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WILLIAM M. COX, SR.  
Commissioner

In the matter of:

[REDACTED]

Contact:

[REDACTED]

FINAL RULING NO. 2008-23  
May 5, 2008

Individual income tax assessment for the tax year ended December 31, 2004

FINAL RULING

The Kentucky Department of Revenue ("DOR") has issued an individual income tax assessment against you for the taxable year 2004 totaling \$ [REDACTED] plus applicable interest. The following table provides a breakdown of the amount of tax and accrued interest due through April 30, 2008.

Tax Year	Notice Number	Tax Due	Interest	Total
2004	[REDACTED]	\$ [REDACTED]	\$ [REDACTED]	\$ [REDACTED]

A summary of the facts are as follows:

1. You filed a 2004 Kentucky Individual Income Tax Return which reported a \$ [REDACTED] tax liability based on taxable net income, \$ [REDACTED] in Kentucky income tax withholding, and a refund to you in the amount of \$ [REDACTED].
2. The Internal Revenue Service ("IRS") subsequently audited your 2004 federal income tax return and disallowed your deduction for alimony paid in the amount of \$ [REDACTED].

3. Upon receipt of the federal audit information, the DOR adjusted your 2004 Kentucky Individual Income Tax Return in an amount equal to the adjustment for federal purposes which resulted in the additional assessment of \$ [REDACTED], plus interest.
4. The DOR received correspondence from you dated [REDACTED] 08 in which you submitted an amended 2004 Kentucky Individual Income Tax Return and requested a refund of Kentucky income tax already paid. The reason you amended the return is based on your interpretation of IRC Secs. 61 and 3401 and how the wording in such statutes exempts you from income taxation.
5. The amended income tax return reflecting an alleged overpayment of income tax has been denied by the DOR.

At issue are the definitions of “income” and “employee.” You state in your letter dated [REDACTED], 2008 that Internal Revenue Code (IRC) “section 61 merely states that ‘income’ is ‘income’ regardless of where the ‘income’ comes from.” You further state that “the actual question at hand here is what actually constitutes ‘income.’” In reality, IRC Sec. 61 states:

Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

1. Compensation for services, including fees, commissions, fringe benefits, and similar items;
2. Gross income derived from business;
3. Gains derived from dealings in property;
4. Interest;
5. Rents;
6. Royalties;
7. Dividends;
8. Alimony and separate maintenance payments;
9. Annuities;
10. Income from life insurance and endowment contracts;
11. Pensions;
12. Income from discharge of indebtedness;
13. Distributive share of partnership income;
14. Income in respect of a decedent; and
15. Income from an interest in an estate or trust.

It is clear that IRC Sec. 61 defines income more broadly than you have described in your writing. Upon review of the statute, you will find that Sec. 61 more than “merely states that ‘income’ is ‘income’, regardless of where the ‘income’ comes from.” The statute, in addition, states that items of income are “not limited to” the items listed. Further, although your letter spends much time discussing the terms “wages” and “employee” you see that Section 61 describes “compensation” in a much broader sense.

While Kentucky income tax uses the federal definition of “income” as a starting point for its calculations, the power of the state to tax income comes from its own constitution and statutes. Whether, and to what extent, you are taxable at the state level is not dependent on whether you are taxable at the federal level or any grant of federal authority.

In light of the fact that you are a Kentucky resident and that you did receive compensation in 2004, your income is taxable based on the following:

For Kentucky income tax purposes, “gross income” in the case of taxpayers other than corporations means “gross income” as defined in Section 61 of the Internal Revenue Code. See KRS 141.010(9).

KRS 141.010(17) defines a “resident” as an individual domiciled within this state.

KRS 141.020(1) states that “an annual tax shall be paid for each taxable year by every resident individual of this state upon his entire net income.” “Net income” is federal gross income with certain adjustments and minus allowable deductions. See KRS 141.010 (10) and (11).

After reviewing your protest and the applicable statutes, it is the position of the Kentucky Department of Revenue that the individual income tax assessment issued against you for the tax year 2004 totaling \$■■■■, plus accrued interest, is a legitimate liability due the Commonwealth of Kentucky. This is a final ruling of the Kentucky Department of Revenue.

### **APPEAL**

You may appeal this final ruling to the Kentucky Board of Tax Appeals pursuant to the provisions of KRS 131.110, KRS 131.340-131.365, 103 KAR 1:010 and 802 KAR 1:010. If you decide to appeal this final ruling, your petition of appeal must be filed at the principal office of the Kentucky Board of Tax Appeals, 128 Brighton Park Boulevard, Frankfort, Kentucky 40602-2120, within thirty (30) days from the date of this final ruling. The rules of the Kentucky Board of Tax Appeals, which are set forth in 802 KAR 1:010, require that the petition of appeal must:

1. Be filed in quintuplicate;
2. Contain a brief statement of the law and facts in issue;
3. Contain the petitioner's or appellant's position as to the law and facts; and
4. Include a copy of this final ruling with each copy of the petition of appeal.

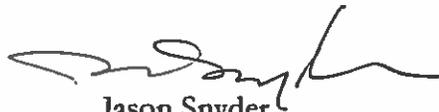
The petition of appeal must be in writing and signed by the petitioner or appellant. Filings by facsimile or other electronic means shall not be accepted.

Proceedings before the Kentucky Board of Tax Appeals are conducted in accordance with 103 KAR 1:010, 802 KAR 1:010 and KRS 131.340-131.365 and KRS Chapter 13B. Formal hearings are held by the Board concerning the tax appeals before it, with all testimony and proceedings officially reported. Legal representation of parties to appeals before the Board is governed by the following rules set forth in Section 2 (3) of 802 KAR 1:010:

1. An individual may represent himself in hearings before the Board;
2. An individual who is not an attorney may not represent any other individual, corporation, trust, estate, or partnership before the Board; and
3. An attorney who is not licensed to practice in Kentucky may practice before the Board if he complies with Rule 3.030(2) of the Rules of the Kentucky Supreme Court.

You will be notified by the Clerk of the Board of the date and time set for any hearing.

Sincerely,  
Finance and Administration Cabinet



Jason Snyder  
Executive Director  
Office of Legal Services

CERTIFIED MAIL  
RETURN RECEIPT REQUESTED