DEPARTMENT OF ENVIRONMENTAL MANAGEMENT
Nonrule Policy Documents

A nonrule policy document is a policy or statement that interprets, supplements, or implements a statute or rule. It is not intended by the department to have the effect of law and is not related solely to internal department organization. Per Indiana Code 13-14-1-11.5, a nonrule policy document may not be put into effect until 30 days after the policy or statement is made available for public inspection and comments and presented to the Water Pollution Control Board.

Nonrule policy documents that are open for inspection and comment are denoted by "comment period deadline: date" in the 'ADOPTED' column of the table below. Comments on a nonrule policy document that is open for comment may be submitted by the comment period deadline to: Nonrule Policy Document ID #: _______, Lawrence Wu, Chief, Rules Development Section, Office of Water Quality; Indiana Department of Environmental Management, 100 North Senate Avenue, Indianapolis, Indiana 46204. If you have questions about any of the documents found on this page, please contact the IDEM staff person or section listed at the end of each nonrule policy document. All documents are in PDF format. Click on a highlighted ID# to view the document.

ID#	POLICY TITLE	POLICY DESCRIPTION	ADOPTED	LAST REVISED	CITATION	CONTACTS
Water-001-NRD	Constructed Wetland Wastewater Treatment Facilities Guidance	Policy and technical guidance for the design, construction and operation of constructed wetland type sanitary wastewater treatment facilities	May 1, 1997	N/A	327 IAC 2,3,5,8 410 IAC 6-10	Jay Hanko (317) 233-8283
Water-002-NRD	Antidegradation Requirements for Outstanding State Resource Waters Inside the Great Lakes Basin	Provides a definition of significant lowering of water quality applicable to Outstanding State Resource Waters Inside the Great Lakes Basin	March 23, 1998	N/A	327 IAC 5-2-11.7(a)(2)(B)	Lonnie Brumfield (317) 233-2547 Dennis Clark (317) 308-3235
Water-003-NRD	Combined Sewer Overflow (CSO) Long-Term Control Plan Use Attainability Analysis Guidance	This document fulfills the mandates of Senate Enrolled Act 431 by providing guidance to municipal National Pollutant Discharge Elimination System (NPDES) permittees with combined sewer collection systems.	December 14, 2001	N/A	327 IAC 2,5	Bruno Pigott (317) 232-8631
Water–005-NRD	Review of Sanitary Sewer Construction Permit Applications For Communities with Combined Sewer Overflow Outfalls	This document outlines IDEM's procedures for review of sewer construction permit applications for communities with combined sewer overflow outfalls	April 9, 2003	N/A	327 IAC 3-1-1 through 327 IAC 3-6-32	Ken Lee (317) 232-8660

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Page URL: http://www.in.gov/idem/rules/policies/index.html#water
Updated: Feb. 10, 2005

NATURAL RESOURCES COMMISSION
Information Bulletin #48

RESOLUTION OF THE NATURAL RESOURCES COMMISSION IN SUPPORT OF THE CONCEPTS EMBODIED IN THE MARQUETTE GREENWAY PROJECT AND EXPANSION OF THE PROJECT TO INCLUDE THE EASTERN PORTION OF THE COASTAL ZONE

WHEREAS, Northwest Indiana includes a diversity of plant and animal species unmatched in the state, including the Karner blue butterfly, sea rocket, Pitcher's thistle, Kalm's St. John's wort, beach pea, dune goldenrod, and Peregrine falcon;

WHEREAS, Northwest Indiana displays ecosystems of special significance, portions of which are preserved within the Indiana Dunes National Lakeshore and the Indiana Dunes State Park, and portions of which are outside these preserves;

WHEREAS, Northwest Indiana contains the Port of Indiana, the busiest port on Lake Michigan and a critical element of Indiana commerce;

WHEREAS, Northwest Indiana maintains a steel industry with state-of-the-art technology that produces 25% of the nation's steel;

WHEREAS, Northwest Indiana possesses a major oil refinery and other critical energy generating industries;

WHEREAS, Northwest Indiana is located adjacent to Chicago, a great metropolitan center, establishing both opportunities for tourism and challenges for providing adequate infrastructure and community services;

WHEREAS, Northwest Indiana includes Lake Michigan, an unparalleled water resource within the state, for boating, sport fishing, and commercial fishing;

WHEREAS, Northwest Indiana shares Lake Michigan, its major source of drinking water, with industrial and other usages within and outside Indiana;

WHEREAS, Northwest Indiana concentrates these diverse and sometimes competing uses within 45 miles of shoreline;

WHEREAS, Northwest Indiana is challenged by environmental degradation, much of it dating from the beginning of the 20th Century, including one of 43 areas of concern designated in the United States and Canada by the International Joint Commission;

WHEREAS, Northwest Indiana is experiencing population growth which both enhances opportunities and exacerbates challenges requiring increased planning;

WHEREAS, Northwest Indiana is governed by a multiplicity of statutory and regulatory standards, some of which are exclusive to the region, and these are administered by a multiplicity of federal, state, and local agencies;

WHEREAS, the Department of Natural Resources through the Lake Michigan Coastal Program funded the Marquette Greenway Project to address regional planning issues in Northwest Indiana;

WHEREAS, five communities in Northwest Indiana through Memorandum of Agreement agreed to support three guiding principles to be incorporated into the project;

WHEREAS, the Marquette plan embodies concepts key to the protection of natural, cultural, and historic resources while incorporating wise redevelopment of industrial sites and builds a foundation for these protections to be included in local planning; and

WHEREAS, the Northwest Indiana Quality of Life Council and the Northwestern Indiana Regional Planning Commission passed resolutions supporting the current efforts embodied in the Marquette Greenway project and encourage the expansion of the project to the full 45 miles of coastline;

NOW BE IT HEREBY RESOLVED BY THE NATURAL RESOURCES COMMISSION THAT

The Natural Resources Commission supports the concepts and ideas regarding resource protection and improved planning for Northwest Indiana put forth by the Marquette Greenway Project.

The Department of Natural Resources is urged to encourage the expansion of this project to include additional areas in the Lake Michigan Coastal Area not already included.

The Department of Natural Resources is urged to work with citizens of Northwest Indiana to help identify and prioritize social and environmental needs addressed in this planning effort.

The Department of Natural Resources is urged to actively pursue improved communication and coordination within the agency and with other state, federal, and Northwest Indiana agencies and governmental units.

The Department of Natural Resources is urged to assure that the Marquette Project adheres to all laws pertaining to environmental management and protection of the Lake Michigan Coastal Area.

The Department of Natural Resources is urged to support the participating local, state, and regional entities as they adopt the planning principles contained in the project.

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 01-0288
Sales and Use Tax
For the Years 1997-Present

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

Sales and Use Tax—Imposition of Sales Tax on Purchase of Aircraft

Authority: IC 6-6-6.5; IC 6-8.1-5-1; IC 6-2.5-5-8; IC 6-8.1-5-1(b); IC 6-2.5-2-1; IC 6-2.5-3-6(d)(2); IC 6-2.5-5-8(b); IC 6-6-6.5-2; Ind. Dep't of Revenue v. Interstate Warehousing, 783 N.E.2d 248, 250 (Ind. Tax 2003)

Taxpayer protests the imposition of sales tax on the purchase of an aircraft Taxpayer asserts is used for leasing.

STATEMENT OF FACTS

Taxpayer purchased an aircraft in a governmental surplus property auction on January 2, 1997. The aircraft previously had been seized in a drug bust—and because of this, a considerable amount of the aircraft's records and documentation was missing.

On May 15, 1997, the Compliance Division sent a letter to Taxpayer noting that the aircraft had yet to be registered with the State of Indiana—as is required by law within 10 days after the purchase date, under IC 6-6-6.5. Taxpayer also was informed that, pursuant to IC 6-8.1-5-1, either the sales/use tax was to be paid or a written protest was to be filed within 60 days.

On May 23, 1997, taxpayer completed and submitted an *Application for Aircraft Registration or Exemption*, **Form 7695**. Taxpayer checked the box to claim the sales/use tax exemption.

On October 1, 1997, Taxpayer notified the Department that he was waiting for the FAA to award clear title of the aircraft. Taxpayer also informed the Department that lease arrangements had been negotiated—but held in abeyance until title and airworthiness were certified. Taxpayer informed the Department that extensive work would be required to make the aircraft airworthy.

The next correspondence noted in the Taxpayer's file is dated four years later on February 14, 2001. The Compliance Division informed Taxpayer that the sales/use tax exemption was denied on the basis that no sales or use tax had been remitted.

The Taxpayer asserts that he purchased the aircraft for resale, rental, or leasing and that the aircraft was not purchased for personal use.

According to a copy of the lease provided to the Department—on June 1, 1998, Taxpayer signed a lease agreement with Lessee No. 1. Lessee No. 1 acquired the aircraft for rental or leasing in the ordinary course of business. On that basis, the Taxpayer asserts that its collection of sales tax is exempted under I.C. 6-2.5-5-8. Taxpayer has provided the Department with a copy of the *Indiana General Sales Tax Exemption Certificate*, **Form ST-105**, signed by Lessee No. 1. The lease was for one year—with an automatic renewal provision unless 30 days notice is provided. According to Taxpayer, the lease renewed in June 1999 and was terminated June 2000. Taxpayer asserts that the aircraft only was flown 24 hours in the two years of the lease and asserts that $5,520 in gross revenue was generated from the lease.

According to a copy of the lease provided to the Department—in June 2000, Taxpayer signed a lease agreement with Lessee No. 2. According to Taxpayer, the lease generated the minimum guaranteed revenue of $30,000. No sales tax was remitted to the Department and no copy of an *Indiana General Sales Tax Exemption Certificate* signed by Lessee No. 2 was provided to the Department as evidence that sales tax is not due to be paid by Taxpayer.

DISCUSSION

Under Indiana code, all tax assessments are presumed to be valid and accurate; the taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b). The state of Indiana imposes a sales tax on the transfer of property in a retail transaction. IC 6-2.5-2-1. In the case of aircraft, taxpayers are to pay the tax directly to the department when registering the aircraft—unless the aircraft qualifies for an exemption. IC 6-2.5-3-6(d)(2). In this case, Taxpayer contends that the aircraft qualifies for an exemption from the sales tax because the taxpayer is a retail merchant in the business of leasing aircraft to the public in the ordinary course of business without changing the form of the aircraft. IC 6-2.5-5-8(b).

Taxpayer has stated to the Department that he has a background in the field of aviation and aircraft. The Department notes this assertion.

Taxpayer was contacted by the Department four months after he acquired the aircraft and the Department notified Taxpayer that his aircraft was not properly registered with the State of Indiana. Code section 6-6-6.5-2 requires that an aircraft be registered with the state—something Taxpayer had neglected to do. The statute makes no mention of registration upon receiving clear title—it refers solely to the purchase of an aircraft. The Purchase Letter provided to the Department states that Taxpayer's auction bid had been accepted and that the Government Agency requires that payment be received within 10 days. The lack of registration is mentioned to evidence the business habits of Taxpayer. Taxpayer knew he had purchased an aircraft, yet neglected to communicate to the Department that he was awaiting clear title. The point of mentioning this event is to evidence that Taxpayer did not act with due diligence—a shortcoming that has continued for seven years in his dealings with the Department.

The Department consistently and persistently has requested that Taxpayer provide documentation to substantiate the sales tax exemption sought by Taxpayer. Taxpayer has been on notice of the nature and character of the documentation sought—but has chosen to provide incomplete, inconclusive, and scattered pieces of documentation.

It is well established that exemption statutes are strictly construed against a taxpayer; as such, Taxpayer has the burden of establishing entitlement to the exemption. *See*, Ind. Dep't of Revenue v. Interstate Warehousing, 783 N.E.2d 248, 250 (Ind. Tax 2003). The Department contacted Taxpayer in 1997—right after Taxpayer acquired the aircraft. Taxpayer has been on notice since 1997 that complete and accurate documentation would be needed to substantiate an exemption. Yet, Taxpayer has not been proactive in collecting and preserving documentation. Numerous and repeated letters sent by Taxpayer state that he cannot find—or has not requested from parties—sufficient substantiating documentation.

Direct and to the point—Taxpayer finally did secure a favorable lease—with Lessee No. 2—and earned $30,000. That lease expired in 2001. As of 2004, the Department has not received sales tax due from that lease—nor has the Department been provided a copy of the General Sales Tax Exemption Certificate signed by Lessee No. 2 evidencing why sales tax was not collected and is not due from Taxpayer.

After seven years of pursuing this matter, the Department is unmoved and unpersuaded by Taxpayer's efforts at providing documentation to prove entitlement to an exemption. Based on this—Taxpayer has yet to submit sales/use tax or demonstrate an exemption from sales/use tax.

FINDING

Taxpayer's protest is denied. Sales tax is due for the purchase of the aircraft in 1997. Penalties and interest are due.

DEPARTMENT OF STATE REVENUE

03-20020068.LOF

LETTER OF FINDINGS NUMBER: 02-0068
Nonresident Withholding Tax
For Tax Periods: 1998-1999

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning specific issues.

ISSUES

I. Nonresident Withholding Tax-Addback of income taxes

Authority: Ind Code. § 6-3-1-3.5; *Aztar Indiana Gaming Corp. v. Indiana Dept. of State Revenue*, 806 N.E.2d 381 (Ind. Tax 2004).

Taxpayer protests the addback of riverboat wagering taxes in determining the adjusted gross income of shareholders for withholding tax purposes.

II. Nonresident Withholding Tax-Applicability

Authority: I.R.C. § 702; I.R.C. § 1366(b); Ind. Code § 6-3-2-2; Ind. Code § 6-3-4-12; Ind. Code § 6-3-4-13; *Dupee v. Tracy,* 708 N.E.2d 698 (Ohio 1999); *Agley v. Tracy*, 719 N.E.2d 951 (Ohio 1999).

Taxpayer argues that the income that is subject to withholding is not Indiana source income, and that it cannot be subject to withholding tax obligations based on its lack of presence in Indiana

III. Nonresident Withholding Tax-Computation

Authority: Ind. Code § 6-3-4-13.

Taxpayer argues that any losses incurred by it prior to adjustments be used to offset the adjustments for determining its ultimate withholding tax liability.

STATEMENT OF FACTS

Taxpayer, an S corporation, is a part-owner of an LLC that operates a casino in Indiana. During the years in question, taxpayer computed its withholding tax liability without adding back riverboat wagering taxes in computing the income subject to withholding. Audit assessed withholding tax liability based on the share of riverboat wagering tax paid by taxpayer. Taxpayer protested the add back of riverboat wagering taxes, the applicability of withholding liability to it, and the computation of its liability.

I. Nonresident Withholding Tax-Addback of income taxes

DISCUSSION

With respect to the validity of the assessment, the Indiana Tax Court has determined that the riverboat wagering tax is a tax "based on or measured by income and levied at the state level by any state of the United States." *Aztar Indiana Gaming Corp. v. Indiana Dept. of State Revenue*, 806 N.E.2d 381, 386 (Ind. Tax 2004). Accordingly, with respect to individuals, the tax must be added back per Ind. Code § 6-3-1-3.5(a)(2) in order to determine the individual's adjusted gross income-the basis for withholding tax liability.

FINDING

Taxpayer's protest is denied.

II. Nonresident Withholding Tax-Applicability

Taxpayer has also argued that it is not subject to tax based on either the character of the income was not Indiana source income, or, in the alternative, that the Department did not have jurisdiction to assess taxpayer for the years in question.

First, taxpayer argues that the character of the income in the hands of the taxpayer was that of holding a membership interest in an LLC, not from doing business in Indiana. However, in the case of a partnership or S corporation, the character of the income for federal purposes is determined at the source, and then taxed to the individual recipient. *See* I.R.C. §§ 702(b), 1366(b). The character of the income in this case was determined at the partnership level-namely, the operation of a riverboat casino within Indiana, clearly subject to Indiana tax per Ind. Code § 6-3-2-2(a)(2). This character remains the same at the S corporation level. *See, e.g., Dupee v. Tracy,* 708 N.E.2d 698, 700 (Ohio 1999) (Florida residents subject to Ohio income tax as a result of S corporation operations in Ohio, based on income being Ohio business income). The income, contrary to taxpayer's argument, does not magically transform from "casino revenues" in the hands of the partnership to "intangible income" (e.g., dividends or interest) in the hands of the taxpayer. It retains its initial character-income from a business conducted in Indiana- as it passes through the various entities until it reaches a taxpayer.

Further, taxpayer's argument creates a legal absurdity. Indiana's non-resident withholding statutes, Ind. Code §§ 6-3-4-12 and -13 are rendered non-existent by taxpayer's arguments. A pass-through entity could always argue that its owners' incomes from the entity was merely income from an intangible (i.e., an ownership interest in the entity doing business in Indiana) and never be subject to Indiana tax, effectively resulting in a situation in which a nonresident who owns a business in Indiana is subject to income tax, but a nonresident who puts a pass-through entity between the individual and the business is insulated from all tax liabilities to Indiana.

Second, taxpayer further argues that Indiana cannot constitutionally tax the income because the taxpayer did not have nexus in Indiana. Taxpayer notes that the LLC and taxpayer are separate entities, and the LLC activities cannot be attributed to the taxpayer generally.

While Indiana has not directly addressed the issue, the highest court of at least one other state has noted that the taxpayer has sought, via the LLC, to invoke valuable rights that were provided to it. *Agley v. Tracy*, 719 N.E.2d 951 (Ohio 1999). In that case, the taxpayers were owners of an S Corporation that conducted business in Ohio; however, the taxpayers did not participate in any activities in Ohio. The taxpayers argued that, since they were not present in Ohio nor had any contacts with Ohio beyond their ownership of the S corporation, they could not be subject to personal income tax in Ohio. However, the court found that the S corporation availed itself of the benefits of Ohio, and that the taxpayers, through that corporation, had sufficient contacts to justify taxation by Ohio on the income derived from the business.

In this protest, the LLC that operated the casino availed itself of the protections and benefits of Indiana. It received one of the rare and extremely difficult to obtain licenses to operate a riverboat casino in Indiana, and proceeded to operate the riverboat. It further utilized the resources of Indiana to allow customers to reach the casino and has had full access to the courts of Indiana in order to seek protection at the casinos and protection in its everyday operations. By extension, the LLC used those protections to earn business income from Indiana, just as the S corporation in *Agley* used the protections of Ohio to earn its income. Taxpayer in this case has utilized those protections provided by Indiana-a separate legal identity and a highly valuable license, among others-to earn its income through the LLC, just as the shareholders in *Agley* used the protections conferred by Ohio to earn their income. Accordingly, taxpayer has sufficient contacts to justify its withholding obligations in Indiana.

FINDING

Taxpayer's protest is denied

III. Nonresident Withholding Tax-Computation

DISCUSSION

Taxpayer has also protested the amount of the assessment. Taxpayer's argument is that the losses at the withholding entity level (in this case, S corporation) must be considered in determining its withholding liability. For example, if a taxpayer incurred a $10,000,000 loss, but had $4,000,000 of taxes added back, then its liability would be based on a $6,000,000 loss rather than $4,000,000. If a taxpayer incurred a $10,000,000 loss but had $19,000,000 of taxes added back, its liability would be based on $9,000,000 rather than $19,000,000.

Ind. Code § 6-3-4-13(a) states in relevant part that "[e]very corporation which is exempt from tax under IC 6-3 pursuant to IC 6-3-2-2.8(2) shall, at the time that it pays or credits amounts to any of its nonresident shareholders as dividends or as their share of the corporation's undistributed taxable income, withhold the amount prescribed by the department."

Here, the net income for withholding tax purposes is its "dividends or undistributed taxable income" within the meaning of the statute. Accordingly, the corporation's liability for withholding is limited to its net income rather than the total amount of taxes added back, if the corporation had a loss prior to the taxes added back. However, if the corporation had a profit or zero income prior to add back, then the full amount of taxes added back are subject to withholding obligations.

FINDING

Taxpayer's protest is sustained subject to audit review of the amount of net income.

DEPARTMENT OF STATE REVENUE

04-20020216.LOF

LETTER OF FINDINGS NUMBER: 02-0216
Sales and Use Tax for the Year 1998

NOTICE: Under IC § 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Sales and Use Tax- Use tax on purchase of riverboat

Authority: I.C. 6-2.5-5-27; *Grand Victoria Casino & Resort LP v. Indiana Department of State Revenue,* 789 N.E.2d 1041(Ind. Tax 2003); *Indiana Department of State Revenue v. Trump Indiana, Inc.*, 814 N.E.2d 1017(Ind. Supreme Court 2004)

Taxpayer protests the assessment of use tax on the purchase of a riverboat.

STATEMENT OF FACTS

Taxpayer owned and operated a gambling casino on a riverboat located on the Ohio River. Taxpayer opened for business in 1998. Taxpayer was assessed use tax on its purchases of the riverboat for its casino operation and related operational items. Taxpayer protested the assessment, and this letter of findings results.

I. Sales and Use Tax- Use tax on purchase of riverboat

DISCUSSION

Taxpayer argued that the riverboat was engaged in public transportation and thus its purchase, and purchases related to its operation, were not subject to use tax pursuant to IC 6-2.5-5-27. By mutual agreement, the Department and Taxpayer deferred the resolution of this protest until two cases addressing this issue were resolved. Both *Grand Victoria Casino & Resort LP v. Indiana Department of State Revenue,* 789 N.E.2d 1041(Ind. Tax 2003) and *Indiana Department of State Revenue v. Trump Indiana, Inc.*, 814 N.E.2d 1017(Ind. Supreme Court 2004) upheld the Department's position. Taxpayer now suggests that the respective courts did not explicitly review their arguments- submitted as amicus curiae briefs in both cases- and thus the issue is not resolved. The Department does not agree.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420020497.LOF

LETTER OF FINDINGS NUMBER: 02-0497
Sales Tax
For Tax Years 1999-00

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Sales Tax—Allocation Percentage

Authority: IC 6-8.1-5-1; 45 IAC 2.2-5-4; 45 IAC 2.2-5-5

Taxpayer protests the imposition of sales tax on a manure spreader and the taxable allocation percentage of a tractor.

STATEMENT OF FACTS

Taxpayer operates a horse riding business. The Indiana Department of Revenue ("Department") determined that several items purchased for the farm during this taxable period should have been subject to sales tax at the time of purchase, but no sales tax had been paid. The Department issued a preliminary report to taxpayer, who then hired a representative to deal with the Department. The representative contacted the Department, claiming that several of the items were not subject to sales tax. Taxpayer's representative sent invoices to support the claim, and the Department removed all but two of the disputed items from the proposed assessment. Several items remained which were never disputed, plus the two which the Department determined were still taxable. These two items are the focus of this protest.

One of the items at issue is a manure spreader, which the Department determined was subject to sales tax. The other item is a tractor, which the Department determined was used four percent (4%) of the time for exempt purposes, and ninety-six percent (96%) for non-exempt purposes. The Department imposed sales tax on ninety-six percent (96%) of the purchase price of the tractor. Taxpayer believes that the allocation percentage on the tractor is incorrect and that the manure spreader should also be subject to allocation.

Taxpayer explains that the size of the property is seventy-eight point five (78.5) acres, with fifteen (15) acres used for the horses and fifteen (15) acres used to grow hay for the horses. Taxpayer believes that only the use of the tractor and manure spreader on the thirty (30) horse-related acres should be taxable, and offers the alternate taxable percentage of thirty-eight point twenty-one (38.21%) for the tractor and manure spreader. Further facts will be supplied as needed.

I. Sales Tax—Allocation Percentage

DISCUSSION

Taxpayer operates a horse riding business. In addition to the horse riding operations, taxpayer grows some grain which it sells. Taxpayer protests imposition of sales tax allocation percentage on a tractor and on a manure spreader. Four percent (4%) of taxpayer's revenues arise from the sale of grain. Ninety-six percent (96%) of taxpayer's revenues arise from the horse riding business. The Department allocated four percent (4%) of the tractor's cost as exempt and ninety-six percent (96%) as taxable based on revenues generated by the use of the tractor. The Department did not allocate sales tax on the manure spreader, which was treated as fully subject to sales tax. As explained in the protest letter, taxpayer believes that allocating on revenues is clearly a decision that is in favor of the Department and one that is not based upon sound accounting principals. Taxpayer believes that the taxable percentage should be based on the percentage of land used for taxable purposes. Taxpayer offers thirty-eight point twenty-one percent (38.21%) as the taxable percentage for the tractor and manure spreader.

In the audit report, the Department refers to 45 IAC 2.2-5-4, which states in relevant part:

(a) Agricultural exemption certificates may be used only if the purchaser is occupationally engaged in the business of producing food or commodities for human, animal, or poultry consumption for sale or for further use in such production.

(b) The department has determined that persons occupied in producing food and commodities as used in the Indiana sales and use tax act, shall mean and include only those persons, partnerships, or corporations whose intention it is to operate a farm at a profit and not those persons who intend to operate a farm for pleasure as a hobby. Operations similar to those of a pony farm, riding stable, or the production and raising of dogs and pets, are not classified as farms for the purpose of the state gross retail tax act.

…

The Department also refers to 45 IAC 2.2-5-5, which states:

(a) The raising of saddle horses, harness horses, ponies, donkeys, or any other similar animals not used directly in direct agricultural production does not qualify as agricultural production for "human consumption" under the gross retail sales and use tax act. Consequently, the purchase of supplies, food, materials, and equipment used in raising or maintaining such animals are subject to the sales tax unless the items are directly used or consumed in the production of such animals for resale in the regular course of the purchaser's business.

(b) The purchase of any of the above animals is subject to the sales tax unless the purchaser is a registered retail merchant and is buying such animal for resale in the regular course of his business.

(c) A valid exemption certificate must be furnished by the purchaser setting out the reasons for any exemption.

(d) An agricultural exemption certificate may be used only for the purchase of draft animals which are to be directly used in direct production of agricultural products.

Since taxpayer operates a horse riding business, 45 IAC 2.2-5-4(b) clearly provides that such a business is not classified as a farm for the state gross retail tax act. Also, 45 IAC 2.2-5-5(a) clearly provides that a horse riding operation does not qualify as agricultural production for human consumption under the gross retail sales and use tax act. The grain production does count as farming under 45 IAC 2.2-5-4(b).

Taxpayer states that acreage is a more accurate allocation method for the taxable percentage on the tractor and manure spreader. The Department refers to IC 6-8.1-5-1(a), which states:

If the department reasonably believes that a person has not reported the proper amount of tax due, the department shall make a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the department. The amount of the assessment is considered a tax payment not made by the due date and is subject to IC 6-8.1-10 concerning the imposition of penalties and interest. The department shall send the person a notice of the proposed assessment through the United States mail.

While taxpayer has offered an alternate method of calculating the taxable percentage of the tractor, taxpayer has offered no evidence or analysis explaining why that method is superior to the Department's method. Taxpayer believes that the Department's method is flawed because it assumes that all activities will generate the exact same amount of revenue for the time and effort expended on the activity.

A flaw with the proposed alternate allocation method is that it does not actually relate to the use of the tractor. Taxpayer's method does not explain what percentage the tractor is used on the thirty horse-related acres and what percentage the tractor is used for the exempt grain growing. Again, taxpayer has submitted no documentation supporting the claim that acreage is a more accurate method for determining allocation.

The Department was able to examine the documents explaining which revenues were raised from exempt sources and which were raised from non-exempt sources. With absolutely no evidence to the contrary, it is logical for the Department to allocate sales tax percentages on the same percentages as exempt and non-exempt revenues. As provided in IC 6-8.1-5-1(a), the Department used the best information available to make its proposed assessments.

Taxpayer also protests the imposition of sales tax on a manure spreader. Taxpayer has provided no evidence to establish that the manure spreader was used in an exempt manner. Unlike the tractor, which the Department agreed was partially used for tax exempt purposes, it has not been established that the manure spreader has been used in those exempt purposes. As previously explained, 45 IAC 2.2-5-5(a) establishes that equipment not directly used in direct agricultural production is subject to sales tax.

Finally, the Department refers to IC 6-8.1-5-1(b), which states in relevant part:

> 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.

In this case, taxpayer has presented insufficient documentation and analysis supporting the proposed alternate allocation method. Taxpayer has insufficiently explained why the manure spreader should be exempt for any percentage. Taxpayer has failed to meet the burden of proving the Department's proposed assessments wrong, as required by IC 6-8.1-5-1(b).

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0120020601.LOF

LETTER OF FINDINGS NUMBER: 02-0601
Adjusted Gross Income Tax
For Tax Period 1998- 2000

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Adjusted Gross Income Tax-Expenses

Authority: IC 6-8.1-5-1(b), IC 6-8.1-5-4.

The taxpayer protests the disallowance of a deduction for certain expenses.

STATEMENT OF FACTS

The taxpayer is a shareholder of a sub chapter S corporation. In an investigation of the corporation, the Indiana Department of Revenue, hereinafter referred to as the "department," increased the corporation's gross receipts and disallowed the deduction of certain corporate expenses. As a result, the department assessed additional income tax, interest, and penalty against the taxpayer as a corporate shareholder. The taxpayer protested the assessment and a hearing was held. This Letter of Findings results.

I. Adjusted Gross Income Tax-Expenses

DISCUSSION

All tax assessments are presumed to be accurate and taxpayers bear the burden of proving that any assessment is incorrect. IC 6-8.1-5-1(b). Taxpayers are required to keep adequate records to allow the department to later determine the taxpayer's proper tax liability by reviewing those records. IC 6-8.1-5-4.

The S corporation manufactures floor and roof trusses used in the construction of buildings. It also preserves engines for another manufacturer by placing the engines and spare parts in sealed moisture proof metal containers. The S corporation deducted its cost of goods sold and engine expenses from its gross income on its federal adjusted gross income tax return. The department disallowed the separate deduction for engine expenses because it appeared that the engine expenses were deducted once in the cost of goods sold and again as separate engine expenses. This disallowance raised the S corporation's income. The higher S corporation income resulted in higher derivative income from the corporation for the taxpayer. The taxpayer protested the disallowance of the deduction for engine expenses.

At the time of the audit, the taxpayer's records were in disarray. The taxpayer was unable to provide a summary schedule for both the cost of goods sold and the engine expense deduction with supporting invoices as requested by the department. Although the taxpayer did provide some documentation after the hearing, the taxpayer did not sustain its burden of proof.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0120020602.LOF

LETTER OF FINDINGS NUMBER: 02-0602
Adjusted Gross Income Tax
For Tax Period 1998- 2000

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Adjusted Gross Income Tax-Expenses

Authority: IC 6-8.1-5-1(b), IC 6-8.1-5-4.

The taxpayer protests the disallowance of a deduction for certain expenses.

STATEMENT OF FACTS

The taxpayer is a shareholder of a sub chapter S corporation. In an investigation of the corporation, the Indiana Department of Revenue, hereinafter referred to as the "department," increased the corporation's gross receipts and disallowed the deduction of certain corporate expenses. As a result, the department assessed additional income tax, interest, and penalty against the taxpayer as a corporate shareholder. The taxpayer protested the assessment and a hearing was held. This Letter of Findings results.

I. Adjusted Gross Income Tax-Expenses

DISCUSSION

All tax assessments are presumed to be accurate and taxpayers bear the burden of proving that any assessment is incorrect. IC 6-8.1-5-1(b). Taxpayers are required to keep adequate records to allow the department to later determine the taxpayer's proper tax liability by reviewing those records. IC 6-8.1-5-4.

The S corporation manufactures floor and roof trusses used in the construction of buildings. It also preserves engines for another manufacturer by placing the engines and spare parts in sealed moisture proof metal containers. The S corporation deducted its cost of goods sold and engine expenses from its gross income on its federal adjusted gross income tax return. The department disallowed the separate deduction for engine expenses because it appeared that the engine expenses were deducted once in the cost of goods sold and again as separate engine expenses. This disallowance raised the S corporation's income. The higher S corporation income resulted in higher derivative income from the corporation for the taxpayer. The taxpayer protested the disallowance of the deduction for engine expenses.

At the time of the audit, the taxpayer's records were in disarray. The taxpayer was unable to provide a summary schedule for both the cost of goods sold and the engine expense deduction with supporting invoices as requested by the department. Although the taxpayer did provide some documentation after the hearing, the taxpayer did not sustain its burden of proof.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0120020603.LOF

LETTER OF FINDINGS NUMBER: 02-0603
Adjusted Gross Income Tax
For Tax Period 1998- 2000

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Adjusted Gross Income Tax-Deduction

Authority: IC 6-8.1-5-1(b), IC 6-8.1-5-4.

The taxpayer protests the disallowance of a deduction for certain expenses.

STATEMENT OF FACTS

The taxpayer is a shareholder of a sub chapter S corporation. In an investigation of the corporation, the Indiana Department of Revenue, hereinafter referred to as the "department," increased the corporate gross income and disallowed the deduction of certain corporate expenses. As a result, the department assessed additional adjusted gross income tax, interest, and penalty against the taxpayer as a corporate shareholder. The taxpayer protested the assessment and a hearing was held. This Letter of Findings results.

I. Adjusted Gross Income Tax-Expenses

DISCUSSION

All tax assessments are presumed to be accurate and taxpayers bear the burden of proving that any assessment is incorrect. IC 6-8.1-5-1(b). Taxpayers are required to keep adequate records to allow the department to later determine the taxpayer's proper tax liability by reviewing those records. IC 6-8.1-5-4.

The S corporation manufactures floor and roof trusses used in the construction of buildings. It also preserves engines for another manufacturer by placing the engines and spare parts in sealed moisture proof metal containers. The S corporation deducted its cost of goods sold and engine expenses from its gross income on its federal adjusted gross income tax return. The department disallowed the separate deduction for engine expenses because it appeared that the engine expenses were deducted once in the cost of goods sold and again as separate engine expenses. This disallowance raised the S corporation's income. The higher S corporation income resulted in higher derivative income from the corporation for the taxpayer. The taxpayer protested the disallowance of the deduction for engine expenses.

At the time of the audit, the taxpayer's records were in disarray. The taxpayer was unable to provide a summary schedule for both the cost of goods sold and the engine expense deduction with supporting invoices as requested by the department. Although the taxpayer did provide some documentation after the hearing, it the taxpayer did not sustain its burden of proof.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20030090.LOF

LETTER OF FINDINGS NUMBER: 03-0090
Sales and Use Tax and Allen County Food & Beverage Tax
For Tax Periods: 1999-2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning specific issues.

ISSUES

I. Sales and Use Tax – Like Kind Exchanges

Authority: Ind. Code § 6-2.5-1-5(a)(1).

Taxpayer protests the lack of credit for sales and use taxes with respect to goods exchanged as partial consideration for other goods in its business.

II. Sales and Use Tax – Software Support Maintenance Agreements

Authority: Ind. Code 6-2.5-3-2, Sales Tax Information Bulletin #2 dated August, 1991.

Taxpayer protests the assessment of tax on software support maintenance agreements.

III. Sales and Use Tax-Purchases for Use Outside Indiana

Authority: Ind. Code § 6-2.5-3-2; Ind. Code § 6-2.5-3-7

Taxpayer protests sales tax assessments with respect to software licenses that taxpayer maintains were used solely outside Indiana.

IV. Sales and Use Tax -Rentals

Authority: Ind. Code § 6-2.5-4-4; Ind. Code § 6-2.5-5-26

Taxpayer protests the assessment of sales and use tax with respect to charges for rental of a room at a not-for-profit museum.

V. Sales and Use Tax - Catering Charges

Authority: 45 IAC 2.2-5-45(b)

Taxpayer protests the assessment of sales tax with respect to service charges at various catered events.

VI. Allen County Food & Beverage Tax-Applicability

Authority: Ind. Code § 6-9-23-4

Taxpayer protests the imposition of Allen County Food and Beverage Tax with respect to several items

VII. Sales and Use Tax- Lawn Services

Authority: None

Taxpayer protests the assessment of sales tax with respect to charges that it maintains are for lawn maintenance services rather than tangible personal property.

STATEMENT OF FACTS

Taxpayer is a company engaged in a number of different businesses. Taxpayer was audited by the Department for sales and use tax for the years 1999 to 2001. As a result of the audit, taxpayer was assessed use tax with respect to a number of items, and also protested a number of payments of sales and use tax that taxpayer had claimed were in error.

First, taxpayer claimed that it had erroneously paid sales and use tax with respect to two items for which taxpayer had traded another piece of property. Taxpayer has claimed that the trade-in-value of the property was part of a like-kind exchange, and therefore was exempt from sales and use tax.

Second, taxpayer protested the imposition of use tax with respect to several software contracts. In particular, taxpayer maintained that the largest portion of the contracts used for sampling consisted of maintenance contracts without the provision of automatic upgrades or only for upgrades if they became available, and therefore these contracts were exempt from use tax.

Third, taxpayer has claimed that it erroneously paid sales and use tax with respect to several software licenses under two contracts. Taxpayer has claimed that a significant number of the licenses that it purchased and for which it remitted Indiana sales and use tax were in fact used in other states.

Fourth, taxpayer protested the imposition of use tax with respect to a rental of a museum for a corporate function. In particular, taxpayer has noted that the museum was a not-for-profit entity, and claimed that the rental was consistent with the overall charitable purpose of the museum.

Fifth, taxpayer protested the imposition of use tax with respect to service charges for catered events. In particular, taxpayer maintained that the charges were not for the sale of tangible personal property, and thus not subject to sales and use tax. Taxpayer has also protested the imposition of a food & beverage tax imposed by Allen County with respect to the food and other items.

Lastly, taxpayer protested the imposition of sales tax with respect to certain lawn services. Taxpayer maintained that the transaction was only for lawn mowing services, and not for any tangible personal property.

I. Sales and Use Tax - Like Kind Exchanges

DISCUSSION

Taxpayer's first contention is that sales tax was improperly assessed on amounts that represented the trade-in value for property in a like-kind exchange, which would not be considered a retail transaction under Ind. Code § 6-2.5-1-5(a)(1).

While taxpayer has provided sufficient information to indicate that the amount paid to the vendor was reduced by the value of the trade-in, taxpayer has not provided the necessary information to substantiate that the property used in the trade-in was of a like kind to that which taxpayer purchased. Accordingly, the full value of the transaction is considered a retail transaction subject to tax.

FINDING

Taxpayer's protest is denied.

II. Sales and Use Tax - Software Support Maintenance Agreements

DISCUSSION

Taxpayer's second point of protest concerns the assessment of use tax on software support maintenance agreements pursuant to Ind. Code § 6-2.5-3-2. Taxpayer purchased software support and maintenance agreements for several software programs. Generally, taxpayer has maintained that the agreements did not constitute licenses otherwise taxable. Some of those agreements, according to taxpayer, include software upgrades if any became available. Other agreements, according to taxpayer, did not include software upgrades, or upgrades with a value of less than 10% of the total value under the contract.

The Indiana Department of Revenue policy concerning warranties and maintenance agreements is stated in Sales Tax Information Bulletin #2 dated August, 1991 as follows:

> Optional extended warranties and maintenance agreements are offered as a separate added amount to the purchase price of property being sold and a fixed sum is charged for the furnishing of tangible personal property throughout the term of the warranty or the agreement. Optional warranties and maintenance agreements are not subject to sales or use tax. Optional warranties and maintenance agreements are not subject to tax because the purchase of the warranty or maintenance agreement is the purchase of an intangible right to have property supplied and there is no certainty that property will be supplied. However, if the agreement includes a charge for property to be periodically supplied the agreement would be subject to tax.

Taxpayer submitted a questionnaire to the various software companies that had supplied taxpayer with the software in question. Taxpayer bases its protest on the answers provided by the vendors in the questionnaire.

As a general rule, while taxpayer has provided voluminous evidence in support of its point, mainly consisting of answers to the questionnaires, the critical information to rebut the auditor's presumption of correctness-the contracts between taxpayer and the vendors-appears nowhere in the file. Thus, the assessment must stand.

With respect to one contract with Microsoft, taxpayer has provided a copy of the relevant contract in question. With respect to that contract, the contract provided that taxpayer received extensive technical documentation, source code, and other software and technical information on CD-ROM.

With respect to another contract with Hewlett-Packard, it appears that the amount in controversy was not listed as part of audit's assessment, and thus this portion of the protest is moot.

FINDING

Taxpayer's protest is denied with the exception of the contract with Hewlett-Packard. The portion of the assessment with respect to Hewlett-Packard is moot due to the lack of assessment.

III. Sales and Use Tax - Purchases for Use Outside Indiana

DISCUSSION

Taxpayer further protests the portion of sales tax due with respect to two contracts that taxpayer maintains represent licenses for property used outside Indiana.

With respect to this, Ind. Code § 6-2.5-3-2(d)(3) provides that use tax is not imposed whenever tangible personal property is "subsequently transported out of state for use solely outside Indiana".

Taxpayer maintains that for two contracts, a significant portion of the price paid for software licenses were in fact used in other states. To support their argument, taxpayer has provided information from internal sources relating to how many licenses are used in Indiana and other states. However, taxpayer has not provided an exact breakdown by user and user's location, and accordingly the protest is denied.

Furthermore, when taxpayer contracted for the software licenses, taxpayer contracted for use in Indiana, with out-of-state use (if any) only occurring after the receipt of those licenses. This is presumed to be taxable in Indiana under Ind. Code § 6-2.5-3-7, and taxpayer has provided insufficient information that the contracts were not for taxpayer's use in Indiana at the time of purchase.

FINDING

Taxpayer's protest is denied.

IV. Sales and Use Tax-Rentals

DISCUSSION

Taxpayer protests the assessment of sales tax with respect to the rental of a museum. The museum was operated as a not-for-profit corporation; however, the museum did rent its space for a dinner and private showing to taxpayer for one evening. No sales tax was paid with respect to the rental.

Taxpayer maintains that the rental of the museum was consistent with the overall not-for-profit purpose of the museum, and thus would be tax-exempt.

Ordinarily, the rental of real estate for less than 30 days is taxable. Ind. Code § 6-2.5-4-4. In reviewing the Indiana statutes, tax-exempt organizations do enjoy an exemption from most sales of tangible personal property. Ind. Code § 6-2.5-5-26. However, taxpayer has not provided sufficient information to allow the Department to conclude that such provision was in furtherance of the charity's overall charitable purpose, and accordingly the protest should be denied.

FINDING

Taxpayer's protest is denied.

V. Sales and Use Tax - Catering Charges

DISCUSSION

Taxpayer protests the imposition of sales and use tax with respect to charges for catering services. In the case of each receipt, the service charges were set forth separately from the charges for concededly taxable items.

Under 45 IAC 2.2-5-45(b), "The [sales] tax applies to the entire charge made by caterers for serving meals, food and drink, inclusive of charges for food, the use of dishes, silverware, glasses, chairs, tables, etc., used in connection with serving meals, and for labor of serving meals." This regulation applies to the full cost of the catering, not just the portions that taxpayer concedes are taxable, and accordingly the full value is taxable.

FINDING

Taxpayer's protest is denied.

VI. Allen County Food and Beverage Tax-Applicability

DISCUSSION

Taxpayer also protests the imposition of Allen County Food and Beverage Tax with respect to various items purchased at catered events.

Ind. Code § 6-9-23-4(a) provides that the tax "applies to any transaction in which food and beverage is furnished, prepared, or served: (1) for consumption at a location, or on equipment, provided by a retail merchant; (2) in the county in which the tax is imposed; and (3) by a retail merchant for consideration."

Here, taxpayer's own receipts indicate that the items in question were food and beverage charges at catered events-either at a location or on equipment provided by the caterer for consideration, and in Allen County. Accordingly, taxpayer has not established that it is exempt from the tax.

FINDING

Taxpayer's protest is denied.

VII. Sales and Use Tax - Lawn Services

DISCUSSION

Taxpayer argues that sales tax was improperly assessed with respect to lawn mowing services provided to taxpayer. Taxpayer provided adequate documentation to sustain its argument.

FINDING

Taxpayer's protest is sustained

DEPARTMENT OF STATE REVENUE

0120030118.LOF

LETTER OF FINDINGS NUMBER: 03-0118
Adjusted Gross Income Tax
For Tax Period 1998- 2000

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Adjusted Gross Income Tax-Deduction

Authority: IC 6-8.1-5-1(b), IC 6-8.1-5-4.

The taxpayer protests the disallowance of a deduction for certain expenses.

STATEMENT OF FACTS

The taxpayer is a shareholder of a sub chapter S corporation. In an investigation of the corporation, the Indiana Department of Revenue, hereinafter referred to as the "department," increased the corporate gross income and disallowed the deduction of certain corporate expenses. As a result, the department assessed additional adjusted gross income tax, interest, and penalty against the taxpayer as a corporate shareholder. The taxpayer protested the assessment and a hearing was held. This Letter of Findings results.

I. Adjusted Gross Income Tax-Deduction

DISCUSSION

All tax assessments are presumed to be accurate and taxpayers bear the burden of proving that any assessment is incorrect. IC 6-8.1-5-1(b). Taxpayers are required to keep adequate records to allow the department to later determine the taxpayer's proper tax liability by reviewing those records. IC 6-8.1-5-4.

The S corporation manufactures floor and roof trusses used in the construction of buildings. It also preserves engines for another manufacturer by placing the engines and spare parts in sealed moisture proof metal containers. The S corporation deducted its cost of goods sold and engine expenses from its gross income on its federal adjusted gross income tax return. The department disallowed the separate deduction for engine expenses because it appeared that the engine expenses were deducted once in the cost of goods sold and again as separate engine expenses. This disallowance raised the S corporation's income. The higher S corporation income resulted in higher derivative income from the corporation for the taxpayer. The taxpayer protested the disallowance of the deduction for engine expenses.

At the time of the audit, the taxpayer's records were in disarray. The taxpayer was unable to provide a summary schedule for both the cost of goods sold and the engine expense deduction with supporting invoices as requested by the department. Although the taxpayer did provide some documentation after the hearing, the taxpayer did not sustain its burden of proof.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0120030224.LOF

LETTER OF FINDINGS: 03-0224
Indiana Adjusted Gross Income Tax
For 1999 and 2000

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of the document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Disallowed Business Expenses – Adjusted Gross Income Tax.

Authority: IC 6-3-1-3.5; IC 6-8.1-5-1(b); 45 IAC 3.1-1-1; Treas. Reg. § 1.162.

Taxpayer challenges the Department of Revenue Decision disallowing certain claimed business expenses.

STATEMENT OF FACTS

Taxpayer operated a lawn care and landscaping business as a sole proprietorship. The Department of Revenue (Department) conducted an audit review of taxpayer's income tax returns and business records. As a result of that audit, a number of adjustments were made whereby items claimed as business expenses were disallowed. Accordingly, taxpayer was assessed additional Indiana income tax. Taxpayer disagreed with the assessments and submitted a protest to that effect. An administrative hearing was conducted during which taxpayer's representative explained the basis for the protest and submitted additional information in support of taxpayer's argument. This Letter of Findings results.

DISCUSSION

I. Disallowed Business Expenses – Adjusted Gross Income Tax.

The audit disallowed expenses claimed on taxpayer's "Schedule C" on the ground that there was insufficient information to verify that the amounts claimed were business and not personal expenses. The audit report stated that there were no "income statements or general ledgers" and that the 1999 and 2000 returns "were based on the check book which included personal expenses."

Following completion of the audit report, taxpayer provided additional information including "Quick Book" and "Profit and Loss" summary statements for 1999 and 2000. These summary statements include listings for items such as supplies, repairs, maintenance, and utilities. In support of the summary statements, taxpayer supplied copies of its check registers. The check registers list amounts paid for both personal and business expenses.

IC 6-3-1-3.5 states as follows: "When used in IC 6-3, the term 'adjusted gross income' shall mean the following: (a) In the case of all individuals 'adjusted gross income' (as defined in Section 62 of the Internal Revenue Code)...." The Department's regulation restates the principal. 45 IAC 3.1-1-1 defines individual adjusted gross income as follows:

> Adjusted Gross Income for Individuals Defined. For individuals, "Adjusted Gross Income" is "Adjusted Gross Income as defined in Internal Revenue Code § 62 modified as follows:
>
> (1) Begin with gross income as defined in section 61 of the Internal Revenue Code.
> (2) Subtract any deductions allowed by section 62 of the Internal Revenue Code.
> (3) Make all modifications required by IC 6-3-1-3.5(a).

Under Treas. Reg. § 1.162, a taxpayer, whether a corporation, an individual, partnership, or a trust or estate, generally may deduct from its gross income the ordinary and necessary expenses of carrying on a trade or business that are paid or incurred during the tax year.

In arriving at the amount of its adjusted gross income, taxpayer – as the sole proprietor of the lawn care and landscaping business – was entitled to deduct "ordinary and necessary expenses" incurred in carrying on that business.

However, the audit disallowed certain of the claimed business expenses on the ground that taxpayer failed to properly distinguish between personal and business expenses. For example, the audit disallowed cable television, credit card, utility, and clothing store expenses. Afterwards, taxpayer supplied "Quick Books" and "Profit and Loss" summaries which were offered to verify the amount of claimed business expenses. In addition, taxpayer provided photocopies of its check ledgers delineating business expenses for each of the two years here at issue.

Under IC 6-8.1-5-1, taxpayer has the responsibility for demonstrating that the proposed assessments were incorrect. In relevant part, the section provides, "The notice of proposed assessment is prima facie evidence 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." IC 6-8.1-5-1(b).

The audit was correct in initially disallowing certain of the claimed expenses; it is unlikely that the costs of cable television service were associated with operating taxpayer's lawn care and landscaping business. However, there is no doubt that taxpayer incurred "ordinary and necessary expenses" in running its lawn care and landscaping business. The problem is in reconciling taxpayer's claimed business expenses with the original documentation offered to support those amounts. For example, taxpayer – on its "Quick Books" summary – claims approximately $60,000 in supply expenses for 1999. Taxpayer's "Profit and Loss" statement for that year, breaks down that amount into more specific categories such as "landscaping," "equipment," and "legal." However, there is not sufficient information or original documentation upon which to verify these totals. The only original materials are photocopies of the check registers. However, the check registers only show amounts paid, to whom the check was issued, and – in some cases – a notation as to the reason for the payment. In some instances, the check registers lists amounts which are plainly personal and not business such as medical expenses, church donations, and payments made to shoe stores. Other amounts are simply listed under a generic heading such as "fuel" or "utility" making it impossible to determine if this amount is a business or a personal expense. Similarly, numerous checks are made payable to credit card companies; because the check register freely mixes personal and business payments, it is not possible to determine with any assurance whether a particular credit payment is for a business or for a personal purpose.

There is no reason to doubt taxpayer's good faith or honesty. There is no doubt that taxpayer incurred expenses in its lawn care and landscaping business, that taxpayer paid these expenses, and that taxpayer has a general notion as to the total amount of business expenses for each of the two years. However, taxpayer's informal method of intermingling personal and business records and the failure to retain original invoices, makes it difficult – if not impossible – to determine with any degree of precision the actual business expenses for 1999 and 2000. Pursuant to IC 6-8.1-5-1, taxpayer has not met its burden of demonstrating that the proposed assessments are incorrect.

FINDING

Taxpayer's protest is respectfully denied.

DEPARTMENT OF STATE REVENUE

0420030285.LOF

LETTER OF FINDINGS NUMBER: 03-0285
Sales and Use Tax
For the Year 1998

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Sales and Use Tax-Print and Copy Center

Authority: IC 6-8.1-5-1 (b), IC 6-2.5-3-2(a), IC 6-2.5-4-10(a), IC 6-2.5-5-3(b), IC 6-2.5-5-5.1, IC 6-2.5-5-3(a)(2), IC 6-2.1-2-4(7),

The taxpayer protests the assessment of use tax on certain machines and supplies.

II. Sales and Use Tax-Phone Cards

Authority: IC 6-2.5-4-13.

The taxpayer protests the exclusion of the phone cards from the sample.

III. Sales and Use Tax-Uniforms and Doormats

Authority: IC 6-2.5-4-10(a), IC 6-2.5-2-1.

The taxpayer protests the imposition of use tax on uniforms and doormats.

IV. Sales and Use Tax-Exempt Sales Error Percentage

Authority: IC 6-8.1-5-1(b).

The taxpayer protests the computation of the exempt sales error percentage.

V. Tax Administration-Penalty

Authority: IC 6-8.1-10-2.1, 45 IAC 15-11-2 (b)

The taxpayer protests the imposition of the ten (10%) percent negligence penalty.

STATEMENT OF FACTS

The taxpayer is a retailer and distributor of office supplies with a number of retail stores throughout Indiana. Until December 27, 1998, the taxpayer was a corporation. On that date, the corporation transferred all of its Indiana assets to a limited partnership and maintained a 1 % interest as a general partner. Sales and use tax audits were performed on both entities. Since operations for sales and use tax purposes remained identical for both entities and the tremendous volume of records involved, one sampling of 34 store days for the period 1998-2000 was chosen to examine exempt sales for both taxpayers. The audits resulted in an assessment of sales and use tax, interest, and penalty. The taxpayer protested a portion of the assessment. A hearing was held. This Letter of Findings results.

I. Sales and Use Tax-Print and Copy Center

DISCUSSION

The department assessed use tax on certain items of machinery purchased for the taxpayer's print and copy center. The department also assessed use tax on the lease of three machines for the print and copy center. The taxpayer protested the following assessments.

The taxpayer protested the use tax assessed on the following items:

Fastback Model II	Tape binding machine to create bound books
Starter Kit #1	Supplies for binding units
Triumph 3905	Manual heavy duty paper cutter
Multi 1217	Paper folding machine
General Graphic Kit	Consumable supplies
EP10 System, 1 dye	Coil binding unit with a dye (paper punch)
Martin Yale Stack Wagon	Steel rolling wagon to store, stage, and compile paper jobs
Rapid 106	Stand mounted stapler that is used to staple booklets
Spiral bind OD new store package	Supplies for spiral bonding
Fastfold 22 folder	Paper folder-automatic
Powis printer	Printer that enables putting printing on the spines of the Fastback II bound copies
Baum 714	High speed heavy duty folding unit

The taxpayer also protested the use tax assessed on several photocopiers rented from Eastman Kodak. The photocopiers were for use in the copy and print center.

All tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC 6-8.1-5-1 (b).

Indiana imposes an excise tax on tangible personal property stored, used or consumed in Indiana when no sales tax was paid at the time of purchase. IC 6-2.5-3-2(a). The sales and use taxes are also imposed on the use of tangible personal property that is leased. IC 6-2.5-4-10(a). A number of exemptions are available from use tax. IC 6-2.5-5-3(b) provides for the exemption of "manufacturing machinery, tools and equipment which is to be directly used by the purchaser in the direct production, manufacture, fabrication... of tangible personal property." IC 6-2.5-5-5.1 provides exemption to property consumed "in the direct production of other tangible personal property." Commercial printing is "treated as the production and manufacture of tangible personal property." IC 6-2.5-5-3(a)(2). Commercial printing is defined at IC 6-2.1-2-4(7) as follows:

The business of commercial printing that results in printed materials, excluding the business of photocopying.

The taxpayer's operations separate the business of photocopying from the business of producing printed materials. The self service photocopying machines are located outside the full service copy centers. The taxpayer properly paid sales tax on its self service photocopiers when purchased.

In contrast, the taxpayer offers full service print and copy centers in each of its retail establishments. The copy centers are in partially enclosed separate areas of the facility. Patrons bring their materials to the copy centers where the materials can be photocopied in color or black and white, bound, and tabs attached. A common sort of job includes one hundred (100) copies of a fifty (50) page document. It is not unusual for orders to cost $1,000.00. Jobs are paid for at a register in the center or an invoice is prepared and paid for at the general store registers. Sales tax is charged to patrons and remitted to the state on all jobs completed in the copy center. In this situation, the taxpayer is producing printed materials for sale. Machines that are directly used in the direct production of these printed materials qualify for exemption. Supplies that are consumed in the direct production of these printed materials also qualify for exemption. Each of the protested items is either a machine used in the direct production of the taxpayer's product or supplies consumed in the direct production of the taxpayer's product and exempt from Indiana use tax.

FINDING

The taxpayer's protest is sustained.

II. Sales and Use Tax-Phone Cards

DISCUSSION

The taxpayer protests two issues concerning the assessment of sales tax on the sale of phone cards. First the taxpayer contends that the separate assessment related to the phone card sales should be removed and the phone card transactions should be included in the random sample. The sale of phone cards is subject to Indiana sales tax. IC 6-2.5-4-13. The taxpayer acknowledged that it had at times not charged sales tax on the sale of phone cards. Further the taxpayer could not determine when the taxability of phone cards had been changed in its registers and billing systems. Therefore it was appropriate for the auditor to exclude the sales of phone cards from the sampling method used in the audit and tax the sales of phone cards as a "stand alone" item. The taxpayer was unable to provide the auditor with documentation concerning the exact amount of phone card sales. Therefore the auditor made an appropriate and reasonable estimate of the transactions selling phone cards.

FINDING

The taxpayer's protest is denied.

III. Sales and Use Tax-Rental of Uniforms and Door Mats

DISCUSSION

The taxpayer protests the assessment of sales tax on the rentals of uniforms and door mats.

Retail transactions made in Indiana are subject to sales tax. IC 6-2.5-2-1. Leases of tangible personal property are defined as a taxable retail transaction. IC 6-2.5-4-10(a). The taxpayer agrees that it rented uniforms and doormats and that sales tax was due on the transactions. The taxpayer argues that it actually paid the sales taxes due at the time of the rentals. In support of this contention, the taxpayer submitted statements of the amounts paid to the rental company. These statements, however, do not indicate that sales taxes were paid. Therefore, the taxpayer did not sustain its burden of proving that the assessment is incorrect.

FINDING

The taxpayer's protest is denied.

IV. Sales and Use Tax-Exempt Sales Error Percentage

DISCUSSION

The taxpayer protests the auditor's determination of the denominator for the error percentage calculation. The auditor used the figures provided by the taxpayer to determine the denominator of the error percentage. However the auditor dropped the cents which made the denominator a smaller number and increased the final amount of tax due. An estimate of the denominator should not be used when accurate figures are available.

Secondly the taxpayer contends that the auditor should have excluded the value of untaxed phone card sales from the denominator of the error percentage calculation. The taxpayer provided listings of figures to be deducted from the denominator of the error percentage calculation. There is, however, no back up information or other way to verify these figures. This submission does not sustain the taxpayer's burden of proving that the assessment was incorrect. IC 6-8.1-5-1(b).

FINDING

The taxpayer's protest concerning the accurate calculation of the denominator of the error percentage calculation is sustained. The taxpayer's protest concerning the exclusion of the untaxed phone card sales from the denominator of the error percentage calculation is denied.

V. Tax Administration-Imposition of Penalty

DISCUSSION

The taxpayer protests the imposition of the ten percent (10%) negligence penalty pursuant to IC 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2 (b) clarifies the standard for the imposition of the negligence penalty as follows:

> Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The taxpayer's carelessness and inattention to details caused it to fail to pay sales or use tax on many clearly taxable items such as business cards, uniform rental, hand trucks, and ladders. Further, many of the assessments resulted from issues similar to those in a previous audit. This breach of the taxpayer's duty to pay the proper amount of taxes constitutes negligence.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420030286.LOF

LETTER OF FINDINGS NUMBER: 03-0286
Sales and Use Tax
For the Year 1999-2000

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Sales and Use Tax-Print and Copy Center

Authority: IC 6-8.1-5-1 (b), IC 6-2.5-3-2(a), IC 6-2.5-4-10(a), IC 6-2.5-5-3(b), IC 6-2.5-5-5.1, IC 6-2.5-5-3(a)(2), IC 6-2.1-2-4(7),

The taxpayer protests the assessment of use tax on certain machines and supplies.

II. Sales and Use Tax-Phone Cards

Authority: IC 6-2.5-4-13.

The taxpayer protests the exclusion of the phone cards from the sample.

III. Sales and Use Tax-Uniforms and Doormats

Authority: IC 6-2.5-4-10(a), IC 6-2.5-2-1.

The taxpayer protests the imposition of use tax on uniforms and doormats.

IV. Sales and Use Tax-Exempt Sales Error Percentage

Authority: IC 6-8.1-5-1(b).

The taxpayer protests the computation of the exempt sales error percentage.

V. Tax Administration-Penalty

Authority: IC 6-8.1-10-2.1, 45 IAC 15-11-2 (b)

The taxpayer protests the imposition of the ten (10%) percent negligence penalty.

STATEMENT OF FACTS

The taxpayer is a retailer and distributor of office supplies with a number of retail stores throughout Indiana. Until December 27, 1998, the taxpayer was a corporation. On that date, the corporation transferred all of its Indiana assets to a limited partnership and maintained a 1 % interest as a general partner. Sales and use tax audits were performed on both entities. Since operations for sales and use tax purposes remained identical for both entities and the tremendous volume of records involved, one sampling of 34 store days for the period 1998-2000 was chosen to examine exempt sales for both taxpayers. The audits resulted in an assessment of sales and use tax, interest, and penalty. The taxpayer protested a portion of the assessment. A hearing was held. This Letter of Findings results.

I. Sales and Use Tax-Print and Copy Center

DISCUSSION

The department assessed use tax on certain items of machinery purchased for the taxpayer's print and copy center. The department also assessed use tax on the lease of three machines for the print and copy center. The taxpayer protested the following assessments.

The taxpayer protested the use tax assessed on the following items:

Fastback Model II	Tape binding machine to create bound books
Starter Kit #1	Supplies for binding units
Triumph 3905	Manual heavy duty paper cutter
Multi 1217	Paper folding machine
General Graphic Kit	Consumable supplies
EP10 System, 1 dye	Coil binding unit with a dye (paper punch)
Martin Yale Stack Wagon	Steel rolling wagon to store, stage, and compile paper jobs
Rapid 106	Stand mounted stapler that is used to staple booklets
Spiral bind OD new store package	Supplies for spiral bonding
Fastfold 22 folder	Paper folder-automatic
Powis printer	Printer that enables putting printing on the spines of the Fastback II bound copies
Baum 714	High speed heavy duty folding unit

The taxpayer also protested the use tax assessed on several photocopiers rented from Eastman Kodak. The photocopiers were for use in the copy and print center.

All tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC 6-8.1-5-1 (b).

Indiana imposes an excise tax on tangible personal property stored, used or consumed in Indiana when no sales tax was paid at the time of purchase. IC 6-2.5-3-2(a). The sales and use taxes are also imposed on the use of tangible personal property that is leased. IC 6-2.5-4-10(a). A number of exemptions are available from use tax. IC 6-2.5-5-3(b) provides for the exemption of "manufacturing machinery, tools and equipment which is to be directly used by the purchaser in the direct production, manufacture, fabrication... of tangible personal property." IC 6-2.5-5-5.1 provides exemption to property consumed "in the direct production of other tangible personal property." Commercial printing is "treated as the production and manufacture of tangible personal property." IC 6-2.5-5-3(a)(2). Commercial printing is defined at IC 6-2.1-2-4(7) as follows:

The business of commercial printing that results in printed materials, excluding the business of photocopying.

The taxpayer's operations separate the business of photocopying from the business of producing printed materials. The self service photocopying machines are located outside the full service copy centers. The taxpayer properly paid sales tax on its self service photocopiers when purchased.

In contrast, the taxpayer offers full service print and copy centers in each of its retail establishments. The copy centers are in partially enclosed separate areas of the facility. Patrons bring their materials to the copy centers where the materials can be photocopied in color or black and white, bound, and tabs attached. A common sort of job includes one hundred (100) copies of a fifty (50) page document. It is not unusual for orders to cost $1,000.00. Jobs are paid for at a register in the center or an invoice is prepared and paid for at the general store registers. Sales tax is charged to patrons and remitted to the state on all jobs completed in the copy center. In this situation, the taxpayer is producing printed materials for sale. Machines that are directly used in the direct production of these printed materials qualify for exemption. Supplies that are consumed in the direct production of these printed materials also qualify for exemption. Each of the protested items is either a machine used in the direct production of the taxpayer's product or supplies consumed in the direct production of the taxpayer's product and exempt from Indiana use tax.

FINDING

The taxpayer's protest is sustained.

II. Sales and Use Tax-Phone Cards

DISCUSSION

The taxpayer protests two issues concerning the assessment of sales tax on the sale of phone cards. First the taxpayer contends that the separate assessment related to the phone card sales should be removed and the phone card transactions should be included in the random sample. The sale of phone cards is subject to Indiana sales tax. IC 6-2.5-4-13. The taxpayer acknowledged that it had at times not charged sales tax on the sale of phone cards. Further the taxpayer could not determine when the taxability of phone cards had been changed in its registers and billing systems. Therefore it was appropriate for the auditor to exclude the sales of phone cards from the sampling method used in the audit and tax the sales of phone cards as a "stand alone" item. The taxpayer was unable to provide the auditor with documentation concerning the exact amount of phone card sales. Therefore the auditor made an appropriate and reasonable estimate of the transactions selling phone cards.

FINDING

The taxpayer's protest is denied.

III. Sales and Use Tax-Rental of Uniforms and Door Mats

DISCUSSION

The taxpayer protests the assessment of sales tax on the rentals of uniforms and door mats.

Retail transactions made in Indiana are subject to sales tax. IC 6-2.5-2-1. Leases of tangible personal property are defined as a taxable retail transaction. IC 6-2.5-4-10(a). The taxpayer agrees that it rented uniforms and doormats and that sales tax was due on the transactions. The taxpayer argues that it actually paid the sales taxes due at the time of the rentals. In support of this contention, the taxpayer submitted statements of the amounts paid to the rental company. These statements, however, do not indicate that sales taxes were paid. Therefore, the taxpayer did not sustain its burden of proving that the assessment is incorrect.

FINDING

The taxpayer's protest is denied.

IV. Sales and Use Tax-Exempt Sales Error Percentage

DISCUSSION

The taxpayer protests the auditor's determination of the denominator for the error percentage calculation. The auditor used the figures provided by the taxpayer to determine the denominator of the error percentage. However the auditor dropped the cents which made the denominator a smaller number and increased the final amount of tax due. An estimate of the denominator should not be used when accurate figures are available.

Secondly the taxpayer contends that the auditor should have excluded the value of untaxed phone card sales from the denominator of the error percentage calculation. The taxpayer provided listings of figures to be deducted from the denominator of the error percentage calculation. There is, however, no back up information or other way to verify these figures. This submission does not sustain the taxpayer's burden of proving that the assessment was incorrect. IC 6-8.1-5-1(b).

FINDING

The taxpayer's protest concerning the accurate calculation of the denominator of the error percentage calculation is sustained. The taxpayer's protest concerning the exclusion of the untaxed phone card sales from the denominator of the error percentage calculation is denied.

V. Tax Administration-Imposition of Penalty

DISCUSSION

The taxpayer protests the imposition of the ten percent (10%) negligence penalty pursuant to IC 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2 (b) clarifies the standard for the imposition of the negligence penalty as follows:

> Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The taxpayer's carelessness and inattention to details caused it to fail to pay sales or use tax on many clearly taxable items such as business cards, uniform rental, hand trucks, and ladders. Further, many of the assessments resulted from issues similar to those in a previous audit. This breach of the taxpayer's duty to pay the proper amount of taxes constitutes negligence.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 03-0314
Sales Tax
For the Year 2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

Sales Tax—Assessment

Authority: IC 6-8.1-5-1(b); IC 6-2.5-2-1; IC 6-2.5-6-1; IC 6-2.5-4-1(g); IC 6-2.5-5-20; IC 6-2.5-6-6; 45 IAC 2.2**.**

Taxpayer protests the additional assessment of sales tax on January 2001 sales income.

STATEMENT OF FACTS

Taxpayer operates a family restaurant. Discrepancies existed between the amount of sales income Taxpayer reported in January 2001 as income for sales tax purposes and the amount of sales income reported for income tax purposes.

DISCUSSION

All tax assessments are presumed to be accurate. The taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b). Indiana retail transactions are subject to the imposition of an excise tax—known as the state gross retail tax; the retailer merchant shall collect the tax as agent for the state. IC 6-2.5-2-1 and IC 6-2.5-6-1. Generally, meals served in a restaurant are taxable retail transactions. *See* IC 6-2.5-4-1(g) and IC 6-2.5-5-20. The payment and reporting of sales tax is coordinated with the payment and reporting of income tax. *See* IC 6-2.5-6-6. A retail merchant is required to create and keep records of sales transactions. *See* 45 IAC 2.2.

Taxpayer entered sales into a computer spreadsheet program—programmed by Taxpayer. When Taxpayer ran a recap report for tax year 2001, Taxpayer made a programming error in the parameters of the report dates. Sale from the first thirteen days of January 2002 were included in the sales of January 2001. Taxpayer filed an income tax return that included the additional thirteen dates. When the error was discovered, Taxpayer chose not to amend the return to correct the additional inclusion—citing as a reason that it was not worth the bother to do so. This discrepancy between reported sales for sales tax purposes and reported sale for income tax purposes explains the concern of the Department.

A tax protest hearing was held and the Hearing Officer received a copy of the spreadsheet programming code. As well, the Hearing Officer received a copy of the monthly sales for the tax years 1999 – 2004. After reviewing the spreadsheet code and the monthly sales trend, the Department is satisfied that the discrepancy is an aberrant error—despite the fact Taxpayer did not amend the income tax returns to correct the error.

FINDING

Taxpayer's protest is sustained. The assessment of additional sales tax is not due.

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 03-0324
Income Tax
For the Years 1999-2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

Corporate Income Tax—Assessment

Authority: IC 6-8.1-5-1(b); 45 IAC 3.1-1-1-1; 45 IAC 3.1-1-1-3; IRC § 62; IRC § 162 Enterprise Leasing Co. v. Ind. Dep't of State Revenue, 779 N.E.2d 1284 (Ind. Tax 2002)

Taxpayer protests the denial of a payroll deduction—resulting in an assessment of income tax.

STATEMENT OF FACTS

Taxpayer is incorporated and operates a family restaurant. The previous owner of the restaurant was in financial trouble and stepped aside from all ownership. Taxpayer incorporated the business and began paying the previous owner from payroll. Taxpayer deducted payroll expenses in 1999 and 2000 for the previous owner and the net salary was sent to a bankruptcy trustee assigned to the previous owner's bankruptcy. The Auditor for the Department deemed these deducted payroll expenses not to be necessary and ordinary as required by Internal Revenue Code Section 162. The Department levied an income tax assessment on the denied deduction. Audit increased the adjusted gross income by the amount of direct payroll, employer social security, and federal unemployment tax that was deducted by Taxpayer. The audit report states that the previous owner confirmed to the department that the amounts paid to him were for his interest in the business.

DISCUSSION

All tax assessments are presumed to be accurate. The taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b). Adjusted gross income is defined according to IRC § 62—with subsequent adjustments. *See* 45 IAC 3.1-1-1. In arriving at Adjusted Gross Income, Indiana allows a deduction for business expenses permitted under IRC § 162. *See* 45 IAC 3.1-1-3. IRC § 62 permits the deduction of qualified business expenses allowed under IRC § 162. IRC § 162 permits the deduction of a reasonable allowance for salaries or other compensation for personal services actually rendered.

Taxpayer states that the previous owner of the restaurant was in financial trouble and that the restaurant was going to close operations because the debts could not be paid. Previous Owner had no income to pay the debts he owed and he filed Chapter 13 bankruptcy. Among the debts owed were priority claims of Indiana back-taxes of over $24,000. The total base amount of the bankruptcy plan was over $30,000. The bankruptcy plan decreed that Previous Owner—himself—directly make payments of $607 per month of future earnings into the plan fund. Taxpayer agreed to help Previous Owner pay this debt by making payments from Taxpayer's payroll, on behalf of Previous Owner—at the suggestion of Taxpayer's accountant. The net payroll salary was sent to Previous Owner's bankruptcy trustee. Of important note is the fact that Taxpayer would be paying Previous Owner's tax obligation to the Department through the use of a reduction and deduction of Taxpayer's tax liability to the department. This is a self-feeding transaction producing no sustainable gain.

Taxpayer asserts that Previous Owner provided consulting services to Taxpayer. According to Previous Owner as stated in the audit report, Previous Owner lived over 700 miles away in South Carolina. The net pay derived from the W-2 statements issued to Previous Owner for 1999 and 2000 sum to $31,800. This amount is similar to the over $30,000 due under the bankruptcy plan.

Indiana determines tax consequences based on the substance, not the form, of a transaction. Enterprise Leasing Co. v. Ind. Dep't of State Revenue, 779 N.E.2d 1284, 1291 (Ind. Tax 2002). Purchases of an ownership interest are not deductible. While assets may depreciate and a deduction may be taken for depreciation—no deduction exists allowing a purchase of an ownership interest to be deductible. More importantly—a corporation may not and cannot purchase itself—but must be owned by others, namely shareholders. The substance of Taxpayer corporation's payroll deduction is an attempt by Taxpayer to have the corporation purchase the restaurant on behalf of the shareholder(s) of the corporation. Since Previous Owner has stated that the payroll salary he was receiving is for his ownership interest—it becomes evident that this is the substance of the transaction.

FINDING

Taxpayer's protest is denied. The assessment of income tax on the denied deduction is due.

DEPARTMENT OF STATE REVENUE

04-20030468.LOF

LETTER OF FINDINGS NUMBER: 03-0468
Sales and Withholding Tax
Responsible Officer
For the Tax Period 1993-2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

1. Sales and Withholding Tax-Responsible Officer Liability

Authority: IC 6-2.5-9-3, IC 6-8.1-5-1(b), IC 6-3-4-8(f), Indiana Department of Revenue v. Safayan 654 N.E. 2nd 279 (Ind.1995).

The taxpayer protests the assessment of responsible officer liability for unpaid corporate sales and withholding taxes.

STATEMENT OF FACTS

The taxpayer was the President of a corporation that did not properly remit sales and withholding taxes to the state during the tax period 1993-2001. The Indiana Department of Revenue, hereinafter referred to as the "department," assessed the unpaid sales taxes, withholding taxes, interest, and penalty against the taxpayer as a responsible officer of that corporation. The taxpayer protested the assessment of tax. A hearing was held and this Letter of Findings results.

1. Sales and Withholding Tax-Responsible Officer Liability

DISCUSSION

Indiana Department of Revenue assessments are prima facie evidence that the taxes are owed by the taxpayer who has the burden of proving that the assessment is incorrect. IC 6-8-1-5-1(b).

The proposed sales tax liability was issued under authority of IC 6-2.5-9-3 that provides as follows:

An individual who:

(1) is an individual retail merchant or is an employee, officer, or member of a corporate or partnership retail merchant; and

(2) has a duty to remit state gross retail or use taxes to the department;

holds those taxes in trust for the state and is personally liable for the payment of those taxes, plus any penalties and interest attributable to those taxes, to the state.

The proposed withholding taxes were assessed against the taxpayer pursuant to IC 6-3-4-8(f), which provides that "In the case of a corporate or partnership employer, every officer, employee, or member of such employer, who, as such officer, employee, or member is under a duty to deduct and remit such taxes shall be personally liable for such taxes, penalties, and interest."

Pursuant to Indiana Department of Revenue v. Safayan 654 N.E. 2nd 279 (Ind.1995) any officer, employee, or other person who has the authority to see that they are paid has the statutory duty to remit sales and withholding taxes to the state. As the President of the corporation, the taxpayer had the responsibility to oversee the corporation. The taxpayer failed to insure that the corporation fulfilled its financial responsibilities by remitting trust taxes to the Indiana Department of Revenue. The taxpayer had the statutory duty to remit the sales and withholding taxes due during his term as President of the corporation. Therefore, he is personally liable for the payment of those taxes not remitted to the state during that period.

The taxpayer produced substantial documentation that he sold his interest in the corporation and was no longer President after March 31, 1996. Therefore the taxpayer is not personally responsible for the withholding and sales taxes that were due and not remitted after March 31, 1996.

FINDING

The taxpayer's protest is denied as to taxes due prior to or on March 31, 1996. The taxpayer's protest is sustained as to taxes not due until after March 31, 1996.

DEPARTMENT OF STATE REVENUE

04-20040019.LOF

LETTER OF FINDINGS NUMBER: 04-0019
Sales and Use Tax
Aircraft Excise Tax
For The Tax Period 2002

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Sales and Use Tax and Aircraft Excise Tax - Imposition

Authority: IC 6-8.1-5-1 (b), IC 6-2.5-3-2 (a), IC 6-2.5-2(c)(1), IC 6-6-6.5-12, IC 6-6-6.5-2, IC 6-6-6.5-3, IC 6-6-6.5-2, IC 6-6-6.5-8(d), IC 6-6-6.5-9, IC 6-2.5-2-1.

The taxpayer protests the assessment of use tax and aircraft excise tax on an airplane**.**

II. Tax Administration-Penalty

Authority: IC 6-8.1-10-2.1, 45 IAC 15-11-2 (b).

The taxpayer protests the imposition of the ten percent (10%) negligence penalty.

STATEMENT OF FACTS

The taxpayer is a corporate subsidiary of an Indiana corporation. The taxpayer purchased an airplane in 2002. The Indiana Department of Revenue, hereinafter referred to as the "department," assessed Indiana use tax and Indiana aircraft excise tax, interest, and penalty. The taxpayer protested the assessments. A hearing was held and this Letter of Findings results.

I. Sales and Use Tax and Aircraft Excise Tax-Imposition

DISCUSSION

All tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC 6-8.1-5-1 (b).

Indiana imposes a sales tax on the transfer of tangible personal property in a retail transaction. IC 6-2.5-2-1. Indiana imposes a complementary excise tax, the use tax, on tangible personal property purchased in a retail transaction and stored, used, or consumed in Indiana. IC 6-2.5-3-2 (a). Payment of sales tax at the time of purchase exempts the use of tangible personal property from the use tax. IC 6-2.5-2(c)(1).

IC 6-6-6.5-2 and IC 6-6-6.5-3 establish the necessity of registration and set the parameters of this requirement. IC 6-6-6.5-2 states in relevant part as follows:

(a) Except as otherwise provided in this chapter, any resident of this state who owns an aircraft shall register the aircraft with the department not later than thirty-one (31) days after the purchase date.

IC 6-6-6.5-3 also provides as follows:

(a) Any resident of this state who owns an aircraft, and any nonresident who has established a base in this state and bases an aircraft in this state for more than sixty (60) days, which is not exempt from registration under section 9 of this chapter, shall apply to the department for a certificate of registration for such aircraft. The application for such certificate of registration shall be made upon a form to be provided by the department and shall contain such information as the department may require.

IC 6-6-6.5-8(d) provides for the payment of sales and use tax on an airplane as follows:

A person shall pay the gross retail tax or use tax to the department on the earlier of:

(1) The time the aircraft is registered; or

(2) not later than thirty-one (31) days after the purchase date;

unless the person presents proof to the department that the gross retail tax or use tax has already been paid with respect to the purchase of the aircraft as proof that the taxes are inapplicable because of an exemption.

The taxpayer bases its claim for exemption on the following provisions of IC 6-6-6.5-9 which states as follows:

(a) The provisions of this chapter pertaining to registration and taxation shall not apply to any of the following:

...

(6) An aircraft owned by a resident of this state that is not a dealer and this is not based in this state at any time, if the owner files the required form not later than thirty-one (31) days after the date of purchase; and furnishes the department with evidence, satisfactory to the department, verifying where the aircraft is based during the year.

This statute offers exemption from the subject taxes if 1. an airplane is owned by an Indiana resident; 2. the airplane is not based in this state at any time; 3. and the taxpayer files a required form within thirty-one (31) days after the date of purchase. In this case the airplane was owned by an Indiana resident. The taxpayer produced some evidence that the plane was not based in Indiana at least at certain times. This evidence included statements by airport employees, receipts for hangar rentals at an Illinois airport, and an Illinois Aircraft Registration dated March 8, 2004. This evidence did not, however, fulfill the taxpayer's burden of proving that the plane was never based in Indiana. Even if it had risen to that standard, however, the taxpayer did not file the proper form within the statutorily prescribed time period.

The taxpayer argued that it did not know that it needed to file the form. A review of the timeline from the purchase of the airplane to the time of hearing contradicts this contention. The taxpayer purchased the airplane on September 19, 2002. The department sent the taxpayer a letter concerning registration of the plane in Indiana on November 8, 2002. That letter contained the following language.

We have received notification that you are the owner of the subject aircraft. In checking our records, your aircraft is not properly registered with the State of Indiana which is required by law within 31 days after the purchase date. (IC 6-6-6.5) We have enclosed an application which must be completed and returned with your remittance.

The enclosed application included the following language:

If your aircraft is not based in Indiana at <u>any</u> time, you may be entitled to a Based Out Of State Exemption. You must call for and complete Form AE-1 before 2-28.

Rather than requesting the form, the taxpayer sent a letter stating that the aircraft qualified for the out of state exemption on November 27, 2002. Upon receipt of this letter, the department mailed the taxpayer the form to be completed and returned. The taxpayer failed to do so. The department issued a proposed assessment of use tax, aircraft excise tax, interest and penalty on September 25, 2003. The taxpayer protested this assessment. The taxpayer did not submit the properly completed "Based Out Of State Certificate of Exemption For Aircraft" Form AE-1 until February 23, 2004.

The taxpayer did not complete the third requirement for exemption from the use tax and aircraft excise tax within the time period required by the law. Therefore, the department properly imposed the taxes.

The taxpayer also argues that the provisions in IC 6-2.5 et al control the imposition of use tax and exemptions from use tax. Therefore, the provisions of IC 6-6-6.5-8(d) cannot control the determination of whether use tax was properly imposed on or an exemption properly denied to a particular airplane. However, the provisions of IC 6-6-6.5-8(d), as previously cited, clearly state that

"A person shall pay the gross retail tax or use tax to the department..." The provision directly states that it applies to gross retail and use tax. The statutory provision provides the process for payment and determination of qualification for an exemption in this particular situation, the sale and use of an airplane. The statutory procedures requiring the completion of a form within thirty one (31) days confirm the intent and nature of the transaction transferring title to the airplane and the subsequent use of the airplane. Therefore, they do control in the instant case.

FINDING

The taxpayer's protest is denied.

II. Tax Administration-Penalty

DISCUSSION

The taxpayer protests the imposition of the ten percent (10%) negligence penalty pursuant to IC 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2 (b) clarifies the standard for the imposition of the negligence penalty as follows:

> Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The taxpayer failed to complete the forms required by the department to establish the taxpayer's qualification for exemption from the use tax and aircraft excise tax. The taxpayer's inattention to its duty, constitutes negligence on the part of the taxpayer.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

41-20040032.LOF
42-20040031.LOF

LETTER OF FINDINGS NUMBERS: 04-0031 & 04-0032
International Fuel Tax Agreement (IFTA), Interstate Registration Program(IRP) and Single State Registration Tax
For the Years 2000 to 2002

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. IFTA – Sufficiency of documentation

Authority: IFTA Article VII R700; IFTA Article XII R12010.300

The taxpayer protested the auditor's calculation of fuel tax liability after an IFTA audit assessment was made based on taxpayer's records.

II. IRP – Sufficiency of documentation

Authority: IC 6-8.1-3-14; IC 6-6-4.1-14; IRP 1500; IRP 1502; IRP Audit Procedures Manual 603

The registrant protested the auditor's calculation of miles traveled after an IRP audit assessment was made based on registrant's records.

III. Single State Registration System Fee – Record keeping

Authority: IC 8-2.1.20-7; IC 8-2.1-22-39

Taxpayer protested the auditor's assessment on an unreported vehicle for the audit period.

STATEMENT OF FACTS

Taxpayer operated a trucking business hauling sand and gravel. Audit was conducted for the years 2000, 2001, and 2002 and resulted in additional assessments for IFTA. Taxpayer protested the assessment, hearing was held, and this LOF results.

I. IFTA – Sufficiency of documentation

DISCUSSION

The department, pursuant to an IFTA audit, requested taxpayer records pursuant to IFTA Article VII R700:

> Every licensee shall maintain records to substantiate information reported on the quarterly and annual tax returns. Operational records shall be maintained or be made available for audit in the base jurisdiction. Recordkeeping requirements shall be specified in the IFTA Procedures Manual.

Taxpayer did not provide complete records for the audit review. The auditor was never provided records or receipts for the 2000 audit year period. The mileage records did not include jurisdictional miles, routes, or odometer readings. The taxpayer also failed to maintain monthly and/or quarterly vehicle mileage summaries. The taxpayer failed to maintain complete fuel purchase receipts. Taxpayer now argues that the assessment should have given credit for records not available and taxpayer has provided- during the protest- additional receipts from the audit periods at issue.

IFTA Article XII R12010.300 addresses this, stating in relevant part:

> The base jurisdiction shall, after adding the appropriate penalties and interest, serve an assessment issued pursuant to.200.005 upon the licensee in the same manner as an audit assessment or in accordance with the laws of the base jurisdiction. The assessment made by a base jurisdiction pursuant to this procedure shall be presumed to be correct and in any case where the validity of the assessment is questioned, the burden shall be on the licensee to establish by a fair preponderance of evidence that the assessment is erroneous or excessive.

Taxpayer indicated that his drivers did not keep complete records due to difficulties in stopping at state lines and writing mileage down. Taxpayer's contention has no merit. The above statute requires maintenance of books in a form amenable to review by the department for tax liability. The Department will review the additional receipts that have been provided and grant applicable credits to taxpayer, but will not otherwise adjust the audit results.

FINDINGS

Taxpayer's appeal is sustained subject to review by the audit division of new records provided during the protest process and denied as to any adjustments that are not supported by appropriate documentation.

II. IRP – Record Keeping

DISCUSSION

The issue is based on IRP 1500, 1502, and IRP Audit Procedures Manual 603.

The Indiana Code provides for the joining of Indiana to the IRP agreement via IC 6-6-4.1-14 and IC 6-8.1-3-14. IC 6-6-4.1-14 states in relevant part:

> The commissioner or, with the commissioner's approval, the reciprocity commission created by IC 9-28-4 may enter into the International Registration Plan, the International Fuel Tax Agreement, or other reciprocal agreements with the appropriate official or officials of any other state or jurisdiction to exempt commercial motor vehicles licensed in the other state or jurisdiction from any of the requirements that would otherwise be imposed by this chapter...

The IRP manuals lend guidance in this area; IRP 1500 states:

> The base jurisdiction shall require a registrant to preserve the records on which the registrant's application is based for a period of three years after the close of the registration year. The registrant shall be required to make the records available to the base jurisdiction at its request.

IRP 1502 states:

> If a registrant fails to maintain records, or after 30 days from receiving written notice, fails to make records available to the member jurisdiction, the member jurisdiction may impose an assessment. The assessment must be based on the member jurisdiction's estimate of true liability established from:
>
> 1. information the registrant furnished;
> 2. information the member jurisdiction gathered;
> 3. information relative to other similar registrants based in the jurisdiction; or
> 4. any other information available to the member jurisdiction.

IRP Audit Procedures Manual 603 states in relevant part:

> During the preliminary phase of the audit, the auditor will have made a request for records that support the apportioned registration application as filed. Records must be adequate and complete for each fleet being audited. If the records are not made available, or if the records made available are inadequate for examination purposes, an assessment of liability may be imposed in accordance with Article XV of the Plan. If an estimate of the registrant's true liability cannot be determined, the registrant may be assessed 100% registration fees for the jurisdiction. Any credits calculated for jurisdictions which are caused by the inadequacy of the records will not be reflected in the fees netted under Article XVII of the Plan.

Registrant protested that information he had received from some source indicated that he did not have to keep records for trips of less than 100 miles. Registrant did not cite to, nor are there any, IRP regulations to support this contention. If the registrant's records had included either route information or number of trips, an estimate of the miles traveled in each jurisdiction might have been possible. Absent information on both of these variables, no means exist to make a determination of the miles traveled in each jurisdiction. Consequently, the evaluation of the records as inadequate was supported by the audit findings.

FINDINGS

Registrant's protest is denied.

III. Single State Registration System Fee – Record keeping

Taxpayer protests that the Department incorrectly determined the number of vehicles that he was operating at any given time and incorrectly assessed Single State Registration fees against him. The Singe State Registration system is established under IC 8-

2.1.20-7 and taxpayer was assessed under IC 8-2.1-22-39 which states in relevant part:

All registrations of motor vehicles required in this chapter expire on December 31 of each year, and each motor vehicle continued in service shall be registered for each such year.

The taxpayer has failed to demonstrate that this assessment was not correct. The records available to the auditor substantiate this assessment. Taxpayer protest is denied.

FINDINGS

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

02-20040085P.LOF

LETTER OF FINDINGS NUMBER: 04-0085P
Income
For Tax Years 1997 through 2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration—Negligence Penalty

Authority: IC 6-8.1-10-1; IC 6-8.1-10-2.1; 45 IAC 15-11-2

Taxpayer protests a ten percent (10%) negligence penalty.

STATEMENT OF FACTS

As the result of an audit, the Indiana Department of Revenue ("Department") issued proposed assessments, ten percent (10%) negligence penalty and interest. Taxpayer protests the imposition of penalty. Further facts will be provided as necessary.

I. Tax Administration—Negligence Penalty

DISCUSSION

The Department issued proposed assessments and the ten percent (10%) negligence penalty for the tax years in question. Taxpayer protests the imposition of penalty. The Department refers to IC 6-8.1-10-2.1(a), which states in relevant part:

If a person:

…

(3) incurs, upon examination by the department, a deficiency that is due to negligence;

…

the person is subject to a penalty.

The Department refers to 45 IAC 15-11-2(b), which states:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to reach and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

45 IAC 15-11-2(c) provides in pertinent part:

The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. 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 this section.

In this case, taxpayer incurred a deficiency which the Department determined was due to negligence under 45 IAC 15-11-2(b), and so was subject to a penalty under IC 6-8.1-10-2.1(a). In its protest letter, taxpayer states that it timely filed and timely paid all tax liabilities. Since the Department issued assessments for unpaid tax, and taxpayer paid the assessments except for the penalties, it stands to reason that taxpayer did not timely pay all tax liabilities. Taxpayer has not affirmatively established that its failure to pay the deficiency was due to reasonable cause and not due to negligence, as required by 45 IAC 15-11-2(c).

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 04-0141
SALES TAX
For Years 1998 and 1999

NOTICE: Under Ind. Code § 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Sales and Use Tax—Assessment of Sales/Use Tax on Computer

Authority: IC 6-8.1-5-1(b); Panhandle Eastern Pipeline Company v. Dept. of Revenue, 741 N.E.2d 816, 818 (Ind. Tax 2001).

Taxpayer protests the assessment of sales/use tax by the Department on the purchase of a computer. Taxpayer claims that the part of the purchase was for programming.

II. Sales and Use Tax—Direct Use in Direct Production

Authority: IC 6-8.1-5-1(b); IC 6-2.5-3-2 (a); IC 6-2.5-5-3; 45 IAC 2.2-5-10 (c); 45 IAC 2.2-5-8 (k); Panhandle Eastern Pipeline Company v. Dept. of Revenue, 741 N.E.2d 816, 818 (Ind. Tax 2001); Indiana Department of Revenue v. Cave Stone, 457 N.E. 2d 520 (Ind. 1983)

Taxpayer protests the assessment of sales/use tax by the Department on items Taxpayer claims are used in direct manufacturing.

III. Sales and Use Tax— Incorporation into Product for Sale

Authority: IC 6-8.1-5-1(b); IC 6-2.5-3-2 (a); IC 6-2.5-5-6; 45 IAC 2.2-5-14; Panhandle Eastern Pipeline Company v. Dept. of Revenue, 741 N.E.2d 816, 818 (Ind. Tax 2001)

Taxpayer protests the assessment of sales/use tax by the Department on items taxpayer claims are incorporated into finished goods or are directly consumed in direct manufacturing.

STATEMENT OF FACTS

Taxpayer operates a sign company. It manufactures and installs signs. The Department conducted an audit and assessed sales/use tax on the purchase of a computer and on the purchase of items that the Department considered not to be equipment directly used in direct production, tangible personal property incorporated into finished goods, or tangible personal property consumed in direct production. All tax assessments are presumed to be accurate; the taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b). A hearing was conducted and Taxpayer attended—but did not bring complete evidence to substantiate whether the various items met an applicable exemption. The Hearing Officer accepted oral testimony concerning the items.

I. Sales Tax—Assessment of Sales/Use Tax on Computer

DISCUSSION

Taxpayer purchased a computer. Taxpayer claims that part of the purchase price of the computer was for programming services. Taxpayer cannot produce an invoice to substantiate the billing of the purchase price. All tax assessments are presumed to be accurate; the taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b). Tax exemption statutes are construed strictly in favor of taxation. *See, e.g.,* Panhandle Eastern Pipeline Company v. Dept. of Revenue, 741 N.E.2d 816, 818 (Ind. Tax 2001). Taxpayer has not produced documentation that part of the purchase price was for programming services; Taxpayer also has not presented convincing evidence that it is entitled to an exemption.

FINDING

Taxpayer's protest is denied.

II. Sales and Use Tax—Direct Use in Direct Production

DISCUSSION

The Department conducted an audit and assessed sales/use tax on the purchase of items that the Department considered not to have been acquired for direct use in direct production. All tax assessments are presumed to be accurate; the taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b). IC 6-2.5-3-2 (a) imposes an excise tax on tangible personal property stored, used, or consumed in Indiana when the sales tax was not paid. A number of exemptions are available from sales/use tax, including those collectively referred to as the manufacturing exemptions. Tax exemption statutes are construed strictly in favor of taxation. *See, e.g.,* Panhandle Eastern Pipeline Company v. Dept. of Revenue, 741 N.E.2d 816, 818 (Ind. Tax 2001). IC 6-2.5-5-3 provides for the exemption of manufacturing machinery, tools, and equipment which are to be directly used by the purchaser in the direct production, manufacture, or fabrication of tangible personal property.

In Indiana Department of Revenue v. Cave Stone, 457 N.E. 2d 520 (Ind. 1983), the Indiana Supreme Court found that a piece of equipment qualifies for the manufacturing exemption if it is essential and integral to the production process. 45 IAC 2.2-5-10 (c) further describes manufacturing machinery and tools as exempt if they have an immediate effect on the property in production. The manufacturing process starts when there is a change in a form, composition, or character different from that in which it was acquired. Pursuant to 45 IAC 2.2-5-8 (k), the use of the machinery and the time of its use then determines whether or not it qualifies for exemption. The following are listed and named in the audit report.

Letter LOK 2000 Fastening machine

This machine produces fasteners from two pieces of aluminum. Lettering is attached to a sign with these fasteners. The Department determines that this machine can be used only in the production of signs and is part of the direct manufacturing of signs.

Paint System

This machine is used to mix base colors of different paints to come up with custom colors for the signs. The Department determines that this machine is used in the production of signs and is part of the direct manufacturing of signs.

Paint cabinet

This is a booth with infrared heating used to bake the signs that have been painted. The cabinet also keeps the signs clean while drying. The Department determines that this is used in the production of signs and is part of the direct manufacturing of signs.

Paint machine

This is a high volume, low-pressure sprayer used in the painting of certain signs. The Department determines that this is being used only in the production of signs and is part of the direct manufacturing process.

Indiana Oxygen—Welder

This is a welder used to connect two pieces of metal in the production of metal and plastic signs. The Department determines that this is being used only in the production of signs and is part of the direct manufacturing process.

¼ CED 80 Router bits Donai

These special bits are used to finish the edges of aluminum and plastic. The Department determines that these are being used in the production of signs and is part of the direct manufacturing process.

The above pieces of equipment are determined to be directly used in the direct manufacturing process of signs. The below items are determined to not be part of the direct manufacturing process because Taxpayer was unable to provide testimony and documentation to identify the items and to substantiate their use:

Neon accusizer
Cincinnati sign machine
Equipment Cincinnati sign
Gas—100% Argon & 12-liter flushing.

FINDING

Taxpayer's protest is sustained in part and denied in part—as named above.

III. Sales and Use Tax— Incorporation into Product for Sale

DISCUSSION

The Department conducted an audit and assessed sales/use tax on the purchase of items that the Department considered not to be items incorporated into products for sale. All tax assessments are presumed to be accurate; the taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b). IC 6-2.5-3-2 (a) imposes an excise tax on tangible personal property stored, used, or consumed in Indiana when the sales tax was not paid. A number of exemptions are available from use tax, including those collectively referred to as the manufacturing exemptions. Tax exemption statutes are construed strictly in favor of taxation. *See, e.g.,* Panhandle Eastern Pipeline Company v. Dept. of Revenue, 741 N.E.2d 816, 818 (Ind. Tax 2001). IC 6-2.5-5-6 provides an exemption for tangible personal property acquired for incorporation into a product for sale. The Department has promulgated 45 IAC 2.2-5-14 to address this exemption. The following are listed and named in the audit report.

Eurocom equipment

This is an electrode fastener for neon tubes to maintain electric current going through neon tubes. The Department determines that these are being incorporated into the signs for sale.

Eurocom EL 15MM 4565

This is an electrode fastener for neon tubes—named with a specific part number. The Department determines that these are being incorporated into the signs for sale.

Eurocom EL 50R60 12 MM

This is an electrode fastener for neon tubes—named with a specific part number. The Department determines that these are being incorporated into the signs for sale.

Eurocom, Inc.

This is an electrode fastener for neon tubes. The Department determines that these are being incorporated into the signs for sale.

FINDING

Taxpayer's protest is sustained—as named above.

DEPARTMENT OF STATE REVENUE

0320040190P.LOF

LETTER OF FINDINGS NUMBER: 04-0190P
Withholding Tax
For the month February 2002

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2;

The taxpayer protests the late penalty.

STATEMENT OF FACTS

The late penalty was assessed on the late payment of a monthly withholding tax return for the month of February 2002.

The taxpayer is a company located out-of-state.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer argues the late penalty should be abated as (1)the taxpayer did not act with willful neglect, (2) there was a change in personnel, and (3) the Indiana tax laws allow waiver of penalty if the tax is paid within 30 days of the due date.

With regard to the change in personnel, the Department points out that Indiana tax regulations state the taxpayer is liable for the actions of any of the taxpayer's employees. This would include the completion of tax duties by new personnel. As such, the taxpayer fails to establish reasonable cause on this point.

The taxpayer has quoted a statute that states "The penalty may be waived if the return is filed or tax paid within 30 days after the due date." The taxpayer refers to IC 6-3-4-8, IC 6-3-6-10, IC 6-3-6-11, 45 IAC 1-1-218, and 45 IAC 3.1-1-146. 45 IAC 3.1-1-146 was repealed in 1987. The remaining cites make no mention of this "30 days". As such, the taxpayer fails to establish reasonable cause on this point.

45 IAC 15-11-2(b) states, "Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer."

The Department finds the taxpayer was inattentive of tax duties. Inattention is negligence and negligence is subject to penalty. As such, the Department finds the penalty proper and denies the penalty protest.

FINDING

The taxpayer's penalty protest is denied.

DEPARTMENT OF STATE REVENUE

0220040251.LOF

LETTER OF FINDINGS: 04-0251
Indiana Individual Income Tax
For the Year 2000

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of the document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Part-Time Residency Status.

Authority: IC 6-3-1-12; IC 6-3-2-1(a); IC 6-8.1-5-1(b); 45 IAC 3.1-1-21(a); 45 IAC 3.1-1-22; 45 IAC 3.1-1-23(2).

Taxpayer argues that the Department of Revenue erred when it determined that taxpayer was not a part-time Indiana resident during 2000.

STATEMENT OF FACTS

Taxpayer filed a form IT-40 ("Indiana Full-Year Resident Individual Income Tax Return") reporting income received during 2000. Thereafter, taxpayer amended that return by filing a form IT-40X ("Indiana Amended Individual Income Tax Return"). Taxpayer did so believing that "according to the Indiana Tax Code, we should have filed Form IT-40PNR because in 2000 [taxpayer] was a part-year resident and [taxpayer's] wife was a full-year resident of Indiana, and we filed a joint federal return in 2000."

The Department of Revenue (Department) sent taxpayer notices of proposed assessment based upon a purported discrepancy between taxpayer's amended state return and taxpayer's joint federal returns. Taxpayer did not agree with the proposed assessments believing that the amended IT-40X was correct as submitted. After various communications with the Department attempting to resolve the issue, taxpayer submitted a protest. An administrative hearing was conducted during which taxpayer explained further the basis for the protest. This Letter of Findings results.

DISCUSSION

I. Part-Time Residency Status.

Indiana imposes a state income tax in the following manner. IC 6-3-2-1(a) states that, "Each taxable year, a tax at the rate of three and four-tenths percent (3.4%) of adjusted gross income is imposed upon the adjusted gross income of every *resident* person, and that part of the adjusted gross income derived from sources within Indiana of every nonresident person." (*Emphasis added*).

Taxpayer maintains that he was not a full-time resident of Indiana during 2000. 45 IAC 3.1-1-21(a) defines the term "resident" and states that an Indiana resident is "Any individual who was domiciled in Indiana during the taxable year, or [] Any individual who maintains a permanent place of residence in this state and spends more than 183 days of the taxable year within this state...." *See also* IC 6-3-1-12 ("The term 'resident' includes [] any individual who was domiciled in this state during the taxable year, or [] any individual who maintains a permanent place of residence in this state and spends more than one hundred eighty-three (183) days of the taxable year within this state....")

45 IAC 3.1-1-22 defines "domicile" stating that,

> For the purposes of this Act, a person has only one domicile at a given time even though that person maintains more than one residence at that time. Once a domicile has been established, it remains until the conditions necessary for a change of domicile occur. In order to establish a new domicile, the person must be physically present at a place, must have the simultaneous intent of establishing a home at that place. It is not necessary that the person intend to remain there until death; however, if the person, at the time of moving to the new location, has definite plans to leave that new location, then no new domicile has been established.
>
> The determination of a person's intent in relocating is necessarily a subjective determination. There is no one set of standards that will accurately indicate the person's intent in every relocation. The determination must be made on the facts present in each individual case. Relevant facts in determining whether a new domicile has been established include, but are not limited to:
>
> (1) Purchasing or renting residential property.
> (2) Registering to vote
> (3) Seeking elective office
> (4) Filing a resident state income tax return or complying with the homestead laws of a state.
> (5) Receiving public assistance.
> (6) Titling and registering a motor vehicle.
> (7) Preparing a new last will and testament which includes the state of domicile.

The significance of the distinction lies in the effect that domiciliary status has on an individual's state income tax liability. 45 IAC 3.1-1-23(2) states that, "Any person who, on or before the last day of the taxable year, changes his residence or domicile from Indiana to a place without Indiana, with the intent of abiding permanently without Indiana, is subject to adjusted gross income tax on all taxable income earned while an Indiana resident. Indiana will not tax income of a taxpayer who moves from Indiana and becomes an actual domiciliary of another state or country except that income received from Indiana sources will continue to be taxable."

The Department's "2000 IT-40 PNR Forms and Instruction Booklet" states that, "If you were a part-year resident and received income while you lived in Indiana, you must file Form IT-40PNR, Part-Year Resident or Nonresident Individual Income Tax Return."

The issue is whether taxpayer was originally entitled to file an IT-40PNR return and to report his Indiana income in a manner which reflected taxpayer's purported part-time residency status.

Taxpayer moved to Israel in April 2000 and remained there for nine months. Taxpayer did so with the intention of purchasing an interest in a geriatric hospital and of making Israel his and his wife's retirement home. Taxpayer produced documentation indicating that taxpayer served as a volunteer at the geriatric hospital from April to December 2000.

As required by law, taxpayer obtained an Israeli passport. The passport was initially issued for a one year term. The passport term was later extended to five years.

Taxpayer registered to vote while in Israel; having done so, taxpayer voted in a local Israeli election.

While in Israel, taxpayer signed a one-year condominium lease. Taxpayer opened up an account with an Israeli bank. Taxpayer purchased an automobile while in Israel; this vehicle was titled and licensed in Israel. Taxpayer obtained an Israeli driver's license. Taxpayer filed the Israeli equivalent of income tax returns but, because of the nature of his income – patent royalties, investment income, and Social Security benefits – was not required to pay Israeli income tax. Taxpayer did make monthly contributions to the "Israel National Medical Fund" which is equivalent to the American Medicaid/Medicare scheme.

Taxpayer's wife remained in Indiana during this nine month time with the intention of selling their home, completing her work at an Indiana geriatric hospital, selling the couple's possessions, and continuing to care for her elderly father.

The plans of taxpayer and his wife went astray when the wife became seriously ill and permanently disabled. Taxpayer returned to Indiana where he currently resides with his wife.

Taxpayer has the burden of demonstrating that he was a part-time Indiana resident during 2000, that he was originally entitled to file an IT-40 PNR return, and that he correctly filed an amended return reflecting his part-time residency status. IC 6-8.1-5-1(b) states in part that, "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 person against whom the proposed assessment is made."

Pursuant to IC 6-8.1-5-1(b), taxpayer has met his burden of demonstrating he moved to Israel with the expectation that Israel would become his permanent home. Taxpayer was physically present in Israel for approximately nine months, took steps which would lead a reasonable person to conclude he intended to make Israel his permanent home, and spent less than 183 days in Indiana during 2000.

Taxpayer was a part-time resident of Indiana during 2000. To the extent that the Department has found to the contrary, taxpayer's protest is sustained.

FINDING

Taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

04-20040254.LOF

LETTER OF FINDINGS NUMBER: 04-0254
Sales/Use Tax
For the Period: 2000-2002

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration – Penalty

Authority: IC 6-8.1-5-1; 45 IAC 15-11-2

The taxpayer protests the assessment of a penalty.

STATEMENT OF FACTS

The taxpayer is a supplier of office imaging equipment.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty assessment be abated. The taxpayer states,

As a result of the recent audit of [the taxpayer], the Indiana Department of Revenue has issued a proposed assessment…. [Taxpayer] hereby formally requests the abatement of penalty….

And further:

Under unusually difficult circumstances [the taxpayer] cooperated fully with the auditor. During the audit examination [taxpayer] experienced the loss of its Sales Tax Manager. The key contact internally and externally for sales tax information. Additionally, during the audit examination [taxpayer] was in the process of implementing a new financial system.

The system implementation consumed a great deal of the sales tax staff time leaving limited resources to address the audit….

45 IAC 15-11-2(b) states:

"Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

Under IC 6-8.1-5-1 the burden of proof is on the taxpayer and the Department's assessment is considered as *prima facie* valid. The taxpayer offers no real arguments or evidence. Cooperation with the auditor is to be expected from taxpayer, and staff loss is not a mitigating factor in the negligence examination. As such, the taxpayer's penalty protest is denied.

FINDING

The taxpayer's penalty protest is denied.

DEPARTMENT OF STATE REVENUE

04-20040256P.LOF

LETTER OF FINDINGS NUMBER: 04-0256P
Sales/Use Tax
For the Period: 1998-2002

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration – Penalty

Authority: IC 6-8.1-5-1; 45 IAC 15-11-2

The taxpayer protests the proposed assessment of a penalty.

STATEMENT OF FACTS

The taxpayer is a distributor of paper and related products.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the proposed penalty assessment be abated. The taxpayer states,

I respectively request that all associated penalties be abated, as there was no willful neglect to collect sales tax or self assess use tax during the audit period. Additional taxes were assessed due to normal human errors that sometime occur when dealing with very high volumes of transactions, customers and invoices.

And further:

It is due only to human error that all taxes were not collected and remitted during the audit period. At no time did [the taxpayer] have material disagreements as to the taxability of product for sale nor do we dispute our responsibility to collect the tax. As we all know, humans are fallible and sometimes make errors in judgment and performance.

45 IAC 15-11-2(b) states:

"Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

And 45 IAC 15-11-2(c) states:

The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. 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 this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

(1) the nature of the tax involved;
(2) judicial precedents set by Indiana courts;
(3) judicial precedents established in jurisdictions outside Indiana;
(4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc.
(5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

Under IC 6-8.1-5-1 the burden of proof is on the taxpayer and the Department's proposed assessment is considered as *prima facie* valid. The taxpayer states that, "It is due only to human error that all taxes were not collected and remitted during the audit period." The taxpayer has not met its burden of proof, nor has it shown under 45 IAC 15-11-2(c) that its failures were due to "reasonable cause" and "not due to negligence."

FINDING

The taxpayer's penalty protest is denied.

DEPARTMENT OF STATE REVENUE

0120040265.LOF

LETTER OF FINDINGS: 04-0265
Indiana Individual Income Tax
For 2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of the document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Involuntary Servitude – Indiana Adjusted Gross Income Tax.

Authority: U.S. Const. amend. XIII; United States v. Drefke, 707 F.2d 978 (8th Cir. 1983); Ginter v. Southern, 644 F.2d 1226 (8th Cir. 1979); Kasey v. Commissioner, 457 F.2d 369 (9th Cir. 1972); Porth v. Brodrick, 214 F.2d 925 (10th Cir. 1954).

Taxpayer maintains that requiring him to pay state income tax constitutes "involuntary servitude" in violation of U.S. Const. amend. XIII.

II. Citizenship.

Authority: 26 U.S.C.S. § 7701(a)(14); United States v. Collins, 920 F.2d 619 (10th Cir. 1990); In re Becraft, 885 F2d 547 (9th Cir. 1989); United States v. Ward, 833 F2d 1538 (11th Cir. 1987).

Taxpayer argues that he is not required to pay federal or state income taxes because he is a "nonresident alien" and a "national of the United States."

III. Applicability of the State Adjusted Gross Income Tax.

Authority: 26 U.S.C.S. § 7701(a)(1); 26 U.S.C.S. § 7701(a)(14); United States v. Karlin, 785 F.2d 90 (3d Cir. 1986); United States v. Studley, 783 F.2d 934 (9th Cir. 1986); McKeown v. Ott, No. H 84-169, 1985 WL 11176 (N.D. Ind. Oct. 30, 1985)

Taxpayer argues that he is not a "person" required to report his income for federal or state income tax purposes.

IV. State Income Tax Liability.

Authority: IC 6-3-2-1(a); Black's Law Dictionary (7th ed. 1999).

Taxpayer maintains that there is nothing in Indiana law which makes him "liable" for paying income tax and that any tax payment made under Indiana law is a "donation."

STATEMENT OF FACTS

The Department of Revenue (Department) determined that taxpayer owed additional state income taxes for 2001. Accordingly, notices of "Proposed Assessment" were sent to taxpayer at his out-of-state location. Taxpayer disagreed and sent a 15-page document outlining the basis for his disagreement. The Department treated the document as a protest of the 2001 assessment. Taxpayer was invited to participate in an administrative hearing and to further explain the basis for the protest. Taxpayer chose not to take part. This Letter of Findings is based upon the taxpayer's protest letter.

This Letter of Findings refers to the petitioner as "taxpayer" a designation which taxpayer vigorously challenges. However, in the absence of a more suitable term, the Letter of Findings employs the term in its most generic sense and without any prejudice to the substance of taxpayer's legal arguments.

DISCUSSION

I. Involuntary Servitude – Indiana Adjusted Gross Income Tax.

Taxpayer claims that imposition of the state's adjusted gross income tax constitutes a form of involuntary servitude in violation of the U.S. Const. amend. XIII.

U.S. Const. amend. XIII provides that, "Neither slavery nor involuntary servitude except as a punishment for crime whereof the party shall have been duly convicted shall exist within the United States, or any place subject to their jurisdiction."

The courts have uniformly rejected arguments that income tax is a form of "involuntary servitude" forbidden under U.S. Const. amend. XIII. "If the requirements of the tax laws were to be classed as servitude, they would not be the kind of involuntary servitude referred to in the Thirteenth Amendment." Porth v. Brodrick, 214 F.2d 925, 926 (10th Cir. 1954). *See also* United States v. Drefke, 707 F.2d 978, 983 (8th Cir. 1983); Ginter v. Southern, 644 F.2d 1226 (8th Cir. 1979); Kasey v. Commissioner, 457 F.2d 369 (9th Cir. 1972).

The Department does not agree with taxpayer's contention that imposition of the state's income tax places taxpayer in bondage; the Department concludes that taxpayer's argument is "clearly unsubstantial and without merit," as well as "far-fetched and frivolous." Porth, 214 F.2d at 926.

FINDING

Taxpayer's protest is denied.

II. Citizenship.

Taxpayer maintains that only those persons living in the District of Columbia or on land ceded to the federal government are subject to federal income tax or – by extension – Indiana income tax. In support of that contention, taxpayer cites to 26 U.S.C.S. § 7701(a)(10) which states that, "The term 'State' shall be construed to include the District of Columbia, where such construction is necessary to carry out provisions of this title."

The Internal Revenue Code imposes federal income tax upon all United States citizens and residents not simply those who reside in the District of Columbia, federal territories, and federal enclaves. United States v. Collins, 920 F.2d 619, 629 (10th Cir. 1990), *cert denied* 500 U.S. 920 (1991). "For seventy-five years, the Supreme Court has recognized that the sixteenth amendment authorizes a direct nonapportioned tax upon United States citizens throughout the nation, not just in federal enclaves." *See also* In re Becraft, 885 F2d 547, 549-50 (9th Cir. 1989); United States v. Ward, 833 F2d 1538, 1539 (11th Cir. 1987), *cert denied,* 485 U.S. 1022 (1988).

Taxpayer's reliance on 26 U.S.C.S. § 7701(a)(10) is misplaced; the cited provision means that the District of Columbia comes within the purview of the Internal Revenue Code. It does not means that *only* residents of the District of Columbia are subject to the IRC. It is plain that the use of the term "include" within 26 U.S.C.S. § 7701(a)(1) is a term of enlargement not limitation, and the reference to the District of Columbia is not intended to exclude other jurisdictions.

FINDING

Taxpayer's protest is denied.

III. Applicability of the State Adjusted Gross Income Tax.

Taxpayer argues that he is not a "person" required to report his income or to pay tax on that income. Taxpayer predicates this proposition on the ground that he is not subject to the provisions of the Internal Revenue Code (IRC). Taxpayer errs. The IRC clearly defines "persons" and sets out which persons are subject to federal taxes. 26 U.S.C.S. § 7701(a)(14) defines "taxpayer" as any person subject to any internal revenue tax. 26 U.S.C.S. § 7701(a)(1) defines a "person" as any individual, trust, estate, partnership, or corporation. Taxpayer's argument that an individual – such as himself – is not a "person" within the meaning of the IRC has been uniformly rejected. In United States v. Karlin, 785 F.2d 90, 91 (3d Cir. 1986), the court affirmed the defendant's conviction for failing to file income returns and rejected the defendant's contention that he was "not a 'person' within the meaning of 26 U.S.C. § 7203" as "frivolous and require[ing] no discussion." In United States v. Studley, 783 F.2d 934, 937 n.3 (9th Cir. 1986), the court affirmed defendant's conviction for failing to file income tax returns on the ground that defendant was "an absolute freeborn, and natural individual" stating that "this argument has been consistently and thoroughly rejected by every branch of the government for decades." "*[A]rguments about who is a 'person' under the tax laws,* the assertion that 'wages are not income', and maintaining that payment of taxes is a purely voluntary function do not comport with common sense - let alone the law." McKeown v. Ott, No. H 84-169, 1985 WL 11176 at *2 (N.D. Ind. Oct. 30, 1985) (*Emphasis added*).

Taxpayer's argument, that he is not a "person" subject to the IRC or to the Indiana individual income tax, does not warrant serious consideration.

FINDING

Taxpayer's protest is denied.

IV. State Income Tax Liability.

Taxpayer states that nothing in Indiana law makes him "liable" for paying Indiana income taxes. Taxpayer is mistaken. IC 6-3-2-1(a) states that, "Each taxable year, a tax at the rate of three and four-tenths percent (3.4%) of adjusted gross income is *imposed* upon the adjusted gross income of every resident person, and on that part of the adjusted gross income derived from sources within Indiana of every non-resident person." (*Emphasis added*). The word "impose" means "to levy or exact a tax or duty." Black's Law Dictionary 759 (7th ed. 1999); "levy" means the "imposition of a fine or tax." Id. at 919. As a matter of law and simple common sense, whether a tax is levied or imposed, the person against whom the levy is made is "liable" for that amount.

Taxpayer set out other objections to the "Proposed Assessment" citing authorities such as former President Taft, the Congressional Record, the Copyright Act, Restatement (Second) Contracts, and Saint Paul's second letter to the apostle Timothy. Notwithstanding taxpayer's reliance on historical, legal, and Biblical authority, the Department will not expend further resources attempting to discern or refute taxpayer's wholly frivolous arguments.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

42-20040272.LOF

LETTER OF FINDINGS NUMBER: 04-0272
IFTA
For The Period: 2001 and 2002

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. IFTA: Sufficiency of documentation

Authority: IFTA R1210.300; IC 6-8.1-5-1(b)

The taxpayer protests the proposed assessments regarding "Nevada calculated miles."

STATEMENT OF FACTS

The taxpayer is a "common contract carrier" that hauls "dump loads of various products…." More facts will be provided as needed.

I. IFTA: Sufficiency of documentation

DISCUSSION

In correspondence from May of 2004 the taxpayer said its "Nevada operation consisted of transportation of solid waste for [Company R], a private carrier of municipal waste for the City of [X]. [Taxpayer] employed an average of 50 drivers and leased an average of 3 owner-operators to haul these loads."

The taxpayer also stated:

> [Company R] garbage trucks would bring their waste to one of three transfer stations…. They would dump their loads into our larger trailers. Our tractor-trailers would then transport the waste to the [landfill]. Our units were of exceptional weight, 92,000 pounds. [Taxpayer] secured over weight permits from the State of Nevada for this hauling….

Further, the taxpayer stated that its tax accountant "went out to Arizona and found original records that will substantiate" that its M.P.G. should be lower for Nevada. The taxpayer shipped "two boxes" with "the original driver tickets that show both the miles traveled and gallons consumed on a daily basis. There are approximately 7,400 tickets. These tickets are grouped by the day with a summary sheet of the day's activity attached." The taxpayer stated that "[t]here is also a Four Page Summary of these daily reports…." The taxpayer noted that "[t]hese reports are not intended to be a full accounting of miles traveled and/or gallons consumed. They are strictly evidence to support the lower M.P.G. experienced in Nevada as this is the factor that the Auditor used to determine miles traveled in Nevada."

And in a recent document (October 2004), the taxpayer stated at length:

> [O]ur protest of the audit findings is limited to the 'gross up' miles used to recalculate the miles traveled in Nevada. The auditor used our fleet MPG to recalculate the taxable miles in Nevada. Since the moves in Nevada actually experienced a much lower MPG, the miles assessed and the resulting tax computation is artificially inflated.
>
> Our MPG factor in Nevada was much lower due to the numerous short hauls, the extra weight carried, the fuel consumed while the load was sitting idle in line at the [landfill] and while the load was being tarped for movement in Nevada. Although we could not produce the desired records requested, in May of 2004 I traveled to Arizona where any remaining records of 2001 for Nevada are stored. Working with 7,500 "Driver Tickets" I produced a four-page summary of dates, miles and gallons. A sample copy of this ticket and the Four-page summary is attached. The purpose of this exercise was not to determine total miles or gallons for the period, but to establish from original documents that these Nevada units experienced a much lower MPG that [*sic.*] experienced by our entire fleet.

In late June of 2004, the Department mailed the taxpayer a letter. The letter stated that, "The Department has reviewed the submitted driver tickets and compared these to the records viewed during the audit." The letter then stated several conclusions. Among them, that the "submitted miles and gallons (per the driver tickets) do not equal the miles and gallons" the taxpayer originally reported. That the "submitted driver tickets cannot be audited to determine if reasonable. There are no odometer readings, no origins or destinations by city and state, and no routes of travel." The Department's letter also noted:

> A review of the units and unit totals for July, 2001 (per the submitted driver tickets) was conducted by the auditor. It was determined that the unit numbers recorded on the time sheets differ from the unit numbers recorded on the mileage summaries originally provided for the audit….
>
> And:
>
> Some of the driver tickets showed that the truck was operating but no miles or gallons were recorded for that activity. No estimation of miles and fuel was included for this omission. Sometimes only a portion of the unit's month's activity was recorded.

And the Department stated:

The quarterly MPGs (4.80, 4.88, and 4.47) utilized in the audit were calculated by using figures of terminal groups who had no missing miles or gallons. Your request to lower Nevada's MPGs does not include documentation of why the trucks operating in Nevada would get a significantly lower MPG than the remaining fleet.

The Department further noted in the letter that "MPGs calculated for the audit are a fleet MPG—not by jurisdiction (as you are requesting)…."

At the hearing the taxpayer provided "additional documentary information" which included (among other things): (1) a map "indicating the route traveled" from the transfer station to the landfill; (2) a description of the landfill; and a (3) a performance summary for the taxpayer's "tractor/trailer configuration."

Taxpayer basically recapitulates the argument that it initially made to the Department, but the taxpayer fails to address in a specific way the problems the Department raised in the June 2004 letter. The new "additional documentary information" the taxpayer submitted at hearing does not help in this regard either.

Under IFTA R1210.300 (in relevant part):

The assessment made by a base jurisdiction pursuant to this procedure shall be presumed to be correct and, in any case where the validity of the assessment is questioned, the burden shall be on the licensee to establish by a fair preponderance of evidence that the assessment is erroneous or excessive.

And the Indiana Code 6-8.1-5-1(b) states in part:

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.

The taxpayer has not met its burden of proof. (It should be noted that a negligence penalty was also imposed; the taxpayer did not develop any arguments regarding the penalty and thus is denied regarding the penalty too).

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20040299P.LOF

LETTER OF FINDINGS NUMBER 04-0299P
TAX ADMINISTRATION—NEGLIGENCE PENALTY FOR
THE PERIOD COVERING CALENDAR YEARS 2001-2002

NOTICE: Under IC § 4-22-7-7, this document is required to be published in the *Indiana Register* and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the *Indiana Register*. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration—Negligence Penalty

Authority: IC §§ 6-8.1-5-1(b), -10-2.1 (1998) (2004); *United States v. Boyle,* 105 S.Ct. 687 (U.S. 1985); 45 IAC §§ 2.2-3-20 and -21, 15-5-3(b)(8) and 15-11-2 (1996) (2001)

The taxpayer protests the assessment of the negligence penalty.

STATEMENT OF FACTS

The taxpayer has been admitted to do business in Indiana as a foreign corporation since 1961. It is engaged in the wholesale distribution of chemicals to a variety of industrial customers. It maintains two storage and distribution centers in Indiana.

The Department of State Revenue (hereinafter "the Department") audited the taxpayer for gross retail (i.e., sales) and use taxes for calendar years 2001-2002 (hereinafter "the audit period") and issued Notices of Proposed Assessment of use taxes, including a proposed negligence penalty, based on the results of that audit. The taxpayer timely protested only the proposed negligence penalty, but not the respective proposed base taxes, which remain outstanding at this writing together with accrued and accruing interest. The Department will provide additional facts as needed.

I. Tax Administration—Negligence Penalty

DISCUSSION

The taxpayer argues that it exercised ordinary care and prudence in filing its Indiana sales and use tax returns and that based on its payment history, it did not willfully neglect to remit tax due.

The taxpayer's use tax self-assessment system missed purchases, made without remitting sales tax, of certain equipment in 2001 used to move product during loading and shipping, as well as fuel bought in both years and consumed in the loading and delivery vehicles at its Indiana locations. The discovery of the untaxed fuel purchases in particular prompted the field auditor and the taxpayer to enter into an Agreement for Projecting Audit Results (Form AD-10A) for selected expense accounts of the taxpayer, mainly vehicle fuel purchase accounts. The use taxes calculated as due based on the Form AD-10A form the vast majority of the proposed assessments. The auditor cited 45 IAC § 2.2-3-20 (1996), which states that "[a]ll purchases of tangible personal property which are delivered to the purchaser for storage, use or consumption in the state of Indiana are subject to the use tax[,]" *id.*, as authority for both the equipment and expense adjustments. As additional authority for the expense adjustment, she also cited 45 IAC § 2.2-3-21, which states that "[a]ll purchases of tangible personal property which are accepted by the purchaser outside the state of Indiana but which are stored, used or otherwise consumed in Indiana are subject to the use tax[,]" *id.*.

IC § 6-8.1-10-2.1 (1998) (current version at *id.* (2004)) is the statute that authorizes the Department to impose a penalty for any negligence of a taxpayer in failing to comply with the tax laws that the Department administers. These taxes are listed in IC § 6-8.1-1-1 and include the gross retail and use tax. IC § 6-8.1-10-2.1(a)(3) states that "(a) [i]f a person:… (3) [i]ncurs, upon examination by the department, a deficiency that is due to *negligence*;… the person is subject to a penalty." *Id* (emphasis added). The amount is set by IC § 6-8.1-10-2.1(b)(4), which states that "(b) [e]xcept as provided in subsection (g) [,] [not in issue here], the penalty described in subsection (a) is ten percent (10%) of:… (4) the amount of deficiency as finally determined by the department[.]" *Id.* However, IC § 6-8.1-10-2.1(d) states that "[i]f a person subject to the penalty imposed under this section can show that the failure to…pay the deficiency determined by the department was due to *reasonable cause* and not due to willful neglect, the department shall waive the penalty." *Id* (emphasis added).

Title 45 IAC § 15-11-2(b) states:

> (b) "Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's *carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence.* Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

Id (emphasis added). The next subsection of the regulation sets out the standard of care a taxpayer must prove pursuant to IC § 6-8.1-10-2.1(e) to establish reasonable cause for failing to meet its tax compliance duties to the Department. Subsection (c) of 45 IAC § 15-11-2 reads in relevant part as follows:

> (c) The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 [sic; should read IC 6-8.1-10-2, repealed and re-enacted in 1991 as IC 6-8.1-10-2.1] if the taxpayer affirmatively establishes that the failure to…pay a deficiency was due to reasonable cause and not due to negligence. *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 this section.….*
>
> …
>
> Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

Id (emphasis added).

Under IC § 6-8.1-5-1(b) (1998) (current version at *id.* (2004)) and 45 IAC § 15-5-3(b)(8) (1996) (2001), the person against whom a proposed assessment is made has the burden of proving that it is wrong. That burden applies to abatement of penalty assessments, as well as substantive tax assessments. *"A person who wishes to avoid the penalty imposed under [IC § 6-8.1-10-2.1(a) and (b)] must make an affirmative showing of all facts alleged as a reasonable cause* for the person's failure to file the return, pay the amount of tax shown on the person's return, pay the deficiency, or timely remit tax held in trust[.]" IC § 6-8.1-10-2.1(e) (emphasis added). Moreover, the legislature's use of the conjunction "and" between the phrases "due to reasonable cause" and "not due to willful neglect" in IC § 6-8.1-10-2.1(d) means that a taxpayer protesting a proposed negligence penalty must prove both the existence reasonable cause and the absence of willful neglect, not just one of these elements. *Cf. United States v. Boyle,* 105 S.Ct. 687, 689-690 (U.S. 1985) ("To escape the penalty, the taxpayer bears the heavy burden of proving both (1) that the failure did not result from 'willful neglect,' and (2) that the failure was 'due to 'reasonable cause.' 26 U.S.C. [I.R.C.] § 6651(a)(1) [the federal negligence penalty statute]."). The burden of proof is not on the Department to show negligence, willful or otherwise, by, or the absence of reasonable cause for the actions or inaction of, a taxpayer.

The taxpayer has been doing business in Indiana for over forty-three years and has been subject to the Gross Retail and Use Tax Act, chapter 30 (Special Session), 1963 Indiana Acts 60, codified as amended at IC article 6-2.5, for forty-one of those years. The Department promulgated the two regulations the auditor cited on December 1, 1982. LSA Doc. #82-86(F), 6 I.R. 8, 15 and 15 (Jan. 1, 1983), respectively. They thus have each been in effect for over twenty-two years. The taxpayer is charged with constructive knowledge of all of these authorities. Its failures to remit use tax on the assessed transactions is evidence of "carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code [and] department regulations" or "[i]gnorance of the listed tax laws, rules and/or regulations[.]" 45 IAC § 15-11-2(b). Those failures therefore constituted "negligence" as 45 IAC § 15-11-2(b) defines that word.

The taxpayer's argument that it exercised ordinary care and prudence in filing its Indiana sales and use tax returns, thereby implying that it had "reasonable cause" as 45 IAC § 15-11-2(c) defines that term, for its failures to remit use tax, is irrelevant to the present protest. The Department did not penalize the taxpayer under IC § 6-8.1-10-2.1(a)(1) or (2) for failing to file sales and use tax returns, or for failing to pay the full amount of tax shown on those returns. It was penalized under IC § 6-8.1-10-2.1(a)(3) for "[i]ncur[ring], upon examination by the department, a deficiency that is due to negligence[.]" *Id.* The fact that the taxpayer filed its returns promptly and paid all the tax it reported has no tendency to prove that the present deficiencies, resulting from its omissions of tax from those returns, were incurred for reasonable cause. Since the taxpayer has failed to sustain its burden of proof on the existence of reasonable cause, it is unnecessary for the Department to address the taxpayer's assertion that the incurring of the deficiencies was not due to willful neglect.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0220040394.LOF

LETTER OF FINDINGS NUMBER: 04-0311
Corporate Income Tax
For the Years 1995-2002

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

Corporate Income Tax—Assessment

Authority: IC 6-8.1-5-1(b); IC 4-30; IC 4-31; IC 4-32; IC 4-33; IC 4-30-1-1; IC 4-30-18-1; IC 4-31-1-2; 4-31-6; IC 4-31-9; IC 4-32-1-2; IC 4-32-4-1; IC 4-32-4-2; IC 4-32-9; IC 4-32-9-16; IC 4-32-9-18; IC 4-32-9-30, -31, -32, -33; IC 4-33-1-1; IC 4-33-1-2; IC 4-33-6; IC 4-33-6-1; 4-33-6-3.5; IC 4-33-7; IC 4-33-8; IC 4-33-8-2; IC 4-33-8-4; IC 4-33-8-6; IC 4-33-8-3; IC 4-33-8-2; IC 4-33-8-4(2); IC 4-33-9-8; IC 4-33-9-12; 4-33-13-1; IC 4-33-13-1.5; IC 6-3-2-1(b); 68 IAC 2-6-29(1); IRC § 501(c)(19); IRS Publication 3386; IRS Publication 598; IRS Publication 3079

Taxpayer does not dispute the audit adjustment, but has submitted a request for additional losses to offset the income.

STATEMENT OF FACTS

Taxpayer is a tax exempt veterans organization under IRC § 501(c)(19). Taxpayer was assessed unrelated business income on receipts from nineteen unsanctioned slot machines operated by Taxpayer. The income was computed by deducting payouts and a portion of the business expenses from the gambling receipts. The building expenses were calculated based on the square footage of floor space covered by the slot machines.

Taxpayer does not dispute the audit adjustment, but has submitted a request for additional "losses" to offset the slot machine income. Taxpayer maintains that "losses" in the computation of food & beverage income is directly related to gambling receipts.

Taxpayer claims that total food & beverage operations exceed income. Taxpayer states that the food & beverage operations function at a loss so that food prices are kept low—which in turn brings people into the establishment to gamble.

DISCUSSION

Under Indiana code—passed into law by the Indiana General Assembly—all tax assessments are presumed to be valid and accurate; the taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b). The Indiana General Assembly has passed into law what is permitted and unpermissive gambling in the State of Indiana. IC 4-30 establishes an Indiana state lottery. IC 4-31 establishes pari-mutuel wagering on horse races. 4-32 establishes games of chance. And IC 4-33 establishes riverboat gambling. Gambling in Indiana is regulated—organizations are required to be registered and licensed.

The Indiana General Assembly has stated that the purpose of establishing state lottery games is to "enable the people of Indiana to benefit from significant additional money for capital improvements." IC 4-30-1-1. No person or organization may operate a lottery in Indiana; only the state lottery commission may operate a lottery. IC 4-30-18-1.

The Indiana General Assembly has stated that the purpose of permitting pari-mutuel wagering on horse races in Indiana is "to ensure that [it] will be conducted with the highest of standards and the greatest level of integrity." IC 4-31-1-2. Racetrack personnel and racing participants are required to be licensed. *See* 4-31-6. Taxation and distribution of pari-mutuel revenues is highly regulated. *See* IC 4-31-9.

The Indiana General Assembly has stated that the purpose of permitting games of chance is "to permit a licensed qualified organization (1) to conduct bingo events, charity game nights, door prize drawings, and raffles; and (2) to sell pull tabs, punchboards, and tip boards; as a fund raising activity for lawful purposes of the organization." IC 4-32-1-2. Organizers are required to withhold state income tax on prizes awarded to a winner and to submit that tax. *See* IC 4-32-4-1 and IC 4-32-4-2. Organizations are required to be licensed and are regulated in the conduct of the games. *See* IC 4-32-9. Under IC 4-32-9-16, the Department is permitted by rule to set the allowable expenditures of a qualified organization. This is significant to note—the Department has the authority, as granted by the Indiana General Assembly to set the guidelines for allowable expenditures. This directly implies that the Department also may set the guidelines for permissible deductions of expenses. All net proceeds from an allowable event and related activities may only be used for the lawful purposes of the qualified organization. *Id*. There are limits on the number and frequency of events that may be held. IC 4-32-9-18. There are limits on the value of prizes. IC 4-32-9-30, -31, -32, -33. There are many more statutes regulating charity gaming; these are named to demonstrate that strict regulations and statutes exist.

Then there is casino gambling. The people of Indiana—acting through the General Assembly—restrict casino gambling solely to licensed riverboats. Casino gambling is restricted to counties that border Lake Michigan, the Ohio River, or a historic hotel district. *See* IC 4-33-1-1. The General Assembly highly restricts where casino gambling may be conducted. The Indiana General Assembly has stated that the purpose of permitting riverboat casino gambling is "to benefit the people of Indiana by promoting tourism and assisting economic development. The public's confidence and trust will be maintained only through: (1) comprehensive law enforcement supervision; and (2) the strict regulation of facilities, persons, associations, and gambling operations under this article." IC 4-33-1-2, **Legislative intent**. Owners are to be licensed. *See* IC 4-33-6. There are restrictions on who may be an owner, *id*., and how many licenses may be issued, IC 4-33-6-1 and 4-33-6-3.5. Suppliers are to be licensed. *See* IC 4-33-7. The occupational employees of a riverboat are to be licensed. *See* IC 4-33-8. The backgrounds of the employees are investigated and they are fingerprinted. *See* IC 4-33-8-2, IC 4-33-8-4, and IC 4-33-8-6. Felons are not permitted to hold an occupational license. IC 4-33-8-3. An occupational license is valid for only one year—it must be renewed annually. IC 4-33-8-2. The person only may be employed by one riverboat. IC 4-33-8-4(2). All of the above mentioned statutes have been named, so as to outline the strict regulatory guidelines established by the people of the State of Indiana—acting through their elected voice in the General Assembly.

Under IC 4-33-9-8 casino gambling equipment and supplies may be purchased or leased only from licensed suppliers. IC 4-33-9-12 does not permit those under the age of twenty-one to be in any area in which casino gambling is occurring. IC 4-33-13-1 and IC 4-33-13-1.5 state the tax schedules for revenues earned from casino gambling. This tax rate is as low as 15% and as high as 35%. Currently, the corporate income tax rate is 8.5%. See IC 6-3-2-1(b). The 8.5% corporate income rate is greatly less than the 15% minimum tax assessed against casino gambling on riverboats—at a little over one-half. Stated another way—were Taxpayer legally sanctioned to operate a casino, it would have to pay almost double the tax rate that the Department assessed for Taxpayer's unsanctioned operation of slot machines. Were Taxpayer legally operating these slot machines, it would be held to the gaming regulations as to the payout requirements. *See* 68 IAC 2-6-29(1). According to the Indiana Gaming Commission, riverboat casinos payout—on average—around 93%. Taxpayer pays out at around 80%. Taxpayer states that the bartender at the post pays out any winnings.

It is important to note that tax assessments on activities are not based upon the morality or legality of the activities. The Department does not base an assessment upon whether the income earned by a taxpayer is earned legally; the Department simply applies the tax statutes and regulations. At issue in this case is income earned by Taxpayer from unrelated business activities. This requires a discussion as to the functions and purposes of an IRC § 501(c)(19) veterans organization.

The IRS has issued three publications useful to this discussion:

Publication 3386 Tax Guide—Veterans' Organizations (6/99)
Publication 598 Tax on Unrelated Business Income of Exempt Organizations (3/00)
Publication 3079 Gaming Publication for Tax-Exempt Organizations (4/98).

The first thing that Publication 3386 states is: "Veterans' organizations occupy a special place in the world of exempt organizations." *Id.* at 3. Over the years, Congress has provided more flexible exemption provisions to veterans' organizations to help keep them vibrant contributors to veterans and their communities at large. *See id*. Originally, veterans' organizations were required to have a membership of at least 75% war veterans in order to be tax-exempt; but because of waning membership over the years, Congress changed the membership requirement to 75% veterans. *See id,* and IRC § 501(c)(19)(B). However, Congress still requires that no more than 2.5% of the members be non-veteran related persons in order for the organization to maintain tax-exempt status. *See id*.

Congress has stated that appropriate purposes of an IRC 501(c)(19) veterans' organization include:

A. promoting the social welfare of the community,
B. assisting needy and disabled veterans, widows, or orphans of deceased veterans,
C. providing entertainment, care and assistance to hospitalized veterans or members of the Armed Forces of the United States,
D. perpetuating the memory of veterans and comforting their survivors,
E. conducting programs for religious, charitable, scientific, literary, or educational purposes,
F. sponsoring or participating in patriotic activities,
G. providing insurance benefits to members or members' dependents, and
H. providing social and recreational activities for members.

See IRS Pub. 3386 at 9. IRS Publication 3386 states that a veterans organization can jeopardize its tax-exempt status if it does not limit its activities and operations to post members—but instead opens its facilities to the general public. A post may operate a bar & restaurant and also may provide gambling—but these must be restricted to members and their invited guests. All expenses of an invited guest are to be paid by the post member.

Taxpayer openly states that it serves food to the general public at lunch—those who come in to eat without being an invited guest of a member. Taxpayer estimates that 75% of its lunch revenue is from meals served to these non-members who pay for their own lunches. It is worth noting that Taxpayer engages in many activities and opens its post to the general public for many reasons. In the Department's audit of Taxpayer, only the income from the unsanctioned slot machines was assessed tax as being unrelated business income. The income from the lunch sales was not assessed tax. Taxpayer's attempt to secure a double benefit is inequitable. Taxpayer has not been assessed income tax on the lunch sales to the general public and now it seeks a deduction for the cost of the lunch sales. General tax policy does not permit deductions for that which is not taxed. Taxpayer is seeking to blur the line between the income which is not taxed and the income which is taxed. Taxpayer may not do so. The Department has sought only to tax the unsanctioned gambling as unrelated business income. The Department has computed the reasonable deductions related to the generation of that income.

Expenses—but not losses—directly related to the earning of unrelated business income can be used as a deduction in calculating the income. There is no evidence to establish that any of the food & beverage related expenses are directly related to gambling receipts. Taxpayer's organizational purpose would have to be gambling in order for Taxpayer's position to be valid. The Department has allowed a reasonable estimate of building expenses to offset the unrelated business income. No evidence has been submitted to support further deductions for expenses.

FINDING

Taxpayer's protest is denied. The assessment of corporate income tax is due.

DEPARTMENT OF STATE REVENUE

0220040312P.LOF

LETTER OF FINDINGS NUMBER: 04-0312P
Income Tax
For the Calendar Year 2002

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2;

The taxpayer protests the late penalty.

STATEMENT OF FACTS

The late penalty was assessed on the late payment of an annual income tax return for the calendar year 2002.

The taxpayer is a company residing in Indiana.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer argues the late penalty should be abated as the taxpayer has an exemplary payment history, and, the error is an unusual error.

The Department points out the taxpayer was six months late in paying the deficiency.

The Department will waive penalty if the error is unusual, and, the taxpayer has an exemplary payment history.

The Department agrees the taxpayer has an exemplary payment history. However, the payment was six months late, and, a change in personnel is not considered an unusual error.

45 IAC 15-11-2(b) states, "Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer."

The Department finds the taxpayer was inattentive of tax duties. Inattention is negligence and negligence is subject to penalty.

As such, the Department finds the penalty proper and denies the penalty protest.

FINDING

The taxpayer's penalty protest is denied.

DEPARTMENT OF STATE REVENUE

03-20040327.LOF

LETTER OF FINDINGS NUMBER: 04-0327
Nonresident Withholding Tax
For Tax Periods: 2000-2002

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning specific issues.

ISSUES

I. Nonresident Withholding Tax-Addback of income taxes

Authority: Ind Code. § 6-3-1-3.5; *Aztar Indiana Gaming Corp. v. Indiana Dept. of State Revenue*, 806 N.E.2d 381 (Ind. Tax 2004).

Taxpayer protests the addback of riverboat wagering taxes in determining the adjusted gross income of shareholders for withholding tax purposes.

II. Nonresident Withholding Tax-Applicability

Authority: I.R.C. § 702; I.R.C. § 1366(b); Ind. Code § 6-3-2-2; Ind. Code § 6-3-4-12; Ind. Code § 6-3-4-13; *Dupee v. Tracy,* 708 N.E.2d 698 (Ohio 1999); *Agley v. Tracy*, 719 N.E.2d 951 (Ohio 1999).

Taxpayer argues that the income that is subject to withholding is not Indiana source income, and that it cannot be subject to withholding tax obligations based on its lack of presence in Indiana

III. Nonresident Withholding Tax-Computation

Authority: Ind. Code § 6-3-4-13.

Taxpayer argues that any losses incurred by it prior to adjustments be used to offset the adjustments for determining its ultimate withholding tax liability.

IV. Tax Administration-Penalty

Authority: 6-8.1-10-2.1; 45 IAC 15-11-2.

Taxpayer protests the imposition of the ten percent penalty for negligence.

STATEMENT OF FACTS

Taxpayer, an S corporation, is a part-owner of an LLC that operates a casino in Indiana. During the years in question, taxpayer computed its withholding tax liability without adding back riverboat wagering taxes in computing the income subject to withholding. Audit assessed withholding tax liability based on the share of riverboat wagering tax paid by taxpayer. Taxpayer protested the add back of riverboat wagering taxes, the applicability of withholding liability to it, the computation of its liability, and negligence penalties.

I. Nonresident Withholding Tax-Addback of income taxes

DISCUSSION

With respect to the validity of the assessment, the Indiana Tax Court has determined that the riverboat wagering tax is a tax "based on or measured by income and levied at the state level by any state of the United States." *Aztar Indiana Gaming Corp. v. Indiana Dept. of State Revenue*, 806 N.E.2d 381, 386 (Ind. Tax 2004). Accordingly, with respect to individuals, the tax must be added back per Ind. Code § 6-3-1-3.5(a)(2) in order to determine the individual's adjusted gross income-the basis for withholding tax liability.

FINDING

Taxpayer's protest is denied.

II. Nonresident Withholding Tax-Applicability

Taxpayer has also argued that it is not subject to tax based on either the character of the income was not Indiana source income, or, in the alternative, that the Department did not have jurisdiction to assess taxpayer for the years in question.

First, taxpayer argues that the character of the income in the hands of the taxpayer was that of holding a membership interest in an LLC, not from doing business in Indiana. However, in the case of a partnership or S corporation, the character of the income for federal purposes is determined at the source, and then taxed to the individual recipient. *See* I.R.C. §§ 702(b), 1366(b). The character of the income in this case was determined at the partnership level-namely, the operation of a riverboat casino within Indiana, clearly subject to Indiana tax per Ind. Code § 6-3-2-2(a)(2). This character remains the same at the S corporation level. *See, e.g.,* *Dupee v. Tracy,* 708 N.E.2d 698, 700 (Ohio 1999) (Florida residents subject to Ohio income tax as a result of S corporation operations in Ohio, based on income being Ohio business income). The income, contrary to taxpayer's argument, does not magically transform from "casino revenues" in the hands of the partnership to "intangible income" (e.g., dividends or interest) in the hands of the taxpayer. It retains its initial character-income from a business conducted in Indiana- as it passes through the various entities until it reaches a taxpayer.

Further, taxpayer's argument creates a legal absurdity. Indiana's non-resident withholding statutes, Ind. Code §§ 6-3-4-12 and -13 are rendered non-existent by taxpayer's arguments. A pass-through entity could always argue that its owners' incomes from the entity was merely income from an intangible (i.e., an ownership interest in the entity doing business in Indiana) and never be subject to Indiana tax, effectively resulting in a situation in which a nonresident who owns a business in Indiana is subject to income tax, but a nonresident who puts a pass-through entity between the individual and the business is insulated from all tax liabilities to Indiana.

Second, taxpayer further argues that Indiana cannot constitutionally tax the income because the taxpayer did not have nexus in Indiana. Taxpayer notes that the LLC and taxpayer are separate entities, and the LLC activities cannot be attributed to the taxpayer generally.

While Indiana has not directly addressed the issue, the highest court of at least one other state has noted that the taxpayer has sought, via the LLC, to invoke valuable rights that were provided to it. *Agley v. Tracy*, 719 N.E.2d 951 (Ohio 1999). In that case, the taxpayers were owners of an S Corporation that conducted business in Ohio; however, the taxpayers did not participate in any activities in Ohio. The taxpayers argued that, since they were not present in Ohio nor had any contacts with Ohio beyond their ownership of the S corporation, they could not be subject to personal income tax in Ohio. However, the court found that the S corporation availed itself of the benefits of Ohio, and that the taxpayers, through that corporation, had sufficient contacts to justify taxation by Ohio on the income derived from the business.

In this protest, the LLC that operated the casino availed itself of the protections and benefits of Indiana. It received one of the rare and extremely difficult to obtain licenses to operate a riverboat casino in Indiana, and proceeded to operate the riverboat. It further utilized the resources of Indiana to allow customers to reach the casino and has had full access to the courts of Indiana in order to seek protection at the casinos and protection in its everyday operations. By extension, the LLC used those protections to earn business income from Indiana, just as the S corporation in *Agley* used the protections of Ohio to earn its income. Taxpayer in this case has utilized those protections provided by Indiana-a separate legal identity and a highly valuable license, among others-to earn its income through the LLC, just as the shareholders in *Agley* used the protections conferred by Ohio to earn their income. Accordingly, taxpayer has sufficient contacts to justify its withholding obligations in Indiana.

FINDING

Taxpayer's protest is denied

III. Nonresident Withholding Tax-Computation

DISCUSSION

Taxpayer has also protested the amount of the assessment. Taxpayer's argument is that the losses at the withholding entity level (in this case, S corporation) must be considered in determining its withholding liability. For example, if a taxpayer incurred a $10,000,000 loss, but had $4,000,000 of taxes added back, then its liability would be based on a $6,000,000 loss rather than $4,000,000. If a taxpayer incurred a $10,000,000 loss but had $19,000,000 of taxes added back, its liability would be based on $9,000,000 rather than $19,000,000.

Ind. Code § 6-3-4-13(a) states in relevant part that "[e]very corporation which is exempt from tax under IC 6-3 pursuant to IC 6-3-2-2.8(2) shall, at the time that it pays or credits amounts to any of its nonresident shareholders as dividends or as their share of the corporation's undistributed taxable income, withhold the amount prescribed by the department."

Here, the net income for withholding tax purposes is its "dividends or undistributed taxable income" within the meaning of the statute. Accordingly, the corporation's liability for withholding is limited to its net income rather than the total amount of taxes added back, if the corporation had a loss prior to the taxes added back. However, if the corporation had a profit or zero income prior to add back, then the full amount of taxes added back are subject to withholding obligations.

FINDING

Taxpayer's protest is sustained subject to audit review of the amount of net income.

IV. Tax Administration-Penalty

DISCUSSION

Taxpayer also protests the imposition of the penalty for negligence for the years in question. Penalty waiver is permitted if the taxpayer shows that the failure to pay the full amount of the tax was due to reasonable cause and not due to willful neglect. IC 6-8.1-10-2.1. The Indiana Administrative Code further provides:

(b) "Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

(c) The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. 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 this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

(1) the nature of the tax involved;
(2) judicial precedents set by Indiana courts;
(3) judicial precedents established in jurisdictions outside Indiana;
(4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc.;
(5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

45 IAC 15-11-2.

With respect to the penalty, Taxpayer has presented a case that it acted with reasonable care expected of taxpayers generally, and thus the penalty should be waived.

FINDING

Taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

02-20040329.LOF
02-20040330.LOF

LETTER OF FINDINGS NUMBER: 04-0329, 04-0330
Adjusted Gross Income Tax
For the Years 2000-2002

NOTICE: Under IC § 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Adjusted Gross Income Tax- Addback of state and local income taxes

Authority: Ind. Code § 4-33-2-2; Ind. Code § 4-33-13-1; Ind. Code § 6-3-1-3.5(b); *Aztar Indiana Gaming Corp. v. Indiana Dept. of State Revenue*, 806 N.E.2d 381 (Ind. Tax 2004).

Taxpayer protests the addback of riverboat wagering tax for adjusted gross income tax.

II. Tax Administration-Penalty

Authority: Ind. Code § 6-8.1-10-2.1; 45 IAC 15-11-2

Taxpayer protests the imposition of the ten percent (10%) penalty for negligence.

STATEMENT OF FACTS

Taxpayer was a corporate member of an LLC that operated a casino in Indiana. Taxpayer was assessed additional corporate income tax based on the adding back of riverboat wagering tax. Taxpayer protested the assessment, and this letter of findings results.

I. Adjusted Gross Income Tax- Addback of state and local income taxes

DISCUSSION

Taxpayer argues that the riverboat wagering tax is not a "tax based on or measured by income" under Ind. Code § 6-3-1-3.5(b). Taxpayer noted the history of both taxes involved in this protest. Taxpayer also noted that the riverboat wagering tax under Ind. Code § 4-33-13-1 *et seq.*, limits the allowance for uncollectible receivables under Ind. Code § 4-33-2-2, which may have resulted in amounts not subject to federal income tax being subject to riverboat wagering tax. Thus, by taxpayer's argument, the riverboat wagering tax is one not "based on or measured by income". The Indiana Tax Court has considered the issue of adding back the riverboat wagering tax and concluded that the tax is subject to add back for corporate income tax in a published opinion. *Aztar Indiana Gaming Corp. v. Indiana Dept. of State Revenue*, 806 N.E.2d 381 (Ind. Tax 2004).

FINDING

Taxpayer's protest is denied.

II. Tax Administration-Penalty.

Taxpayer also protests the imposition of the penalty for negligence for the years in question. Penalty waiver is permitted if the taxpayer shows that the failure to pay the full amount of the tax was due to reasonable cause and not due to willful neglect. IC 6-8.1-10-2.1. The Indiana Administrative Code further provides:

(b) "Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

(c) The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. 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 this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

(1) the nature of the tax involved;
(2) judicial precedents set by Indiana courts;
(3) judicial precedents established in jurisdictions outside Indiana;
(4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc.;
(5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

45 IAC 15-11-2.

With respect to the penalty, Taxpayer has presented a case that it acted with reasonable care and thus, the penalty should be waived.

FINDING

Taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

04990557.SLOF

SUPPLEMENTAL LETTER OF FINDINGS NUMBER: 99-0557
Sales Tax
For Calendar Years 1994, 1995, 1996, 1997, and 1998

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration – Proposed Assessment of Tax
Authority: IC 6-8.1-5-1

Taxpayer protests the assessment because it was made without an examination of the actual records and he asserts that he is not liable for sales tax because he is a broker.

STATEMENT OF FACTS

Taxpayer was originally assessed as part of an audit and protested, a hearing was held and taxpayer's protest of the best information available assessment was denied, taxpayer requested a rehearing and it was granted, this letter of finding results. Taxpayer sold- or arranged sales of- new and used medical equipment and medical supplies and operated out of his home. Taxpayer was organized as a sole proprietor for federal income tax purposes. Taxpayer did not register as a retail merchant with the State of Indiana, making purchases from his vendors claiming exemption for resale. During the field audit, the taxpayer indicated that he did not sell equipment and merely facilitated the sale of the equipment by matching up the sellers with the buyers. Taxpayer argued that he did not take title to any equipment, and was not a retail merchant, and did not need to be registered. Taxpayer further stated he acted as an agent and sold the equipment on behalf of the seller and received a commission from the sale. However, an entity sold equipment to the taxpayer, invoicing and shipping directly to the taxpayer's home in Indiana. This entity billed the taxpayer sales tax, but the taxpayer refused to pay it claiming exemption for resale. Taxpayer issued an improper exemption certificate to the entity after several attempts were made by this entity to collect the sales tax.

Taxpayer was advised of the impending audit and initially agreed to provide records. However, the taxpayer failed to fulfill the initial records request and subsequently failed to respond to any of the auditor's requests for records and failed to reply to any of the auditor's contacts. The audit proposed a "Best Information Audit" assessment for sales tax on unreported sales. The assessment is based upon the average annual taxable sales of a local new and used medical equipment retailer believed to be about the same size and volume as the taxpayer.

I. Tax Administration – Proposed Assessment of Tax

DISCUSSION

Taxpayer has not filed Indiana income tax returns since 1993. Records examined include information obtained from the Internal Revenue Service on income reported for the years 1994, 1995, and 1996, and other working papers.

IC 6-8.1-5-1 (a) provides, in part: "[i] f the department believes that a person has not reported the proper amount of tax due, the department shall make a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the department." The statute also provides: "[t]he notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid, and the burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made."

Here, the Department proposed an assessment of tax that the taxpayer protested. The taxpayer merely sent a few copies of invoices and/or offers to buy and sell and stated he is a broker prior to the first hearing. As part of taxpayer's protest for the second hearing taxpayer's counsel has provided additional documentation.

Barron's Law Dictionary defines a broker as "one who for commission or fee, brings parties together and assists in negotiating contracts between them." At best, the taxpayer may be classed as a jobber. Barron's Law Dictionary defines a jobber or "a middleman in the sale of goods, or typically, one who buys goods from a wholesaler and then sells them to a retailer. A jobber is distinguished from a broker or agent, who sells goods on another's behalf; a jobber actually purchases the goods himself, and then resells them."

The evidence provided by the taxpayer indicates it made purchases to be resold. No other evidence was provided.

IC 6-8.1-5-1 (c) provides, in part: "{t}he department shall demand payment...of any part of the proposed tax assessment, interest and penalties that is finds owing because:...after consideration of the evidence presented in the protest or hearing, the department finds the person still owes the tax.

Here, the taxpayer failed to provide evidence either to the auditor or the initial hearing officer after subsequent opportunities to present evidence were afforded. The charging of sales tax against "best information available" income was appropriate because no alternative means for the tax assessment existed. The auditor used the best and only information available at the commencement of the audit and the taxpayer initially failed to present any viable evidence to rebut the presumptive validity of the assessment. At the rehearing, taxpayer repeated his earlier arguments but did not, despite an initial letter of findings that clearly outlined the department's position, address any of his numerous failures to provide documentation, to file personal returns for the years at issue, or to reconcile his asserted position that no products were shipped into Indiana with the receipts demonstrating shipment to his residence. As far as the documents provided by taxpayer, these did not substantiate taxpayer's assertions. The documents consisted of portions of sales agreements and potential contracts for purchase. At no point has taxpayer provided evidence that these transactions actually occurred out of state- indeed, if, as taxpayer asserts, these transactions occurred out of state, taxpayer has not provided proof of sales or income tax paid to the appropriate jurisdictions.

FINDING

Taxpayer's protest is denied.