DEPARTMENT OF STATE REVENUE

02-20210056.LOF

Letter of Findings: 02-20210056
Indiana Corporate Income Tax
For the Year 2018, 2019, and 2020

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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 agreed with Utility Company that - to the extent and amount limited by Indiana law - Utility Company was entitled to claim a portion of the bonus depreciation claimed on its federal returns.

ISSUE

I. Indiana Corporate Income Tax - Bonus Depreciation

Authority: IC § 6-3-1-33; IC § 6-8.1-5-1; *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Income Tax Information Bulletin 118 (July 2021); *Bonus Business Definition - Investopedia,* https://www.investopedia.com/terms/b/bonusdepreciation.asp.

Taxpayer argues that the Department erred in denying its claim to a five-year bonus depreciation deduction, but then failed to allow the lesser amount of depreciation to which it was otherwise entitled under Indiana law.

STATEMENT OF FACTS

Taxpayer is an Indiana local utilities company. Taxpayer submitted its Indiana corporate income tax returns. The Indiana Department of Revenue ("Department") reviewed the returns eventually disagreeing with Taxpayer's depreciation claim. The Department's adjustment resulted in an assessment of additional income tax. Taxpayer disagreed with the result and submitted a protest to that effect. An administrative hearing was conducted by telephone during which Taxpayer's representative explained the basis for its protest. This Letter of Findings results.

I. Indiana Corporate Income Tax - Bonus Depreciation

DISCUSSION

The issue is whether Taxpayer has met the burden of proof in arguing that the Department erred in failing to allow it a depreciation deduction on its Indiana corporate returns.

As with any assessment, it is Taxpayer's responsibility to establish that the adjustment which led to this particular tax assessment was 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 Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463, 466 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

On its Indiana returns, Taxpayer claimed a "bonus depreciation" attributable to equipment it purchased to operate its utility company. For simplicity's sake, this Letter of Findings refers to *Bonus Business Definition - Investopedia* https://www.investopedia.com/terms/b/bonusdepreciation.asp (Last visited July 30, 2021).

> Bonus depreciation is a tax incentive that allows a business to immediately deduct a large percentage of the purchase price of eligible assets, such as machinery, rather than write them off over the "useful life" of that asset.

However, as explained in Income Tax Information Bulletin 118 (July 2021), 20210728-Ind. Reg.-045210298NRA (retroactive to January 1, 2018). "Since 2002, Indiana has largely decoupled from the federal allowances for bonus depreciation and Section 179 expensing."

Indiana's statute, IC § 6-3-1-33 (effective January 1, 2019) provides as follows:

> As used in this article, "bonus depreciation" means an amount equal to that part of any depreciation allowance allowed in computing the taxpayer's federal adjusted gross income or federal taxable income that is attributable to the additional first-year special depreciation allowance (bonus depreciation) for qualified property allowed under Section 168(k) of the Internal Revenue Code, including the special depreciation allowance for 50-percent bonus depreciation property. For taxable years beginning after December 31, 2017, the term does not include any amount of additional first-year special depreciation allowance under Section 168(k) of the Internal Revenue Code in the amount of adjusted gross income realized on the exchange of property that otherwise would have been deferred under Section 1031 of the Internal Revenue Code in effect on January 1, 2017, if:
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> (1) the exchange would have been eligible for nonrecognition of gain or loss under Section 1031 of the Internal Revenue Code in effect on January 1, 2017;
> (2) the exchange is not eligible for nonrecognition of gain or loss under Section 1031 of the Internal Revenue Code; and
> (3) the taxpayer claimed a deduction for the additional first-year special depreciation allowance under Section 168(k) of the Internal Revenue Code with regard to the acquired property.
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> For purposes of this section, if the taxpayer elected to claim a deduction under Section 179 of the Internal Revenue Code with regard to an item of acquired property, the adjusted gross income realized on the exchange must be reduced (but not below zero dollars ($0)) by the amount of the deduction under Section 179 of the Internal Revenue Code elected to be claimed on the acquired property. (*See also* IC § 6-3-1-33 effective to December 31, 2018).

What does all that mean? Information Bulletin 118 explains.

> In general, if a taxpayer makes an election to claim a Federal Section 179 Allowance, Indiana *caps the overall Indiana Section 179 Allowance at $25,000* against such property. In the first year, the difference between the Federal Section 179 Allowance and the Indiana Section 179 Allowance is an *addback for Indiana tax purposes*. In subsequent years, the difference between depreciation computed using the Federal Section 179 Allowance and the Indiana Section 179 Allowance will be permitted as a deduction. (*Emphasis added*).

The example provided in the Bulletin is even more helpful:

> Taxpayer purchases property for $225,000. Taxpayer makes an election to expense the entire $225,000 for federal purposes. Because Indiana caps the Section 179 Allowance at $25,000, Taxpayer is required to add back the $200,000 difference. However, the remaining $200,000 is subject to depreciation allowances.

Taxpayer agrees with Department's initial decision; Taxpayer can claim the federal bonus depreciation, but Indiana requires an "addback" of a large portion of that amount. Where Taxpayer and the Department apparently disagree is that Taxpayer claims that the Department's adjustment failed to allow Taxpayer the limited depreciation expense provided for under Indiana law. In other words, Taxpayer agrees that it was not entitled to claim the bonus deprecation as reflected on its federal returns, but it was entitled to claim a portion of that amount as a regular depreciation, and further deduct the previously disallowed amount over the life of the property.

Taxpayer has provided calculations and spreadsheets explaining its position and detailing the amount of depreciation Taxpayer believes it is entitled.

The Department's Audit Division is requested to review the depreciation schedule submitted by Taxpayer and to adjust the assessment as permitted by Indiana law and substantiated by the Taxpayer's documentation.

FINDING

Subject to the Audit Division's review and adjustment, Taxpayer's protest is sustained.

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An html version of this document.