bureau's conclusion that Petitioner had an Idaho filing requirement.<sup>4</sup> According to the CPA:

[Petitioner] provides internet services such as high-speed internet, data center storage, firewall protection, and voice plus data packages to individuals and businesses located in Southern California.

The company employs a single employee in Idaho who performs code writing for the internal systems of the company. The employee has no contact with customers and is engaged in no solicitation activities. The employee in no way establishes or enhances a market for the company's services in the state nor do they provide other activities directly related to the employer's commercial business activities.

Idaho Revenue and Taxable Code section 63-3030 states "Persons Required to Make Returns of Income. (a) Returns with respect to taxes measured by income in this chapter shall be made by the following: (3) Every corporation which is transacting business in this state, authorized to transact business in this state or having income attributable to this state, unless exempt from the tax imposed in this chapter;"

Idaho Code section 63-3023 defines "transacting business" as owning or leasing, whether as lessor or lessee, of any property, including real and personal property, located in this state, or engaging in or the transacting of any activity in this state, for the purpose of or resulting in economic or pecuniary gain or profit.

The 2016 Idaho Corporation Income Tax instructions for Form 41 states that transacting business in Idaho is indicated by, but not limited to, the following activities: "...having an agent, such as a

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<sup>4</sup> Letter dated August 10, 2017, from [Redacted]

collector, repair person, delivery person, etc. acting on your behalf in Idaho”.

Based upon the above, it does not appear that merely having an employee located in the State of Idaho in itself constitutes “transacting business” in Idaho. If this were the case, there would be no need to state anything other than this fact.

We believe that since the employee’s duties were not directed at customers so as to develop the company’s market in the state, the employee has no contact with customers, did not engage in any solicitation activities, and did not act as an agent of the company, the company’s employment of the Idaho employee does not reach the level of “transacting business” as defined by the State of Idaho. As such, [Petitioner] would have no corporate filing requirement to the State of Idaho.

*Id*

On July 28, 2017, the Bureau issued the Notice finding that Petitioner was required to file Idaho corporate income tax returns for 2014 and 2015. The Bureau did not pursue 2011, 2012, and 2013, because the potential amount at-issue was too small or Petitioner incurred a loss.<sup>5</sup>

The Bureau calculated Idaho tax based upon the information available to the Bureau. The Bureau asserts that Petitioner owes Idaho tax in the amount of \$228 and \$83 for 2014 and 2015, respectively.<sup>6</sup> Additionally, in its Notice, the Bureau included interest in accordance with Idaho Code § 63-3045 and included the 25 percent failure to file a return penalty in accordance with Idaho Code § 63-3046(c). The Bureau’s total proposed assessment amounted to \$307 and \$108 for tax years 2014 and 2015, respectively, for a total of \$415.

In its Petition, Petitioner argues that its Idaho employee only works on its internal controls and is not generating any income for Petitioner, thus no business transaction is taking place. Therefore, Petitioner is not “transacting business” within Idaho as that term is defined under Idaho

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<sup>5</sup> Protest Summary, Page 2, Case History, entry dated August 22, 2017.

<sup>6</sup> See Exhibit A at the end of this decision (page 8) for more detail on the calculation of the tax liability. The Idaho tax includes the \$10 Idaho Code § 63-3082 additional tax commonly referred to as the Permanent Building Fund tax.

Code § 63-3023.<sup>7</sup> Furthermore, as stated in the letter provided by Petitioner’s CPA, the Idaho employee:

1. Has no contact with Petitioner’s customers.
2. Does not engaged in solicitation activities on behalf of Petitioner.
3. Does not establish or enhance a market for Petitioner’s services in Idaho.
4. Does not provide other activities directly related to Petitioner’s commercial business activities.

On April 5, 2018, an informal hearing was held in which Petitioner participated by telephone. During the informal hearing, Petitioner mentioned that it provides its Idaho employee with a computer. Nonetheless, Petitioner restated that it did not have any customers outside of California and its Idaho employee did not have anything to do with Petitioner’s generation of income; accordingly, Petitioner was not transacting business within Idaho.

#### **IV. ANALYSIS**

If Petitioner is “transacting business” within Idaho, Petitioner is required to file an Idaho income tax return.<sup>8</sup> The disagreement in this docket involves what is “transacting business” in Idaho. Idaho’s definition of “transacting business,” contained in Idaho Code § 63-3023, states:

Transacting business. Subject only to the limitations of the constitutions of the United States and of the state of Idaho, the term “transacting business” shall include owning or leasing, whether as lessor or lessee, of any property, including real and personal property, located in this state, or engaging in or the transacting of any activity in this state, for the purpose of or resulting in economic or pecuniary gain or profit.

The statutory language contains two concepts, satisfying either of which requires a finding that a corporation, such as Petitioner, is “transacting business” in Idaho. First, if a corporation

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<sup>7</sup> Petitioner’s letter dated August 28, 2017.

<sup>8</sup> Idaho Code § 63-3030(a)(3).

owns or leases any property located in Idaho for the purpose of or resulting in economic or pecuniary gain or profit, the corporation is transacting business in Idaho. Second, if the corporation engages in or transacts any activity in Idaho for the purpose of or resulting in economic or pecuniary gain or profit, the corporation is transacting business in Idaho.

Petitioner does not dispute that it is engaged in a trade or business to make a profit. Petitioner has both property in Idaho and an employee engaging in activity supporting Petitioner's commercial business activity. While it may be true that the computer and the Idaho employee's activities only relate to the writing of computer code for the business's internal systems and the Idaho employee does not have personal contact with Petitioner's California customers, the Idaho statute simply requires that the property or activity be for the "purpose of or resulting in economic or pecuniary gain or profit." The purpose of the activities of the employee and his computer in Idaho is to contribute to Petitioner's overall business activity that would "result in economic or pecuniary gain or profit. Finally, Petitioner has not provided the Commission with any court decisions interpreting the Idaho constitution or the United States Constitution as prohibiting the taxation of an out-of-state business in situations where the business had one of its employee's residing in State A and performing only administrative functions for the business in State A.

Given the facts in this case, the Commission finds that Petitioner is transacting business within Idaho since Petitioner owns a computer (property) and has an employee in Idaho (activity) for the purpose of or resulting in economic or pecuniary gain or profit. In addition, the Commission upholds the imposition of interest and penalty.

## **V. ORDER**

The Notice dated August 22, 2017, and directed to [Redacted] is hereby

**APPROVED and MADE FINAL.**

The Commission ORDERS that Petitioner pay the following tax, penalty, and interest:

YEAR	TAX	PENALTY	INTEREST	TOTAL
2014	\$228	\$57	\$29	\$314
2015	83	21	7	111
			TOTAL DUE	<u>\$425</u>

The Commission calculated the interest shown above through September 30, 2018.

The Commission now DEMANDS immediate payment of this amount.

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

DATED this \_\_\_\_\_ day of \_\_\_\_\_ 2018.

IDAHO STATE TAX COMMISSION

\_\_\_\_\_  
COMMISSIONER

**Exhibit A - Idaho Tax Calculation**

	<u>2014</u>	<u>2015</u>
Federal taxable income	\$209,223	\$70,543
Idaho adjustments to apportionable income	<u>0</u>	<u>0</u>
Business income subject to apportionment	209,223	70,543
Idaho apportionment factor:		
Idaho sales factor	0.0000%	0.0000%
Idaho property factor	0.0000%	0.0000%
Idaho payroll factor	<u>5.6319%</u>	<u>5.6167%</u>
Total	5.6319%	5.6167%
Divide by four	<u>4</u>	<u>4</u>
Idaho apportionment factor:	<u>1.4080%</u>	<u>1.4042%</u>
Income apportioned to Idaho	2,946	991
Idaho adjustments in arriving at Idaho taxable income	<u>0</u>	<u>0</u>
Idaho taxable income	2,946	991
Idaho corporate income tax rate	<u>7.4%</u>	<u>7.4%</u>
Idaho corporate income tax	218	73
Idaho Permanent Building Fund tax	<u>10</u>	<u>10</u>
Total Idaho tax	<u><u>\$228</u></u>	<u><u>\$83</u></u>

**CERTIFICATE OF SERVICE**

I hereby certify that on this \_\_\_\_\_ day of \_\_\_\_\_ 2018,  
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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