JURISDICTION: **OKLAHOMA TAX COMMISSION**
CITE: **2010-02-02-02 / NON-PRECEDENTIAL**
ID: **P-09-051-K**
DATE: **FEBRUARY 2, 2010**
DISPOSITION: **DENIED**
TAX TYPE: **INCOME**
APPEAL: **NO APPEAL TAKEN**

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Protestants, HUSBAND AND WIFE, are represented by CPA, Certified Public Accountant. The Compliance Division of the Oklahoma Tax Commission (hereinafter "Division") is represented by OTC ATTORNEY, Assistant General Counsel, Office of the General Counsel, Oklahoma Tax Commission.

STATEMENT OF THE CASE

Protestants timely filed amended Oklahoma Resident Individual Income Tax Returns (Forms 511X) for tax years 2004, 2005 and 2006, and an original Oklahoma Resident Individual Income Tax Return (Form 511) for tax year 2007 which returns requested income tax refunds in the aggregate amount of $14,469.00. The Division audited the returns, disallowed the out-of state income deduction claimed on each of the returns and by letters dated September 15, 2008 (tax years 2004 and 2005), March 7, 2008 (tax year 2006) and September 2, 2008 (tax year 2007) notified Protestants of the adjustments to the returns. As a result of the disallowance of the deductions, the refunds for tax years 2004, 2005 and 2006 were reduced to zero and the claims were denied, and the refund claim for tax year 2007 was denied and the Division proposed the assessment of additional income tax in the amount of $3,018.00. The file and records reflect Protestants timely protested the Division's proposed adjustments for tax years 2004, 2005 and 2007 by letters received October 6, 2008. There is no record of a timely filed protest to the Division's proposed adjustment for tax year 2006.

On March 27, 2007, the Division referred its file with respect to the 2004, 2005 and 2007 tax years to the Office of the Administrative Law Judges for further proceedings pursuant to the Uniform Tax Procedure Code[1], the Rules of Practice and Procedure before the Office of Administrative Law Judges[2] and the Oklahoma Income Tax Act[3]. The case was docketed as Case No. P-09-051-K and assigned to ALJ, Administrative Law Judge.[4]

A pre-hearing conference was scheduled for May 19, 2009, which was rescheduled for June 16, 2009, by *Notice of Prehearing Conference* issued May 14, 2009.[5] Pursuant to the rescheduled conference, a *Scheduling Order and Notice of Hearing* was issued June 18, 2009

[1] 68 O.S. 2001, § 201 et seq.

[2] Rules 710:1-5-20 through 710:1-5-47 of the *Oklahoma Administrative Code* ("*OAC*")

[3] 68 O.S. 2001, § 2351 et seq., as amended.

[4] *OAC*, 710:1-5-22(b).

[5] *OAC*, 710:1-5-28.

setting forth the procedure by which this cause would be submitted for decision.[6] On June 16, 2009, the ALJ's Office requested the Division's file and records in regard to the 2006 tax year. A second request for the 2006 tax year records was made September 3, 2009. On September 14, 2009, the Office received the Division's file and records with respect to the 2006 tax year.

On September 4, 2009, the Division filed the *Compliance Division's Motion to Compel Discovery and for Continuance of Scheduling Order*. By letter dated September 9, 2009, the Scheduling Order's scheduling dates and the hearing set for September 30, 2009 were cancelled and Protestants were directed to respond to the *Motion to Compel* on or before September 24, 2009. By *Interim Status Report* filed September 24, 2009, the Division advised that Protestants had responded to its discovery requests, withdrew its *Motion to Compel* and requested the issuance of a new scheduling order. On September 25, 2009, a *Scheduling Order and Notice of Hearing* was issued which *Order* was amended by *Amended Scheduling Order and Notice of Hearing* issued October 22, 2009. The hearing was scheduled for November 17, 2009.

A closed hearing was held as scheduled.[7] Neither Protestant appeared for the hearing. Protestants' Exhibits 1 through 4 and Division's Exhibits 1 through 23 were admitted into evidence by stipulation. Protestants' representative stated Protestants' case. The Division's witness, AUDITOR, Auditor 1, Amended Section of the Division, identified the Division's Exhibits and testified in regard to the reason for the Division's adjustment of Protestants' returns. Upon conclusion of closing statements, the record was closed and the protest was submitted for decision.[8]

FINDINGS OF FACT

Upon review of the file and records, including the recording of the hearing and the exhibits received into evidence, the undersigned finds:

1. At all times relevant, Protestants were residents of Oklahoma. Division's Exhibits 1 through 4, and 14 through 16; Protestants' Exhibit 1.

2. COMPANY is a subchapter S corporation organized and existing under the laws of the State of Oklahoma. COMPANY is a single member subchapter S corporation owned one hundred percent (100%) by Protestant, HUSBAND. Division's Exhibit 9 through 12; Protestants' Exhibit 4. COMPANY'S corporate headquarters is located at Protestants' residence in CITY, Oklahoma. See, Division's Exhibits 1 through 4, and 9 through 12; Protestants' Exhibits 1 and 4.

3. Protestant, HUSBAND, is a landman. Division's Exhibits 5 through 8. COMPANY'S type or kind of business is described as "Landman" and its activity code is 541360 which is generally described as "Geophysical Surveying & Mapping Services".[9] Division's Exhibits 9 through 12; Protestants' Exhibit 4.

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[6] *OAC*, 710:1-5-28(b).

[7] Protestant's representative invoked confidentiality. See 68 O.S. Supp. 2009, § 205

[8] *Id*. See, 68 O.S. Supp. 2002, § 221(D).

[9] The detailed description of this code is "[t]his industry comprises establishments primarily engaged in gathering, interpreting, and mapping geophysical data. Establishments in this industry often specialize in locating

5. Protestants timely filed amended Oklahoma Resident Individual Income Tax Returns (Forms 511X) for tax years 2004, 2005 and 2006, and an original Oklahoma Resident Individual Income Tax Return (Form 511) for tax year 2007. On the returns, Protestants sought to exclude from Oklahoma adjusted gross income as out-of-state income the net distributable income Protestant, HUSBAND, received from COMPANY for tax years 2004, 2005 and 2006, and a portion of the net distributable income Protestant, HUSBAND, received from COMPANY for tax year 2007. The returns in the aggregate claim refunds totaling $14,469.00. Division's Exhibits 1 through 4.

6. The Division audited the returns, disallowed the out-of state income deduction claimed on each of the returns and by letters dated September 15, 2008 (tax years 2004 and 2005), March 7, 2008 (tax year 2006) and September 2, 2008 (tax year 2007) notified Protestants of the adjustments to the returns. Division's Exhibits 17 through 20; Protestants' Exhibits 2 and 3.

7. The income tax refunds for tax years 2004, 2005 and 2006 were reduced to zero and the claims were denied as a result of the Division's proposed adjustment to each of the returns. The refund claim for tax year 2007 was denied and additional income tax in the amount of $3,018.00 was assessed as a result of the Division's proposed adjustment to the 2007 return. Division's Exhibits 17 through 20; Protestants' Exhibits 2 and 3.

8. Protestants timely protested the Division's proposed adjustments for tax years 2004, 2005 and 2007 by letters received October 6, 2008. Division's Exhibits 21 through 23.

9. There is no record of a timely filed protest to the Division's proposed adjustment for tax year 2006.

ISSUES AND CONTENTIONS

The issue presented for decision is whether Protestants sustained their burden of proving that the income in question is derived from business transacted outside the state as opposed to professional or personal services.

Protestants contend that the income is derived from a business activity conducted in the states of Oklahoma, Texas, Colorado, West Virginia and Pennsylvania. In support of this contention, Protestants argue that they have developed a mineral title ownership data base that they market to oil companies and oil and gas lease brokers in the named states.

The Division contends that the proposed adjustments are proper since the income in question was derived from the landman services performed by Protestant.

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and measuring the extent of subsurface resources, such as oil, gas, and minerals, but they may also conduct surveys for engineering purposes. Establishments in this industry use a variety of surveying techniques depending on the purpose of the survey, including magnetic surveys, gravity surveys, seismic surveys, or electrical and electromagnetic surveys." See, http://www.naicscode.com/Search/MoreNAICSDetail.asp?N=541360#Description.

CONCLUSIONS OF LAW

WHEREFORE, premises considered, the undersigned concludes as a matter of law that:

1. Jurisdiction of the parties and subject matter of this action is vested in the Oklahoma Tax Commission. 68 O.S. 2001, §§ 207(c) and (d), and 221(D).

2. An income tax is imposed upon the "Oklahoma taxable income" of every resident individual. 68 O.S. 2001, § 2355(A). "Oklahoma taxable income" is defined to mean "'taxable income' as reported (or as would have been reported by the taxpayer had a return been filed) to the federal government, and in the event of adjustments thereto by the federal government as finally ascertained under the Internal Revenue Code, adjusted further as hereinafter provided." 68 O.S. 2001, § 2353(12).

3. The provisions of § 2358 of the Oklahoma Income Tax Act[10]; in general, specify the adjustments to the taxable income of any taxpayer to arrive at the Oklahoma adjusted gross income for individual taxpayers. 68 O.S. 2001, § 2358(A). None of the adjustments permit the deduction or subtraction of wages or salary earned by an individual for services performed either partly or wholly outside the state from taxable income to arrive at Oklahoma adjusted gross income.

4. "Deductions [and credits against tax] are a matter of legislative grace rather than judicial intervention." ***Flint Resources Company v. Oklahoma Tax Commission***, 1989 OK 9, 780 P.2d 665, 673. In order to be allowed, authority for the deduction sought must be clearly expressed. ***Home-State Royalty Corporation v. Weems***, 1935 OK 1043, 175 Okla. 340, 52 P.2d 806 (1935). None may be allowed in absence of a statutory provision therefor. *Id*. *See*, ***New Colonial Ice Co. v. Helvering***, 292 U.S. 435, 440, 54 S.Ct. 788, 78 L.Ed. 1348 (1934).

5. Income received by a resident of Oklahoma for services performed wholly without the state is subject to Oklahoma income tax. ***Colchensky v. Oklahoma Tax Commission***, 1938 OK 612, 184 Okla. 207, 86 P.2d 329. *See*, ***Oklahoma Tax Commission v. Benham***, 1947 OK 104, 198 Okla. 384, 179 P.2d 123. In ***Colchensky***, the Oklahoma Supreme Court cited the holding of the U.S. Supreme Court in ***Lawrence et al. v. State Tax Commission of Mississippi***[11], wherein it held: "[a] state has constitutional power to tax its own citizens on their net incomes though derived wholly from activities carried on by them outside of the State. Domicile in itself establishes a basis for taxation" and said "[e]njoyment of the privileges of residence within the state, and the attendant right to invoke the protection of its laws, are inseparable from the responsibility for sharing the costs of government."

6. Protestants have the burden of proof to show the action or proposed action of the Division is incorrect, and in what respect. *OAC*, 710:1-5-47. *See*, ***Enterprise Management Consultants, Inc. v. Oklahoma Tax Commission***, 1988 OK 91, 768 P.2d 359. The burden of proof standard is "preponderance of evidence." 2 Am.Jur.2d *Administrative Law* § 357. "Preponderance of evidence" means "[e]vidence which is of greater weight or more convincing than the evidence

[10] 68 O.S. 2001, § 2351 et seq., as amended.

[11] 286 U.S. 276, 52 S.Ct. 556, 76 L.Ed. 1102, 87 A.L.R. 374.

offered in opposition to it; that is, evidence which as a whole shows the fact sought to be proved is more probable than not * * * evidence which is more credible and convincing to the mind * * * that which best accords with reason and probability." Black's Law Dictionary 1064 (5th ed. 1979). Each element of the claim must be supported by reliable, probative, and substantial evidence of sufficient quality and quantity as to show the existence of the facts supporting the claim are more probable than their nonexistence. 2 Am.Jur.2d *Administrative Law* § 357. If the taxpayer fails to prove a prima facie case, the protest may be denied solely on the grounds of failure to prove sufficient facts which would entitle the taxpayer to the requested relief. *OAC*, 710:1-5-47; ***Continental Oil Company v. Oklahoma Tax Commission***, 1976 OK 23, 570 P.2d 315.

7. Here, Protestants have failed to come forward with any evidence to show the net distributable income from COMPANY was derived from the marketing of a data base of mineral title ownership. Accordingly, the Division's adjustments to the amended returns for tax years 2004 and 2005, and the adjustment and proposed assessment of additional income tax on the original return for tax year 2007 should be sustained.

8. The Division's adjustment to the 2006 amended return is not before the undersigned since the adjustment has not been protested. See, 68 O.S. 2001, § 207(c) and Oklahoma Tax Commission Order No. 2000-09-19-041[12].

DISPOSITION

THEREFORE, based on the above and foregoing findings of fact and conclusions of law, it is ORDERED that the protest of Protestants, HUSBAND AND WIFE, be denied. It is further ORDERED that the additional income tax assessed for the 2007 tax year, inclusive any accrued and accruing interest, be fixed as the deficiency due and owing.

OKLAHOMA TAX COMMISSION

CAVEAT: This decision was NOT deemed precedential by the Commission. This means that the legal conclusions are generally applicable or are limited in time and/or effect. Non-precedential decisions are not considered binding upon the Commission. Thus, similar issues may be determined on a case-by-case basis.

NOTE: The distinction between a Commission Order designated as "Precedential" or "Non-Precedential" has been blurred because all OTC Orders resulting from cases heard by the Office of Administrative Law Judges are now published, not just "Precedential" Orders. *See* OKLA. STAT. ANN. tit.68, § 221(G) (West Supp. 2009) and OKLA. STAT. ANN. tit. 75, § 302 (West 2002). *See also* OTC Orders 2009-06-23-02 and 2009-06-23-03 (June 23, 2009), which also conclude the language of the Statute is "clear and unambiguous."

[12] In this Order the Commission determined that where an adjustment to an income tax return does not result in the assessment of additional income tax, the taxpayer's right to challenge the adjustment is prescribed by § 207 of the Uniform Tax Procedure Code which does not mandate a time limit for protesting the proposed action.