

APPEAL # 22-1486  
TAX TYPE: INDIVIDUAL INCOME TAX  
TAX YEAR: 2018  
DATE SIGNED: 3/12/2024  
COMMISSIONERS: J.VALENTINE, M.CRAGUN, R.ROCKWELL, AND J.FRESQUES

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BEFORE THE UTAH STATE TAX COMMISSION

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<p>TAXPAYER,</p> <p style="text-align: center;">Petitioner,</p> <p>v.</p> <p>INCOME TAX AND EDUCATION DIVISION OF THE UTAH STATE TAX COMMISSION,</p> <p style="text-align: center;">Respondent.</p>	<p><b>INITIAL HEARING ORDER</b></p> <p>Appeal No. 22-1486</p> <p>Account No: #####</p> <p>Tax Type: Individual Income Tax</p> <p>Tax Year: 2018</p> <p>Judge: Phan</p>
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**Presiding:**

Jane Phan, Administrative Law Judge

**Appearances:**

For Petitioner: PETITIONER'S REP-1, CPA  
TAXPAYER

For Respondent: RESPONDENT'S REP-1, Audit Manager

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission on November 20, 2023 for an Initial Hearing in accordance with Utah Code Ann. §59-1-502.5. Petitioner (“Taxpayer”) timely appealed the Respondent’s (“Division”) individual income tax audit for the 2018 tax year pursuant to Utah Code §59-1-501. The Division issued an audit deficiency of \$\$\$\$ in tax, and interest of \$\$\$\$ through September 2, 2022. Interest continues to accrue on any unpaid balance. No penalties were assessed with the audit. The Taxpayer had filed a Utah individual income tax return for tax year 2018. The only change made by the Division in the audit to the income tax return filed by the Taxpayer was to disallow an equitable adjustment in the amount of \$\$\$\$.

APPLICABLE LAW

State tax is imposed on a Utah resident individual pursuant to Utah Code §59-10-104, as follows:<sup>1</sup>

- (1) A tax is imposed on the state taxable income of a resident individual as provided in this section.
- (2) For purposes of Subsection (1), for a taxable year, the tax is an amount equal to the product of: (a) the resident individual's state taxable income for that taxable year; and (b) 4.95%.

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Utah Code Ann. §59-10-103 defines “adjusted gross income,” “federal taxable income,” and “taxable income” or “state taxable income,” as follows:

- (1) As used in this chapter:
  - (a) "Adjusted gross income":
    - (i) for a resident or nonresident individual, is as defined in Section 62, Internal Revenue Code; or
  - .....
  - (f) “Federal taxable income”:
    - (i) for a resident or nonresident individual, means taxable income as defined by Section 63, Internal Revenue Code; or
  - .....
  - (w) "Taxable income" or "state taxable income":
    - (i) subject to Section 59-10-1404.5, for a resident individual, means the resident individual's adjusted gross income after making the:
      - (A) additions and subtractions required by Section 59-10-114; and
      - (B) adjustments required by Section 59-10-115;
  - .....

“Adjusted gross income” is defined in Internal Revenue Code (“IRC”) §62, in pertinent part, to mean “in the case of an individual, gross income minus the following deductions[.]”

Utah Code §59-10-114 provides the following additions and subtractions to a resident individual’s adjusted gross income as follows:

- (1) There shall be added to adjusted gross income of a resident or nonresident individual:
  - (a) a lump sum distribution that the taxpayer does not include in adjusted gross income on the taxpayer's federal individual income tax return for the taxable year;
  - (b) the amount of a child's income calculated under Subsection (4) that:
    - (i) a parent elects to report on the parent's federal individual income tax return for the taxable year; and
    - (ii) the parent does not include in adjusted gross income on the parent's federal individual income tax return for the taxable year;
  - (c) (i) a withdrawal from a medical care savings account . . .

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<sup>1</sup> All substantive law citations are to the 2018 version of Utah law, unless otherwise noted.

- (d) the amount withdrawn under Title 53B, Chapter 8a, Utah Educational Savings Plan . . .
- (e) except as provided in Subsection (5), for bonds, notes, and other evidences of indebtedness acquired on or after January 1, 2003, the interest from bonds, notes, and other evidences of indebtedness:
  - (i) issued by one or more of the following entities: (A) a state other than this state; (B) the District of Columbia; (C) a political subdivision of a state other than this state; or (D) an agency or instrumentality of an entity described in Subsections (1)(e)(i)(A) through (C); and
  - (ii) to the extent the interest is not included in adjusted gross income on the taxpayer's federal income tax return for the taxable year;
- (f) subject to Subsection (2)(c), any distribution received by a resident beneficiary of a resident trust of income that was taxed at the trust level for federal tax purposes, but was subtracted from state taxable income of the trust pursuant to Subsection 59-10-202(2)(b);
- (g) any distribution received by a resident beneficiary of a nonresident trust of undistributed distributable net income realized by the trust on or after January 1, 2004, if that undistributed distributable net income was taxed at the trust level for federal tax purposes, but was not taxed at the trust level by any state, with undistributed distributable net income considered to be distributed from the most recently accumulated undistributed distributable net income; and
- (h) any adoption expense . . . .

(2) There shall be subtracted from adjusted gross income of a resident or nonresident individual:

- (a) the difference between:
  - (i) the interest or a dividend on an obligation or security of the United States or an authority, commission, instrumentality, or possession of the United States, to the extent that interest or dividend is: (A) included in adjusted gross income for federal income tax purposes for the taxable year; and (B) exempt from state income taxes under the laws of the United States; and
  - (ii) any interest on indebtedness incurred or continued to purchase or carry the obligation or security described in Subsection (2)(a)(i);
- (b) for taxable years beginning on or after January 1, 2000, if the conditions of Subsection (3)(a) are met, the amount of income derived by a Ute tribal member . . . .
- (c) an amount received by a resident or nonresident individual or distribution received by a resident or nonresident beneficiary of a resident trust:
  - (i) if that amount or distribution constitutes a refund of taxes imposed by: (A) a state; or (B) the District of Columbia; and
  - (ii) to the extent that amount or distribution is included in adjusted gross income for that taxable year on the federal individual income tax return of the resident or nonresident individual or resident or nonresident beneficiary of a resident trust;
- (d) the amount of a railroad retirement benefit . . .
- (e) an amount:
  - (i) received by an enrolled member of an American Indian tribe . . .
- (f) an amount received:
  - (i) for the interest on a bond, note, or other obligation issued by an entity for which state statute provides an exemption of interest on its bonds from state individual income tax;
  - (ii) by a resident or nonresident individual;

- (iii) for the taxable year; and
- (iv) to the extent the amount is included in adjusted gross income on the taxpayer's federal income tax return for the taxable year; and
- (g) the amount of all income, including income apportioned to another state, of a nonmilitary spouse of an active duty military member . . .

Utah Code Ann. §59-10-115 provides for an equitable adjustment to Utah taxable income, as follows in pertinent part:

- (1) As used in this section:
  - (a) "Net foreign source taxable income" means:
    - (i) the amount calculated on line 17 of Internal Revenue Code Form 1116, Foreign Tax Credit; or
    - (ii) if, for purposes of federal individual income taxes, the amount calculated on line 17 of Form 1116 is reported on a line other than line 17 of Form 1116, the amount on a line of a federal individual income tax form designated by the commission as being substantially similar to line 17 of the 2015 version of Form 1116.
  - (b) "Pass-through entity taxpayer" means the same as that term is defined in Section 59-10-1402.
- (2) The commission shall allow an adjustment to adjusted gross income of a resident or nonresident individual if the resident or nonresident individual would otherwise:
  - (a) receive a double tax benefit under this part; or
  - (b) suffer a double tax detriment under this part.
- (3) (a) For a pass-through entity taxpayer generating taxable income primarily from establishments classified in Code Section 33242, Metal Tank (Heavy Gauge) Manufacturing, of the 2002 or 2007 North American Industry Classification System of the federal Executive Office of the President, Office of Management and Budget, an adjustment described in Subsection (2) includes net foreign source taxable income generated from Metal Tank (Heavy Gauge) Manufacturing establishments.
  - (b) The adjustment described in Subsection (3)(a) applies to a taxable year beginning on or after January 1, 2017.

For corporate taxpayers Utah Code §59-7-106(1)(k) provides an adjustment for certain income as follows:

- (k) subject to Subsection (3), 50% of a dividend considered to be received or received from a subsidiary that:
  - (i) is a member of the unitary group;
  - (ii) is organized or incorporated outside of the United States; and
  - (iii) is not included in a combined report under Section 59-7-402 or 59-7-403;

Utah Code Ann. §59-1-1417(1) addresses burden of proof and statutory construction, as follows:

- (1) In a proceeding before the commission, the burden of proof is on the petitioner . . .

- (2) Regardless of whether a taxpayer has paid or remitted a tax, fee, or charge, the commission or a court considering a case involving the tax, fee, or charge shall:
  - (a) construe a statute imposing the tax, fee, or charge strictly in favor of the taxpayer; and
  - (b) construe a statute providing an exemption from or credit against the tax, fee, or charge strictly against the taxpayer.

### DISCUSSION

The Taxpayer was a Utah resident individual for purposes of Utah Code §59-10-104, and had filed a Utah individual income tax return for the 2018 tax year. On his return, the Taxpayer claimed an equitable adjustment in the amount of \$\$\$\$\$. The Division later audited the Taxpayer's 2018 Utah individual income tax return and denied the equitable adjustment. At the hearing, the Division's representative explained that Utah Code §59-10-115 allows for an equitable adjustment to gross income if the individual suffers a double tax detriment "under this part." The Division's representative stated that "under this part" referred to the Individual Income Tax Act. The Division's representative stated that there had been no double tax detriment under the Individual Income Tax Act. Therefore, the Division disallowed the equitable adjustment, resulting in the audit tax deficiency. There were no other audit adjustments for 2018.

At the hearing, the Taxpayer and his representative acknowledged that there had not been a double tax determinant under the Utah Individual Income Tax Act. The Taxpayer's representative explained that they had made the equitable adjustment claim on the Utah Individual Income Tax Return because there was no other place on the Utah Individual Income Tax Return to make the same type of adjustment that is allowed on a Utah corporate tax return under Utah Code § 59-7-106(1)(k). At the hearing, the Taxpayer's representative explained that on the Taxpayer's 2018 federal return he was required to report Sec. 965 foreign income from the Taxpayer's Utah S-Corporation, BUSINESS-1. The Taxpayer was the 100% owner of BUSINESS-1, so the total Sec. 965 income was reported on the Taxpayer's federal Individual Income Tax Return on Line 21-Other income. Line 21 of the Taxpayer's 2018 federal return reported Sec. 965 income in the amount of \$\$\$\$\$. One-half of this amount is \$\$\$\$\$, which was the amount the Taxpayer had deducted on his federal return. Line 21 on the federal form is included in Line 22 -Total Income and the Taxpayer's total income claimed on his 2018 return on that line was \$\$\$\$\$. Total income is subject to some adjustments in calculating the Taxpayer's federal adjusted gross income, which the Taxpayer reported on Line 31 of his 2018 federal return as \$\$\$\$\$. Thus, the Sec. 965 income is part of the Taxpayer's federal adjusted gross income as claimed by the Taxpayer on his 2018 federal individual income tax return. The Taxpayer's

representative explained that federal tax law allows taxpayers a “break” on this tax. He pointed to Line 44 of the federal return, where -\$\$\$\$ was listed as 965 tax and was subtracted from the tax amount.

The Taxpayer’s representative pointed out that Utah and other states also allow a subtraction for this income on C-corporation returns. He stated that based on Utah Code § 59-7-106(1)(k), a C-corporation would file a TC-20R and receive a 50% subtraction. However, as BUSINESS-1. was a pass-through entity and not a C-corporation, there was no equivalent subtraction provided under Title 59, Chapter 10, Individual Income Tax Act. The Taxpayer’s representative argued that a taxpayer that files an individual income tax return should be treated the same as a corporation, but did not cite any Utah statute, Tax Commission administrative rule, Tax Commission decision or case law that allowed this adjustment on an individual income tax return, or that supported the position that a taxpayer that files an individual income tax return is allowed the same tax treatment as a C-corporation. The Taxpayer’s representative did not present a hearing brief or a written explanation regarding its arguments in this matter. The Taxpayer’s representative stated at the hearing that this income was problematic for the Taxpayer because the federal 965 income was not necessarily received by the Taxpayer, instead “it is pushed forward and may never be received.”

At the hearing, the representative for the Division stated that there was no factual dispute, and he could not find any statutes that provided the 50% subtraction allowed on a corporate income tax return to be allowed on an individual income tax return. He pointed out that for individual income tax purposes, Utah taxable income is based on the federal adjusted gross income. The Sec. 965 income was included in the Taxpayer’s federal adjusted gross income. The Division’s representative also pointed out that the subtraction allowed under Utah Code §59-7-106(1)(k) was from unadjusted income and there was a difference between how the corporate income tax and the individual income tax was derived.

The Commission reviews the information provided by the parties and the applicable law. The Commission affirms that the equitable adjustment in the amount of \$145,111 was improper and the Division’s denial of this equitable adjustment is consistent with Utah law. Utah Code §59-10-104 and §59-10-103(1) impose a tax on a resident individual’s state taxable income, which is based on the individual’s federal “adjusted gross income.” There was no dispute that the Sec. 965 income was included in the Taxpayer’s 2018 federal adjusted gross income. Utah Code §59-10-114 provides a number of specific additions to or subtractions from federal adjusted gross income, none of which are relevant in this situation. Neither of the parties could point to any statute, administrative rule or case law that allows Sec. 965 foreign income to be subtracted from

federal adjusted gross income. Therefore, the Sec. 965 foreign income is included in federal adjusted gross income for the purpose of determining the Taxpayer's Utah individual income tax. Utah law does provide an equitable adjustment under Utah Code §59-10-115(2) to federal adjusted gross income "if the resident or nonresident individual would otherwise: (a) receive a double tax benefit under *this part*; or (b) suffer a double tax detriment under *this part* (emphasis added)." As the Tax Commission has concluded in many prior appeal decisions and the Utah Supreme Court affirmed in *Steiner v. Utah State Tax Comm'n*, 2019 UT 47, "this part" refers to Title 59, Chapter 10, Part 1, which is a part of the Utah Code within the Individual Income Tax Act.<sup>2</sup> The Taxpayer's representative acknowledges that the Taxpayer did not suffer a double tax detriment and thus did not meet the statutory criteria of Utah Code §59-10-115 to be allowed an equitable adjustment in this matter. The Taxpayer was only paying tax one time to the state of Utah on the Sec. 965 income for 2018. The Taxpayer stated that at some point the income may be realized and speculated that the Taxpayer might then be required to claim the income again. However, those are not the facts in 2018. In 2018, the Taxpayer was required to report this Sec. 965 income on his federal individual income tax return and this income was included in his federal adjusted gross income for tax year 2018.

Although the Taxpayer recognized that the deduction he made for his Sec. 965 income was not properly an equitable adjustment, the Taxpayer's representative argued at the hearing that the Taxpayer should be given the same tax benefit as is given to a C-corporation in Utah. The Taxpayer cited no legal authority for this assertion. As the Utah Supreme Court noted in *Steiner v. Utah State Tax Comm'n*, 2019 UT 47, ¶48, "Thus despite the Court's insistence that individuals are entitled to be treated no "less favorably" than corporations under the Dormant Commerce Clause, it is clear that they can be treated differently. Crucial distinctions between individuals and corporations continue to exist as a doctrinal matter." There is simply no basis for the Taxpayer's position that he should be able to subtract his Sec. 965 foreign income as is statutorily provided to a C-corporation taxpayer.

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<sup>2</sup> See also *Utah State Tax Commission Findings of Fact, Conclusions of Law and Final Decision, Appeal No. 08-0590* (August 5, 2010); *Utah State Tax Commission Order, Appeal No. 05-1787* (September 5, 2006); *Utah State Tax Commission Initial Hearing Order, Appeal No. 12-915* (April 15, 2014); *Utah State Tax Commission Findings of Fact, Conclusions of Law, and Final Decision, Appeal No. 14-374* (November 11, 2015); and *Utah State Tax Commission Initial Hearing Order Appeal No. 15-1332* (June 27, 2016). These and other decisions issued by the Utah State Tax Commission are available for review in a redacted format at [tax.utah.gov/commission-office/decisions](http://tax.utah.gov/commission-office/decisions).

The Taxpayer's appeal of the tax year 2018 audit deficiency should be denied.

Jane Phan  
Administrative Law Judge

**DECISION AND ORDER**

Based on the foregoing, the Commission finds that the Division's disallowance of the Taxpayer's claimed equitable adjustment for tax year 2018 was proper. The Commission sustains the Division's audit deficiency of income tax and interest for tax year 2018. 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, or emailed, 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

or emailed to:

taxappeals@utah.gov

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

DATED this \_\_\_\_ day of \_\_\_\_\_, 2024.

John L. Valentine  
Commission Chair

Michael J. Cragun  
Commissioner

Rebecca L. Rockwell  
Commissioner

Jennifer N. Fresques  
Commissioner

**Notice of Payment Requirement: Any balance due as a result of this order must be paid within thirty (30) days of the date of this order, or a late payment penalty could be applied.**