

# Minnesota Department of Revenue

## Revenue Notice # 17-02: Individual Income and Corporate Franchise Tax – *Nadler v. Commissioner* – Minnesota Allocation Policy

### Introduction

This Revenue Notice, promulgated pursuant to *Minnesota Statutes*, section 270C.07, advises non-resident individuals that the department does not administer the income allocation provisions in Chapter 290 of the *Minnesota Statutes* identified below using the Minnesota Tax Court's reasoning in *Nadler v. Commissioner*, No. 7736 R, 2006 WL 1084260 (Minn. Tax Ct.). See *Kmart Corp. v. County of Stearns*, 710 N.W.2d 761, 769 (Minn. 2006).

### Department Position

#### Classification of Income

The department recognizes only two categories of income for the purpose of determining the correct method of allocation under Chapter 290:

- 1) Business income – that must be apportioned to Minnesota.
- 2) Nonbusiness income – that cannot be apportioned to Minnesota because of limitations on state taxing authority set forth in the Minnesota and United States Constitutions. Nonbusiness income must be assigned.

The *Nadler* opinion reaches the conclusion that three categories of income are necessary to give full effect to the relevant statutes. Accordingly, the decision recognizes three types of income:

- 1) Business income – subject to apportionment.
- 2) Nonbusiness income that is income derived from a trade or business.
- 3) Nonbusiness income that is not income derived from a trade or business – that the court ruled was subject to allocation under *Minnesota Statutes*, section 290.17, subdivision 2.

The department does not recognize a distinction between types of nonbusiness income. In accordance with the plain meaning of *Minnesota Statutes*, section 290.17, subdivision 6, the department requires that all business income be apportioned to Minnesota under section 290.191, and all nonbusiness income be assigned in accordance with section 290.17, subdivision 2.

#### Fixed Limitation on Allocation of Gain from the Sale of Goodwill

The proper method for calculating allocable gains following a sale of goodwill under *Minnesota Statutes*, section 290.17, subdivision 2(c), is to multiply the taxpayer's gain by the business's prior year apportionment factor.

The *Nadler* opinion construes *Minnesota Statutes*, section 290.17, subdivision 2(c), to impose a fixed cap on the allocation of gains from the sale of goodwill. Specifically, the court ruled that there is a cap on allocation fixed at "the actual amount of the income apportioned to Minnesota in the preceding year." *Nadler v. Commissioner of Revenue*, No. 7736 R, 2006 WL 1084260, at \*9 (Minn. Tax Ct.). This interpretation is not consistent with the plain meaning of the statute.

Additionally, placing a fixed limitation on assignment distorts the relationship between economic activity and the calculation of taxable income. Accordingly, the department does not recognize a fixed limitation on the assignment of gains from the sale of goodwill.

Publication Date: July 3, 2017

  
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Ryan Church, Deputy Commissioner