BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of [redacted] Petitioner.	))))))	DOCKET NO. 1-204-184-064 DECISION

[redacted] (Petitioner) protested the Notice of Deficiency Determination (Notice) for tax year 2021 dated February 23, 2024. This protest was carried forward to a modified Notice dated May 2, 2024. The Tax Commission reviewed the matter and hereby issues its final decision to accept Petitioner's 2021 income tax return as filed.

Background

Petitioner filed federal and Idaho income tax returns for tax year 2021. In conjunction with a separate examination of Petitioner's 2019 and 2020 tax returns, the Tax Commission's Income Tax Audit Bureau (Audit) selected her 2021 return for review. Audit issued the Notice on February 23, 2024, after determining that Petitioner was not eligible to exclude from gross income the $306,000 reported gain from the sale of her California home because she was domiciled in Idaho. Audit also recalculated the gain using a lower basis than Petitioner claimed on her return, thereby significantly increasing her taxable income.

On March 28, 2024, Petitioner's attorney-in-fact (AIF) sent Audit an email providing copies of Petitioner's purchase and sales agreements for her California property, along with his calculation of the gain from the sale. On April 25, 2024, AIF formally protested the Notice via email. On May 2, 2024, Audit issued a modified Notice reducing the gain from the sale of the property but still disallowing the exclusion of the gain from gross income.

At AIF's request, Audit forwarded the matter to the Tax Commission's Appeals unit (Appeals). On July 2, 2024, Appeals sent Petitioner and AIF letters outlining the options available for redetermining a protested Notice. Neither AIF nor Petitioner requested an informal hearing, but additional information was provided. The Tax Commission now renders its decision based on available information.

Law & Analysis

The issue in this case is whether Petitioner is eligible to claim an exclusion of income, specifically the gain from the sale of a home, under Internal Revenue Code (IRC) section 121.

IRC section 121(a) states "Gross income shall not include gain from the sale or exchange of property if, during the 5-year period ending on the date of the sale or exchange, such property has been owned and used by the taxpayer as the taxpayer's principal residence for periods aggregating 2 years or more." The maximum amount that Petitioner would be able to exclude is $250,000[1]. There are requirements a taxpayer must meet to be eligible to claim the maximum exclusion:

- The property must not have been acquired through a like-kind exchange within five years of the sale date, and the taxpayer must not be subject to expatriate tax.
- The taxpayer must have owned the property for at least two of the five years immediately preceding the sale of the property.
- The taxpayer must have used the property as their residence for at least two years (24 months or 730 days) of the five years immediately preceding the sale of the property. This does not have to be a single block of consecutive time. Vacations and short absences count as time the taxpayer lived in the home.
- The taxpayer may not have excluded from income the gain from a property sale under IRC section 121 within two years immediately preceding the sale.

[1] IRC section 121 allows a maximum $250,000 exclusion unless a husband and wife filing a joint return meet the requirements for the exclusion. Then the maximum exclusion is $500,000.

In some instances where a taxpayer is not eligible to claim the maximum exclusion, they might be able to claim a partial exclusion.

AIF provided Audit with documentation showing that Petitioner purchased the property located at [redacted] California, on October 9, 2014, and sold it on April 5, 2021, confirming that the ownership requirement was met. Petitioner did not acquire the property through a like-kind exchange, is not subject to expatriate tax, and did not claim a section 121 exclusion between April 5, 2019, and April 5, 2021. The remaining question, therefore, is whether Petitioner used the California home as her "principal residence" for the required time.

At the same time that Petitioner owned the California property, she also owned the property located at [redacted] Idaho. In the Notice from the separate examination for tax years 2019 and 2020, Audit presented an analysis of primary and secondary factors and determined that Petitioner was domiciled in Idaho. Using this conclusion, Audit wrote in the Notice for tax year 2021, "your legal residence (domicile) has been established in Idaho since 2004 and remains unchanged up to the present date, establishing Idaho as your primary residence." Audit continued, "In 2021, you sold your California property and excluded the entire gain under section 121. Since this property is not your primary residence, it does not qualify for the exclusion."

Domicile refers to a person's true, fixed, permanent home. It is the place where a person intends to return to when they are absent. The terms domicile and residence are often used interchangeably in everyday speech, but for Idaho income tax purposes, they carry distinct meanings. Domicile refers to a general place or area where the person considers "home," whereas a "residence" is merely a dwelling place or place of abode. A person can have multiple residences but only one domicile. In Petitioner's case, she had a residence in California and a residence in Idaho. The Tax Commission agrees with Audit's determination that Petitioner was domiciled in

Idaho, and Petitioner's AIF withdrew the protest in the related case, indicating acceptance of that same conclusion.

It should be noted that IRC section 121 and related Treasury Regulations do not use the term "domicile." Instead, they refer to a person's "principal residence." Domicile is a state issue rather than a federal one. Since the section 121 exclusion is a federal issue, the Tax Commission disagrees with Audit's focus on Petitioner's domicile as the determination of her principal residence.

Analogous to a U.S. resident claiming the section 121 exclusion for a property located outside the country – neither IRC section 121 nor Treasury Regulations require a principal residence to be located in the U.S. – an Idaho resident should be allowed to claim the exclusion for a property located outside the state as long as all other requirements are met. As established earlier, the remaining question of qualification for the exclusion is that of Petitioner's use of the California property as her principal residence for at least two years (24 months, 730 days) in the five years leading up to the sale of the property. Since the sale of the property took place on April 5, 2021, we focus on the period from April 4, 2016, through April 4, 2021.

There are a multitude of factors that go into determining whether a residence is a person's principal residence, and the determination is based on all the facts and circumstances. Principal residence is not defined in IRC section 121, but guidance is provided in Treasury Regulation 1.121-1(b)(2):

> In the case of a taxpayer using more than one property as a residence, whether property is used by the taxpayer as the taxpayer's principal residence depends upon all the facts and circumstances. If a taxpayer alternates between 2 properties, using each as a residence for successive periods of time, the property that the taxpayer uses a majority of the time during the year ordinarily will be considered the taxpayer's principal residence. In addition to the taxpayer's use of the property, relevant factors in determining a taxpayer's principal residence, include, but are not limited to—

(i) The taxpayer's place of employment;
(ii) The principal place of abode of the taxpayer's family members;
(iii) The address listed on the taxpayer's federal and state tax returns, driver's license, automobile registration, and voter registration card;
(iv) The taxpayer's mailing address for bills and correspondence;
(v) The location of the taxpayer's banks; and
(vi) The location of religious organizations and recreational clubs with which the taxpayer is affiliated.

These secondary factors are similar to those used in determining a person's domicile. Some point towards Idaho and others point to California. Petitioner's employment was based in the San Francisco Bay area. Her minor children attended school and engaged in sports and clubs (like 4H and rowing) in California. According to a written statement from her daughter, Petitioner was a very present and active part of her children's lives, attending teacher conferences, sporting events, concerts, etc., driving to rowing practice six days each week, carpooling teammates to practices, driving to doctor's appointments, participating in fundraisers and fairs, attending monthly 4H meetings and helping with projects. Petitioner maintained an Idaho driver's license, never seeing the necessity to obtain a California license. She registered vehicles in Idaho because she had an Idaho property. She also had at least one vehicle in California. Her banks had locations in multiple states, including both California and Idaho. She was a member of athletic clubs in both states. She had multiple doctors in California, but her dentist was in Idaho.

As stated prior, domicile and residence are separate concepts, and the Tax Commission must focus on determining whether Petitioner used her California home as her *principal* residence for at least two of the five years leading up to the sale of the property. Since the secondary factors are not indicative of only one property being her principal residence, time must be the determining factor and definitive evidence is needed.

Petitioner provided statements for multiple credit and bank cards for 2016 through 2021. Statements for November and December 2016 were not included, but all other months between

April 2016 and April 2021 were represented. The Tax Commission analyzed these documents to estimate a pattern of where Petitioner was residing throughout the five years leading up to the sale of the California property. Three categories were established. Days on which purchases were made only in California fell into the first category ("in California"). Likewise, days on which purchases were made only in Idaho fell into the second category ("in Idaho"). Days on which purchases were made in both states or in neither state fell into the third category ("unsure").

The IRS provides guidance in Publication 523, *Selling Your Home*: "If you were ever away from home, you need to determine whether that time counts toward your residence requirement. A vacation or other short absence counts as time you lived at home." Any "unsure" days that were bounded on both ends by one state or the other were included in that state's classification. Therefore, if Petitioner left from California on a trip to Detroit, then returned to California (as evidenced by purchases made via credit or bank card), those days in Detroit were credited as time residing in California. The same applies to leaving from and returning to Idaho. However, if Petitioner left from California and arrived back in Idaho, or vice versa, those days were not counted as residence in either state; they maintained their "unsure" classification. Using this system, the Tax Commission created a calendar to track Petitioner's residency. Since the requirement involves the five years immediately preceding the sale of the property, each "year" began on April 5 and ended on April 4. The findings are presented below:

	4/5/16-4/4/17	4/5/17-4/4/18	4/5/18-4/4/19	4/5/19-4/4/20	4/5/20-4/4/21	Totals
In California	167	189	129	217	80	782
In Idaho	126	156	217	130	275	904
Unsure	72	20	19	19	10	140
	365	365	365	366	365	1826

For a "majority of time" during the year to occur, Petitioner must have spent a minimum of 183 days in a given year (184 for the year including February 29, 2020) in a specified state.

Based on the Tax Commission's analysis, Petitioner met that requirement for two of the year-long timeframes outlined above. The IRS requires 730 days of using a home as a principal residence for eligibility for the section 121 exclusion. Petitioner met this requirement with at least 782 days with the California property as her principal residence. That total could be as high as 922. Therefore, the Tax Commission determined that Petitioner met all the requirements to claim the section 121 exclusion.

On her return, Petitioner reported a gain of $306,000 and claimed the section 121 exclusion on the full amount. This exceeds the $250,000 maximum exclusion available for an individual filing as Head of Household. AIF provided Audit with documentation showing that Petitioner purchased the California property for $742,000 and sold it for $1,048,000 with selling costs of $61,981. In the modified Notice, Audit determined the gain from the sale of the property was $244,019[2]. The Tax Commission determined that this calculation is accurate based on the documents provided. As this gain is below the maximum allowable exclusion for a taxpayer in Petitioner's circumstances, the full amount of the gain is excluded from gross income. The net result is the same; Petitioner does not have to include any gain from the sale of the California property in taxable income for 2021.

Conclusion

Petitioner met all the eligibility requirements to exclude from gross income the gain from the sale of her California property in 2021. Her gain on the sale was $244,019. She is eligible to exclude up to $250,000, so none of the gain is taxable.

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[2] $1,048,000 selling price minus $742,000 purchase price minus $61,981 selling costs.

THEREFORE, the adjustments in the Notice dated February 23, 2024, and the modified Notice dated May 2, 2024, directed to [redacted] are unwarranted and Petitioner's return for tax year 2021 is accepted as filed.

An explanation of Petitioner's 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:

[redacted]

Receipt No.

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