**DEPARTMENT OF STATE REVENUE**

02-20210037.LOF

**Letter of Findings: 02-20210037**
**Indiana Corporate Income Tax**
**For the Years 2015, 2016, and 2017**

**NOTICE:** IC § 6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

## HOLDING

The Department disagreed with Casino Company's argument that the Department erred in requiring Casino Company to addback taxes measured by income and paid to the states in which Casino Company operated its gaming facilities; the Department disagreed that excise, privilege, or casino license fees - measured by casino income - should not have been added back. In addition, the Department disagreed that the Department's audit erred when it failed to overrule the Indiana Tax Court's *Aztar* decision requiring the addback of Indiana's Riverboat Wagering Tax.

## ISSUES

### I. Indiana Corporate Income Tax - Addback of Taxes Paid in Other States.

**Authority:** U.S. Const. amend. 5; U.S. Const. amend. XIV; U.S. Const. art. I, § 8 cl. 4; IC § 1-1-4-1; IC § 6-3-1-3.5; IC § 6-8.1-5-1; *Dept. of State Revenue v. Caterpillar, Inc*., 15 N.E.3d 579 (Ind. 2014); *Indiana Dept. of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463 (Ind. 2012); *Siwinski v. Town of Ogden Dunes*, 949 N.E.2d 825 (Ind. 2011); *Consolidatation Coal Company v. Indiana Dept. of State Revenue*, 583 N.E.2d 1199 (Ind. 1991); *State Bd. of Tax Comm'rs v. Jewell Grain Co*., 556 N.E.2d 920 (Ind. 1990); *Ind. Dep't of State Revenue, Ind. Revenue Bd., Ind. Gross Income Tax Division v. Colpaert Realty Corp*., 109 N.E.2d 415 (Ind. 1952); *Treasury of Ind. v. Dietzen's Estate*, 528 N.E.2d 137 (Ind. 1939); *Miles v. Department of Treasury*, 199 N.E. 372 (Ind. 1935); *Lafayette Square Amoco, Inc. v. Indiana Dept. of State Revenue*, 867 N.E.2d 289, (Ind. Tax Ct. 2007); *Aztar Indiana Gaming Corporation v. Indiana Department of State Revenue* 806 N.E.2d 381 (Tax Ct. 2004); *Mynsberge v. Indiana Dep't of State Revenue*, 716 N.E.2d 629 (Ind. Tax Ct. 1999); *Tri-States Double Cola Bottling Co. v. Department of State Revenue*, 706 N.E.2d 282 (Ind. Tax Ct. 1999); *Jefferson Smurfit Corp. v. Indiana Dep't of State Revenue*, 681 N.E.2d 806 (Ind. Tax Ct. 1997); *State Bd. of Accounts v. Ind. Univ. Found.*, 647 N.E.2d 342 (Ind. Ct. App. 1995); *Leehaug v. State Bd. of Tax Comm'rs*, 583 N.E.2d 211 (Ind. Tax Ct. 1991); *Montgomery Ward & Co. v. Gregg*, 554 N.E.2d 1145 (Ind. Ct. App. 1990); *Fell v. West*, 73 N.E. 719 (Ind. App. 1905); *VFW Ventures, Inc. v. Surtees*, 8 So.3d 983 (Ala. S. Ct. 2008); *Surtees* v. *VFJ Ventures, Inc.* 8 So.3d 950 (Ala. Ct. App. 2008); Black's Law Dictionary (9th ed. 2014); Richard Weiss *Achieving Uniformity in State Income Taxes: A Worthwhile Goal*, 18 Sep J. Multistate Tax'n (September 2008); Henry Campbell Black, *A Treatise on the Law of Income Taxation under Federal and State Laws* § 1 (1913); Investopedia *https://www.investopedia.com/terms/e/excisetax.asp.* (Last visited June 27, 2021); Cal. Bus & Prof. Code § 19951; 230 Ill. Comp. Stat. Ann § 10/13(a-3); Kan. Stat. Ann. § 74-8734; 8 M.R.S. § 1036; Mass. Gen. Laws G.L. c. 23K, § 55; Miss. Code § 75-76-177; Mo. Rev. Stat. § 312.822; Nev. Rev. Stat. § 463.370; Ohio Rev. Code Ann. § 5753.02; 4 Pa. Cons. Stat. § 1403; 4 Pa. Cons. Stat. § 13A62; W.Va. Code § 29-22C-26; Letter of Findings 01-20170142 (August 7, 2017); Letter of Findings 04-20140409 (September 24, 2014); American Heritage Dictionary of the English Language (3rd ed. 1996).

Taxpayer argues that the Department erred in assessing additional corporate income tax on the ground that Taxpayer was not required to "add back" taxes paid to other states in which Taxpayer operates casinos and other gambling facilities.

### II. Indiana Corporate Income Tax - Penalty.

**Authority:** IC § 6-3-4-4.1; IC § 6-8.1-5-1; IC § 6-8.1-10-2.1; 45 IAC 15-11-2.

Taxpayer maintains that the Department was unjustified in assessing penalties on the amount of the additional tax assessments.

## STATEMENT OF FACTS

Taxpayer is an out-of-state company in the business of operating gaming, racing, and video gaming facilities. Taxpayer is the owner and operator of gaming, racing, and video gaming operations in multiple states including an Indiana gaming facility.

The Indiana Department of Revenue (Department) conducted an audit review of Taxpayer's federal and Indiana corporate income tax returns. The Department determined that Taxpayer failed to add back taxes "based on income" paid to other states. The Department assessed additional corporate income tax based on the determination that those state taxes should have been added back in determining the amount of Taxpayer's income subject to Indiana tax.

Taxpayer disagreed with the decision and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representative explained the basis for the protest. This Letter of Findings results.

**I. Indiana Corporate Income Tax - Addback of Taxes Paid in Other States.**

## DISCUSSION

The issue is whether Taxpayer has met its burden of proof necessary to establish that the Department's assessment of additional corporate income tax - based on the addback of taxes paid in other states - was wrong.

### A. Audit Assessment.

During the course of the Department's audit, Taxpayer provided the Department its federal consolidated returns. On those federal returns, Taxpayer "deducted gaming taxes for several casinos and gaming facilities located throughout the United States." However, the audit report noted that in preparing its Indiana returns, Taxpayer "did not add this tax back on the Indiana return[s]."

The audit determined these "other state" taxes should have been added back in determining Taxpayer's Indiana tax liability. The audit cited to IC § 6-3-1-3.5(b) as authority. That provision explains the calculation of Indiana "taxable income" in part:

> In the case of corporations, the same as "taxable income" (as defined in Section 63 of the Internal Revenue Code) adjusted as follows:
>
> (1) Subtract income that is exempt from taxation under this article by the Constitution and statutes of the United States.
>
> (2) Add an amount equal to any deduction or deductions allowed or allowable pursuant to Section 170 of the Internal Revenue Code (concerning charitable contributions).
>
> (3) Except as provided in subsection (c), add an amount equal to any deduction or deductions allowed or allowable pursuant to Section 63 of the Internal Revenue Code for taxes *based on or measured by income and levied at the state level by any state of the United States.* (*Emphasis added*).

According to the audit report, Taxpayer "was under the impression that only the Indiana gaming tax was an addback." The Department disagreed concluding that "the law does not limit the addback to Indiana income taxes but requires the addback for all state income taxes." Therefore - and again according to the report - since the other state taxes were "based on income [they] were required to be added back upon audit."

### B. The Rules for Interpreting Indiana Law and Taxpayer's Burden of Proof.

Statutory construction always starts with the "plain and ordinary meaning of the language used." *E.g.*, *Leehaug v. State Bd. of Tax Comm'rs*, 583 N.E.2d 211, 212 (Ind. Tax Ct. 1991). IC § 1-1-4-1 explains in part:

> The construction of all statutes of this state shall be by the following rules, unless the construction is plainly repugnant to the intent of the legislature or of the context of the statute:

> (1) Words and phrases shall be taken in their *plain, or ordinary and usual, sense. Technical words and phrases* having a peculiar and appropriate meaning in law shall be understood according to their technical import. (*Emphasis added*).

A technical word has a "peculiar and appropriate meaning in law" if, for example, that word is defined elsewhere in a related code provision. *State Bd. of Accounts v. Ind. Univ. Found.*, 647 N.E.2d 342, 347 (Ind. Ct. App. 1995). Otherwise, "[W]hen a particular construction has not been expressly provided, the legislature intends that words and phrases be given their plain and ordinary meaning." *Montgomery Ward & Co. v. Gregg*, 554 N.E.2d 1145, 1155 (Ind. Ct. App. 1990). This is particularly true if a word is well understood by the lay public and has been brought into the law from ordinary life experiences, not from legal treatises. *Ind. Dep't of State Revenue, Ind. Revenue Bd., Ind. Gross Income Tax Division v. Colpaert Realty Corp*., 109 N.E.2d 415, 419 (Ind. 1952).

Only after trying and failing to make sense of the statute utilizing the "plain meaning" rule can a court conclude that the statute is ambiguous and therefore construe the statute. *Siwinski v. Town of Ogden Dunes*, 949 N.E.2d 825, 828-29 (Ind. 2011); IC § 1-1-4-1. It is well-established that a statute is not ambiguous merely because of a "[s]imple disagreement between the parties." *Leehaug v. State Bd. of Tax Comm'rs*, 583 N.E.2d 211, 212 (Ind. Tax Ct. 1991) (internal citations omitted). An unambiguous statute must be read to "mean what it plainly expresses, and its plain and obvious meaning may not be enlarged or restricted." *Jefferson Smurfit Corp. v. Indiana Dep't of State Revenue*, 681 N.E.2d 806, 811 (Ind. Tax Ct. 1997).

Once it is clear that statutory provision is plain on its face, it is the Taxpayer's responsibility to establish that the corporate tax assessments are incorrect. As stated in IC § 6-8.1-5-1(c), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." *Indiana Dept. of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463, 466 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dept. of State Revenue*, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

With that threshold burden in mind, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Further, "[w]hen [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] defer to the agency's reasonable interpretation of [the] statute even over an equally reasonable interpretation by another party.'" *Dept. of State Revenue v. Caterpillar, Inc*., 15 N.E.3d 579, 583 (Ind. 2014). Thus, interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

Nevertheless, in determining whether a taxpayer has met that burden of proof, the Department bears in mind its own responsibility. [A] tax imposition statutory provision . . . is to be strictly construed against the imposition of tax. See *State Bd. of Tax Comm'rs v. Jewell Grain Co*., 556 N.E.2d 920, 921 (Ind. 1990); *Tri-States Double Cola Bottling Co. v. Department of State Revenue*, 706 N.E.2d 282, 285 n.9 (Ind. Tax Ct. 1999). However, the policy of strict construction will not override the plain language of a tax imposition provision. *Mynsberge v. Indiana Dep't of State Revenue*, 716 N.E.2d 629, 632-33 (Ind. Tax Ct. 1999).

At the same time the Department also bears in mind that "In construing tax statutes a liberal rule of interpretation must be indulged in order to aid the taxing power of the state." *Treasury of Ind. v. Dietzen's Estate*, 215 Ind. 528, 532, 21 N.E.2d 137, 139 (1939). The statutes of this state relating to the assessment and collection of taxes are liberally construed in favor of the taxing powers. *Fell v. West*, 73 N.E. 719, 722 (Ind. App. 1905).

**C. Taxpayer's Primary Objections.**

Taxpayer challenges the Department's assessment on three grounds which are briefly outlined by Taxpayer as follows:

- [T]he proposed assessments of the foreign excise taxes, license fees, distributions and contract payments violate the purpose of the add-back statute, both in Indiana and in all other states, which is to add back apportioned income taxes.

- "[T]he Auditor's addback of the foreign excise taxes and other non-tax payments would violate the U.S. Constitution in numerous respects." The assessment violates the Commerce Clause and the Due Process Clause because the assessments constitute "not just taxing revenue from transactions already taxed in the Other States, the [Department] is taxing the tax payments themselves made to other jurisdictions . . ." in effect, Indiana here imposes a "tax on a tax" which constitutes "an extraordinary violation of the Commerce Clause."

> • The Department's audit "fails to address the erroneous add-back of the Indiana riverboat gaming tax . . . which violates Indiana law." Taxpayer acknowledges the Tax Court's decision contrary to Taxpayer's own view in *Aztar Indiana Gaming Corporation v. Indiana Department of Revenue*, 806 N.E.2d 381 (Ind. Tax Ct. 2004) (review denied 822 N.E.2d 976) but argues that the Tax Court's *Aztar* decision "failed to adhere to Indiana Supreme Court precedent and was in erroneous for numerous other reasons . . . ."

This Letter of Finding briefly summarizes Taxpayer's primary arguments as follows: (1) The Department improperly added back excise tax and non-tax payments made in other states; (2) The Department's interpretation and application of IC § 6-3-1-3.5(b) violates both the United States and Indiana's constitution; (3) The Tax Court's *Aztar* decision was wrongly decided, and the Department's audit failed to correct that wrongly decided decision.

**1. The Department Erroneously Added Back Out-of-State Excise Taxes, Fees, and Contract Payments.**

In addition to wrongly adding back "contract payments and fees," Taxpayer maintains that the Department erroneously added back other states' excise and privilege taxes not measured by income. As Taxpayer succinctly puts it:

> There is nothing "rational" about Indiana adding back and taxing excise tax payments to the Other States on transactions occurring solely in those states by entities doing business solely in those other states in order to grossly inflate and distort the apportioned base in Indiana.

For simplicity and reference sake, the Department here notes a commonly recognized definition of "excise" taxes. Black's Law Dictionary 1749 (9th ed. 2014) defines excise tax as:

> A tax imposed on the manufacture, sale, or use of goods (such as a cigarette tax), or on an occupation or activity (such as a license tax or an attorney occupation fee).

Elsewhere, "excise tax" is defined as:

> An excise tax is a legislated tax on specific goods or services at purchase such as fuel, tobacco, and alcohol. Excise taxes are intranational taxes imposed within a government infrastructure rather than international taxes imposed across country borders. A federal excise tax is usually collected from motor fuel sales, airline tickets, tobacco, and other goods and services. Investopedia *https://www.investopedia.com/terms/e/excisetax.asp.* (Last visited June 27, 2021).

Black's Law Dictionary defines "income tax" as "[a] tax on an individual's or entity's net income." *Id. 159.* Black's, in turn, cites to Henry Campbell Black, *A Treatise on the Law of Income Taxation under Federal and State Laws* § 1, at 1 (1913).

> An income tax is distinguished from other forms of taxation in this respect, that it is not levied upon property, nor upon the operations of trade and business or the subjects employed therein, nor upon the practice of a profession or the pursuit of a trade or calling, but upon the acquisitions of the taxpayer arising from one or more of these sources or from all combined, annually or at other state intervals, and generally, but not necessarily, only upon the excess of such acquisitions over a certain minimum sum. It is not a tax upon accumulated wealth, but upon its periodical accretions. It is not a tax upon personal exertion for gain, whether combined with the employment of capital or not, but upon the fruits thereof. An income tax is in effect a tax upon earnings, taking that term in its broadest sense, and irrespective of the question whether the person whose income is taxed has actively earned it or has merely profited by loaning his capital for active employment by another. *Id.* at 1759-60

Taxpayer also objects to the Department's decision adding back "fees." Black's Law Dictionary 758 (9th ed. 2014) defines "fees" as "a charge or payment for labor or services [especially] professional Services." American Heritage Dictionary of the English Language 669 (3rd ed. 1996) states in part that a fee is "[a] fixed sum charged, as by an institution or by law, for a privilege." Clearly the term is ambiguous. Standing alone and without context, it is not possible to determine that any cost attributable to the payment of a "fee" should or should not be added back for the purposes of Indiana's addback provision.

Taxpayer points to and relies on its own secondary, contemporaneous documentation to bolster its argument that

the Department erred in adding back taxes as it did because neither the Indiana Legislature or the Department ever contemplated that out-of-state excise and other privilege taxes would be subject to the addback provision.

> The add back language was originally drafted in 1963 to cover all state taxes, and the State quickly recognized its drafting error. In June of 1964, the Indiana Commission on State Tax and Financing Policy formed an advisory committee to assist in making recommendations to improve and clarify the AGIT. The advisory committee included James Courtney, then Commissioner of the Indiana Department of Revenue. In January of 1965, the Commission issued its recommendations in its report entitled "Proposed Amendments to the Adjusted Gross Income Tax Act of 1963" (the "*Report*") . . . which included, on page 1:
>
> > The requirement that the taxpayer add back any deductions taken for taxes levied by any state or subdivision has been eliminated for all classes of taxpayers. **This provision has proved to be difficult to administer particularly as it applies to various excise taxes (sic), and in any event is inconsistent with the "adjusted gross income" concept**, which presumably would allow a deduction for all expenses incurred in earning income, including tax expenses.
>
> House Bill 1141 was then introduced that session (1965). House Bill 1141 adopted the Commission's recommendation, and the bill was later amended to add back property taxes and taxes "based on or measured by income" but not excise taxes. *See*, Acts of 1965, c. 233, s. 1.
>
> Finally, the Department's own interpretation of the revised statute was set forth in "The Indiana Adjusted Gross Income Tax - A Guide for Auditors" published by the Department in 1968 . . . which stated. . .
> > The 1965 general assembly clarified the 1963 wording of the law by saying that, in effect, **the only taxes which would be added back were state income taxes and local property taxes.** It is readily apparent that city income taxes or state property taxes are not required to be added back, neither is capital stock tax, sales tax nor use tax. **Likewise, privilege taxes and franchise taxes are not add-backs. One exception would be a franchise tax that is based on or measured by income and levied at the state level. This type of tax is usually found as a substitute for a state income tax** where a state's constitution forbids a direct income tax. (**Taxpayer's emphasis**).

Specifically, Taxpayer challenges the Department's decision adding back the following state taxes in part based on the secondary evidence provided above.

**a. California.**

Cal. Bus & Prof. Code § 19951 imposes nonrefundable initial license fees, license renewal fees based on the number of each casinos' gaming tables, and an incremental "annual fee" based on the casino's "gross income." In part, the California statute provides:

(a) Every application for a license or approval shall be accompanied by a nonrefundable fee, the amount of which shall be adopted by regulation on or before January 1, 2009. The adopted fee shall not exceed one thousand two hundred dollars ($1,200). Prior to adoption of the regulation, the nonrefundable application fee shall be five hundred dollars ($500).

. . . .

(b)(2)(A) The fee for initial issuance of a state gambling license shall be an amount determined by the commission in accordance with regulations adopted pursuant to this chapter.

(B) The fee for the renewal of a state gambling license shall be determined pursuant to the schedule in subdivision (c) or the schedule in subdivision (d), whichever amount is greater.

(C) The holder of a provisional license shall pay an annual fee pursuant to the schedule in subdivision (c).

(c) The schedule based on the number of tables is as follows:

(1) For a license authorizing one to five tables, inclusive, at which games are played, three hundred dollars ($300) for each table.

. . . .

(6) For a license authorizing 71 or more tables at which games are played, four thousand seven hundred dollars ($4,700) for each table.

(d) Without regard to the number of tables at which games may be played pursuant to a gambling license, if,

at any time of any license renewal, or when a licensee is required to pay the fee described in subparagraph (C) of paragraph (2) of subdivision (b) it is determined that the gross revenues of an owner licensee during the licensee's previous fiscal year fell within the following ranges, the annual fee shall be as follows:

> (1) For a gross revenue of two hundred thousand dollars ($200,000) to four hundred ninety-nine thousand nine hundred ninety-nine dollars ($499,999), inclusive, the amount specified by the department pursuant to paragraph

. . . .

> (5) For a gross revenue of thirty million dollars ($30,000,000) or more, the amount specified by the department pursuant to paragraph (6) of subdivision (c).

. . . .

> (C) The holder of a provisional license shall pay an annual fee pursuant to the schedule in subdivision (c).

**b. Illinois.**

230 Ill. Comp. Stat. Ann § 10/13(a-3) imposes a "privilege tax" on riverboat casino operations. That tax is "based on the adjusted gross receipts received" and measured on a graduated percentage of each casino's receipts. In relevant part, the Illinois statute provides.

> Beginning July 1, 2003, a privilege tax is imposed on persons engaged in the business of conducting riverboat gambling operations, other than licensed managers conducting riverboat gambling operations on behalf of the State, based on the adjusted gross receipts received by a licensed owner from gambling games authorized under this Act at the following rates:
>
> 15[percent] of annual adjusted gross receipts up to and including $25,000,000;

. . . .

> 70[percent] of annual adjusted gross receipts in excess of $250,000,000.

**c. Kansas.**

Kan. Stat. Ann. § 74-8734, in relevant part, imposes a state tax on the gaming facilities' "revenues."

> [I]nclude a provision for the state to receive not less than 22[percent] of lottery gaming facility revenues, which shall be paid to the expanded lottery act revenues fund established by K.S.A. 74-8768, and amendments thereto[.]

**d. Maine.**

8 M.R.S. § 1036(2) imposes essentially a tax on "net slot machine income." In part, the statute provides:

> A slot machine operator licensed under section 1011, subsection 2 or a casino operator that is a commercial track that was licensed to operate slot machines under section 1011, subsection 2 on January 1, 2011 shall collect and distribute 39 percent of the net slot machine income from slot machines operated by the slot machine operator to the board for distribution by the board as follows:
>
> A. Three percent of the net slot machine income must be deposited to the General Fund for administrative expenses of the board in accordance with rules adopted by the board, except that of the amount calculated pursuant to this paragraph, the following amounts must be transferred annually to the Gambling Addiction Prevention and Treatment Fund established by Title 5, section 20006-B:
>
> (1) For the fiscal year beginning July 1, 2011, $50,000;
>
> (2) For the fiscal year beginning July 1, 2012, $50,000; and
>
> (3) For the fiscal year beginning July 1, 2013 and for each fiscal year thereafter, $100,000;
>
> B. Ten percent of the net slot machine income must be forwarded by the board to the Treasurer of State, who shall credit the money to the fund established in section 298 to supplement harness racing purses[.]

**e. Massachusetts.**

Mass. Gen. Laws G.L. c. 23K, § 55 imposes a tax on "gross gaming revenues" as follows:

> (a) A category 1 licensee shall pay a daily tax of 25 per cent on gross gaming revenues.
> (b) A category 2 licensee shall pay a daily tax of 40 per cent on gross gaming revenue.
> (c) In addition to the tax imposed under subsection (b), a category 2 licensee shall pay a daily assessment of 9 per cent of its gross gaming revenue to the Race Horse Development Fund established in section 60.
> (d) Taxes imposed under this section shall be remitted to the commission by a gaming licensee the day following each day of wagering.

**f. Mississippi.**

Miss. Code § 75-76-177, in relevant part, imposes a "license fee" which based on a gaming licensee's "gross revenue."

> From and after August 1, 1990, there is hereby imposed and levied on each gaming licensee a license fee based upon all the gross revenue of the licensee as follows:
> (a) Four percent (4[percent]) of all the gross revenue of the licensee which does not exceed Fifty Thousand Dollars ($50,000.00) per calendar month;
> (b) Six percent (6 percent) of all the gross revenue of the licensee which exceeds Fifty Thousand Dollars ($50,000.00) per calendar month and does not exceed One Hundred Thirty-four Thousand Dollars ($134,000.00) per calendar month; and
> (c) Eight percent (8[percent]) of all the gross revenue of the licensee which exceeds One Hundred Thirty-four Thousand Dollars ($134,000.00) per calendar month.

**g. Missouri.**

Mo. Rev. Stat. § 312.822 imposes a tax on each casino's adjusted gross income as follows:

> A tax is imposed on the adjusted gross receipts received from gambling games authorized pursuant to sections 313.800 to 313.850 at the rate of twenty-one percent.

**h. Nevada.**

NRS § 463.370 imposes a "license" fee based on each casino licensee's "gross revenue." In relevant part, the Nevada statute provides:

> 1. Except as otherwise provided in NRS 463.373 the Commission shall charge and collect from each licensee a license fee based upon all the gross revenue of the licensee as follows:
>
> (a) Three and one-half percent of all the gross revenue of the licensee which does not exceed $50,000 per calendar month;
> (b) Four and one-half percent of all the gross revenue of the licensee which exceeds $50,000 per calendar month and does not exceed $134,000 per calendar month; and
> (c) Six and three-quarters percent of all the gross revenue of the licensee which exceeds $134,000 per calendar month.

. . . .

In addition, the Nevada statute provides that "gross revenue" includes "[a]ll revenue received from any game or gaming device." NRS § 463.370(4).

**i. Ohio.**

Ohio's gaming tax is straight-forward. Casinos pay a 33 percent tax on their "gross casino revenue." R.C. 5753.02 states:

> For the purpose of funding the needs of cities, counties, public school districts, law enforcement, and the horse racing industry; funding efforts to alleviate problem gambling and substance abuse; defraying Ohio casino control commission operating costs; and defraying the costs of administering the tax, a tax is levied on the gross casino revenue received by a casino operator of a casino facility at the rate of thirty-three per cent of the casino operator's gross casino revenue at the casino facility. The tax is in addition to any other taxes or

fees imposed under the Revised Code or other law and for which the casino operator is liable under Section 6(C)(2) of Article XV, Ohio Constitution.

**j. Pennsylvania.**

Pennsylvania imposes a 34 percent tax on each casino's "daily gross" slot machine revenue. 4 Pa. C.S. § 1403(b) provides:

> The department shall determine and each slot machine licensee shall pay a daily tax of 34[percent] from its daily gross terminal revenue from the slot machines in operation at its facility and a local share assessment as provided in subsection (c). All funds owed to the Commonwealth, a county or a municipality under this section shall be held in trust by the licensed gaming entity for the Commonwealth, the county and the municipality until the funds are paid or transferred to the fund. Unless otherwise agreed to by the board, a licensed gaming entity shall establish a separate bank account to maintain gross terminal revenue until such time as the funds are paid or transferred under this section. Moneys in the fund are hereby appropriated to the department on a continuing basis for the purposes set forth in subsection (c).

Pennsylvania saw fit to address income received from casino gaming tables separately. 4 Pa. C.S. § 13A62 provides:

> (1) Except as provided in paragraph (2), each certificate holder and a Category 4 slot machine licensee who is a holder of a table game operation certificate at a Category 4 licensed facility shall report to the department and pay from its daily gross table game revenue, on a form and in the manner prescribed by the department, a tax of 12[percent] of its daily gross table game revenue.
>
> (2) In addition to the tax payable under paragraph (1), each certificate holder and Category 4 slot machine licensee who is a holder of a table game operation certificate at a Category 4 licensed facility shall report to the department and pay from its daily gross table game revenue, on a form and in the manner prescribed by the department, a tax of 34[percent] of its daily gross table game revenue from each table game played on a fully automated electronic gaming table.

**k. West Virginia.**

West Virginia taxes casinos 35 percent of each licensee's "adjusted gross receipts" in exchange for "the privilege of holding a license." W.Va. Code § 29-22C-26 provides in part:

> For the privilege of holding a license under this article to operate table games, there is levied and shall be collected from the racetrack table games licensee the annual privilege tax imposed by this section. The tax shall be thirty-five percent of the licensee's adjusted gross receipts from the operation of West Virginia Lottery table games. For purposes of calculating the amount of tax due under this section, the licensee shall use the accrual method of accounting.

**2. The Department's Decision to Add Back State Excise, Privilege, and Other Fees Violates both the Indiana and U.S. Constitutions.**

Taxpayer explains that it is not challenging the constitutionality of Indiana's addback provision but that the audit's decision applying that provision "would violate the U.S. and Indiana Constitutions." The Department's "misinterpretation and misapplication of the statute resulted in proposed assessments by the Department that violate both Constitutions." Taxpayer reminds the Department that it has issued administrative decisions which address just such constitutional issues. Taxpayer is correct. *See* Letter of Findings 01-20170142 August 7, 2017), 20171129-IR-045170501NRS (Finding that an assessment of individual income tax did not violate the Due Process Clause); Letter of Findings 04-20140409 (September 24, 2014), 20141126-IR-04514066NRS (Holding that imposing sales tax on the Indiana purchase of a recreational vehicle was not precluded by the U.S. Constitution.)

Taxpayer explains that the Department's application and interpretation of the addback provision violates the U.S. Commerce Clause (U.S. Const. art. I, § 8 cl. 4) because the Department's analysis does not result in a "fair apportionment" of Taxpayer's Indiana income. Taxpayer concludes that the audit's decision "causes Indiana's income tax base and consequently it's apportioned income to be out of all proportion to the 'fair' apportionment of [Taxpayer's] income in violation of the Commerce Clause."

In support of that argument, Taxpayer points to the Indiana Supreme Court's decision in *Consolidation Coal Company v. Indiana Department of State Revenue*, 583 N.E.2d 1199 (Ind. 1991) in which the court stated:

> We conclude that the add-back provisions at issue in this case are designed to describe the kind of tax to be added back permitting the add-back of taxes based on income but not those such as *property or excise taxes*. *Id.* at 1202. (*Emphasis added*).

Taxpayer also argues that the Department's assessment violates the Due Process Clause (U.S. Const. amend. 5; U.S. Const. amend. XIV) which, according to Taxpayer, "requires Indiana's taxing scheme be rationally related to the [T]axpayer's Indiana activities." Taxpayer explains:

> There is no connection between Indiana and the out-of-state transactions it seeks to tax which were already taxed by the Other States. The "income" from those out-of-state transactions, which is actually the tax "payments" on those transactions to the Other States, is not rationally related to the values connected with Indiana, as they bear no fiscal relation to protection, opportunities and benefits given by Indiana. Indiana taxing almost two billion dollars of excise tax payments to Other States, incurred solely with respect to activities in those Other States, offends all notions of fair play and substantial justice and amounts to unjustified "confiscation," in violation of the Due Process Clause.

**3. The Department's Audit Failed to Address Taxpayer's Own Erroneous Addback of Riverboat Wagering Taxes.**

Taxpayer argues that the Department's audit failed to correct the Taxpayer's own initial error in adding back Indiana's Riverboat Wagering Tax ("RWT") as otherwise called for in the Indiana Tax Court's decision in *Aztar Indiana Gaming Corporation v. Indiana Department of State Revenue* 806 N.E.2d 381 (Tax Ct. 2004) (Transfer denied September 28, 2004, 806 N.E.2d 976). In that case, the court found that the sole issue was whether or not the RWT was or was not a tax "based on or measured by income." *Id.* 383. The court found that although denoted as an "excise tax," the RWT was "not payable unless the privilege of conducting riverboat gambling is exercised and the exercising of those privileges is the occasion for the imposition of the tax." *Id.* at 386. The court held that however designated, "Aztar's liability calculation is measured by the adjusted gross receipts it receives from its gaming operations." *Id*. The court concluded that "Aztar's RWT liability is subject to the add-back provision of IC § 6-3-1-3.5(b)(3)."

Although on its original returns, Taxpayer added back the RWT, the Department's audit did not challenge that addback. Because of this purported error, Taxpayer now states that it has "filed protective amended returns for the 'Years at Issue' to correct its erroneous addback of the Indiana RWT and [the] understatement of its net operating losses carryforwards."

**D. Analysis and Conclusions.**

**1. Adding Back Taxes Based on Income.**

This Letter of Findings' analysis begins with a plain statement of the law at issue. IC § 6-3-1-3.5(b)(3) provides.

> Except as provided in subsection (c), add an amount equal to any deduction or deductions allowed or allowable pursuant to Section 63 of the Internal Revenue Code for taxes *based on or measured by income and levied at the state level by any state of the United States.* (*Emphasis added*).

Taxpayer's most basic argument is that the Department added back expenses and costs other than those "taxes based on or measured by income . . ." such as out-of-state excise taxes. The Department finds the Indiana Supreme Court's explanation in *Miles v. Dept. of Treasury,* 199 N.E. 372 (Ind. 1935) instructive. In that case, the court considered whether a tax constituted a property tax or a non-property tax.

> While there may be a "theoretical distinction" or a "very slight" difference between a net income tax and an excise [tax] measured by income, it is difficult to find any practical distinction to be made between a gross income tax and an ordinary excise tax. It is a tax on the recipient of the income, the tax being upon the right or ability to produce, create receive, and enjoy, and not upon specific property. *Id.* at 377.

Indiana, and numerous other states have imposed taxes described as excise taxes, franchise taxes, or taxes imposed on the simple privilege of doing business in the state.

> A franchise tax is imposed on a domestic corporation for the right to exist that is bestowed by the state in which the entity was incorporated. A privilege tax is enacted as a charge on foreign corporations for permission to do business in state. Richard Weiss *Achieving Uniformity in State Income Taxes: A Worthwhile Goal*, 18 Sep J. Multistate Tax'n (September 2008).

. . . .

> Where the franchise or privilege tax is based on a corporation's net income, the *effect is the same as an income tax*. The differing designations have no real practical effect on the taxpayer . . . . [T]hese designations are a *relic of the developmental history of these provisions*. *Id.* (*Emphasis added*).

However, the Indiana statute says nothing about these developmental distinctions; it simply requires the addback of taxes "based on or measured by income" and the Department finds nothing ambiguous or peculiar in the provision. The Department concludes that IC § 6-3-1-3.5(b)(3) "needs no interpretation." *Caterpillar*, 988 N.E.2d at 1271. The Department finds the provision unambiguous and requires that the statute be read to "mean what it plainly expresses, and [that] its plain and obvious meaning may not be enlarged or restricted." *Jefferson Smurfit*, 681 N.E.2d at 811. Whether denoted as a state excise tax, state fee, or state privilege tax, if the tax is "measured by income" it's subject to the IC § 6-3-1-3.5(b)(3) addback requirement. While the Department and Taxpayer may disagree on this point, that disagreement does not necessarily render IC § 6-3-1-3.5(b)(3) ambiguous.

Taxpayer is correct when it points out that "[A] tax imposition statutory provision . . . . is to be strictly construed against the imposition of tax." *Jewell Grain*, 556 N.E.2d at 921; *Tri-State Double Cola*, 706 N.E.2d at 285 n.9. However, even a "strict reading" of IC § 6-3-1-3.5(b)(3) does not lead to the conclusion Taxpayer here seeks.

**2. Application and Implementation of the Addback in Calculation Corporate Income Tax.**

Indiana's and most other state's basic corporate tax structure can be fairly summarized as followed

> In analyzing the basic structure of all corporate income taxes, the computations are based on a common system that is simple and straightforward. Each tax starts with a taxable base derived from book income. The base income is apportioned and/or allocated to the applicable jurisdiction, and a tax rate is applied to the resulting taxable income to arrive a tax liability. Then credits are subtracted and other assessments (e.g., credit recapture, alternative minimum tax) are added to determine the final tax. These few steps give rise to an extraordinarily large number of permutations and combinations. Each step involves multiple computations which, in turn, have multiple options. The basic structure, however, is fairly simple process. Still, the "devil is in the details." Richard Weiss *Achieving Uniformity in State Income Taxes: A Worthwhile Goal*, 18 Sep J. Multistate Tax'n (September 2008).

When a taxpayer calculates its federal taxable income, it is entitled to deduct state and local taxes pursuant to I.R.C. § 164. However, in calculating its Indiana adjusted income, taxpayer begins with federal taxable income as defined under I.R.C. § 63 but is thereafter required to make certain adjustments. IC § 6-3-1-3.5(b).

One of these adjustments is found at IC § 6-3-1-3.5(b)(3) which requires that the taxpayer "[a]dd an amount equal to any deduction or deductions allowed or allowable pursuant to Section 63 of the Internal Revenue Code for taxes *based on or measured by income* and levied at the state level by any state of the United States." (*Emphasis added*). Taxpayer is entitled to deduct state and local income taxes when calculating its federal adjusted income; it may not do so for Indiana income tax purposes and must addback taxes paid to other states which are based on income. IC § 6-3-1-3.5(b) means what says and says what it means.

**3. Adding Back Other State's Taxes Based on or Measure by Income.**

If it is a tax "based on or measured by income," Taxpayer must add back that amount when computing its Indiana liability. Whether the states denotes that tax as an excise tax, a privilege tax, or casino table fee, the statute pays no mind to these artifacts of the tax's origin or the manner in which the state chose to label the tax; if the tax is "based on or measured by income," Indiana law requires that the tax be added back.

As such, the initial license fees, renewal fees, and the "incremental" annual fee under Cal. Bus. & Prof. Code § 19951 are added back for purposes of determining Taxpayer's Indiana tax because the fees are based on the California Casinos' "gross income." The "privilege tax" imposed under 230 Ill. Comp. Stat. Ann. § 10/13(a-3) is added back for purposes of determining Taxpayer's Indiana tax because the tax is "based on the adjusted gross receipts . . . of each casino's receipts." The state tax imposed on Kansas casinos imposed under Kansas Statutes

Ann. § 748734 is added back for purposes of determining Taxpayer's Indiana tax because the tax is measured and imposed on each facility's revenues.

Each of the other taxes cited above including Maine, Massachusetts, Mississippi, Missouri, Nevada, Ohio, Pennsylvania, and West Virginia are likewise added back under IC § 6-3-1-3.5(b) because those taxes are based on "gross income," "adjusted gross receipts," gaming "revenues," "gross gaming revenues," "net slot machine income," "gross revenue," "gross casino revenues," "daily gross slot machine revenue," "daily gross table game revenue," or "adjusted gross receipts." In other words, each of these states impose a tax "based on or measured by income and levied at the state level . . . ." IC § 6-3-13.5(b)(3).

**4. Constitutional Considerations.**

Taxpayer asserts that the addback provision, as implemented by the Department, violates the Due Process Clause and the Commerce Clause. According to Taxpayer, the Department reached outside its borders to interfere with and tax the income earned in other states, tax transactions which occurred entirely outside Indiana, in a decision which violates both Indiana and U.S. Supreme Court's decisions precluding the addback of excise taxes.

In addressing these concerns, the Department turns first to the Alabama Supreme Court's decision in *VFW Ventures, Inc. v. Surtees*, 8 So.3d 983 (Ala. S. Ct. 2008) upholding in its entirely the court of appeals decision in *Surtees* v. *VFJ Ventures, Inc.* 8 So.3d 950 (Ct. of Civil Appeals of Alabama 2008). While not controlling in Indiana, the Department finds the court's reasoning sound and instructive. In that decision, the petitioner challenged the Alabama Department of Revenue's decision requiring petitioner to add back of certain intangible and interest expenses paid to out-of-state management companies in calculating petitioner's own Alabama income tax. *Id.* at 950. The Alabama statute, Ala. § 40-18-35(b), required that "For purposes of computing its taxable income, a corporation shall add back otherwise deductible interest expenses and costs and intangible expenses and costs directly or indirectly paid, accrued, or incurred to, or in connection directly with one or more direct or indirect transactions, with one or more related members." *Id.* at 960.

The court concluded that the Alabama addback provision did not violate the Commerce Clause because the addback did not violate that Clause's substantial nexus requirements; the disallowance of the petitioner's expense deduction for the petitioner with nexus did not implicitly impose a tax on the out-of-state management companies. *Id.* at 979. In addition, the court found that Alabama's corporate income tax was fairly apportioned because the petitioner failed to establish by "clear and cogent evidence" that the addback provision resulted in a tax that was out of proportion or grossly distorted the petitioner's in-state activities. *Id.*

Closer to home, this Letter of Finding also cites to the Indiana Supreme Court's decision in *Consolidation Coal Company v. Indiana Dept. of State Revenue*, 583 N.E.2d 1199 (Ind. 1991). The court addressed the issue of whether the West Virginia Business & Occupation Tax was a tax "based on or measured by income" such that it was subject to the add-back provision in IC § 6-3-1-3.5(b)(3). *Id*. at 1201. The court disagreed with Consolidated's argument that the West Virginia was not an income tax because it did not "allow a deduction for cost of goods sold" and because its income did "not include the recovery of capital investment." *Id.*

The court cited to *Miles*, 199 N.E. 372 in which the Indiana Supreme Court found that Indiana's own Gross Income Tax was a tax measured by income in the face of Consolidated's argument that the "tax was a property tax." *Id*. *at* 310. In *Miles*, the court found as follows:

> We conclude that the tax in question is an excise levied upon those domiciled within the state, or who derived income from sources within the state, upon the basis of the privilege of transacting business within the state and that the burden *may reasonably be measured by the amount of income. Miles*, 199 N.E. at 379. (*Emphasis added*).

In *Consolidated,* the court found that the "measured by income" benchmark analysis was straightforward. The court explained:

> Is the tax which the payor wishes to add back measure by income? Or measured by value of property held? *Id.* at 1202.

Despite both Miles' and Consolidated's arguments to the contrary, the court found that both the West Virginia and Indiana's former gross income tax were "measured by income," and that the West Virginia tax should be "added back" in determining Consolidated's taxable income. *Id.*

**5. The Department's Failure to Address the Tax Court's *Aztar* Decision.**

In addition to challenging the Department's decision adding back other states' income taxes, Taxpayer argues that the Department's audit erred in failing to overrule the Tax Court's decision in *Aztar* which found that Indiana's RWT was a tax based on or measured by income. According to Taxpayer, the decision was wrongly decided and the Department overlooked the statutory and constitutional shortcomings of that decision.

The Department must reject Taxpayer's argument. Although the Department has addressed statutory and constitutional questions at both the audit and administrative level, what Taxpayer here suggests would constitute a ~~brazen~~ overreaching of the Department's authority and would constitute an unwarranted interference with the ~~responsibility of and~~ authority of the Indiana judiciary. Even if the Department were to agree that it was within the Department's authority to overturn a decision issued by the Indiana Tax Court and reviewed by this state's Supreme Court and even if the *Aztar* decision somehow needs the Department's approval, the Department agrees with the Tax Court's decision and reasoning as set out in that decision.

**6. Conclusion and Final Words.**

Taxpayer's argument fails at each level of consideration. IC § 6-3-1-3.5(b) contains no ambiguity and requires no elaborate construction. The Department finds that this unambiguous statute must be given its "plain and obvious meaning and may not be enlarged or restricted." *Jefferson Smurfit*, 681 N.E.2d at 811. The out-of-state's gambling taxes cited here are plainly and obviously being measured by those casinos' "income" and that archaic designations as "fees," "excise taxes," or "privilege taxes" are irrelevant when - after examining the plain meaning of those imposition statutes are "based on or measured by *income*."

In addition, the Department finds no indication that the Department's application IC § 6-3-1-3.5(b) violates either Indiana's or the United States Constitution, and there is nothing in the provision which suggests that Indiana is imposing a tax on an out-of-state's own gambling income. The Department finds that Taxpayer has failed to meet its statutory burden, under IC § 6-3-1-3.5(b) of establishing by clear and cogent evidence that the addback provision resulted in an Indiana tax that was out of proportion or distortive of Taxpayer's Indiana's activities.

The addback provision merely stipulates the means by which Indiana measures and then taxes Taxpayer's ***Indiana*** casino income. The Department rejects entirely Taxpayer's suggestion that Indiana is taxing "transactions occurring in those [other] states" or that Indiana is taxing casinos "doing business solely in [ ] other states" as a misinterpretation of an addback provision whereby Indiana measures the income of a casino doing business in this state.

Whether that level of taxation is excessive or burdensome is not a question for the Department to determine but is purely a legislative question. Just as it is not for the Department to decide that Indiana's seven percent sales tax is too great or unduly burdensome to its fellow Hoosiers, it is not for the Department to decide that a straightforward addback provision unduly or inequitably burdens Taxpayer's Indiana casino operation.

Nonetheless, Taxpayer suggests that the Department added back costs and charges which constitute "contract costs" and or one-time casino fees. For example, there are certain provisions of California's Bus & Prof. Code which appear to impose on its casinos fees which are entirely unrelated to the casinos' income; Taxpayer has not yet pointed out which of these unrelated one-time fees are or were the subject of its protest. Any of the Department's decisions to addback such fees were incorrect to the limited extent that these fees were not tied to or measured by the out-of-state casinos' income. Governmental fees not measured by or based on income should not have been added back; any governmental fees which *are* based on or measured by income clearly are subject to Indiana's addback requirement.

However, Taxpayer has not delineated why or how any of these out-of-state expenses fall outside Indiana's addback provision. Therefore, to the extent that Taxpayer can explain clearly which of these charges were not tied to or measured by the out-of-state casinos' income, the Department recognizes its responsibility to correct those specific errors.

**FINDING**

The Department finds that Taxpayer's arguments as outlined above are without merit; however, to the extent that Taxpayer clearly and cogently establishes that any of the expenses added back during the audit were not based on or measured by income, the Taxpayer's protest is sustained, and the Department will correct those

misapplication of the addback statute.

**II. Indiana Corporate Income Tax - Penalty.**

**DISCUSSION**

The Department assessed Taxpayer "negligence," "late payment," and "underpayment" penalties. Taxpayer challenges each of these penalties as unwarranted and excessive.

Taxpayer objects to the imposition of the ten percent "underpayment penalty."

IC § 6-3-4-4.1(b) imposes on each taxpayer the responsibility to make and pay a "declaration of estimated tax for the taxable years" if the amount of that estimated is more than $1,000. *Id.*

> Every corporation subject to the adjusted gross income tax liability imposed by this article shall be required to report and pay an estimated tax equal to the lesser of:
>
> (1) twenty-five percent (25[percent]) of such corporation's estimated adjusted gross income tax liability for the taxable year; or
> (2) the annualized income installment calculated in the manner provided by Section 6655(e) of the Internal Revenue Code as applied to the corporation's liability for adjusted gross income tax. IC § 6-3-4-4.1(c).

IC § 6-3-4-4.1(d) imposes a penalty if a taxpayer fails to pay the correct amount of estimated tax.

> The penalty prescribed by IC 6-8.1-10-2.1(b) shall be assessed by the department on corporations failing to make payments as required in subsection (c) or (f). However, no penalty shall be assessed as to any estimated payments of adjusted gross income tax which equal or exceed:
>
> (1) the annualized income installment calculated under subsection (c); or
> (2) twenty-five percent (25[percent]) of the final tax liability for the taxpayer's previous taxable year. *Id.*

IC § 6-8.1-10-2.1(a)(3) requires that a ten-percent penalty be imposed if the tax deficiency results from the taxpayer's negligence. IC § 6-8.1-10-2.1(a)(2) requires a ten-percent penalty if the taxpayer "fails to pay the full amount of tax shown on the person's return on or before the due date for the return or payment."

IC § 6-8.1-10-2.1(d) states that, "If a person subject to the penalty imposed under this section can show that the failure to . . . pay the full amount of tax shown on the person's return . . . or pay the deficiency determined by the department was due to reasonable cause and not due to willful neglect, the department shall waive the penalty."

Departmental regulation 45 IAC 15-11-2(b) defines negligence as "the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." Negligence is to "be determined on a case-by-case basis according to the facts and circumstances of each taxpayer." *Id*.

Departmental regulation 45 IAC 15-11-2(c) requires that in order to establish "reasonable cause," the taxpayer must demonstrate that it "exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed . . . ."

Under IC § 6-8.1-5-1(c), "The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." An assessment – including the negligence penalty – is presumptively valid.

As discussed in Part I above, the Department disagrees entirely with Taxpayer's interpretation of Indiana's addback provision. While the Department finds that Taxpayer's interpretation is aggressive and skirts the edge of simple reasonableness, Taxpayer's interpretation does not rise to the level of negligence.

**FINDING**

Taxpayer's protest is sustained.

**SUMMARY**

Taxpayer's protest is sustained to the extent that Taxpayer can now clearly establish that the Department erred in adding back non-tax contract costs or one-time operational fees not measured by the out-of-state casino income. Taxpayer's substantive protests challenging the application and implementation of Indiana's addback provision is respectfully denied. The Department agrees that the penalties should be abated.

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