

05-1355
Individual Income Tax
Signed 03/20/2007

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER,)		
	)	ORDER	
Petitioner,)		
	)	Appeal No.	05-1355
v.)		
	)	Tax Type:	Individual Income Tax
AUDITING DIVISION OF THE	)	Account No:	#####
UTAH STATE TAX COMMISSION,	)	Tax Year:	2002 & 2003
)		
Respondent.	)	Judge:	Jensen

Presiding:
Clinton Jensen, Administrative Law Judge

Appearances:
For Petitioner: PETITIONER REPRESENTATIVE, C.P.A.
For Respondent: RESPONDENT REPRESENTATIVE 1, Assistant Attorney General
RESPONDENT REPRESENTATIVE 2, from the Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for an Initial Hearing pursuant to the provisions of Utah Code Ann. §59-1-502.5, on May 23, 2006.

On September 19, 2005, Auditing Division (“Division”) issued Statutory Notices of Audit Change (“Statutory Notices”) to the Petitioner, imposing additional Utah income tax for the 2002 and 2003 tax years. The Division imposed \$\$\$\$ in additional tax for the 2002 tax year, plus interest, and \$\$\$\$ in additional tax for the 2003 tax year, plus interest. The Division did not impose any penalties.

For tax years 2002 and 2003, the Petitioner claimed equitable adjustments to offset taxes paid by the (X)Trust to the state of STATE. The Petitioner is both a trustee and beneficiary of this trust.¹ The

¹ The other trustee and beneficiary of the trust is the Petitioner’s sister, (X). (X) has also filed an appeal with the Utah Tax Commission which is pending as appeal number 05-1428. Because both cases deal with the same trust and the same issues, the parties requested a simultaneous briefing and argument of both cases. The Commission agreed and heard the cases at the same

Petitioner explained that all of the trust's assets are located in STATE. The trust assets generate income, which STATE taxes as part of the trust's STATE Fiduciary Income Tax Return. Because the trust is not a Utah resident and has no Utah income, the trust does not file a Utah return and does not pay Utah state taxes. STATE does not then tax distributions to individuals from the trust because the trust income has already been taxed. Utah, on the other hand, does not tax trust income but does tax income to individuals when the trust makes distributions.

The Petitioner is a resident of Utah and files Utah resident tax returns. In 2002 and 2003 the trust made distributions to the Petitioner, which, according to Utah rules, counts as income subject to Utah state income tax. The Petitioner found this to be double taxation on the same income, since the (X) Trust had already paid STATE state tax on the trust's income. On this basis, the Petitioner made an equitable adjustment to remove the income from the Utah resident tax return for the Petitioner.

The Respondent's position is that the distribution from the trust to the Petitioner is income to a Utah resident. While STATE may have levied tax on the trust, the circumstances of STATES tax policies do not meet Utah's requirements for an equitable adjustment.

APPLICABLE LAW

Under Utah Code Ann. §59-10-104(1), "a tax is imposed on the state taxable income . . . of every **resident individual**" (emphasis added). "State taxable income" is defined in UCA §59-10-112 to mean "in the case of a resident individual means his federal taxable income (as defined by §59-10-111) with the modifications, subtractions, and adjustments provided in §59-10-114 . . ."

Equitable Adjustments. For the 2002 and 2003 tax years, UCA §59-10-115 specifically provided that a taxpayer could claim an equitable adjustment where: 1) an item of gross income in the

time. Although the cases involve different parties and cannot technically be consolidated, the decisions for these cases are issued at the same time and are, with minor exceptions, alike.

Appeal No. 05-1355

taxpayer's current year federal adjusted gross income was taxed by a state in a prior year; 2) the taxpayer reports certain gains or losses associated with the ownership of property; or 3) the taxpayer receives certain distributions from an electing small business corporation. In addition, Subsection 59-10-115(4) provided that the Commission could specify in rule other circumstances allowing for equitable adjustment, as follows in pertinent part:

The commission shall by rule prescribe for adjustments to state taxable income of the taxpayer in circumstances other than those specified by Subsection (1), (2), and (3) of this section where, solely by reason of the enactment of this chapter, the taxpayer would otherwise receive or have received a double tax benefit or suffer or have suffered a double tax detriment. . . .

The Commission adopted Utah Administrative Rule R865-9I-4 to address other amounts of income that may qualify as an equitable adjustment to Utah taxable income, as follows:

A. Every taxpayer shall report and the Tax Commission shall make or allow such adjustments to the taxpayer's state taxable income as are necessary to prevent the inclusion or deduction for a second time on his Utah income tax return of items involved in determining his federal taxable income. Such adjustments shall be made or allowed in an equitable manner as defined in Utah Code Ann. 59-10-115 or as determined by the Tax Commission consistent with provisions of the Individual Income Tax Act.

B. In computing the Utah portion of a nonresident's federal adjusted gross income; any capital losses, net long-term capital gains, and net operating losses shall be included only to the extent that these items were not taken into account in computing the taxable income of the taxpayer for state income tax purposes for any taxable year prior to January 2, 1973.

Credit for Taxes Paid to Another State. During the tax years at issue, UCA §59-10-106(1) provides that a credit may be allowed against a person's Utah tax liability for taxes paid to another governmental entity, as follows:

A resident individual shall be allowed a credit against the tax otherwise due under this chapter equal to the amount of the tax imposed on him for the taxable year by another state of the United States, the District of Columbia, or a possession of the United States, on income derived from sources therein which is also subject to tax under this chapter.

DISCUSSION

The parties generally agree that the Petitioner's request for equitable adjustment does not flow from one of the first three sections of Utah Code Ann. §59-10-115. Subsection 1 refers to taxes paid in a prior year, not taxes paid to another state. Subsection 2 makes reference to situations in which Utah law is different from federal law with reference to calculation of income. Here, STATE law is different from Utah law and federal law but Utah law calculates this income in the same manner as federal law. Subsection 3 refers to corporate distributions and is silent with regard to trusts. Thus, if Utah law allows an equitable adjustment in this case, the authority for that adjustment will come under subsection 4 of Utah Code Ann. §59-10-115. The parties appropriately refer to subsection 4 as a catchall section because, by definition, it refers to reasons for an equitable adjustment in circumstances other than those specified in subsections 1, 2, and 3 of Utah Code Ann. § 59-10-115.

Although subsection 4 of Utah Code Ann. §59-10-115 grants some discretion to the Commission in making equitable adjustments, the legislature has placed limits on the discretion granted the Commission. Among other criteria, if the Commission is going to provide for an equitable adjustment, it must make provision for the adjustment "by rule." Unless the Commission has prepared a rule allowing for an equitable adjustment, it has no authority to allow the adjustment. Although the Commission has authority to promulgate rules that provide for an "equitable adjustment" to Utah taxable income under certain circumstances, the taxation of trust income by another state is not one of the circumstances listed in Utah Administrative Rule R865-9I-4. Accordingly, there is no basis to support an equitable adjustment in this manner. Because the Tax Commission has no rule allowing for equitable adjustment under these circumstances, it has no authority to approve an equitable adjustment in connection with this appeal.²

² For more current tax years, the Commission directs the parties to Utah Code Ann. §59-10-210 which became effective May 1, 2006.

Appeal No. 05-1355

DECISION AND ORDER

Based upon the foregoing, the Commission finds the income that the (X) Trust Petitioner earned during the 2002 and 2003 tax years and that was taxable in STATE is also subject to Utah taxation when it is distributed to Utah residents. On this basis, the Commission denies the Petitioner's appeal and sustains the Division's assessments of tax for the 2002 and 2003 tax years. It is so ordered.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission
Appeals Division
210 North 1950 West
Salt Lake City, Utah 84134

Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this _____ day of _____, 2006.

Clinton Jensen
Administrative Law Judge

Appeal No. 05-1355

BY ORDER OF THE UTAH STATE TAX COMMISSION.

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this _____ day of _____, 2006.

Pam Hendrickson
Commission Chair

R. Bruce Johnson
Commissioner

Marc B. Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

Notice: If a Formal Hearing is not requested as discussed above, failure to pay any remaining balance resulting from this order within thirty (30) days from the date of this order may result in a late payment penalty.

CJ/05-1355.int