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91 Ohio St.3d 420, 746 N.E.2d 1073, 2001 -Ohio- 92
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Kemppel v. Zaino
 Ohio,2001.

Supreme Court of Ohio.
KEMPPPEL et al., Appellants,
 v.
 ZAINO, Tax Commr., Appellee.
No. 00-358.

Submitted Feb. 27, 2001.
 Decided May 23, 2001.

Out-of-state taxpayers who were shareholders of Ohio subchapter S corporation filed for reassessment of their nonresident tax credit in connection with net proceeds they received from sale of corporate assets upon corporation's dissolution. The Tax Commissioner affirmed his assessment, but reduced statutory interest penalty by one-half. Taxpayers appealed. The Board Tax Appeals affirmed. Taxpayers again appealed. The Supreme Court, Alice Robie Resnick, J., held that: (1) income resulting from gain on sale of corporation's intangible personal property was nonbusiness income, and (2) Commissioner was authorized to impose statutory interest penalty on taxpayers for their failure to pay proper amount of Ohio income taxes.

Affirmed in part, reversed in part, and remanded.

Douglas, J., dissented.

West Headnotes

[1] **Internal Revenue 220** ⚡**3885**

220 Internal Revenue
 220V Income Taxes
 220V(O) Small Business Corporations
 (Subchapter S Corporations)
 220k3885 k. In General. Most Cited Cases

Taxation 371 ⚡**3485**

371 Taxation
 371VIII Income Taxes
 371VIII(D) Persons Liable
 371k3485 k. Corporations in General.

Most Cited Cases
 (Formerly 371k1015)

For tax purposes, the character of the income attributed to shareholders from a subchapter S corporation is determined as though they had received it directly from the same source as the corporation; thus, if income is business income to the corporation it is business income to the shareholders, but if income is nonbusiness income to the corporation it is nonbusiness income to the shareholders. 26 U.S.C.A. § 1366(b).

[2] **Taxation 371** ⚡**3485**

371 Taxation
 371VIII Income Taxes
 371VIII(D) Persons Liable
 371k3485 k. Corporations in General.

Most Cited Cases
 (Formerly 371k1015)

Taxation 371 ⚡**3517**

371 Taxation
 371VIII Income Taxes
 371VIII(E) Deductions, Credits, and Exemptions

371k3517 k. Credits. Most Cited Cases
 (Formerly 371k1047)

Income resulting from gain on sale of subchapter S corporation's intangible personal property as part of liquidation of assets followed by dissolution was "nonbusiness income," rather than "business income," to corporation and out-of-state shareholders, and thus, shareholders' pro rata gain from such sale did not reduce their nonresident tax credit or increase their Ohio tax; income did not result from sale in regular course of trade or business, but rather from

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one-time event that terminated business. R.C. §§
 5747.01(B, C), 5747.20(B)(2)(c).

[3] Taxation 371 ↪3451

371 Taxation

371VIII Income Taxes

371VIII(C) Incomes Taxable

371k3451 k. Source of Income in General.

Most Cited Cases

(Formerly 371k983)

Under the “transactional test,” whether income is business or nonbusiness, for tax purposes, depends on whether it arises from a transaction or activity that occurs in the regular course of the business in which the taxpayer engages; the nature, frequency, and regularity of the transaction are relevant factors. R.C. § 5747.01(B).

[4] Taxation 371 ↪3451

371 Taxation

371VIII Income Taxes

371VIII(C) Incomes Taxable

371k3451 k. Source of Income in General.

Most Cited Cases

(Formerly 371k983)

Under the “functional test,” business income includes income from sale of personal property if use of the property constituted an integral part of the regular course of a trade or business operation. R.C. § 5747.01(B).

[5] Taxation 371 ↪3563

371 Taxation

371VIII Income Taxes

371VIII(I) Collection and Enforcement

371k3563 k. Penalties, Forfeitures,

Offenses and Prosecutions. Most Cited Cases

(Formerly 371k1103)

Tax Commissioner was authorized to impose statutory interest penalty on out-of-state taxpayers for their failure to pay proper amount of Ohio income taxes, even if such failure were based on advice of national accounting firm. R.C. § 5747.15(A)(2) (2000).

****1074 *424** Witschey & Witschey Co., L.P.A.,

Jeffrey T. Witschey and Frank J. Witschey, Akron, for appellants.

Betty D. Montgomery, Attorney General, and Robert C. Maier, Assistant Attorney General, for appellee.

Jones, Day, Reavis & Pogue and Charles M. Steines, Cleveland, urging reversal for amicus curiae Lewis W. Dickey.

Taft, Stettinius & Hollister, L.L.P., and Stephen M. Nechemias, Cincinnati, urging reversal for amici curiae David S. and Linda K. Paresky.

***420** ALICE ROBIE RESNICK, J.

ALICE ROBIE RESNICK, J. In 1989 the assets of the Logan Machine Co. (“Logan”), an Ohio subchapter S corporation located in Akron, were liquidated and the corporation dissolved. The net proceeds from the sale of the assets were distributed to the shareholders, including appellants, Russell and Carrie Kempffel, [FN1]*421 who were residents of and domiciled in Florida at the time of the sale. As shareholders of Logan, each of the Kempffels received his or her pro rata share of the net proceeds of the sale, including gain from the sale of intangible personal property, which was attributed to goodwill.

FN1. On February 5, 2001, a suggestion of death was filed for Carrie M. Kempffel. Russell E. Kempffel as administrator of the estate of Carrie M. Kempffel has been substituted as a party.

To calculate the amount of their nonresident tax credit under R.C. 5745.05(A), the Kempffels calculated the ratio of their non-Ohio income to their total income. In calculating this ratio, the Kempffels included as non-Ohio income all income attributed to them from Logan, except that from ordinary business operations prior to the sale. The Tax Commissioner audited the Kempffels' return and treated all of the income attributed to them from Logan as business income and therefore subject to allocation to Ohio, including the gain from **1075 the sale of the intangible personal property (goodwill). As a result, the ratio of the Kempffels' non-Ohio income to total income was reduced, thereby reducing the amount of the Kempffels'

