

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of

██████████ ██████████ ██████████ ██████████

Petitioners.

DOCKET NO. 0-501-453-824

DECISION

██████████ ██████████ ██████████ ██████████ ██████████ ██████████ (Petitioners) protested the Notice of Deficiency Determination (Notice) dated January 3, 2025. Petitioners disagreed with Income Tax Audit's (Audit) determination of their Idaho taxable income for tax years 2021 through 2023. The Idaho State Tax Commission (Tax Commission) reviewed the matter and hereby upholds the modified Notice for the reasons stated below.

BACKGROUND

Audit selected Petitioners' 2021 through 2023 Idaho individual income tax returns for review. The specific issues examined were domicile, community property, and filing status.

Petitioners were married at all times relevant to this decision. Also, during all such times, Ms. ██████████ was domiciled in Washington and Mr. ██████████ was domiciled in Idaho. Petitioners filed joint tax returns for all years with the Internal Revenue Service (IRS). Petitioners' filing history with Idaho is as follows:

<u>Tax Year</u>	<u>Form</u>	<u>Filing Status</u>	<u>Ms. ██████████</u>	<u>Mr. ██████████</u>
2019	43	joint	nonresident	part-year
2020	40	separately	not included	resident
2021	40	separately	not included	resident
2022	40	separately	not included	resident
2023	40	joint	resident	resident
2024	40	joint	resident	resident

The Idaho returns submitted by Petitioners for tax years 2021 through 2023 did not include any allocation of Petitioners' community income. Audit adjusted the returns for each tax year to

include the community property portion of Petitioners' income that was taxable to Idaho. This adjustment changed Petitioners' Idaho income tax liability. Audit also changed Petitioners' filing status on the 2021 and 2022 returns to match the federal returns.

Petitioners protested the Notice arguing that it did not take into consideration itemized deductions, qualified business income (QBI), taxes paid, and they also stated the Form 43 is not suited for calculating community property income. Audit acknowledged Petitioners' protest and modified the Notice for tax years 2021 and 2022, allowing a deduction for itemized deductions, as shown on the federal returns, and QBI. When Petitioners did not respond to the modified Notice, Audit forwarded the case to the Tax Commission's Appeals Unit (Appeals) for administrative review.

Appeals reviewed the matter and sent Petitioners a letter that discussed the methods available for redetermining a Notice. Petitioners did not respond. Therefore, the Tax Commission decides the matter based on the information available.

LAW AND ANALYSIS

Both the state of Idaho and the state of Washington are community property states, and both treat earnings as community property and therefore, community income. Under Idaho law, earnings of a spouse are presumed to be community property. Idaho Code section 32-906(1); *Martsch v. Martsch*, 103 Idaho 142, 645 P.2d 882 (1982). This is true even if the husband and wife are separated and living apart. *Suter v. Suter*, 97 Idaho 461, 546 P.2d 1169 (1976) *Desfosses v. Desfosses*, 120 Idaho 354, 815 P.2d 1094 (Ct. App. 1991). Thus, under Idaho law, only death or a legal divorce will disband the community.

Washington community property law also provides that income earned through the labor of a spouse is presumed to be community income. Revised Code of Washington (R.C.W.) section

26.16.030; *In re Marriage of Hurd*, 848 P.2d 185 (Wa.Ct.App. 1993) (“Earnings arising from services performed during marriage are community property.”). However, Washington community property law provides an exception to this general principle where the husband and wife are living separate and apart even though they are not legally divorced. Specifically, R.C.W. section 26.16.140 provides that “[w]hen a husband and wife are living separate and apart, their respective earnings and accumulations shall be the separate property of each.” Thus, under Washington law, earnings of a spouse are community property except where the spouses are separated and living apart, in which case each spouse’s earnings are treated as his or her separate property. However, Washington courts have consistently held that in order for R.C.W. section 26.16.140 to apply, the married couple must be living separate and apart as a result of marital discord.

As mentioned previously, for tax years 2021 through 2023, Ms. [REDACTED] domicile was Washington. Petitioners have made no claim that the decision to be domiciled in separate states was a result of marital discord. Therefore, for the period Ms. [REDACTED] was domiciled in Washington, the community property laws of Idaho and Washington are applicable. Petitioners’ earnings would be considered community income. Since the earnings of Petitioners are considered community property, the issue now becomes how to determine Petitioners’ Idaho taxable income and Idaho income tax liability.

Idaho Code section 63-3002 states the purpose of the Idaho income tax act is to impose a tax on residents of the state of Idaho measured by income wherever derived, and on the income of nonresidents derived from activity or sources within Idaho. Therefore, for community property purposes, generally Idaho taxable income consists of all the income from Idaho sources plus one-half the income of the non-resident spouse living in the other community property state. *Parker v. Idaho State Tax Commission* 148 Idaho 842 (2010).

Since Washington is a community property state, Ms. [REDACTED] Washington income is attributed equally to both Petitioners. And because Mr. [REDACTED] was a resident of Idaho, his half of the community income from Washington is reportable to Idaho and becomes part of Petitioners' Idaho taxable income.

Idaho Code section 63-3031(c) states that if taxpayers file a joint federal return, they must file a joint return for state purposes. Petitioners filed their 2021 through 2023 federal returns as Married Filing Jointly, yet their 2021 and 2022 Idaho returns were filed as Married Filing Separate. Following Idaho Code, Petitioners' filing status on their 2021 and 2022 Idaho returns must be adjusted to match their federal returns.

CONCLUSION

Petitioners were domiciled in community property states where their earnings were considered community income. As such, half of Ms. [REDACTED] earnings are attributable to Mr. [REDACTED] and half of Mr. [REDACTED] earnings or losses are attributable to Ms. [REDACTED]. All other community income (interest, dividends, capital gains and losses, etc.) is also divided equally between Petitioners. Audit's division of Petitioners' income is in accordance with the applicable laws governing community property. Therefore, the Tax Commission finds that Audit's inclusion of one-half of Ms. [REDACTED] income and all of Mr. [REDACTED] income, along with the filing status of Married Filing Jointly, is correct.

Audit added interest and penalty to Petitioners' tax deficiency. The Tax Commission reviewed those additions and found them to be appropriate and in accordance with Idaho Code sections 63-3045 and 63-3046, respectively.

THEREFORE, the modified Notice dated March 25, 2025, and directed to Ms. [REDACTED] [REDACTED] and Mr. [REDACTED] [REDACTED] is hereby AFFIRMED and MADE FINAL.

IT IS ORDERED that Petitioners pay the following tax, penalty, and interest calculated per Idaho Code section 63-3045:

<u>YEAR</u>	<u>TAX</u>	<u>PENALTY</u>	<u>INTEREST</u>	<u>TOTAL</u>
2021	\$9,505	\$475	\$1,167	\$11,147
2022	12,163	608	1,056	13,827
2023	(11,429)	0	(173)	<u>(12,214)</u>
			TOTAL	\$12,760

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 _____ 2025.

IDAHO STATE TAX COMMISSION

CERTIFICATE OF SERVICE

I hereby certify that on this _____ day of _____, 2025,
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:

Receipt No.


