

Dear Senators JOHNSON, Bayer, Burgoyne, and
Representatives COLLINS, Kauffman, Erpelding:

The Legislative Services Office, Research and Legislation, has received the enclosed rules of
the State Tax Commission:

IDAPA 35.01.01 - Income Tax Administrative Rules - Proposed Rule (Docket No. 35-0101-1804).

Pursuant to Section 67-454, Idaho Code, a meeting on the enclosed rules may be called by the
cochairmen or by two (2) or more members of the subcommittee giving oral or written notice to Research
and Legislation no later than fourteen (14) days after receipt of the rules' analysis from Legislative
Services. The final date to call a meeting on the enclosed rules is no later than 10/26/2018. If a meeting is
called, the subcommittee must hold the meeting within forty-two (42) days of receipt of the rules' analysis
from Legislative Services. The final date to hold a meeting on the enclosed rules is 11/27/2018.

The germane joint subcommittee may request a statement of economic impact with respect to a
proposed rule by notifying Research and Legislation. There is no time limit on requesting this statement,
and it may be requested whether or not a meeting on the proposed rule is called or after a meeting has
been held.

To notify Research and Legislation, call 334-4854, or send a written request to the address on the
memorandum attached below.



Eric Milstead
Director

Legislative Services Office

Idaho State Legislature

Serving Idaho's Citizen Legislature

MEMORANDUM

TO: Rules Review Subcommittee of the Senate Local Government & Taxation Committee and the House Revenue & Taxation Committee

FROM: Division Manager - Kristin Ford

DATE: October 09, 2018

SUBJECT: State Tax Commission

IDAPA 35.01.01 - Income Tax Administrative Rules - Proposed Rule (Docket No. 35-0101-1804)

Summary and Stated Reasons for the Rule

The State Tax Commission submits notice of proposed rulemaking relating to the Income Tax. The proposed rule amends Rule 171 to remove certain partnership interests from the list of nonqualifying property for the purpose of capital gains deductions. The newly deductible qualifying partnership interest was enacted by the Legislature in 2018 House Bill 514. The proposed rule also clarifies the use of the method used to determine the fair market value of the partnership's qualified real property as set forth in the Code of Federal Regulations, also specified in 2018 HB 514.

Negotiated Rulemaking / Fiscal Impact

The agency states that negotiated rulemaking was not conducted due to the simple nature of the proposed rule changes. No negative fiscal impact to the General Fund exceeding \$10,000 is expected

Statutory Authority

The proposed rule appears to be within the agency's statutory authority pursuant to sections 63-105 and 63-3039, Idaho Code.

cc: State Tax Commission
Kimberlee Stratton

*** PLEASE NOTE ***

Per the Idaho Constitution, all administrative rules must be reviewed by the Legislature during the next legislative session. The Legislature has 3 options with this rulemaking docket: **1)** Approve the docket in its entirety; **2)** Reject the docket in its entirety; or **3)** Reject the docket in part.

Kristin Ford, Manager
Research & Legislation

Paul Headlee, Manager
Budget & Policy Analysis

April Renfro, Manager
Legislative Audits

Glenn Harris, Manager
Information Technology

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IDAPA 35 – STATE TAX COMMISSION
35.01.01 – INCOME TAX ADMINISTRATIVE RULES
DOCKET NO. 35-0101-1804
NOTICE OF RULEMAKING – PROPOSED RULE

AUTHORITY: In compliance with Section 67-5221(1), Idaho Code, notice is hereby given that this agency has initiated proposed rulemaking procedures. The action is authorized pursuant to Sections 63-105 and 63-3039, Idaho Code.

PUBLIC HEARING SCHEDULE: Public hearing(s) concerning this rulemaking will be scheduled if requested in writing by twenty-five (25) persons, a political subdivision, or an agency, not later than October 17, 2018.

The hearing site(s) will be accessible to persons with disabilities. Requests for accommodation must be made not later than five (5) days prior to the hearing, to the agency address below.

DESCRIPTIVE SUMMARY: The following is a nontechnical explanation of the substance and purpose of the proposed rulemaking:

Income Tax Rule 171 – Rule 171 is being amended consistent with 2018 HB514. This change deletes the reference to a partnership interest as nonqualifying property for the Idaho capital gains deduction.

FEE SUMMARY: The following is a specific description of the fee or charge imposed or increased: N/A

FISCAL IMPACT: The following is a specific description, if applicable, of any negative fiscal impact on the state general fund greater than ten thousand dollars (\$10,000) during the fiscal year resulting from this rulemaking: N/A

NEGOTIATED RULEMAKING: Pursuant to Section 67-5220(2), Idaho Code, negotiated rulemaking was not conducted because of the simple nature of the proposed rule changes.

INCORPORATION BY REFERENCE: Pursuant to Section 67-5229(2)(a), Idaho Code, the following is a brief synopsis of why the materials cited are being incorporated by reference into this rule: N/A

ASSISTANCE ON TECHNICAL QUESTIONS, SUBMISSION OF WRITTEN COMMENTS: For assistance on technical questions concerning the proposed rule, contact Cynthia Adrian, (208) 334-7670. For general questions, contact Kimberlee Stratton, (208) 334-7544.

Anyone may submit written comments regarding this proposed rulemaking. All written comments must be directed to the undersigned and must be delivered on or before October 24, 2018.

Dated this 3rd day of October, 2018.

Cynthia Adrian, Tax Policy Specialist
Idaho State Tax Commission
800 Park Blvd Plaza IV
P.O. Box 36
Boise, ID 83722-0410
Phone: (208) 334-7670
Fax: (208) 334-7844

THE FOLLOWING IS THE PROPOSED TEXT OF DOCKET NO. 35-0101-1804
(Only Those Sections With Amendments Are Shown.)

171. IDAHO CAPITAL GAINS DEDUCTION -- QUALIFIED PROPERTY (RULE 171).
Section 63-3022H, Idaho Code

01. Tangible Personal Property. Tangible personal property qualifies for the Idaho capital gains deduction if it was used in Idaho for at least twelve (12) months by a revenue-producing enterprise as defined by Section 63-3022H(4), Idaho Code, and Rule 172 of these rules. (3-7-11)

02. Real Property. Idaho real property qualifies for the Idaho capital gains deduction if it was held by the taxpayer for twelve (12) months. See Subsection 171.05 of this rule for examples of nonqualifying property. (3-25-16)

03. Gain from Forfeited Rights and Payments. Gain attributable to a cancellation, lapse, expiration, or other termination of a contract right or obligation does not qualify for the Idaho capital gains deduction. This includes any gain from the lapse of an option or from forfeited earnest money, down payment, or similar payments, related to otherwise qualifying property. (4-7-11)

04. Timber. As used in Section 63-3022H(3)(e), Idaho Code, qualified timber grown in Idaho includes: (3-20-97)

a. Standing timber held as investment property that is a capital asset pursuant to Section 1221, Internal Revenue Code; and (3-20-97)

b. Cut timber if the taxpayer elects to treat the cutting of timber as a sale or exchange pursuant to Section 631(a), Internal Revenue Code. (3-20-97)

05. Nonqualifying Property. Nonqualifying property includes: (4-4-13)

a. Real or tangible personal property not having an Idaho situs. (4-4-13)

b. Tangible personal property not used by a revenue-producing enterprise. (4-4-13)

c. Intangible property. Some examples of intangible property include, but are not limited to: (4-4-13)

i. Stocks and bonds; (4-4-13)

ii. Interests in a partnership (except for interests identified in Section 63-3022H(3)(f), Idaho Code, LLC, or S corporation. ~~(4-4-13)~~ ()

06. Holding Periods. (3-20-97)

a. In General. To qualify for the capital gains deduction, property otherwise eligible for the Idaho capital gains deduction must be held for specific time periods. The holding periods for Idaho purposes generally follow Sections 1223 and 735, Internal Revenue Code. (5-8-09)

b. Exception to the Tacked-On Holding Period. The holding period of property given up in a tax-free exchange is not tacked on to the holding period of the property received if the property given up was nonqualifying property based on the requirements of Section 63-3022H(3), Idaho Code. (4-4-13)

c. Installment Sales. The determination of whether the property meets the required holding period is made using the laws applicable for the year of the sale. If the required holding period is not met in the year of sale, the

gain is not from qualified property. The classification as nonqualified property will not change even though the gain may be reported in subsequent years when a reduced holding period is applicable. (4-5-00)

d. Examples of nonqualifying property. (7-1-98)

i. A taxpayer purchased land in California. After owning the land three (3) years, he gave up the California land in a tax-free exchange for land in Idaho. He owned the Idaho land for ten (10) months until selling it at a gain. For federal purposes the holding period of the California land tacks on to the holding period of the Idaho land. The gain from the sale of the California land would not qualify for the Idaho capital gains deduction since it is real property located outside Idaho. The holding period of the California land does not tack on to the holding period of the Idaho land for purposes of the Idaho capital gains deduction. Because the Idaho land was not held for twelve (12) months, the gain from the sale of the Idaho land does not qualify for the Idaho capital gains deduction. (3-30-07)

ii. Assume the same facts as in the example in Subparagraph 171.05.d.i. except the taxpayer's original purchase was land in Idaho. Because the taxpayer owned real property in Idaho that was exchanged for a second parcel of real property in Idaho, the holding period of the Idaho land given up tacks on to the holding period of the second parcel of Idaho land. Because the holding period of the second property, which includes the holding period of the first property, was at least twelve (12) months, the gain from the sale of the second parcel of real property qualifies for the Idaho capital gains deduction. (4-7-11)

07. Holding Periods of S Corporation and Partnership Property. (7-1-98)

a. Property Contributed by a Shareholder to an S Corporation or by a Partner to a Partnership. A shareholder or partner who contributes otherwise qualified property to an S corporation or partnership may treat the pass-through gain on the sale of that property as a qualifying Idaho capital gain if the property has, in total, been held by the shareholder or partner and the S corporation or partnership for the required holding period. The noncontributing shareholders or partners may treat the pass-through gain as a qualifying Idaho capital gain only if the S corporation or partnership held the property for the required holding period. (5-8-09)

b. Property Distributed by an S Corporation or Partnership. (2-27-12)

i. Distributions. For purposes of this rule, the holding period of property received in a distribution from a partnership or from an S corporation other than in liquidation of stock includes the time the entity held the property. (3-25-16)

08. Sale of a Partnership Interest. For taxable years beginning on or after January 1, 2018, when 26 CFR 1.170A-13(c)(3) is used to determine the fair market value of the partnership's qualified real property, the language of that federal regulation is to be treated as if it sets forth an appraisal method for determining the value of the qualified real property due to the sale of the partnership interest rather than a donation of property. ()