

- The LLC consisted of two members, a married couple.
- Beginning in 2017, the LLC was treated as a disregarded entity for tax purposes (AIF referenced IRS Revenue Procedure 2002-69). The LLC's taxable income was reported on Schedule C attached to the members' individual returns.
- The LLC was not required to file a partnership return for the years listed in the Notice.
- The penalty imposed does not apply.

The Bureau sent a letter acknowledging the timely protest and provided a schedule for filing correct returns. The letter indicated that if the requested information was not received, the Bureau would transfer the matter to the Tax Commission's Tax Appeals unit (Appeals) for resolution.

AIF submitted individual income tax returns for tax years 2017 in late December 2024, 2018 in early January 2025, 2019 in late January 2025, and 2020 in early February 2025 generally following the Bureau's prescribed schedule. The LLC's income and expenses were reported on the owners' Schedule C. After a reminder and extension to file the next return, AIF submitted a return for 2021 in late March 2025. After receiving each return, the Bureau sent a letter cancelling the Notice for the specific year for which the return had been filed.

In May 2025, AIF informed the Bureau that he had not received from the owners the information needed to file a correct return for 2022. After another month, the final return had not been filed, so the Bureau transferred the matter to Appeals. In August 2025, Appeals sent a letter providing the options available for redetermining a protested Notice. AIF contacted Appeals, stating that the owners still had not provided the necessary information, but he was willing to reach out to the owners again. Appeals granted an extension to file the last missing return, but it was never filed. In the absence of an actual return, the Tax Commission must make its decision based on the information currently available.

Law & Analysis

The Bureau's Notice dated October 1, 2024, included tax years 2017, 2018, 2019, 2020, 2021, and 2022. Returns including income and expenses for the LLC were filed for 2017, 2018, 2019, 2020, and 2021. The Bureau cancelled the Notice for these specific years after receiving each year's return. These years will not be mentioned further in this decision. The only year included in the Notice left unfiled is 2022.

When the Bureau prepared the Notice, the LLC's most recent filed returns were partnership returns of income. At the time, the Bureau had no reason to believe that the reporting method for the LLC's income and expenses had changed, because no returns had yet been filed showing a new reporting method. AIF mentioned IRS Revenue Procedure 2002-69 in communications with the Bureau. This Revenue Procedure states that the IRS will respect a taxpayer's treatment of a business entity wholly owned by a husband and wife as community property under the laws of a state. The LLC in this case is a qualified entity under Revenue Procedure 2002-69. Section 4.03 of the Revenue Procedure states, "A change in reporting position will be treated for federal tax purposes as a conversion of the entity."

Once the first missing return was filed including the LLC's income and expenses on the owners' Schedule C, the reporting position changed, and the entity was no longer considered a partnership for tax purposes. Because of this, the Notice asserting partnership income passed through to the owners is incorrect and should be canceled. Additionally, because the LLC no longer reports as a partnership and was not required to file a partnership return for 2022, the penalty included for failure to file a partnership return is not applicable.

The Tax Commission will estimate the LLC's income and expenses and include them in a decision for a separate but related Appeals docket, 0-277-844-992.

Conclusion

With the filing of their 2017 income tax return, the LLC's owners, a married couple, changed the reporting method for the LLC from partnership (reported on federal Form 1065 and Idaho Form 65) to sole proprietorship (reported on federal Schedule C).

THEREFORE, the Notice dated October 1, 2024, and directed to [REDACTED] [REDACTED] [REDACTED] is hereby CANCELED.

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

DATED this _____ day of _____ 2026.

IDAHO STATE TAX COMMISSION

CERTIFICATE OF SERVICE

I hereby certify that on this _____ day of _____ 2026,
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.

[REDACTED]

[REDACTED]