

12-2275

TAX TYPE: INCOME

TAX YEAR: 2006

DATE SIGNED: 8-29-13

COMMISSIONERS: B. JOHNSON, D. DIXON, M. CRAGUN, R. PERO

GUIDING DECISION

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BEFORE THE UTAH STATE TAX COMMISSION

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TAXPAYER

Petitioner,

v.

AUDITING DIVISION OF THE  
UTAH STATE TAX COMMISSION,

Respondent.

**INITIAL HEARING ORDER**

Appeal No. 12-2275

Account No. #####

Tax Type: Income Tax

Tax Year: 2006

Judge: Phan

**Presiding:**

Jane Phan, Administrative Judge

**Appearances:**

For Petitioner: PETITIONER REP., Representative By Telephone  
TAXPAYER, By Telephone

For Respondent: RESPONDENT REPRESENTATIVE-1, Manager, Income Tax Auditing  
RESPONDENT REPRESENTATIVE-2, Senior Auditor

STATEMENT OF THE CASE

This matter came before the Commission for an Initial Hearing in accordance with Utah Code §59-1-502.5, on June 3, 2013. Petitioner (“Taxpayer”) is appealing a Utah Individual Income Tax audit deficiency. The Notice of Deficiency and Estimated Income Tax was issued on August 14, 2012, indicating a deficiency for tax year 2006 in the amount of \$\$\$\$ in additional tax, \$\$\$\$ in penalties and \$\$\$\$ in interest as of the date of the notice.

APPLICABLE LAW

Except as provided in Subsection (3), a tax is imposed on a nonresident individual in an amount equal to the product of the nonresident individual’s (a) unapportioned state tax; and (b) state income tax percentage. (Utah Code §59-10-116(2).(2006))<sup>1</sup>

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<sup>1</sup> The Commission applies the substantive legal provisions in affect during

A nonresident partner's distributive share of partnership income, gain, loss, and deduction derived from or connected with Utah sources shall be determined under Section 59-1-303. (Utah Code §59-10-117(2)(g)(2006).)

In determining the adjusted gross income of a nonresident partner of any partnership, there shall be included only that part derived from or connected with sources in this state of the partner's distributive share of items of partnership income, gain, loss, and deduction entering into his federal adjusted gross income, as such part is determined under rules prescribed by the commission in accordance with the general rules in Section 59-10-116. (Utah Code §59-10-303(1)(2006).)

- (1) Every partnership having a nonresident partner and income derived from sources in this state shall file a return in accordance with forms and instructions provided by the Tax Commission.
- (2) If the partnership has income derived from or connected with sources both inside and outside Utah and if any partner was not a resident of Utah, the portion derived from or connected with sources in this state must be determined and shown.
  - (a) The Utah portion must be determined and shown for each item of the partnership's, and each nonresident partner's, distributive shares of income, credits, deductions, etc., shown on Schedules K and K-1 of the federal return.
  - (b) The Utah portion may be shown: (i) alongside the total for each item on the federal schedules K and K-1; or (ii) on an attachment to the Utah return.  
 . . . (Utah Admin. Rule R865-9I-21.)

Utah Code §59-1-1417 provides, “[i]n a proceeding before the commission, the burden of proof is on the petitioner...”

Upon making a record of its actions, and upon reasonable cause shown, the commission may waive, reduce, or compromise any of the penalties or interest imposed under this part. (Utah Code 59-1-401(13).)

#### DISCUSSION

Taxpayer was a resident of STATE prior to 2006 and continuing to the present time. He had a partnership interest in COMPANY, and during the 2006 tax year the partnership experienced a long term capital gain which the Taxpayer represents was from the exchange of real property owned by the partnership in STATE. During 2006 the partnership had exchanged ##### acres of land in STATE for a residence in STATE-2, another ##### acre STATE property, property in CITY, Utah, a PROPERTY and

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the 2006 tax year. The Utah Code has had some revisions subsequent to the audit period.

\$\$\$\$\$ in cash. It was the \$\$\$\$\$ that was the gain from the transaction to the COMPANY. The Taxpayer states that he had claimed his portion of the gain on his federal return and had filed his STATE resident return as he always did, claiming on that return his portion of the gain from the sale. Because he was a resident of STATE and the property that was sold had been located in STATE, the Taxpayer and his representative had no idea that the Taxpayer would have a requirement to file a Utah nonresident return and report a portion of this gain to Utah. As the 2006 tax year was not audited until 2012, it was too late for the Taxpayer to request a refund of taxes paid on this gain to STATE.

The COMPANY had filed a Utah COMPANY PARTNERSHIP return for the 2006 tax year. On the return they reported total income of \$\$\$\$\$ which was computed from the long term capital gain from the property exchange, minus a small real estate loss of \$\$\$\$\$. The return reported an apportionment fraction of %%% as Utah income. Therefore \$\$\$\$\$ of the total income was reported as Utah Income. Of this amount the return reported %%% to the Taxpayer.

The Division's audit was based on the income reported as a gain to TAXPAYER as was apportioned to Utah by the COMPANY on the COMPANY PARTNERSHIP return. The Division noted that the COMPANY was a registered Utah COMPANY PARTNERSHIP. The Division argued that the gain was received from the sale of investments and as such the proceeds would be taxed to the COMPANY PARTNERSHIP domicile and not to where the property had been located. The Division also noted that the address for the COMPANY was in Utah and the COMPANY PARTNERSHIP tax preparer was in Utah. The Division had indicated if the COMPANY filed an amended return or if the Taxpayer were to provide evidence that the COMPANY PARTNERSHIP filing was in error, that the gain should have been reported by the COMPANY to STATE instead of Utah, the Division might consider that information. However, in the absence of such evidence showing that the COMPANY PARTNERSHIP original filing had the wrong apportionment factors, requested that the audit stand.

The Taxpayer explained that he had owned the ##### acres. When the COMPANY PARTNERSHIP had been set up, it was done by the Utah partner. The Taxpayer put in the land and the Utah partner put in legal services for the COMPANY PARTNERSHIP and exchange. The Taxpayer's representative indicated that he did talk to the Utah partner about possibly amending the COMPANY PARTNERSHIP return, but was unsure if anything further had been done by the COMPANY PARTNERSHIP and did not point to anything in Utah statute or case law to support that the COMPANY PARTNERSHIP original return was erroneous.

Upon review of the facts and the law in this matter, the Division's audit appears consistent with the COMPANY PARTNERSHIP return that reported Utah source income as being paid to the Taxpayer during the 2006 tax year. Had the Taxpayer owned the ##### acre STATE property outright in his own name and sold it outright, the gain would have been taxable to STATE. However, by placing the property

into a Utah COMPANY PARTNERSHIP, there are tax consequences and the COMPANY PARTNERSHIP reported %%% of the gain as its apportionment fraction taxable to Utah. The Taxpayer had not shown that this fraction was wrong.

Penalties for failure to file a Utah return and failure to pay taxes had been assessed with the audit. The Division did note at the hearing that this would have been a first time filing in Utah for the Taxpayer. This is an unfortunate circumstance where the Division had not issued the audit until after the expiration of the Statute of Limitations for refund in STATE. The Taxpayer has paid tax on this income to STATE and with this audit will have to pay taxes again to Utah. There is reasonable cause for waiver of the penalties under Utah Code Sec. 59-1-401(13). However, based on the law and information submitted at the hearing, the audit assessment of tax and interest should be upheld.

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Jane Phan  
Administrative Law Judge

DECISION AND ORDER

Based on the foregoing, the Commission sustains the audit deficiency pertaining to the additional tax and interest for the 2006 tax year. The Commission waives the penalties assessed with the audit. 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 \_\_\_\_\_, 2013.

R. Bruce Johnson  
Commission Chair

D'Arcy Dixon Pignanelli  
Commissioner

Appeal No. 12-2275

Michael J. Cragun  
Commissioner

Robert P. Pero  
Commissioner