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September 8, 2010

**To: Office of the Attorney General, Attention Lawrence Wasden and Steve Olsen
Via Email**

Re: Tax Commission Investigation; Possible Violation of Criminal Statutes

Dear General Wasden and Mr. Olsen:

I am getting the impression that there is an intent to “stonewall” this inquiry and not cooperate with us in the establishment of an independent Investigative Panel in the public interest.

It appears to me that there is a strong possibility that the conduct which has been reported by the eight present and former auditors discloses actual criminal activity by way of appropriation of public funds in violation of the Idaho Statutes and the Constitution.

I am providing you with the most recent story from the Twin Falls Times News under date of September 8, 2010 which indicates that members of the “Fourth Estate” understand the significance and seriousness of the situation. This is not something that will bathe any public official who engages in a cover-up with a level of “glory”.

As I understand the process and authority of the Tax Commission, when the Auditors provide the taxpayer with an assessment, the monies owed are constructively monies of the State until and unless the taxpayer enters a protest and until and unless **there is a legitimate reduction of the assessment made in accordance with the authority given the Commission by statute.**

The affidavits of the eight Auditors which have been provided to you demonstrate example after example where there was no basis in law for the reduction or elimination of the assessment and, therefore, the official or officials who provided the reduction or elimination were violating the law.

We have sought to work this case out by offering an opportunity to have the litigation “stand down” pending a proper investigation. At the moment our offer has been rejected and I am fearful that there are certain officers of government who have decided to “stonewall” and hope the matter will go away. Any officers who adopt that position may well be accomplices to activities in violation of the statutes.

I respectfully invite your attention to Title 18, Idaho Code, Chapter 57:

Section 18-5701. Misuse of public monies by officers.

“Each officer of this state . . . and every other person charged with the receipt, safe keeping, or disbursement of public monies, who either:

1. Without authority of law, appropriates the same or any portion thereof to his own use, or to the use of another; or
2. Loans the same or any portion thereof; or having the possession or **control** of any public money, makes a profit out of, **or uses the same for any purpose not authorized by law**; or (emphasis supplied)

* * *

6. Knowingly keeps any false account, **or makes any false entry** or erasure in any account of or relating to the same; or (emphasis supplied)
7. Fraudulently alters, falsifies, conceals, or destroys or obliterates any such account; or

* * *

Is punishable by imprisonment in the State prison for not less than one (1) nor more than ten (10) years, and is disqualified from holding any office in this state.

Idaho Code § 18-5703 provides: **Public monies defined:**

“The phrase ‘public monies’ as used in the two preceding sections includes all bonds and **evidences of indebtedness, and all monies belonging to the state . . . and all evidences of indebtedness received or held by state . . . in the official capacity.**”

We are providing as Appendix A hereto a proposed decision of the Tax Commission which appears to unlawfully provide a taxpayer with forgiveness of a properly assessed obligation to the State of tax, penalty and interest in the sum of **\$202,252**.

That proposed decision which we understand may be issued within a week or ten days involves a taxpayer who seeks to receive an Investment Tax Credit (ITC) against income taxes connected with the purchase of an aircraft costing approximately **\$7,097,100**.

This proposed decision violates Idaho Code § 63-3027(s) adopted in 1997 and also violates the IDAPA Rule applicable to Commission assessments of taxpayers entitled “**560 Special Rules**.” The

decision is written by Steve Wynn, a tax policy specialist with the Commission, who functions in the same capacity on multistate cases as does Deputy Attorney General Larry Allen. Mr. Wynn is not a lawyer and we understand he is engaged in authoring additional opinions of great consequence for the Commission.

The decision in Docket No. 22399, 22400, and 23012 provided here as Appendix A has tremendous potential for great damage to the revenues to be received by the State of Idaho. If permitted to become precedent, it not only illegally reduces the tax liability of the taxpayer involved in future investments, but will also result in inappropriate tax relief to banking institutions which provide funding for leases of equipment utilized within and without the State of Idaho.

The basic procedure utilized by tax commissions nationwide for apportioning Investment Tax Credit on aircraft by utilizing a ratio of "departures" from the given state to departures outside the state has been well established. The procedure has been to the Idaho Supreme Court twice in cases involving the rolling stock of the Union Pacific Railroad and the Burlington Northern Railroad. *Burlington Northern and Union Pacific v. Idaho State Tax Commission*, 8 P.2d 837, 121 Idaho 808 (1992).

The rules provide for some very rare circumstances where the Commission may deviate from the methodology if the taxpayer can establish that another method should be utilized if such is necessary to more accurately reflect the apportionment of the taxpayers operations in Idaho as distinguished from operations in another state. In the case in Appendix A, the taxpayer has not provided evidence providing a basis for a deviation in the apportionment formula uniformly utilized for the rolling stock of railroads, aircraft, and other similar situations.

We respectfully request that the Office of the Attorney General:

- (1) Immediately intercede in this particular case before violation of Idaho law is incurred and before a precedent is set which will seriously diminish the Idaho tax base when our economy is in great distress; and
- (2) Secondly, that the Office of the Attorney General consider the affidavits supplied from eight Auditors in the "Ringo" lawsuit which provide evidence of likely violation of Title 18 Chapter 57 of the Idaho Code.

In summary, my client, Representative Shirley Ringo, seeks only that an appropriate Investigative Panel be convened in accordance with her offer made to the State and the Attorney General's Office several weeks ago. If such an investigation in the public interest is conducted, she remains willing to hold the litigation in abeyance.

Please advise.

Very truly yours,



Robert C. Huntley

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)
)
XXXXXXXXXXXX) DOCKET NO. 22399, 22400, 23012
XXXXXXXXXXXX) and 23013
XXXXXXXXXXXX)
) DECISION
)

Petitioner(s).)

On September 11, 2009, the Idaho Tax Commission's (Commission) Income Tax Audit Bureau (ITA) issued a Notice of Deficiency Determination (NODD) to Husband and Wife (petitioner-HW) for taxable years 2006 and 2007 proposing additional income tax, penalty, and interest for the taxable years in the amount of \$157,123. On June 3, 2010, the ITA issued a second NODD to petitioner-HW for taxable year 2007 proposing additional income tax, penalty, and interest in the amount of \$46,129. The total proposed additional tax, penalty, and interest is \$203,252.

On September 11, 2009 the ITA issued an NODD to XXXXXXXX (petitioner-XX) for taxable years 2006 and 2007. On June 3, 2010, the ITA issued a second NODD to petitioner-XX for taxable year 2007. The adjustments proposed by the ITA in the NODDs to petitioner-XX did not result in any additional tax due since the petitioner-XX filed as an S corporation; however, the adjustments do have a tax impact to its sole shareholder.

The petitioners filed a timely protest and petition for redetermination. The petitioners were informed of their appeal rights. The Idaho Code section 63-3045(2) hearing was held on June 1, 2010, for the September 11, 2010, NODD's and the petitioners waived their right to an Idaho Code section 63-3045(2) hearing on the June 3, 2010, NODDs. The petitioners requested that the Commission combine the June 3, 2010, NODDs with the September 11, 2009, NODDs when rendering its decision. The Commission, after having reviewed the file, hereby issues its decision.

A. ISSUES

1. The petitioner-XX protests the ITA's treatment of including a percentage of the cost of an airplane purchased in 2006 (2006 airplane) in the Idaho property numerator. The petitioner-XX argues it is entitled to include the entire cost of the 2006 airplane.

2. The petitioner-XX protests the ITA's treatment of allowing a percentage of the cost of the 2006 airplane as "qualified property" for purposes of the Idaho investment tax credit (ITC). The petitioner-XX argues that it is entitled to include the entire cost of the 2006 airplane.

3. The petitioner-XX does not dispute that the sale in 2007 of a 2002 airplane (2002 airplane) acquired in 2005 triggered ITC recapture.

4. The petitioner-HW protests the ITA's decrease in the amount of ITC flowing to the petitioner-HW from the petitioner-XX.

5. The petitioner-HW does not protest the recapture of ITC; however, the petitioner-HW does protest the proposed assessment of penalties relating to the ITC recapture.

B. FINDINGS

The Commission's finds that the petitioner-XX is entitled to include 100 percent of its cost in the 2006 airplane in the calculation of its Idaho property numerator and as "qualified property" for purposes of Idaho ITC. Additionally, the Commission declines to impose the penalties asserted in the NODD issued to petitioner-HW.

C. PETITIONER-XX

The petitioner-XX is the sole shareholder of a corporation that under federal law is treated as a qualified Subchapter S corporation (QSSS). The QSSS purchased the 2006 airplane. Under federal law, a QSSS is disregarded and the assets and liabilities of the QSSS are simply

treated as if the S Corporation parent owned the assets and liabilities. The 2006 airplane can hold up to eight people, including the pilots.

The petitioner-XX filed its Idaho Form 41S Idaho S Corporation Income Tax Return for taxable years 2006, and 2007, on October 15, 2007, and September 15, 2008, respectively. In these filings, the petitioner-XX apparently when calculating its Idaho property factor percentage, one of three factors used to determine the Idaho apportionment percentage, included in its Idaho property factor numerator and denominator 100 percent of its cost in the 2006 airplane. However, when determining the amount of “qualified property” for purposes of the ITC, the petitioner-XX only included \$2,973,407 of its \$7,079,100 cost of the 2006 airplane based upon the following formula:

	Airplane Cost	Times Departures	Idaho Departures	Divided By	Total Departures	Equals	Amount
2006 Airplane	\$7,079,100		45		107		\$2,977,193

On October 15, 2007, the petitioner-XX filed an amended Idaho Form 41S and claimed the entire \$7,079,100 as qualified property eligible for the ITC.

In addition to the purchase of the 2006 airplane, the petitioner-XX had additional qualifying property of \$230,791 for a total amount of qualifying property of \$7,309,891. When multiplied by 3%, the amount of Idaho ITC that passes through from petitioner-XX to petitioner-HW is \$219,297.

The ITA audited the petitioner-XX’s 2006 (original and amended) income tax return and its 2007 income tax return and disagreed with the petitioner-XX’s inclusion of the 2006 airplane at 100 percent of cost in the petitioner-XX’s Idaho property factor numerator and as qualified property for purposes of the ITC calculation.

The ITA obtained the 2006 airplane’s flight log. The flight log, for the period July 1,

2006 through December 31, 2006, reflects that approximately 38 percent (35/93) of the 2006 plane's departures were from departures within Idaho as follows:

	-----Departures-----				-----Pilots1[1]-----							Total	(a)2[2]
	Total	xx	xy	xz	Idaho Total	Pilot A	Pilot B	Name 1	Name 2	Name 3			
July	11	3		1	4	3	3	2	6	8	22	0	
August	19	7	1	1	9	6			13	15	34	4	
September	23	10			10	11			12	14	37	9	
October	22	5			5	8			14	19	41	3	
November	6	3			3	5			1	4	10	2	
December	12	4			4	3			9	9	21	3	
	93	32	1	2	35	36	3	2	55	69	165	21	

The amount of the 2006 airplane cost to be included in the petitioner-XX's 2006 and 2007 Idaho property numerator was determined by the ITA as follows:

	Airplane Cost	Idaho Departures	Divided By	Total Departures	Equals	Amount
2006 Airplane	\$7,079,100	35		93		\$2,690,058

As authority for its position, the ITA cites Idaho Income Tax Administrative Rule 475.03 which requires the use of Idaho departures over total departures when determining that portion of an airplane to be included in the property factor.

Based upon the same formula above, the ITA disallowed all but \$2,690,058 of the \$7,079,100 cost of the 2006 airplane as qualifying for the ITC. As authority for its position, the ITA cites Idaho Income Tax Administrative Rule 714.02.a which requires the use of Idaho departures over total departures when determining that portion of an airplane, used within and without Idaho, to be included in the ITC calculation or the Idaho Income Tax Administrative

1[1] Pilot A is the sole shareholder of petitioner-XX and is also the husband component of the petitioner-HW; Pilots B and C are not employees of either the petitioner-XX or the QSSS; and Pilots D and E are employees of the QSSS.
 2[2] This column (a) represents the number of times that the petitioner-XX's sole shareholder flew the 2006 airplane as the sole pilot.

Rule 714.02.b requirement that the cost of the airplane be the same amount as included in the Idaho property numerator; which, as previously discussed, under ITA's interpretation, the petitioner-XX would still be required to use Idaho departures over total departures.

The petitioner-XX argued in its letter dated November 12, 2009, that it:

. . . treats all revenue, payroll and property factors associated with their aircraft operations as Idaho sourced. This treatment is based on the fact that the operations are controlled from and centered in Idaho, the majority of the costs associated with the operations are incurred in Idaho, and the airplane is domiciled in Idaho, with all roundtrip flights departing from and returning to Idaho. When the aircraft is leased by a third party, the destination of the aircraft is ancillary to its business purpose. The owner has no control over its destination and no visibility to purpose of the trip. Rather, from the aircraft owner's perspective, the critical factor is the location of the property at the time it is leased and that it returns to that location when the leasing period is ended. The actual use of the aircraft is not related to the primary operations of the Company [the petitioner-XX]. As such, there is no business connection established with the destination state when the plane is leased and it would not be appropriate to attribute any of the leasing activity to any state other than Idaho. Attributing all business activity related to the aircraft to Idaho reflects the economic realities of the use of the aircraft.

The 2006 airplane is at times leased through an independent charter company as part of its pool of aircraft available for charter, or leased by the officers of the petitioner-XX for personal use. The petitioner-XX is compensated for both types of lease arrangements.

D. PETITIONER-HW

The petitioner-HW is comprised of a husband and wife both of which are Idaho residents and for the taxable years 2006 and 2007 filed an Idaho Form 40 Individual Income Tax Return on a filing joint basis. The husband is the sole shareholder of the petitioner-XX.

For taxable year 2006, the petitioner-XX passed the \$219,297 of ITC through to the petitioner-HW; however, the petitioner-HW, due to certain limitations, was unable to claim most of the \$219,297 on their Idaho Form 40 Individual Income Tax Return for taxable year 2006 and instead carried the majority of the ITC into taxable year 2007 and claimed it against their 2007 income tax liability. The ITA audited the petitioner-HW's individual income tax returns for

taxable years 2006 and 2007. As a result of the ITA's audit, the ITA disallowed \$131,672 of ITC claimed on the petitioner-HW's 2007 income tax return. The ITA issued a second NODD in June 2010 to both petitioner-HW and petitioner-XX which resulted in additional tax due by the petitioner-HW relating to the recapture of ITC on the sale of the 2002 airplane in 2007.

LAW AND ANALYSIS

For a multistate corporation transacting business within Idaho, the allocation and apportionment provisions are found in Idaho Code section 63-3027.3³ The Idaho apportionment percentage is governed by Idaho Code sections 63-3027(i) through (q). Idaho Code sections 63-3027(k) through (m) govern the calculation of the Idaho property factor percentage, which is the factor at issue in this docket number, and these sections state:

(k) The property factor is a fraction, the numerator of which is the average value of the taxpayer's real and tangible personal property owned or rented and used in this state during the tax period and the denominator of which is the average value of all the taxpayer's real and tangible personal property owned or rented and used during the tax period.

(l) Property owned by the taxpayer is valued at its original cost. Property rented by the taxpayer is valued at eight (8) times the net annual rental rate. Net annual rental rate is the annual rental rate paid by the taxpayer less any annual rental rate received by the taxpayer from subrentals.

(m) The average value of property shall be determined by averaging the values at the beginning and ending of the tax period, but the state tax commission may require the averaging of monthly values during the tax period if reasonably required to reflect properly the average value of the taxpayer's property.

Idaho Income Tax Administrative Rule 475.03.c specifically states that "The value of aircraft used within and without Idaho during the taxable year shall be determined by multiplying the value of the aircraft by the ratio of departures from locations in Idaho to total departures." Therefore, unless otherwise allowed by another statute or administrative rule, the petitioner-XX is required to include the cost of the 2006 airplane based upon Idaho departures to total departures.⁴ However, Idaho Code section 63-3027(s) states:

(s) If the allocation and apportionment provisions of this section do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for or the state tax commission may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

(1) Separate accounting, provided that only that portion of general expenses clearly identifiable with Idaho business operations shall be allowed as a deduction;

³[3] References to Idaho Code or Rules refer to the Idaho Code or Income Tax Administrative Rules in effect for the taxable year 2007 unless otherwise stated.

⁴[4] IDAPA 35.01.01.475.03.c.

- (2) The exclusion of any one (1) or more of the factors;
- (3) The inclusion of one (1) or more additional factors which will fairly represent the taxpayer's business activity in this state; or
- (4) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

The Commission, after review of the facts and circumstances in this docket number is satisfied that including the basis of the 2006 airplane in the Idaho numerator based upon Idaho departures to total departures does not fairly represent the extent of the petitioner-XX's business within Idaho. Therefore, it is the Commission's finding that the petitioner-XX should include the full cost of the 2006 airplane (\$7,079,100) in the Idaho property factor numerator when calculating the Idaho property factor percentage.

As for the amount of the 2006 airplane that qualifies for the Idaho Code section 63-3029B Income Tax Credit For Capital Investment, subsection (10) of the Idaho statute provides the following:

(10) In the case of property used both in and outside Idaho, the taxpayer, electing to claim the credit provided in this section, must elect to compute the qualified investment in property with a situs in Idaho for all such investments first qualifying during that year in one (1), but only one (1), of the following ways:

(a) The amount of each qualified investment in a specific asset shall be separately computed based on the percentage of the actual use of the property in Idaho by using a measure of the use, such as total miles or total machine hours, that most accurately reflects the beneficial use during the taxable year in which it is first acquired, constructed, reconstructed, erected or placed into service; provided, that the asset is placed in service more than ninety (90) days before the end of the taxable year. In the case of assets acquired, constructed, reconstructed, erected or placed into service within ninety (90) days prior to the end of the taxable year in which the investment first qualifies, the measure of the use of that asset within Idaho for that year shall be based upon the percentage of use in Idaho during the first ninety (90) days of use of the asset;

(b) The investment in qualified property used both inside and outside Idaho during the taxable year in which it is first acquired, constructed, reconstructed, erected or placed into service shall be multiplied by the percent of the investment that would be included in the numerator of the Idaho property factor determined pursuant to section 63-3027, Idaho Code, for the same year.

Idaho Income Tax Administrative Rule 714 states, in pertinent part:5[5]

714. IDAHO INVESTMENT TAX CREDIT -- CREDIT EARNED ON PROPERTY USED BOTH IN AND OUTSIDE IDAHO IN TAXABLE YEARS BEGINNING ON OR AFTER JANUARY 1, 1995 (RULE 714). Section 63-3029B, Idaho Code.

5[5] IDAPA 35.01.01.714.

01. In General. Property must be used at least part of the time in Idaho to qualify for the investment tax credit, provided it otherwise qualifies for the credit. It must also be used in Idaho in each succeeding year to which a carryover may be taken.

02. Election of Methods. The taxpayer must elect to compute the investment tax credit on property used both in and outside Idaho using either the percentage-of-use method or the amount of that property included in the Idaho property factor numerator. The credit for all property used both in and outside Idaho must be computed using the method elected.

a. If the percentage-of-use method is elected, the basis of each qualified asset is multiplied by the percentage of time, miles, or other measure that accurately reflects the use of that asset in Idaho. The use of aircraft within and without Idaho during the taxable year shall be determined by the ratio of departures from locations in Idaho to total departures. . . .

b. If the property factor numerator option is elected, the qualified investment is the basis of the asset included in the numerator of the Idaho property factor for the year the credit is earned. . . .

Emphasis added. In 2008, Idaho Income Tax Administrative Rule 714.02.b was amended as follows:6[6]

b. If the property factor numerator option is elected, the qualified investment is the basis of the asset correctly included in the numerator of the Idaho property factor for the year the credit is earned.

i. The amounts of investment tax credit computed under the percentage-of-use method and the property factor numerator option are generally the same. Differences may result when a taxpayer uses certain MTC special industry regulations that allow the taxpayer to vary from using the percentage-of-use method for determining the Idaho numerator for each item of mobile property, and instead allow another method, such as the ratio of mobile property miles in the state compared to total mobile property miles or the ratio of departures of aircraft from locations in the state compared to total departures. These special industry regulations include the regulations for airlines, railroads, and trucking companies. See Rule 580 of these rules for a list of the special industries.

ii. "Correctly included in the numerator of the Idaho property factor" means that the amount included in the Idaho property factor numerator was correctly computed using Section 63-3027, Idaho Code, and related rules including any MTC special industry regulations that apply to the taxpayer. If the amount included in the Idaho property factor numerator exceeds the amount that should have been included using Section 63-3027, Idaho Code and related rules, the investment tax credit shall be allowed only on the amount that reflects the correct calculation for purposes of computing the Idaho property factor

numerator. For example, a taxpayer includes one hundred percent (100%) of the basis of an asset in the Idaho property factor numerator, but the amount correctly computed under Section 63-3027, Idaho Code, should have been fifty percent (50%) of the basis of the asset. The investment tax credit shall be allowed only on the fifty percent (50%) of the basis of the asset.

Emphasis added.

As discussed earlier in this decision, the Commission held that the petitioner-XX could include the entire cost of the 2006 airplane in its Idaho property factor numerator. Accordingly, under Idaho Code section 63-3029B(10)(b), as interpreted under Idaho Income Tax Administrative Rule 714.02.b.ii (2009 version),^{7[7]} the petitioner-XX is entitled to treat the entire cost of the 2006 airplane as “qualified property,” since the entire cost of the airplane is the correct amount to be included in the Idaho Code section 63-3027 Idaho property factor numerator.

The final issue to be addressed is the proposed assessment of penalty on the petitioner-HW’s failure to report ITC recapture tax on the sale in 2007 of the 2002 airplane. The petitioner-HW does not dispute that the tax is owed to Idaho; however, the petitioner-HW argues that there is sufficient reasonable cause for the Commission to provide the petitioner-HW with relief from the imposition of the 10 percent Idaho Code section 63-3046(d)(1) penalty and the 5 percent Idaho code section 63-3046(a) penalty. The Commission agrees and declines to assert either of the two proposed penalties.

WHEREFORE, the Notice of Deficiency Determination dated September 11, 2009, and June 6, 2010, issued to petitioner-XX are hereby MODIFIED, APPROVED, AFFIRMED, and MADE FINAL.

WHEREFORE, the Notice of Deficiency Determination dated September 11, 2009, and

^{7[7]} IDAPA 35.01.01.714.02.b.ii.

June 6, 2010, issued to petitioner-HW are hereby MODIFIED, APPROVED, AFFIRMED, and MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that the petitioner-HW pay the following tax and interest:

Interest is calculated through December 15, 2010, and will continue to accrue at the rate set forth in Idaho Code section 63-3045.

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of the petitioners' rights to appeal this decision is enclosed.

DATED this ____ day of _____, 2010.

IDAHO STATE TAX COMMISSION

COMMISSIONER