INDIANA DEPARTMENT OF ENVIRONMENTAL MANAGEMENT

Title: Risk Integrated System of Closure Technical Guide & User's Guide
Identification Number: W0046
Date Originally Effective: February 15, 2001
Dates Revised: 10/15/2001, 4/20/2006, May 16, 2006
Other Policies Repealed or Amended:
Brief Description of Subject Matter: Technical Guide TPH Chapter provides a method for determining health based closure levels for total petroleum hydrocarbons (TPH).
Citations Affected: IC 13-12-3-2 – Environmental policy: remediation objectives; IC 13-23 – Underground Storage Tanks; 329 IAC 9 – Underground Storage Tanks; and 328 IAC 1 – Underground Storage Tank Financial Assurance Board (ELTF)

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Health-Based Closure Level Determination of Total Petroleum Hydrocarbons (TPH) (This is a new chapter in the RISC document) may be viewed at http://www.in.gov/idem/programs/land/risc/index.html

Contact: Bob Moran, Indiana Department of Environmental Management, Office of Land Quality, 100 North Senate Avenue, Indianapolis, IN 46204, 317/232-4419, or e-mail bmoran@idem.IN.gov.

This new chapter will be effective June 15, 2006 (30 days after presentation to the board)

DEPARTMENT OF STATE REVENUE
INFORMATION BULLETIN #97
INCOME TAX
JUNE 2006

DISCLAIMER: Information bulletins are intended to provide non-technical assistance to the general public. Every attempt is made to provide information that is consistent with the appropriate statutes, rules and court decisions. Any information that is inconsistent with the law, regulations, or court decisions is not binding on either the Department or the taxpayer. Therefore, information provided in this bulletin should serve only as a foundation for further investigation and study of the current law and procedures related to its subject matter.
SUBJECT: Headquarters Relocation Tax Credit
REFERENCES: IC 6-3.1-30; and P.L.137-2006
INTRODUCTION

The Headquarters Relocation Tax Credit was originally passed in 2005 effective for taxable years beginning after December 31, 2006. P.L.137-2006 was subsequently passed making the credit effective for taxable years beginning after December 31, 2005. The credit is intended to provide an incentive for a business to relocate its corporate headquarters into Indiana.

I. DEFINITIONS

A. "Corporate headquarters" means the building where the principal offices of the principal executive officers of the business are located.

B. "Eligible business" means a business that is engaged in intrastate or interstate commerce, maintains a corporate headquarters outside Indiana, has not previously maintained a headquarters inside Indiana, and had annual worldwide revenues of at least one hundred million dollars ($100,000,000) for the immediate preceding taxable year.

C. "Pass through entity" means an S Corporation, partnership, limited liability company, or a limited liability partnership.

D. "Qualifying project" means the relocation of the corporate headquarters from a location outside Indiana to a location in Indiana.

E. "Relocation costs" means the reasonable and necessary expenses incurred by the business for a project. The term includes

moving expenses, purchase of new or replacement equipment, capital investment costs, purchase lease or construction of buildings and land, infrastructure improvements and site development costs.

II. ENTITLEMENT TO THE CREDIT

A taxpayer that is an eligible business that completes a qualifying project, incurs relocation costs, and employs at least seventy-five (75) employees in Indiana is entitled to a credit against the taxpayer's state tax liability for the year in which the relocation costs are incurred.

The amount of the credit that the taxpayer is entitled to is fifty percent (50%) of the amount of the relocation costs incurred in the taxable year. However, the amount claimed may not result in an Indiana tax liability that is lower than the Indiana tax liability in the taxable year immediately proceeding the taxable year in which the taxpayer first incurred the relocation costs.

EXAMPLE: The relocation costs are ten million dollars ($10,000,000). Therefore the amount of the credit is five million dollars ($5,000,000). The taxpayer's tax liability for the year before the relocation costs were incurred was one million dollars ($1,000,000). The current taxable year liability is calculated at one million seven hundred fifty thousand dollars ($1,750,000). The amount of credit allowed in the first year is seven hundred fifty thousand dollars ($750,000).

Any unused credit amount can be carried forward and applied to the nine (9) succeeding taxable years. A taxpayer is not entitled to a refund or carryback of any unused credit.

In future years the taxpayer will be allowed to apply the carry forward to any tax liability amount that exceeds the one million dollars ($1,000,000) base year amount.

If a pass through entity is entitled to the credit, a shareholder, partner or member of the pass through entity is entitled to claim the credit. The amount that the shareholder, partner or member may claim is the percentage of the pass through entity's distributive income to which the shareholder, partner or member is entitled.

III. DETERMINATION OF ELIGIBLE EXPENSES

The Department is required to determine whether an expense resulted from the relocation of the business, and in making that determination shall consider whether the expense would have been incurred by the taxpayer if the business had not relocated to Indiana.

IV. CLAIMING THE TAX CREDIT

A taxpayer must claim the credit on the taxpayer's state tax return and must provide proof of the taxpayer's relocation costs, and proof that the taxpayer is employing at least seventy-five (75) people in the State of Indiana.

John Eckart
Commissioner

DEPARTMENT OF STATE REVENUE

02-990135.LOF

LETTER OF FINDINGS NUMBER: 99-0135
GROSS AND ADJUSTED GROSS INCOME TAX
For Years 1992, 1993, 1994, and 1995

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.

ISSUES

I. Gross Income Tax — Lease Payments from Indiana

Authority: *Enterprise Leasing Co. of Chicago v. Indiana Dep't of State Revenue,* 779 NE.2d 1284 (Ind. Tax Ct. 2002), review denied.

Taxpayer protests the assessment of Gross Income Tax on auto lease payments sourced to Indiana.

II. Adjusted Gross Income Tax — Apportionment of income to Indiana

Authority: IC § 6-3-2-2

Taxpayer protests the proposed assessments based on an increased apportionment of Indiana income.

III. Adjusted Gross Income Tax — Addbacks of local taxes

Authority: 45 IAC 3.1-1-8; 45 IAC 17-3-1.1.(3)

Taxpayer protests the addback of local taxes to taxpayer's adjusted gross income.

STATEMENT OF FACTS

Taxpayer is primarily engaged in the business of retail leasing, retail installment lending, wholesale floor plan lending, third party servicing, and commercial lending such as mortgage and working capital loans (for auto dealers). Taxpayer also offers leasing

and installment lending businesses through various automobile dealerships throughout the United States. These activities are not performed in every state.

Taxpayer filed a protest of an assessment of gross income tax on lease payments and related income from the leases that the auditor sourced to Indiana. The taxpayer and Department determined that the facts related to the protest on lease arrangements were closely related to the *Enterprise Leasing* court case and deferred this Letter of Findings until the resolution of that case.

I. Gross Income Tax — Application to lease payments from Indiana

DISCUSSION

This issue was held pending the resolution of a court case, which has now been resolved. The decision by the tax court, *Enterprise Leasing Co. of Chicago v. Indiana Dep't of State Revenue,* 779 NE.2d 1284 (Ind. Tax Ct. 2002), review denied. By the Department's prior arrangement, taxpayer's protest of this issue is sustained pursuant to the court's holding in that case.

FINDING

Taxpayer's protest is sustained.

II. Adjusted Gross Income Tax — In-state sales

DISCUSSION

Taxpayer argues that other activity, aside from the leases at issue above, was improperly apportioned to Indiana. The relevant statute is IC 6-3-2-2, which states in relevant parts:

(a) With regard to corporations and nonresident persons, "adjusted gross income derived from sources within Indiana", for the purposes of this article, shall mean and include:

(1) income from real or tangible personal property located in this state;

(2) income from doing business in this state;

(3) income from a trade or profession conducted in this state;

(4) compensation for labor or services rendered within this state; and

(5) income from stocks, bonds, notes, bank deposits, patents, copyrights, secret processes and formulas, good will, trademarks, trade brands, franchises, and other intangible personal property if the receipt from the intangible is attributable to Indiana under section 2.2 of this chapter.

…

(b) Except as provided in subsection (*l*), if business income of a corporation or a nonresident person is derived from sources within the state of Indiana and from sources without the state of Indiana, then the business income derived from sources within this state shall be determined by multiplying the business income derived from sources both within and without the state of Indiana by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three (3).

…

Taxpayer asserts that none of the other income apportioned to Indiana was related to Indiana activity. Aside from the income excluded under the holding referenced in Issue, I, taxpayer has made no showing that any other income was improperly sourced to Indiana. Taxpayer has failed to provide either an argument or documentation to refute the audit's findings and the protest is denied.

FINDING

Taxpayer's protest is denied.

III. State Gross Retail Tax —Use tax

DISCUSSION

Taxpayer argues that an audit adjustment to add back property taxes as required by 45 IAC 3.1-1-8 defining adjusted gross income and required addbacks of state and local taxes. Taxpayer offers no explanation as to why the addbacks were reported for two of the first two audit years and then subsequently not included for the remainder of the period.

Taxpayer's argument centers on 45 IAC 17-3-1.1(3) which is a Financial Institutions Tax definition of adjusted gross income and ultimately irrelevant to the Adjusted Gross Income Tax adjustment.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0220020153.LOF

LETTER OF FINDINGS: 02-0153
Indiana Corporate Income Tax
For 1995 through 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. Lease/Sales Transactions – Gross Income Tax.

Authority: IC 6-2.1-1-2(a); IC 6-2.1-1-2(b); IC 6-2.1-2-2; IC 6-2.1-2-2(a); IC 6-2.1-2-2(a)(2); Enterprise Leasing v. Indiana Dept. of Revenue, 779 N.E.2d 1284 (Ind. Tax Ct. 2002); Comdisco, Inc. v. Indiana Dept. of Revenue, No. 49T10-9903-TA-19, 2002 Ind. Tax LEXIS 93 (Ind. Tax Dec. 18, 2002); 45 IAC 1.1-1-3(a), (b).

Taxpayer argues that the Department of Revenue erred when it determined that money received in the form of lease payments and money received from the sale of office equipment to Indiana customers was subject to gross income tax.

II. Ten-Percent Negligence Penalty – Tax Administration.

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

Taxpayer maintains that the Department should exercise its discretionary authority to abate the ten-percent negligence penalty.

STATEMENT OF FACTS

Taxpayer is an out-of-state company in the business of leasing and selling tangible personal property. Taxpayer typically leases items of office equipment such as copiers, fax machines, and phone systems. Taxpayer leases or sells office equipment to Indiana customers. Taxpayer finances the sale of office equipment to Indiana customers. Taxpayer sells used office equipment to Indiana customers.

The Department of Revenue (Department) conducted an audit review of taxpayer's business records and found that taxpayer should have been paying Indiana Gross Income Tax (GIT) on the money received in the form of lease payments and money received from the sale of office equipment to Indiana customers. Accordingly, the Department assessed GIT for 1995 through 2000. 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. This Letter of Findings results.

DISCUSSION

I. Lease/Sales Transactions – Gross Income Tax.

The Department found that taxpayer leased equipment to Indiana customers and concluded that the lease payments were subject to GIT. The audit report stated that, "Most of [taxpayer's] leases are true leases where the property is owned by them, depreciated by them, leased through them or one of their vendors, credit approved by them, and they retain title at the conclusion of the lease." In most cases, after the lease is concluded, the lessee has the right to purchase the item of equipment, but if the lessee decides not to buy the equipment, taxpayer "sells the product to someone else through his vendor in the state of Indiana or through [taxpayer's out-of-state office]."

In addition, the audit found that taxpayer had entered into "financing leases" which the audit described as "similar to an installment contract." Again, the audit found that taxpayer did not "subject any of these sales to the gross income tax." The audit concluded that the money taxpayer received from these sales was subject to GIT and assessed the tax accordingly.

According to taxpayer, its leasing business is conducted as follows:

A potential customer – interested in purchasing or leasing an item of office equipment – contacts an Indiana vendor. Customer decides on the specific item it wants to acquire. Vendor and customer agree on the cost of the equipment. Based upon preexisting "unwritten agreements" between taxpayer and each individual vendor, vendor provides customer a variety of lease options to customer including, presumably, the option of leasing the equipment from taxpayer. If customer decides to do business with taxpayer – and not one of taxpayer's competitors – vendor provides customer with a variety of lease options available through taxpayer. Among other lease or sales options, taxpayer provides a "non-cancelable lease, without a stated purchase option," a "90-day same as cash program," a "standard program with a 90 day deferment," and a "municipal program." In any case, it is the vendor's representative who acts as the intermediary soliciting the customer's lease or sales business on behalf of the taxpayer and describing taxpayer's sale or lease options to the Indiana customer.

After customer has decided to do business with taxpayer and after customer has decided which of taxpayer's lease/sales programs it wishes to choose, vendor supplies customer with the appropriate, blank paperwork; customer fills out a credit application and a "pre-drafted" lease/sales agreement. After customer fills out this paperwork, vendor faxes a copy to taxpayer. Upon receipt at taxpayer's out-of-state location, taxpayer either accepts or declines the proposed agreement.

If the agreement is accepted, vendor delivers the equipment from vendor's own stock to customer. If the delivered equipment is acceptable, customer accepts delivery, and taxpayer pays vendor for the cost of the equipment.

Taxpayer now owns the item of equipment because taxpayer bought the equipment from vendor. Customer thereafter pays money to taxpayer for the privilege of using that equipment at the customer's location or customer pays taxpayer in order to eventually acquire full ownership of the equipment.

Taxpayer maintains that its income from Indiana customers is not subject to gross income tax because it does not have an Indiana business situs.

Taxpayer states that it "has no employees or payroll located within the state of Indiana, nor any employees or agents that spend time in Indiana. [Taxpayer] does not have a sales-force that solicits business in Indiana and does not direct advertising into the Indiana market. All office functions are located [out-of-state]. [Taxpayer] has unwritten agreements with vendors all over the country for them to recommend [taxpayer] as the loan provider for the equipment."

Indiana imposed a tax, known as the "gross income tax," on the taxable gross income of taxpayer who is a resident or domiciliary of Indiana and on the taxable gross income from Indiana sources by a taxpayer who is not a resident or domiciliary of Indiana. IC 6-2.1-2-2. "Gross income" is defined to include "all the gross receipts a taxpayer receives... from the sale, transfer, or exchange of property, real or personal, tangible or intangible." IC 6-2.1-1-2(a).

There is no apparent dispute that the money taxpayer received constitutes "gross income" under IC 6-2.1-1-2(a). The issue is whether the money was "derived from activities or businesses or any other sources within Indiana" pursuant to IC 6-2.1-2-2(a)(2).

In deciding whether the money taxpayer earned was derived from sources within Indiana, "[T]he Court must (1) isolate the transaction giving rise to the income ('the critical transaction'), (2) determine whether the [taxpayer has] a physical presence in, or significant business activities within the taxing state ('business situs'), and (3) determine whether the Indiana activities are related to the critical transaction and are more than minimal, not remote or incidental to the transaction ('tax situs')." Enterprise Leasing v. Indiana Dept. of State Revenue, 779 N.E.2d 1284, 1290 (Ind. Tax Ct. 2002).

A. Critical Transaction.

"The critical transaction is defined as the particular activity that gives rise to the gross income in dispute." Id. In this case, the critical transactions are the various lease and sales agreements entered into between Indiana customers and out-of-state taxpayer.

B. Business Situs.

45 IAC 1.1-1-3(a), (b) provides that, "A 'business situs' arises where possession and control of a property right have been localized in some business or investment activity away from the owner's domicile. A taxpayer may establish a business situs in many ways, including, but not limited to.... [o]wnership, leasing, rental, or other business activity connected with income-producing property...."

Taxpayer has established an Indiana business situs because it leases business equipment to Indiana customers (true leases); taxpayer has established an Indiana business situs because it finances the sale of office equipment to its Indiana customers (financing leases); taxpayer has established an Indiana business situs because it sells used office equipment – following conclusion of a true lease – to Indiana customers who are in the market for purchasing these items. In effect, taxpayer has established an Indiana business situs because it owns office equipment – located within Indiana – from which it derives rental income or from which derives income when it sells the equipment. These activities plainly fall within the purview of 45 IAC 1.1-1-3(a), (b) because taxpayer owns income-producing office equipment located within Indiana. Taxpayer has a "property right" in a "business or investment activity away from [taxpayer's] domicile." Id. The analysis is straightforward. Taxpayer has an Indiana business situs because taxpayer leases or finances the sale of new office equipment to Indiana customers, and taxpayer sells used office equipment to Indiana customers.

C. Tax Situs.

In Indiana, "[A] 'business situs'... is insufficient by itself to impose tax on a nonresident's income." Enterprise Leasing, 779 N.E.2d at 1291-92. A taxpayer may have more than one "business situs." Id. at 1292. "This is especially true for tangible property, especially mobile property such as... cars and trucks...." Id.

In order to establish whether taxpayer has an Indiana tax situs, "[The] Court must examine whether the Petitioners' Indiana activities are related to the critical transaction and are more than minimal, not remote or incidental to the total transaction." Id. In its argument, taxpayer concludes that its leasing and financing business is analogous to that of the petitioner-taxpayers in Enterprise Leasing, 779 N.E.2d 1284. In that case, the Tax Court found that an out-of-state company did not receive Indiana source income when it rented Indiana-titled cars to its customers; therefore, the court concluded that petitioners' rental income was "not subject to Indiana's gross income tax." Id. at 1292. The court found that that money received from renting Indiana-titled cars was not Indiana source income because it was not the petitioners who decided to register and operate the cars within the state. Id. at 1291. Rather, it was the decision of the individual customers to register and operate the cars in Indiana. Id. The court found that the petitioners' activities in sending the cars to its customers "did not rise to the level of 'active participation' in the 'ownership, leasing, or rental' of property in Indiana." Id. The court determined that the "critical transaction" related to the leasing of the cars occurred at the petitioners' out-of-state location. Id. at 1290. Therefore, because the petitioners' activities within the state were "not more than minimal" and were "remote and incidental to the lease transaction from which [petitioners'] income [was] derived," and because *the critical transaction occurred outside the state*, the petitioners did not have an Indiana "tax situs." Id. at 1292. (*Emphasis added*). The court concluded that the petitioners' lease income was not "derived from sources within Indiana" and was not subject to the state's gross income tax. Id.

In addition, taxpayer cites to Comdisco, Inc. v. Indiana Dept. of Revenue, No. 49T10-9903-TA-19, 2002 Ind. Tax LEXIS 93 (Ind. Tax Dec. 18, 2002), in which the court found that income received from leasing "high technology and medical equipment" to customers within Indiana was not subject to gross income tax. Id. at *5. In Comdisco the court found that the petitioner/lessors only Indiana activity was "ownership of high technology equipment that [was] located pursuant to the lessees' direction." Comdisco, 2002

Ind. Tax LEXIS 93 at *22.

The Department is unable to agree that the decisions in either Enterprise or Comdisco are dispositive of the question of whether the taxpayer's receipts earned from the rental or sale of office equipment – brokered by representatives acting on behalf of the taxpayer – is subject to the gross income tax. In both Enterprise and Comdisco the fact that the tangible personal property happened to be located within Indiana was unrelated to the "critical transaction" which formed the basis for the petitioners' income. In taxpayer's situation, the rental and sales income is derived from immobile property located within this state and the "critical transaction[s]" – on which the taxpayer's income is predicated – were solicited and executed within the state.

The critical transactions consist of the agreements brokered between the customer and the vendors' representative. The vendors' representative – acting at the behest of taxpayer – solicits business on behalf of taxpayer from Indiana customers. When one of the vendors' representatives offers a prospective Indiana customer the opportunity to purchase or lease office equipment, that offer is made in Indiana to an Indiana customer; when one of the vendors' representatives solicits business on behalf of the taxpayer, negotiates the sales or lease cost on behalf of the taxpayer, and solicits credit information from the potential customer, those negotiations and solicitations occur at the Indiana location; when the paperwork is completed and customer finally accepts and signs the agreement, the customer does so while seated at a desk located in Indiana; when the Indiana vendor eventually delivers the office equipment – the "object" of each particular critical transaction – the vendor does so to a site specified in the lease or sale agreement.

Taxpayer's transactions are not analogous to the lease agreements in Enterprise. In that case, the court found that because the leased automobiles had little or no connection with the state of Indiana, the petitioner-lessor did not acquire an Indiana tax situs. Instead the leased automobiles were cast adrift into a stream of commerce by means of a "critical transaction" which occurred entirely outside the state. In taxpayer's own leasing and financing business, the critical transactions take place in this state and are facilitated by both the Indiana employees and the Indiana surrogate/agents acting on behalf of taxpayer. Unlike the automobiles in Enterprise, taxpayer's office equipment – the source of taxpayer's income – is determinedly fixed within this state.

Taxpayer has acquired both a business and tax situs within Indiana. Taxpayer earns money from Indiana customers attributable to transactions which – although given a final stamp of approval at an out-of-state location – are solicited, negotiated, and accepted at an Indiana location. There is a direct and immediate connection between the "critical transactions" and the office equipment the location of which is specified in each of the relevant transactions. The sales and lease income attributable to these same critical transactions is subject to Indiana's gross income tax.

FINDING

Taxpayer's protest is respectfully denied.

II. Ten-Percent Negligence Penalty – Tax Administration.

Taxpayer argues that its failure to report and pay gross income tax was not due to negligence and that the Department should exercise its discretion to abate the ten-percent negligence penalty.

IC 6-8.1-10-2.1 requires that a ten-percent penalty be imposed if the tax deficiency results from the taxpayer's negligence. Departmental regulation 45 IAC 15-11-2(b) defines negligence as "the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." Negligence is to "be determined on a case-by-case basis according to the facts and circumstances of each taxpayer." Id.

IC 6-8.1-10-2.1(d) allows the Department to waive the penalty upon a showing that the failure to pay the deficiency was based on "reasonable cause and not due to willful neglect." Departmental regulation 45 IAC 15-11-2(c) requires that in order to establish "reasonable cause," the taxpayer must demonstrate that it "exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed...."

Taxpayer indicates that it relied on certain Tax Court decisions in deciding that it had no gross income tax exposure. Taxpayer believes that its facts "are nearly identical to those in the Indiana cases with presidential (sic) value... and therefore provide a reasonable basis for excluding [its] gross income for purposes of gross income tax."

As noted above, the Department disagrees with taxpayer's position that it was not subject to gross income tax. Nonetheless, the Department is willing to agree that failure to remit the tax was due to "reasonable cause and not due to willful neglect." IC 6-8.1-10-2.1(d).

FINDING

Taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

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LETTER OF FINDINGS: 02-0609
Indiana Sales and Use Tax
For the Years 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.

ISSUES

I. Miscellaneous Purchases of Tangible Personal Property – Use Tax.

Authority: IC 6-2.5-3-5(a); IC 6-8.1-5-1(b).

Taxpayer maintains that it is not responsible for paying use tax on certain items of tangible personal property because taxpayer paid sales tax to another state at the time the items were first purchased or because taxpayer has already self-assessed use tax on these items.

II. Riverboat Purchase – Use Tax.

Authority: IC 6-2.5-1-1 et seq.; IC 6-2.5-3-2; IC 6-2.5-3-2(a); Gregory v. Helvering 293 U.S. 465 (1935); Ind. Dep't of State Revenue v. Trump Indiana, Inc., 814 N.E.2d 1017 (Ind. 2004); Grand Victoria Casino & Resort v. Dept. of State Revenue, 789 N.E.2d 1041 (Ind. Tax Ct. 2003); Bethlehem Steel Corp. v. Ind. Dept. of State Revenue, 597 N.E.2d 1327 (Ind. Tax Ct. 1992).

Taxpayer argues that it is not subject to use tax on the cost of buying a riverboat because the boat was built in a state which provides a sales/use tax exemption and because the boat was received as a consideration-free capital contribution.

III. Computation Error.

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

Taxpayer maintains that it is entitled to an abatement of a use tax assessment because the audit misinterpreted an entry on its record of invoices.

IV. Ten-Percent Negligence Penalty.

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

Taxpayer maintains that it is entitled to an abatement of the ten-percent negligence penalty because it did not intend to deliberately avoid the payment of taxes and because it did not act from negligence or an intentional disregard of the law.

STATEMENT OF FACTS

Taxpayer operates an Indiana riverboat along with an associated hotel, parking garage, golf course, pavilion, restaurants, and gift shop. During 2001, the Indiana Department of Revenue (Department) conducted an audit review of taxpayer's business and tax records. The audit review determined that taxpayer owed additional use tax. In November 2002, the Department issued a notice of "Proposed Assessment" to that effect. Taxpayer disagreed with the assessment and on December 2, 2002, submitted a protest. Following various delays and a change in taxpayer's representation, an administrative hearing was held during which taxpayer's representatives explained the basis for taxpayer's protest. This Letter of Findings results.

DISCUSSION

I. Miscellaneous Purchases of Tangible Personal Property – Use Tax.

Taxpayer maintains that the audit erroneously imposed use tax on certain tangible personal property for which taxpayer had paid sales tax to other states or for which it has already self-assessed use tax.

Taxpayer believes that it is entitled to an offsetting credit for amounts of use tax it paid to other states. IC 6-2.5-3-5(a) states that, "A person is entitled to a credit against the use tax imposed on the use storage or consumption of a particular item of tangible personal property equal to the amount, if any, of sales tax, purchase tax, or use tax paid to another state, territory, or possession of the United States for the acquisition of that property."

Taxpayer has responsibility for demonstrating the proposed assessment is incorrect. IC 6-8.1-5-1(b) provides 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 the person against whom the proposed assessment is made."

Taxpayer indicates that it has provided invoices from out-of-state vendors each of which supports taxpayer's contention that it was billed for and paid sales tax on the items purchased from those out-of-state vendors.

The administrative hearing is not the venue for examining taxpayer's invoices and determining to what extent it is entitled to the specific relief requested. However, taxpayer has met its burden of demonstrating that the invoices – to the extent that those invoices were included in the material provided before or at the time of the hearing – should be reviewed by the audit division. Accordingly, the audit division is requested to review taxpayer's invoices and to make whatever adjustments the audit division deems warranted.

FINDING

Subject to review by the audit division, taxpayer's protest is sustained.

II. Riverboat Purchase – Use Tax.

Taxpayer's parent company entered into a contract with an Alabama shipyard for the construction of a riverboat. Parent company eventually accepted title to and delivery of the riverboat while the riverboat was located in Alabama. Parent company paid Alabama shipyard a substantial amount of money for the riverboat. Parent company's board of directors arranged to transfer the riverboat to taxpayer as a "capital contribution, for no consideration." The riverboat was piloted into international waters at which

time financial responsibility and ownership interest was formally transferred from parent company to taxpayer. Thereafter – with ownership interest firmly vested in taxpayer – the riverboat was sailed up the Mississippi River to the final Indiana docking point.

Based upon taxpayer's description of the events noted above, taxpayer maintains that it does not owe use tax on the cost of the riverboat because it did not pay anything for the riverboat.

Indiana imposes a sales tax on retail transactions and a complimentary use tax on tangible personal property that is stored, used, or consumed in the state. IC 6-2.5-1-1 et seq. The use tax "is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC 6-2.5-3-2.

Taxpayer states that it is not subject to use tax because the riverboat was received in the form of a "capital contribution" from its parent company. If taxpayer's argument is understood correctly, parent company purchased the riverboat and then "contributed" the riverboat to taxpayer. According to taxpayer, because it did not obtain the riverboat in a "retail transaction," taxpayer has no use tax liability.

In Ind. Dep't of State Revenue v. Trump Indiana, Inc., 814 N.E.2d 1017 (Ind. 2004), the Indiana Supreme Court determined that a riverboat was tangible personal property the acquisition of which was subject to use tax. Taxpayer argues that its parent company acquired the riverboat from the shipyard, that the riverboat was transferred to taxpayer in the form of a "capital contribution," and that the intervening transaction immunized taxpayer from paying use tax. Taxpayer points to the Tax Court's decision in Grand Victoria Casino & Resort v. Dept. of State Revenue, 789 N.E.2d 1041 (Ind. Tax Ct. 2003) for support of its position that tangible personal property received in the form of a capital contribution is not subject to use tax. In that case, petitioner Grand Victoria was a company that was formed as the result of the merger of two predecessor companies. Id. at 1043. When the two predecessor companies merged, they made a capital contribution – consisting of a riverboat – to Grand Victoria, the successor company. Id. The Tax Court agreed with petitioner's position that the transfer of the riverboat was not subject to sales tax, "because the capital contribution was a transfer of property without consideration... [and] does not constitute selling at retail and therefore is not subject to sales tax." Id at 1046. In addition, the court went on to reject the Department's alternative argument – that the petitioner's riverboat was subject to use tax – because "a licensed riverboat is real property." Id. at 1048 n.9.

The Department is unwilling to agree that the Tax Court's decision in Grand Victoria is dispositive of the issue here in question. As noted above, the Indiana Supreme Court has determined that – for sales and use tax purposes – a "casino riverboat, like any other boat, is 'tangible personal property.'" Trump Indiana, 814 N.E.2d at 1021.

The issue is whether taxpayer's particular acquisition of its own riverboat is subject to the state's use tax. IC 6-2.5-3-2(a) states that, "An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." Plainly, the casino riverboat is "tangible personal property." Plainly, the riverboat was acquired in a "retail transaction" because parent company paid the Alabama shipyard millions of dollars in exchange for the vessel. Plainly parent company did not pay Alabama sales tax at the time it paid for the completed riverboat because Ala. Stat. § 40-23-4(12) exempts such vessels from Alabama tax. Nevertheless, taxpayer relies on the proposition that parent company's transitory ownership and intervening transfer of the riverboat to taxpayer insulates taxpayer from use tax liability.

The Department is unable to agree that taxpayer's argument is supported by either law or common sense. The fact that parent company bought the riverboat on behalf of taxpayer and that parent company officially transferred ownership of the vehicle during the vessel's brief sojourn in the Gulf of Mexico is little more than an empty formality devoid of either practical or legal substance. As noted in Bethlehem Steel Corp. v. Ind. Dept. of State Revenue, 597 N.E.2d 1327 (Ind. Tax Ct. 1992), "In Indiana, tax consequences generally are determined by the substance rather than the form of a transaction." Id. at 1331. (A corporate business activity undertaken merely for the purpose of avoiding taxes is without substance and "[t]o hold otherwise would be to exalt artifice above reality and to deprive the statutory provision in question of all serious purpose." Gregory v. Helvering 293 U.S. 465 (1935)).

IC 6-2.5-3-2 has a "serious purpose," and use tax liability – whether for a lawn mower, a refrigerator, or riverboat – is not lightly circumvented. The riverboat was acquired in a retail transaction and was transferred to Indiana. Taxpayer now enjoys the "use" and benefit of that riverboat. The riverboat is subject to Indiana use tax.

FINDING

Taxpayer's protest is respectfully denied.

III. Computation Error.

Taxpayer states that the Department erred in assessing use tax on particular tangible personal property. Specifically, taxpayer claims the audit misread a 2000 journal entry as indicating the tangible personal property cost $234,000 when, in fact, the item cost $23,400. To that end, taxpayer has supplied a copy of an invoice indicating the purchase price of the item was $23,400. As set out in Part I above, "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). Taxpayer has met its burden of demonstrating that the audit division should revisit this particular issue and make whatever adjustment the audit division deems warranted.

FINDING

Subject to review by the audit division, taxpayer's protest is sustained.

IV. Ten-Percent Negligence Penalty.

Taxpayer maintains that it has established reasonable cause for failing to pay use tax on the items protested, that it did not willfully neglect its duty to pay use tax, and that it relied on established law in determining that it did not owe use tax on the items assessed. Therefore, taxpayer believes that it is entitled to abatement of the ten-percent negligence penalty.

IC 6-8.1-10-2.1 requires that a ten-percent penalty be imposed if the tax deficiency results from the taxpayer's negligence.

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

IC 6-8.1-10-2.1(d) allows the Department to waive the penalty upon a showing that the failure to pay the deficiency was based on "reasonable cause and not due to willful neglect." Departmental regulation 45 IAC 15-11-2(c) requires that in order to establish "reasonable cause," the taxpayer must demonstrate that it "exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed...."

As noted above in parts I and II, taxpayer is entitled to a correction of the use tax assessment to the extent that it has supplied additional information or the extent that the audit may have made an error in its computation. It follows then, that the ten-percent negligence penalty attached to those particular amounts will resolve itself because any correction in the assessment will lead to a correction in the amount of penalty. Nonetheless, the bulk of the assessment stems from taxpayer's failure to self-assess use tax at the time it – or its parent company – acquired the riverboat. Although, taxpayer's argument is not totally fanciful, the Department is unable to agree that taxpayer exercised "ordinary business care and prudence... " when taxpayer concluded – without seeking guidance from the Department in the form of a formal or informal ruling – that it could wholly avoid use tax liability by gaining control of a multi-million dollar riverboat as a "capital contribution" and thereafter make "use" of that riverboat within Indiana.

FINDING

Taxpayer's protest is respectfully denied.

DEPARTMENT OF STATE REVENUE

02-20030166.LOF

LETTER OF FINDINGS NUMBER: 03-0166
Adjusted Gross Income 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. Business / Non-business Classification – Adjusted Gross Income Tax.

Authority: Ind. Code § 6-3-1-20; Ind. Code § 6-3-1-21; Ind. Code § 6-3-2-2; I.R.C. § 338; *May Dep't Stores Co. v. Indiana Dep't of State Revenue*, 749 N.E.2d 651 (Ind. Tax 2001).

Taxpayer protests the reclassification of income derived from an I.R.C. § 338(h)(10) election from business income to nonbusiness income.

STATEMENT OF FACTS

Sub W was a corporation based in Indiana. For several years prior to 1998, Sub W and a number of other corporations were wholly owned by a parent corporation which filed federal consolidated income tax returns; however, Sub W filed separate Indiana income tax returns.

In 1996, Sub W's parent corporation was acquired by another corporation ("Acquirer"). Because Acquirer was not based in the United States, Sub W and other acquired corporations could not file consolidated income tax returns. Taxpayer and two other subsidiaries were eligible to file consolidated returns in Indiana. On November 30, 1997, Taxpayer and other domestic companies owned by Acquirer were contributed to a new company ("New Company'). New Company was eligible to file a consolidated federal income tax return, of which Taxpayer was the reporting company.

On December 26, 1997, Sub W was sold to an unrelated corporation as part of an agreement entered into on November 17, 1997. As a result of the purchase, New Company made an election under I.R.C. § 338(h)(10) to treat the sale of Sub W's stock as a deemed sale of Sub W's assets for the fair market value of the stock. The effect of this election was to cause Sub W to realize income on the deemed sale of its assets and include that income on New Company's consolidated federal income tax return, while Sub W received a stepped-up basis in its assets.

For the first and only time as part of Taxpayer's consolidated group, Taxpayer filed a consolidated return including Sub W and

treating the gains from the I.R.C. § 388(h)(10) election as business income. Sub W was not included on a consolidated return or a unitary return for several years (possibly never) prior to Taxpayer's return for the year at issue. The Department, however, determined that the sale of assets was in fact non-business income allocable to Sub W's commercial domicile, Indiana. Taxpayer filed a protest, and a hearing was held.

I. Business / Non-business Classification – Adjusted Gross Income Tax

DISCUSSION

In general, the sale of stock in a corporation ('target corporation"), such as Sub W's sale in this protest, results in income to the shareholders that sold the stock. The target corporation retains its basis in the underlying assets.

Generally, if a corporation liquidates its assets, it is treated as selling its assets to its shareholders at the fair market value of the assets, and realizes income or loss accordingly. I.R.C. § 336. The shareholders receive a basis in the assets received equal to the fair market value of the asset at the time of liquidation. I.R.C. § 334. This shall be called "shareholder treatment."

However, a liquidation of a corporation's assets to its parent is ordinarily results in the liquidating corporation not realizing any gain or loss on the sale of its assets, but the parent retains the basis in the assets that the liquidating corporation had in those assets. I.R.C. §§ 332, 337.

Under I.R.C. § 338(a), a purchasing corporation of a target corporation may elect shareholder treatment with respect to its assets. The assets in the deemed liquidation are treated as having the same fair market value of the stock purchased (subject to certain exceptions not material to this case), and are being treated as being distributed back to the target corporation the day after acquisition. Thus, the target corporation is treated as realizing gain or loss on its assets, and it receives a stepped-up (or stepped-down, in rare cases) basis in its assets.

Under I.R.C. § 338(h)(10), shareholder treatment is permissible for the seller's consolidated group. Thus, the gain or loss from the deemed liquidation under § 338(a) is recognized by the consolidated group. However, unlike regular shareholders who are treated as selling their stock for the value of the assets received in liquidation under I.R.C. § 331, the seller's consolidated group does not realize gain or loss from the sale of stock. In the transaction from which this protest arose, New Company made a 338(h)(10) election with respect to the sale of Sub W, and thus Sub W was treated as liquidating its assets on December 26, 1997, and Sub W was treated as realizing income on this sale for federal income tax purposes, while New Company included this income on New Company's consolidated federal income tax return. The question for Indiana is whether the income from the deemed liquidation of Sub W's assets is business income or non-business income. Further, if the income is treated as business income, an issue arises whether Taxpayer's return fairly reflects Indiana income and whether appropriate remedial measures are warranted.

Ind. Code § 6-3-1-20 provides:

> The term "business income" means income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management and disposition of the property constitutes integral parts of the taxpayer's regular trade or business.

Conversely, Ind. Code § 6-3-1-21 provides that "nonbusiness income" means all income other than business income. Under the provisions of Ind. Code § 6-3-2-2, business income of a corporation is subject to apportionment to Indiana, while nonbusiness income is generally allocable to the corporation's domicile.

In *May Dep't Stores Co. v. Indiana Dep't of State Revenue*, 749 N.E.2d 651 (Ind. Tax 2001), the court determined that business income was defined by two tests. The first test, the transactional test looks at

(1) the frequency and regularity of similar transactions;

(2) the former practices of the business; and

(3) the taxpayer's subsequent use of the income.

Id. at 658-659.

In *May*, a corporation that owned several large department store chains purchased a rival department store chain. As a result of the purchase, an antitrust case was launched against the corporation. In settlement of the antitrust claim, the corporation sold the assets of one of its divisions. As a result of the asset sale, the corporation realized a gain that it treated as nonbusiness income, allocable to the corporation's domicile; however, the Indiana Department of State Revenue determined that the income was business income apportionable to Indiana and other states. The court held that, because the sale of the assets was a one-time, extraordinary transaction, the sale did not meet the transactional test for business income. *Id.* at 664. Applying the test from *May,* the deemed asset sale of Sub W did not meet the transactional test because the deemed sale of Sub W's assets was a one-time occurrence, rather than part of Sub W's regular business activities.

The second test, the functional test, "dictates that acquisition, management, use or rental, *and* disposition of property must constitute integral parts of regular business operations." *Id.* at 660 (emphasis added). In *May,* the court noted that the sale of the assets of the division in question was done to benefit a competitor, rather than the corporation that previously owned the division. As a result, the sale could not have been an integral part of the corporation's business, and therefore the sale failed to meet the functional agreement. *Id.* at 665.

Here, the property from which Sub W realized the income at issue was clearly part of its overall business and was generated

as part of its overall business enterprise (goodwill). As such, the income from the deemed sale of Taxpayer was business income within the meaning of Ind. Code § 6-3-1-20.

However, Sub W's situation was an unusual situation under which Indiana law is not entirely clear. Here was Sub W's scenario:

1989-1996—Sub W is owned by a previous owner. Sub W is part of a federal consolidated return but files separate Indiana returns.

1996- November 30, 1997—Sub W is owned by Acquirer. Sub W is ineligible to be part of a consolidated group; however, three subsidiaries are eligible for consolidation for Indiana purposes. (Taxpayer, Sub 1, Sub 2).

November 17, 1997—An unrelated company agrees to purchase Sub W.

November 30, 1997—Sub W's and another subsidiary's (Sub 3) ownership are changed within their affiliated group to New Company, removing the obstacle that prohibited its inclusion on a consolidated return.

December 1, 1997-December 26, 1997—Sub W is part of an affiliated group with Taxpayer, Sub 1, Sub 2, and Sub 3.

December 26, 1997—Sub W's sale to an unrelated third party is completed.

December 27, 1997-March 30, 1998—Taxpayer, Sub 1, Sub 2, and Sub 3 are part of an affiliated group.

Under federal law, it is clear what happens: Taxpayer, Sub 1 and Sub 2 include all of their income on a consolidated return. Sub 3 files a separate return for the period prior to December 1, and includes its income on or after December 1 on a consolidated return. Sub W files a separate return for the period prior to December 1, includes its income from December 1 to December 26 on the consolidated return, and then files yet another short-year return (or includes its income on its buyer's affiliated return) for the period after December 26.

Under Ind. Code § 6-3-2-2(*l*), the Department may take various remedial measures to fairly represent Taxpayer's and Sub W's income from Indiana sources for Taxpayer's and Sub W's business activity. In addition to three methods listed in subsection (*l*), the Department may also employ "any other method to effectuate an equitable allocation and apportionment of the taxpayer's income." Ind. Code § 6-3-2-2(*l)*(4).

While the general rule for consolidated returns is that the "standard method" (i.e., the members of the consolidated group are considered as one business for tax purposes), the current case requires a "stacked" method (i.e., each company Indiana income for Indiana purposes is determined separately, then added together to reach the consolidated group's overall Indiana income) with respect to Sub W due to the normal method's significant underreporting of Indiana income. Sub W historically had an Indiana apportionment factor of approximately 90 percent. Sub W sought to offset its income with business deductions for salaries, equipment, and other necessary expenses for its entire history until November 30, 1997. However, Sub W's sale, agreed to prior to its membership in the consolidated group, resulted in a $120,000,000 gain—derived largely from Indiana sources—transforming into a $9,000,000 gain (basically, computing the income and apportionment factors with Sub W in the consolidated group, and then without Sub W in the consolidated group). In effect, Sub W has sought to benefit from deducting 90 percent of its expenses for Indiana tax purposes for years, but the resulting income generated by the sale of its assets—the converse of its deductions—is only reported at about eight percent of Sub W's total income. Treating Sub W as a separate entity from the rest of the consolidated group would fairly reflect the income of Sub W from Indiana sources in two ways. One, it would reflect the fact that Sub W had always been a separate filer for several years, even when it was eligible to file federal consolidated returns, and had no tax relationship with the other members of the consolidated group other than 26 days in which Sub W's sale to a third party was a foregone conclusion. Second, it would prevent the dilution of Sub W's income, mostly derived from Indiana sources, by increasing the apportionment factor for the income in question from roughly 8 percent to 90 percent—its historical apportionment factor. This method is the best reflection of Sub W's and Taxpayer's income from Indiana sources.

FINDING

Taxpayer's protest is sustained with respect to the classification of income as business income. Taxpayer's protest is denied with respect to the apportionment methodology used by Taxpayer rather than the method set forth in this letter of findings.

DEPARTMENT OF STATE REVENUE

0220040067.LOF

LETTER OF FINDINGS NUMBER: 04-0067
Income Tax
For Tax 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.

ISSUES

I. Adjusted Gross Income Tax—Combined Filing Status

Authority: Harrington v. State Board of Tax Commissioners, 525 N.E. 2d 360 (Ind. Tax 1988); Johnson v. Kosciusko County Drainage Board, 594 N.E. 2d 798 (Ind. App. 1992); IC 6-3-2-2; IC 6-8.1-5-1

Taxpayer protests the Department's decision to require filing a combined return.

II. 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 the imposition of a ten percent negligence penalty.

STATEMENT OF FACTS

Taxpayer operates businesses at several Indiana locations. As the result of an audit, the Indiana Department of Revenue ("Department") determined that taxpayer should file a combined return with related companies forming a unitary group and issued proposed assessments. The related companies interact with each other in a variety of ways, including filing as a consolidated group for Federal income purposes, and taxpayer does not disagree that there is a unitary group. Taxpayer protests the determination that it should file combined returns, the proposed assessments, and the negligence penalty. Further facts will be supplied as required.

I. Adjusted Gross Income Tax—Combined Filing Status

DISCUSSION

Taxpayer protests the determination that it should file combined returns with related companies in the unitary group. Taxpayer also protests the imposition of additional adjusted gross income tax for the tax years in question. The Department conducted an audit of taxpayer and determined that a combined return was necessary to fairly reflect the unitary group's income derived from sources within the state of Indiana. Both taxpayer and the Department agree that the affiliated companies constitute a unitary group. Taxpayer believes that the existence of a unitary group does not automatically require combined filing and that its method of filing as a single company fairly reflected taxpayer's Indiana source income. Taxpayer offers several arguments in support of its protest.

First, taxpayer states that the Department cannot force taxpayer to report its Indiana taxable income on a combined basis without first providing evidence that the separate filing does not fairly reflect Indiana source income. The Department refers to IC 6-8.1-5-1(b), which explains that the notice of proposed assessment is itself prima facie evidence that the Department's claim for unpaid tax is valid and that the burden of proving the claim wrong rests with the taxpayer. Nevertheless, the audit report does list the relationships of the companies involved and provides calculations explaining how the assessments were reached.

Next, taxpayer states that the Department cannot simply force a taxpayer to file a combined return without first showing that the filing method it used does not fairly reflect or represent Indiana source income. The relevant statute is IC 6-3-2-2, which states in relevant parts:

> (a) With regard to corporations and nonresident persons, "adjusted gross income derived from sources within Indiana", for the purposes of this article, shall mean and include:
>
> (1) income from real or tangible personal property located in this state;
>
> (2) income from doing business in this state;
>
> (3) income from a trade or profession conducted in this state;
>
> (4) compensation for labor or services rendered within this state; and
>
> (5) income from stocks, bonds, notes, bank deposits, patents, copyrights, secret processes and formulas, good will, trademarks, trade brands, franchises, and other intangible personal property if the receipt from the intangible is attributable to Indiana under section 2.2 of this chapter.
>
> …
>
> (b) Except as provided in subsection (*l*), if business income of a corporation or a nonresident person is derived from sources within the state of Indiana and from sources without the state of Indiana, then the business income derived from sources within this state shall be determined by multiplying the business income derived from sources both within and without the state of Indiana by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the denominator of which is three (3).
>
> …
>
> (*l*) If the allocation and apportionment provisions of this article do not fairly represent the taxpayer's income derived from sources within the state of Indiana, the taxpayer may petition for or the department may require, in respect to all or any part of the taxpayer's business activity, if reasonable:
>
> (1) separate accounting;
>
> (2) the exclusion of any one (1) or more of the factors;
>
> (3) the inclusion of one (1) or more additional factors which will fairly represent the taxpayer's income derived from sources within the state of Indiana; or
>
> (4) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.
>
> (m) In the case of two (2) or more organizations, trades, or businesses owned or controlled directly or indirectly by the same

interests, the department shall distribute, apportion, or allocate the income derived from sources within the state of Indiana between and among those organizations, trades, or businesses in order to fairly reflect and report the income derived from sources within the state of Indiana by various taxpayers.

…

(o) Notwithstanding subsections (*l*) and (m), the department may not, under any circumstances, require that income, deductions, and credits attributable to a taxpayer and another entity be reported in a combined income tax return for any taxable year, if the other entity is:

(1) a foreign corporation; or

(2) a corporation that is classified as a foreign operating corporation for the taxable year by section 2.4 of this chapter.

(p) Notwithstanding subsections (*l*) and (m), the department may not require that income, deductions, and credits attributable to a taxpayer and another entity not described in subsection (o)(1) or (o)(2) be reported in a combined income tax return for any taxable year, unless the department is unable to fairly reflect the taxpayer's adjusted gross income for the taxable year through use of other powers granted to the department by subsections (*l*) and (m).

Taxpayer's protest states:

IC 6-3-2-2(*l*) grants the Department authority to force a combined filing **if, and only if**, the statutory apportionment method used "…does not fairly represent the taxpayer's income derived from sources within the state of Indiana…."

Taxpayer then states:

This precondition is reemphasized later in the same statute, which states: "…the department may not require that income, deductions, and credits attributable to a taxpayer and another entity…be reported in a combined return **UNLESS** the department is unable to fairly reflect the taxpayer's adjusted gross income…." IC 6-3-2-2(p)(emphasis added).

As IC 6-3-2-2(*l*)(4) plainly states, the Department is permitted to employ any other method to effectuate an equitable allocation and apportionment of the taxpayer's income. Also, as previously explained, the audit report includes calculations detailing how the Department determined the amounts of the proposed assessments. The auditor used the apportionment methods provided in IC 6-3-2-2 to determine the Indiana apportionment factor. As explained in the audit report, the Department believes that a combined return is the only proper method to fairly allocate and apportion this taxpayer's income, as provided in IC 6-3-2-2(p)

Taxpayer refers to a previous Letter of Findings (LOF) issued to an unrelated party in which the Department decided that the taxpayer should not file a combined return. In that LOF, the Department determined that most of the companies in that unitary group did not have nexus with Indiana and had no Indiana source income. The Department ruled that since the companies had no Indiana source income, but did have out-of-state losses, the only reason to include those companies would be to dilute income received by the two companies which did have Indiana source income. Since this would not fairly reflect Indiana adjusted gross income tax, the Department denied that taxpayer's protest to file a combined return.

Taxpayer believes that in the instant case, since it too has companies with no Indiana nexus, then those companies should not be included in a combined return. The fundamental difference is that here the non-Indiana nexus companies do have Indiana-source income. Taxpayer protests that merely being in a unitary group does not automatically require combined filing. Taxpayer is correct that unitary status is not the sole determining factor. However, combined filing is required if members of a unitary group are deriving income from Indiana sources. In this case, members of the unitary group are deriving income from Indiana sources and combined filing is required to fairly reflect the group's Indiana adjusted gross income tax, as provided by the various subsections of IC 6-3-2-2.

Taxpayer also protests that the Department has not promulgated regulations that specifically set forth objective standards to determine whether a taxpayer's use of the statutory apportionment scheme does or does not fairly reflect their Indiana source income. Taxpayer refers to several court cases to establish that Indiana has an "ascertainable standards" rule requiring state agencies to set out rules for those who may have contact with those agencies. In Harrington v. State Board of Tax Commissioners, 525 N.E. 2d 360 (Ind. Tax 1988), the court explained:

In order to satisfy due process, an administrative decision must be in accord with previously stated, ascertainable standards. This requirement is to make certain that administrative decisions are fair, orderly and consistent rather than irrational and arbitrary. The standards should be written with sufficient precision to give fair warning as to what the agency will consider in making its decision. And finally, the standards should be readily available to those having potential contact with the administrative body.

Id., at 361.

In Johnson v. Kosciusko County Drainage Board, 594 N.E. 2d 798, 803 (Ind. App. 1992), the court further clarified, "However, these standards need only be as specific as circumstances permit considering the purpose to be accomplished." The Department believes that its regulations are as specific as circumstances permit considering their purpose. Taxpayer believes that the Department's regulations do not meet this standard, but offers insufficient evidence and analysis to support this position.

Taxpayer also protests that the audit does not give credit for taxes already paid by the previously single-filing member of the unitary group. These taxes flow from Indiana source income. The Indiana source income is included in the apportionment formula used to reach the unitary group's Indiana apportionment percentage. Therefore, taxpayer should get credit for taxes already paid on Indiana source income for these tax years.

In conclusion, the Department is permitted to require combined filing by a unitary group if it fairly reflects Indiana source income, under the various provisions of IC 6-3-2-2. In this case, combined filing does fairly reflect Indiana source income of the unitary group. The proposed assessment is prima facie evidence that the claim for unpaid tax is correct, and the burden is on the taxpayer to prove the proposed assessment incorrect, under IC 6-8.1-5-1(b). Taxpayer has not met this burden. The Department's regulations meet the "ascertainable standards" requirement of Harrington, by being as specific as circumstances permit considering their purpose, as explained in Johnson. Taxes previously paid on Indiana source income should be credited and taken into account when calculating the unitary group's assessment.

FINDING

Taxpayer's protest is denied regarding combined filing status and sustained regarding credit for taxes previously paid.

II. Tax Administration—Negligence Penalty

DISCUSSION

The Department issued proposed assessments and the ten percent negligence penalty and interest for the tax years in question. Taxpayer protests the imposition of penalty and interest. Taxpayer states that interest should be calculated on the amount of tax left after it is credited with taxes previously paid by the single filer member of the unitary group. With regard to interest, the Department refers to IC 6-8.1-10-1, which states in relevant part:

(a) If a person fails to file a return for any of the listed taxes, fails to pay the full amount of tax shown on his return by the due date for the return or the payment, or incurs a deficiency upon a determination by the department, the person is subject to interest on the nonpayment.

…

(e) The department may not waive the interest imposed under this section.

Since taxpayer incurred a deficiency upon a determination by the Department, as explained in Issue I, the Department may not waive interest under IC 6-8.1-10-1. However, the interest should be calculated on the correct amount of tax, which would constitute the underpayment after crediting tax already paid.

With regard to the 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 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.

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). Taxpayer has affirmatively established by documentation and explanation 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). The interest cannot be waived, under IC 6-8.1-10-1, but will be calculated on the amount of unpaid tax after credit is given for taxes already paid. The negligence penalty shall be waived.

FINDING

Taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

02-20040124.LOF

LETTER OF FINDINGS NUMBER: 04-0124
Corporate Income Tax
For Tax Years 1996 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 this document will provide the general public with information about the Department's official position concerning a specific issue.

I. Corporate Income Tax—Consolidated Return

Authority: IC 6-8.1-5-1(b); 45 IAC 15-5-3(b); IC 6-3-4-14; IC 6-3-2-2(l)

Taxpayer protests that it should be included in the Indiana consolidated return.

II. Tax Administration—Negligence Penalty and Interest

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

Taxpayer protests the imposition of a ten percent negligence penalty and interest.

STATEMENT OF FACTS

Taxpayer is a Delaware corporation that is headquartered in California. More facts will be provided as needed below.

I. Corporate Income Tax—Consolidated Return

DISCUSSION

Before examining the taxpayer's protest, it should be noted that the *taxpayer* bears the burden of proof. IC 6-8.1-5-1(b) states in pertinent 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 Indiana Administrative Code also states "[t]he burden of proving that a proposed assessment is incorrect rests with the taxpayer…." 45 IAC 15-5-3(b).

The auditor stated the following regarding the taxpayer:

> [The taxpayer's] function is to provide management services that includes, to supervise and maintain business operations at [Company X] and to promote sales. Management fees were paid to [taxpayer] only in 1996 and 1997…. In 1998 and 2000 [taxpayer's] only income was from a nominal amount of interest income. [Taxpayer] does not have nexus in Indiana nor does it have any income from Indiana sources. The management services, when performed, were performed in California. Its income, losses, apportionment factors are being deleted from the tax returns.

Regarding the taxpayer's argument, it should be noted that taxpayer's initial protest letter and its subsequent protest letter offer what appear to be different arguments (the former unitary, the subsequent consolidated). The taxpayer in the subsequent letter (dated February 23, 2006) states:

> Taxpayer intends that this [2/23/06 letter] Amended Protest and Request for Hearing relate back to the Original Protest and amend same to set forth the following grounds for relief which shall *supersede and strike the Grounds for Taxpayer's Disagreement found in its Original Protest*….

(*Emphasis* added). Thus the arguments from the "Original Protest" letter are not addressed in this Letter of Finding, since the taxpayer in effect told the Department to disregard the initial ("Original Protest") letter.

IC 6-3-4-14 provides that, "An affiliated group of corporations shall have the privilege of making a consolidated return with respect to the taxes imposed by IC 6-3." Thus the taxpayer argues that it "should be included in the consolidated Indiana Return for the Audit Period." Taxpayer states the following:

> [Taxpayer] ("Designated Agent") was a Delaware corporation with its commercial domicile located in Yorba Linda, California. During the Years-at-Issue, Designated Agent was engaged in several business activities within the state of Indiana, including, but not limited to; receipt of management fees from management services it performed for [Company X], its subsidiary, located in Indiana; employment of one employee at [Company X]; reimbursement of travel expenses for multiple officers who met, on several occasions, at the [Company X] facility; the Guarantee and payment of rent obligations on behalf of [Company X] for third-party asset lease obligations in Indiana; payment of royalty expenses on behalf of [Company X] for third-party royalty agreements in Indiana; payment on behalf of [Company X] for certain 1997 real estate and personal property taxes located in Indiana; payment of employee life insurance premiums on behalf of the [Company X] facility in Indiana; and receipt of interest income from loans to [Company X] where the proceeds of such loans were applied in Indiana for the above-mentioned expenses.

Despite taxpayer's above assertions regarding property, payroll, and sales, the audit report does not appear to show any Indiana property, payroll, or sales for the taxpayer. For example, the taxpayer claims to have an Indiana employee, but no Indiana payroll is shown in the audit; the taxpayer claims to have interest from Indiana but no Indiana receipts are reflected in the audit. Taxpayer had no Indiana source income, since there were no Indiana numerators in the taxpayer's apportionment.

Additionally, even if the taxpayer were to prevail, *arguendo*, on its argument regarding nexus the taxpayer still loses on other grounds. Namely, IC 6-3-2-2(l), which states:

> If the allocation and apportionment provisions of this article do not *fairly represent* the taxpayer's income derived from sources within the state of Indiana, the taxpayer may petition for or the department may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

(1) separate accounting;
(2) the exclusion of any one (1) or more of the factors;
(3) the inclusion of one (1) or more additional factors which will fairly represent the taxpayer's income derived from sources within the state of Indiana; or
(4) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

(*Emphasis* added). Since there appears to be no reported property, payroll, or sales, bringing substantial losses into Indiana runs afoul of the "fairly represent" language of IC 6-3-2-2(l).

FINDING

Taxpayer's protest is denied.

II. Tax Administration—Negligence Penalty and Interest

DISCUSSION

Taxpayer protests the imposition of a ten percent penalty. The Department refers to IC 6-8.1-10-2.1 and to 45 IAC 15-11-2(b), the latter of 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 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.

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.

The taxpayer argues its "conduct was based on a bona fide question of law with respect to its activities and was not due to negligence or willful neglect." However, as noted in Section I. *supra*, the taxpayer bears the burden of proof. The taxpayer has failed to adequately develop its argument and meet that burden of proof. (It should also be noted that the taxpayer did not develop any argument regarding interest, and the Department refers to IC 6-8.1-10-1(e)).

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20040353P.LOF

LETTER OF FINDINGS NUMBER 04-0353P
TAX ADMINISTRATION (USE TAX)—
NEGLIGENCE PENALTIES FOR THE REPORTING PERIODS
COVERING CALENDAR YEARS 2001-03

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. Tax Administration—Negligence Penalties—Audit Deficiencies—Ignorance of Law

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); 45 IAC §§ 15-5-3(b)(8) and -11-2 (2004)

II. Tax Administration—Negligence Penalties—Audit Deficiencies (Use Tax)—Reliance on Vendor's Representation It Would Pay Sales Tax—Burden of Proof

Tax Administration—Negligence Penalties—Audit Deficiencies (Use Tax)—Purchaser's Constructive Knowledge of Liability for Use Tax on Interstate Purchases

Authority: IC §§ 6-2.5-3-4(a)(1) and -5 (1998) (current respective versions at *id.* (2004)); IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); *Nelson v. Sears, Roebuck & Co.*, 312 U.S. 359, 363 (1941); *Ind. Dep't of State Rev. v. Trump Ind. Inc.*, 814 N.E.2d 1017, 1019 (Ind. 2004); *State v. Huffman*, 643 N.E.2d 899, 900 (Ind. 1994); *Peabody Coal Co. v. Ralston*, 578 N.E.2d 751, 754 (Ind. Ct. App. 1991); *Porter Mem'l Hosp. v. Malak*, 484 N.E.2d 54, 58 (Ind. Ct. App. 1985); *Morton Bldgs., Inc. v. Ind. Dep't of State Rev. (Morton Bldgs.*

VII), 819 N.E.2d 913, 915 (Ind. Tax Ct. 2004), *review denied* 831 N.E.2d 744 (Ind. 2005) (table); *Canal Sq. Ltd. Partnership v. State Bd. of Tax Comm'rs*, 694 N.E.2d 801, 804 (Ind. Tax Ct. 1998); *Longmire v. Ind. Dep't of State Rev.*, 638 N.E.2d 894, 898 (Ind. Tax Ct. 1994); *USAir, Inc. v. Ind. Dep't of State Rev.* (*USAir II*), 623 N.E.2d 466, 468-69 (Ind. Tax Ct. 1993); *Morton Bldgs., Inc. v. Comm'r of Revenue*, 683 N.E.2d 720, 722 (Mass. App. Ct. 1997); *Bullock v. Foley Bros. Dry Goods Corp.*, 802 S.W.2d 835, 839 (Tex. App. 1990); 45 IAC § 2.2-3-20 (1996) (2001) (current version at *id.* (2004)); 45 IAC §§ 15-3-2(e), -5-3(b)(8) and -11-2 (2004); 68 Am. Jur. 2d *Sales and Use Taxes* § 168 (2004); BLACK'S LAW DICTIONARY 190 (7th ed. 1999) ("burden of persuasion" and "burden of proof")

III. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); *State Bd. of Tax Comm'rs v. New Castle Lodge # 147, L.O.O.M.*, 765 N.E.2d 1257, 1264 (Ind. 2002); *Hoogenboom-Nofziger v. State Bd. of Tax Comm'rs*, 715 N.E.2d 1018, 1024 and 1024-25 (Ind. Tax Ct. 1999); 45 IAC §§ 15-5-3(b)(8) and -11-2 (2004)

The taxpayer protests the Audit Division's proposed assessment of negligence penalties.

STATEMENT OF FACTS

The Department's Audit Division conducted a field audit of the taxpayer for the tax type and reporting periods set out in the heading of this Letter of Findings. As a result of the audit, the taxpayer incurred tax deficiencies. The Audit Division proposed assessing, and the taxpayer has protested only proposed assessment of, negligence penalties. Since filing this protest, the taxpayer has petitioned one of the federal bankruptcy courts sitting in Indiana for reorganization under 11 U.S.C. Chapter 11 (2000 and Supp. V 2005), and the Department has filed a proof of claim in that case for all liabilities owed it, including the negligence penalties. The Department will provide additional information as needed.

I. Tax Administration—Negligence Penalties—Audit Deficiencies—Ignorance of Law

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer failed to accrue and remit use tax on licenses for new software on which its licensors/vendors did not charge it gross retail (sales) tax. The taxpayer submits that one reason the Department should waive the negligence penalties is that the taxpayer was not aware of the specific guidelines on software licenses. In particular, the taxpayer alleges that these failures occurred due to a mistaken belief that two of the software packages it licensed were tax-exempt "custom" software. This latter allegation also implies that the taxpayer did not correctly understand, i.e. that it was ignorant of, this Department's longstanding interpretation of what constitutes taxable "canned" software.

B. ANALYSIS

IC § 6-8.1-10-2.1 (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 and alterations 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 … of: … (4) the amount of deficiency as finally determined by the department[.]" *Id.* (Alterations added.) 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 and alteration 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 and alterations added.)

Under IC § 6-8.1-5-1(b) (2004) and 45 IAC § 15-5-3(b)(8) (2004), 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 and alterations added). 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's argument is in effect that it did not know it was liable for use tax on the software licenses on which the Audit Division ultimately proposed to assess the audit deficiencies against it. The taxpayer thus has admitted that it was "ignoran[t] of the listed tax laws, rules and/or regulations[,][which] is treated as negligence. " 45 IAC § 15-11-2(b) (alterations added). Such ignorance is not an exercise of "ordinary business care and prudence[,]" *id.*(c), and therefore does not establish reasonable cause under IC § 6-8.1-10-2.1(d) and 45 IAC § 15-11-2(c) to waive the proposed negligence penalties.

FINDING

The taxpayer's protest is denied to the extent it is based on this issue.

II. Tax Administration—Negligence Penalties—Audit Deficiencies (Use Tax)—Reliance on Vendor's Representation It Would Pay Sales Tax—Burden of Proof

Tax Administration—Negligence Penalties—Audit Deficiencies (Use Tax)— Purchaser's Constructive Knowledge of Liability for Use Tax on Interstate Purchases

DISCUSSION

A. TAXPAYER'S ARGUMENT

At the end of the term of an equipment lease, the taxpayer exercised an option thereunder to buy the leased equipment, consisting of computer checkout monitors, hardware, electronic scales, printers and associated software. The taxpayer alleges that the lease agreement had language in it to the effect that the purchase price would include sales tax. However, the taxpayer also admits that the invoice it received for the purchase did not have a line item for the sales tax. The lessor/vendor was located outside Indiana and is not authorized to do business in Indiana according to the online records of the Business Services Division of the Indiana Secretary of State's office. The field auditor adjusted the taxpayer's liability on this purchase by assessing use tax pursuant to 45 IAC § 2.2-3-20 (1996) (2001) (current version at *id.* (2004)). The taxpayer has not submitted copies of either the equipment lease or the purchase invoice in evidence in this protest.

B. ANALYSIS

1. The Taxpayer Has Failed to Sustain Its Burden of Proof of Reasonable Cause for Its Failure to Remit Use Tax on the Equipment Purchase.

As previously discussed, a taxpayer has the burden of proof in a protest. IC § 6-8.1-5-1(a) states that "[t]he burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made.") *Id. See also* Black's Law Dictionary 190 (7th ed. 1999) (defining "burden of proof" as a "party's duty to prove a disputed assertion or charge"). The burden of proof is two-fold, consisting of both the burden of persuasion and the burden of production. *Porter Mem'l Hosp. v. Malak*, 484 N.E.2d 54, 58 (Ind. Ct. App. 1985) (noting that "burden of proof" is not a precise term, as it can mean both the burdens of persuasion and production).

The terms "burden of production" and "burden of persuasion" have two distinct meanings. *See State v. Huffman*, 643 N.E.2d 899, 900 (Ind. 1994) (stating that there are "two senses" of the term "burden of proof," the burdens of persuasion and production). The burden of production, also referred to as the burden of going forward, is the taxpayer's "duty to introduce enough evidence on an issue to have the issue decided by the fact-finder." *Id.* In other words, a taxpayer must submit evidence sufficient to establish a prima facie case, i.e., evidence sufficient to establish a given fact and which if not contradicted will remain sufficient to establish that fact. *See Longmire v. Ind. Dep't of State Rev.*, 638 N.E.2d 894, 898 (Ind. Tax Ct. 1994); *Canal Sq. Ltd. Partnership v. State Bd. of Tax Comm'rs*, 694 N.E.2d 801, 804 (Ind. Tax Ct. 1998). *Cf. Bullock v. Foley Bros. Dry Goods Corp.*, 802 S.W.2d 835, 839 (Tex. App. 1990) (observing, in challenge to state's sales and use tax audit, that comptroller's deficiency determination is prima facie correct and that taxpayer must disprove it with documentation). In penalty protests in particular, it is to the burden of production that IC § 6-8.1-10-2.1(e) speaks when it states that the penalized person "must make an affirmative showing of all *facts* alleged as a reasonable cause for the person's failure to" comply with the listed tax laws. *Id.* (Emphasis added).

In contrast to the burden of production component of the burden of proof, the burden of persuasion is the taxpayer's "duty to convince the fact-finder to view the facts in a way that favors that party. … Also loosely termed *burden of proof*." BLACK'S LAW DICTIONARY 190 (7th ed. 1999) (emphasis in original.) Some cases have referenced this dual meaning. *See, e.g., Peabody Coal Co. v. Ralston*, 578 N.E.2d 751, 754 (Ind. Ct. App. 1991) (observing that in criminal cases, the "State carries the ultimate burden of proof, or burden of persuasion").

The present taxpayer has failed to meet its burden of production in that it has failed to submit any evidence concerning the lessor/vendor's alleged representation that it would pay the sales tax. Specifically, it has failed to submit either a copy of the lease purchase agreement which allegedly contains representation/s concerning sales tax being included in the purchase price or a copy of the invoice which it alleges had no line item entry for sales tax. The taxpayer has also failed to meet its burden of persuasion that this part of the negligence penalties should be waived, since there is no evidence, and therefore no established facts, in the record to which the burden of persuasion could apply.

2. The Taxpayer Had Constructive Knowledge It Is Liable for Use Tax on Interstate Purchases of Tangible Personal Property Brought to Indiana, and Therefore to Have Known It Was Liable for Use Tax on the Equipment Purchase.

However, even if the Department were to assume, without necessarily finding, that there was no sales tax line item on the alleged invoice, the absence of such an entry would undercut the taxpayer's argument. The taxpayer is charged with constructive knowledge of 45 IAC § 2.2-3-20, which reads in pertinent part as follows:

> Sec. 20. All 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. … If the seller is not required to collect the tax or fails to collect the tax when required to do so, the purchaser must remit the use tax directly to the Indiana Department of Revenue.

Id. The regulation is consistent with the nationwide general legal view as to the place and role of the use tax in state and local tax systems and the circumstance under which liability for that tax accrues to the jurisdiction in which the property becomes located. As pointedly expressed in one opinion, "*[t]he use tax* is complementary to the sales tax and *bites when the sales tax does not.*" *Morton Bldgs., Inc. v. Comm'r of Rev.*, 683 N.E.2d 720, 722 (Mass. App. Ct. 1997) (emphases and alteration added), *paraphrased and followed in Morton Bldgs., Inc. v. Ind. Dep't of State Rev. (Morton Bldgs. VII)*, 819 N.E.2d 913, 915 (Ind. Tax Ct. 2004), *review denied* 831 N.E.2d 744 (Ind. 2005) (table). This rule follows from the well-settled general law in this country on the purpose and function of a use tax. "It [has long been] one of the well-known functions of the integrated use and sales tax to remove the buyers' temptation to place their orders in other states in the effort *to escape payment of the tax on local sales*." *Nelson v. Sears, Roebuck & Co.*, 312 U.S. 359, 363 (1941) (internal quotation marks omitted) (emphasis and alteration added). In addition to the United States Supreme Court, at least ten courts sitting in jurisdictions other than Indiana have reported opinions discussing this subject and taking the same view. Their consensus, summarized in a secondary source, is that "[t]he use tax is correlative of, and is complementary and supplemental to, the sales tax, *one of its principal purposes being to prevent the evasion of the sales tax.*" 68 Am. Jur. 2d *Sales and Use Taxes* § 168 (2004) (footnote omitted) (emphasis and alteration added).

Morton Buildings VII, cited above, makes it clear that Indiana is in the judicial mainstream regarding the function and role of the use tax. The Indiana Supreme Court settled the law and removed any doubt that might have lingered on this point less than three months before the Indiana Tax Court issued *Morton Buildings VII. See Ind. Dep't of State Rev. v. Trump Ind. Inc.*, 814 N.E.2d 1017, 1019 (Ind. 2004). Admittedly, neither opinion was issued until after the close of the taxpayer's audit period. However, it did have the benefit of the first reported Indiana opinion, issued well before that period began, that made the same point:

> Like most states, Indiana has complementary sales and use taxes. *See* IND. CODE 6-2.5-3-4(a)[(1)] [(1988) (audit period and current versions at *id.* (1998) and (2004), respectively) (exempting the storage, use and consumption of tangible personal property in Indiana from use tax if Indiana sales tax was paid when that property was acquired)]. … *The complementary formulation exists to ensure non-exempt retail transactions that escape sales tax liability are nonetheless taxed.*

USAir, Inc. v. Ind. Dep't of State Rev. (*USAir II*), 623 N.E.2d 466, 468-69 (Ind. Tax Ct. 1993) (citation omitted) (emphasis and alterations added). Title 45 IAC § 2.2-3-20, which was in effect when the Tax Court issued *USAir II* and on which the present taxpayer's auditor relied, is to the same effect as regards interstate transactions. *But cf.* IC § 6-2.5-3-5 (1998) (current version at *id.* (2004)) (granting a credit against use tax for any sales, purchase or use tax paid to another state-level taxing jurisdiction when the tangible personal property was acquired).

The lessor/vendor of the present taxpayer failed to collect and remit sales tax on its purchase of the equipment. It is no defense to the proposed negligence penalty assessments to say, as the taxpayer implies in its protest letter, that the vendor should have done so. The taxpayer knew it was dealing with an out-of-state lessor/vendor, and the absence of a sales tax line item on the purchase invoice should have been a red flag alerting the taxpayer to self-assess, report and remit use tax on that purchase. The taxpayer should have known that if it did not pay sales tax on a non-exempt purchase of tangible personal property later placed in Indiana, the taxpayer would owe use tax to Indiana. The taxpayer nevertheless failed to recognize, report and pay that liability, thereby incurring the part of the present audit deficiencies attributable to that failure, which was due to carelessness. That failure constituted "negligence" as defined in 45 IAC § 15-11-2(b). It is not evidence of an "exercise[ ] [of] ordinary business care and prudence[,]" 45 IAC § 15-11-2(b) (alterations added), and therefore is not "reasonable cause" under IC § 6-8.1-10-2.1(d) and (e) to waive the negligence penalties for the taxpayer's incurring the part of those deficiencies arising from the equipment purchase.

FINDING

The taxpayer's protest is denied to the extent it is based on this issue.

III. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer submits that another reason the Department should waive the negligence penalties is that it files all of its sales and use tax returns and pays all of those taxes on time.

B. ANALYSIS

The taxpayer's argument is in effect that it exercised ordinary care and prudence in filing its returns with this Department, thereby implying that it had "reasonable cause," as 45 IAC § 15-11-2(c) defines that term, for its incurring audit deficiencies. That argument does not support the taxpayer's protest because it does not address the basis on which the negligence penalties were proposed against it. The taxpayer was not penalized by the Compliance Division under IC § 6-8.1-10-2.1(a)(1) or (2) for failing to file returns, for failing to file returns on time, or for failing to pay the full amount of tax shown on those returns. It was penalized by the Audit Division 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.* (Alterations added.) 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. The taxpayer has therefore failed to sustain its burden of proof concerning the proposal of the negligence penalties to the extent it has based its protest on this ground.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20040354.LOF

LETTER OF FINDINGS NUMBER 04-0354
TAX ADMINISTRATION (USE TAX)—
NEGLIGENCE PENALTIES FOR THE REPORTING PERIODS
COVERING CALENDAR YEARS 2001-03

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. Tax Administration—Negligence Penalties—Audit Deficiencies—Ignorance of Law

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); 45 IAC §§ 15-3-2(e), -5-3(b)(8) and -11-2 (2004)

II. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); 45 IAC §§ 15-3-2(e), -5-3(b)(8) and -11-2 (2004)

The taxpayer protests the Audit Division's proposed assessment of negligence penalties.

STATEMENT OF FACTS

The Department's Audit Division conducted a field audit of the taxpayer for the tax type and reporting periods set out in the heading of this Letter of Findings. As a result of the audit, the taxpayer incurred tax deficiencies. The Audit Division proposed assessing, and the taxpayer has protested only proposed assessment of, negligence penalties. Since filing this protest, the taxpayer has petitioned one of the federal bankruptcy courts sitting in Indiana for reorganization under 11 U.S.C. Chapter 11 (2000 and Supp. V 2005), and the Department has filed a proof of claim in that case for all liabilities owed it, including the negligence penalties. The Department will provide additional information as needed.

I. Tax Administration—Negligence Penalties—Audit Deficiencies—Ignorance of Law

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer failed to accrue and remit use tax on new computer hardware on which its vendor/s did not charge it gross retail (sales) tax. The taxpayer submits that one reason the Department should waive the negligence penalties is that the taxpayer was not aware of, or mistakenly interpreted, the specific guidelines on computer hardware. In other words, the taxpayer either did not know or correctly understand, i.e. that it was ignorant of, the Department's interpretation of the relevant sales and use tax statutes and regulations on the uses of computer hardware that make it subject to these taxes.

B. ANALYSIS

IC § 6-8.1-10-2.1 (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) (2004) and 45 IAC § 15-5-3(b)(8) (2004), 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 and alterations added). 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's argument is in effect that it did not know it was liable for use tax on the computer hardware on which the Audit Division ultimately proposed to assess the audit deficiencies against it. The taxpayer thus has admitted that it was "ignoran[t] of the listed tax laws, rules and/or regulations[,][which] is treated as negligence. " 45 IAC § 15-11-2(b) (alterations added). Such ignorance is not an exercise of "ordinary business care and prudence[,]" *id.*(c), and therefore does not establish reasonable cause under IC § 6-8.1-10-2.1(d) and 45 IAC § 15-11-2(c) to waive the proposed negligence penalties.

FINDING

The taxpayer's protest is denied to the extent it is based on this issue.

II. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer submits that the other reason the Department should waive the negligence penalties is that it files all of its returns on time.

B. ANALYSIS

The taxpayer's argument is in effect that it exercised ordinary care and prudence in filing its returns with and remitting its taxes to this Department, thereby implying that it had "reasonable cause," as 45 IAC § 15-11-2(c) defines that term, for its incurring audit deficiencies. That argument does not support the taxpayer's protest because it does not address the basis on which the negligence penalties were proposed against it. The taxpayer was not penalized by the Compliance Division under IC § 6-8.1-10-2.1(a)(1) or (2) for failing to file returns, for failing to file returns on time, or for failing to pay the full amount of tax shown on those returns. It was penalized by the Audit Division 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.* (Alterations added.) 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. The taxpayer has therefore failed to sustain its burden of proof concerning the proposal of the negligence penalties

to the extent it has based its protest on this ground.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20040465P.LOF

LETTER OF FINDINGS NUMBER 04-0465P
TAX ADMINISTRATION (USE TAX)—
NEGLIGENCE PENALTIES FOR THE REPORTING PERIODS
COVERING CALENDAR YEARS 2001-03

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. Tax Administration—Negligence Penalties—Audit Deficiencies—Alleged *De Minimis* Deficiencies

Authority: IC §§ 6-8.1-1-1, -5-1(b), -10-2.1 and 10-7 (2004); 45 IAC § 15-11-2(b) and (c) (2004)

II. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); *State Bd. of Tax Comm'rs v. New Castle Lodge # 147, L.O.O.M.*, 765 N.E.2d 1257, 1264 (Ind. 2002); *Hoogenboom-Nofziger v. State Bd. of Tax Comm'rs*, 715 N.E.2d 1018, 1024 and 1024-25 (Ind. Tax Ct. 1999); 45 IAC § 15-11-2 (2004)

The taxpayer protests the proposed assessment of negligence penalties for its incurring audit deficiencies.

STATEMENT OF FACTS

The Department's Audit Division conducted a field audit of the taxpayer for the tax type and reporting periods set out in the heading of this Letter of Findings. As a result of the audit, the taxpayer incurred tax deficiencies. The Audit Division proposed assessing, and the taxpayer has protested only proposed assessment of, negligence penalties. The Department will provide additional information as needed.

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer argues that the combined deficiencies for the audit period were nominal. The taxpayer is essentially contending that the Department should waive the negligence penalties because the total dollar value of transactions on which it failed to pay use tax is, in the taxpayer's view, *de minimis*.

B. APPLICABLE PENALTY LAW

IC § 6-8.1-10-2.1 (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. 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 and alterations added.) Title 45 IAC § 15-11-2(b) (2004) defines "negligence" in relevant part as follows:

> (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.*

Id. (Emphasis added.) "[L]isted tax laws[,]" *id.* (alterations added), refers to the definition of the term "listed taxes" found in IC § 6-8.1-1-1 (2004). The listed taxes are all of the tax laws for which the General Assembly has explicitly made the Department responsible. They include the gross retail (sales) and use taxes.

"If a person subject to the penalty imposed under this section [IC § 6-8.1-10-2.1] 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." IC § 6-8.1-10-2.1(d) (emphasis and alteration added.). The implementing regulation restates this requirement as requiring the taxpayer to show that the failure to discharge its tax duties "was due to reasonable cause and not due to negligence." 45 IAC § 15-11-2(c). This subsection of the regulation goes on to state:

> 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.)

The taxpayer "must make an affirmative showing of all facts alleged as a reasonable cause for [its] failure to … pay the deficiency[.]" IC § 6-8.1-10-2.1(e) (alterations added). The evidentiary showing the taxpayer must make under IC § 6-8.1-10-2.1(d) and (e) and 45 IAC § 15-11-2(c) is consistent with IC § 6-8.1-5-1(b), which places the burden of proof in all protests on the person against whom a proposed assessment is made to prove that it is wrong. 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.

IC § 6-8.1-10-7 imposes the only other limits, monetary ones, on the Department's authority to assess and enforce a penalty under IC § 6-8.1-10-2.1. That statute provides:

> Notwithstanding the various penalty provisions of [IC] chapter [6-8.1-10], the maximum total penalty that may be assessed against a person under sections 2.1 through 5 of this chapter [i.e., IC §§ 6-8.1-10-2.1 to -5, which all use percentage formulas to calculate the respective penalties they impose] is one hundred percent … of the unpaid tax and *the minimum penalty, if any, that may be assessed under those sections is five dollars ($ 5).*
>
> *Id.* (Emphasis and alterations added).

C. ANALYSIS

IC § 6-8.1-10-7 sets the maximum and minimum amounts of percentage-based penalties, including the negligence penalty, the Department may assess; the minimum is five dollars ($5). However, once the Department has assessed a negligence penalty greater than the minimum, as it did here, IC § 6-8.1-10-2.1(d) and (e) govern the Department's ability to waive that penalty. There is nothing in either of those subsections that even authorizes the Department to waive a negligence penalty on the ground that the amount of unpaid tax is *de minimis*, much less anything setting out an amount, or a formula to determine an amount, of unpaid tax that the Department could treat as being *de minimis*. Nor does IC § 6-8.1-5-1(a), the subsection requiring the Department to make a proposed assessment of tax it reasonably believes was not properly reported, set any minimum figure of unpaid tax below which the Department is excused from doing so. Had the General Assembly wanted to set a floor amount of unpaid tax below which it would deem the taxpayer not liable for any such tax as a matter of law, it easily could have said so.

The only ground on which IC § 6-8.1-10-2.1(d) requires the Department to waive a negligence penalty, once assessed, is "reasonable cause[.]" *Id.* (Alteration added.) The legislature's use of this term necessarily implies that the determinative factor for the Department in deciding whether to waive a negligence penalty is the cause of, not the amount of unpaid tax resulting from, the compliance failure in question. The only material reference to a number concerning the negligence penalties IC § 6-8.1-10-2.1(a) imposes is to the amount of unpaid, underpaid, unreported or underreported taxes. The only use for that figure that IC § 6-8.1-10-2.1 mentions is to compute the negligence penalty; subsection (b) uses that amount as the multiplicand to which the Department applies the ten percent multiplier to determine the amount of the subsection (a) penalty. *See* IC § 6-8.1-10-2.1(b) (setting out the computation formulae). The size of this multiplicand, standing alone, is irrelevant to answering the questions of why and how it came into being, and more precisely to answering the question of whether or not the failure out of which it arose was due to the taxpayer's negligence.

FINDING

The taxpayer's protest is denied to the extent it is based on this issue.

II. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer submits that the other reason the Department should waive the negligence penalties is that it files its returns faithfully.

B. ANALYSIS

The taxpayer's argument is in effect that it exercised ordinary care and prudence in filing its returns with this Department, thereby implying that it had "reasonable cause," as 45 IAC § 15-11-2(c) defines that term, for its incurring audit deficiencies. That argument does not support the taxpayer's protest because it does not address the basis on which the negligence penalties were proposed against it. The taxpayer was not penalized by the Compliance Division under IC § 6-8.1-10-2.1(a)(1) or (2) for failing to file returns, for failing to file returns on time, or for failing to pay the full amount of tax shown on those returns. It was penalized by the Audit Division 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.* (Alterations added.) 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. The taxpayer has therefore failed to sustain its burden of proof concerning the proposal of the negligence penalties to the extent it has based its protest on this ground.

The taxpayer has failed to submit any evidence showing, or make any argument, that it had reasonable cause for incurring the audit deficiencies. Indiana law is settled that this state's taxation hearing officers, and by extension the state-level taxing authorities of which they are agents, "do not have the duty to make a taxpayer's case." *Hoogenboom-Nofziger v. State Bd. of Tax Comm'rs*, 715 N.E.2d 1018, 1024 (Ind. Tax Ct. 1999), *cited with approval in State Bd. of Tax Comm'rs v. New Castle Lodge # 147, L.O.O.M.*, 765

N.E.2d 1257, 1264 (Ind. 2002). The Tax Court stated the rationale for this rule in *Hoogenboom-Nofziger* as follows:

> [T]o allow [a taxpayer] to prevail after it made such a cursory showing at the administrative level would result in a tremendous workload increase for [the Department and] the State Board [now the Indiana Board of Tax Review], … administrative agenc[ies] that already bear[ ] … difficult burden[s] in administering this State's [listed and] property tax system[s]. If taxpayers could make a de minimis showing and then force [the Department or] the State Board to support its decisions with detailed factual findings, the [Indiana taxing authorities] would be overwhelmed with cases such as this one. This would be patently unfair to other taxpayers who do make detailed presentations to the [taxing authorities] because resolution of their appeals would necessarily be delayed.

715 N.E.2d at 1024-25 (alterations added).

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20050011P.LOF

LETTER OF FINDINGS NUMBER 05-0011P
TAX ADMINISTRATION (USE TAX)—NEGLIGENCE PENALTIES FOR THE REPORTING PERIODS COVERING CALENDAR YEARS 2000-01 AND JANUARY 1—NOVEMBER 30, 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. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Payment History
Tax Administration—Negligence Penalties—Audit Deficiencies—Lack of Proof of Neglect

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); 45 IAC §§ 15-5-3(b)(8) and -11-2 (2004)

II. Tax Administration—Negligence Penalties—Audit Deficiencies—Lack of Proof of Intent to Defraud

Authority: IC §§ 6-8-1-24, -8.1-5-1(b), -8.1-10-2.1 and -8.1-10-4 (2004); *State Bd. of Tax Comm'rs v. New Castle Lodge # 147, L.O.O.M.*, 765 N.E.2d 1257, 1264 (Ind. 2002); *Hoogenboom-Nofziger v. State Bd. of Tax Comm'rs*, 715 N.E.2d 1018, 1024 and 1024-25 (Ind. Tax Ct. 1999); 45 IAC §§ 15-3-2(e), -5-3(b)(8) -11-2 -11-4 and (2004)

The taxpayer protests the Audit Division's proposed assessment of negligence penalties.

STATEMENT OF FACTS

The Department's Audit Division conducted a field audit of the taxpayer for the tax type and reporting periods set out in the heading of this Letter of Findings. As a result of the audit, the taxpayer incurred tax deficiencies. The Audit Division proposed assessing, and the taxpayer has protested only proposed assessment of, negligence penalties. The Department will provide additional information as needed.

I. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Payment History
Tax Administration—Negligence Penalties—Audit Deficiencies—Lack of Proof of Neglect

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer submits that one reason the Department should waive the negligence penalties is that it has consistently remitted tax due and that the audit did not disclose any evidence of neglect.

B. ANALYSIS

IC § 6-8.1-10-2.1 (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 and alterations 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 … of:… (4) the amount of deficiency as finally determined by the department[.]" *Id.* (Alterations added.) 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 and alteration 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 and alterations added.)

Under IC § 6-8.1-5-1(b) (2004) and 45 IAC § 15-5-3(b)(8) (2004), 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 and alterations added). The burden of proof is not on the Department to show the absence of reasonable cause for the actions or inaction of a taxpayer. It follows that the Department also is not required to prove negligence, willful or otherwise, by a taxpayer, as the present taxpayer suggests. Accordingly, the Department summarily denies the taxpayer's protest to the extent it is based on this particular argument.

The taxpayer's other argument on this issue is in effect that it exercised ordinary care and prudence in remitting tax to this Department, thereby implying that it had "reasonable cause," as 45 IAC § 15-11-2(c) defines that term, for its incurring audit deficiencies. That argument does not support the taxpayer's protest because it does not address the basis on which the negligence penalties were proposed against it. The taxpayer was not penalized by the Compliance Division under IC § 6-8.1-10-2.1(a)(2) for failing to pay the full amount of tax shown on its returns. It was penalized by the Audit Division 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.* (Alterations added.) The fact that the taxpayer paid all the tax it reported has no tendency to prove that the present deficiencies, resulting from its omissions of tax from its returns, were incurred for reasonable cause. The taxpayer has therefore failed to sustain its burden of proof concerning the proposal of the negligence penalties to the extent it has based its protest on this ground.

FINDING

The taxpayer's protest is denied to the extent it is based on this issue.

II. Tax Administration—Negligence Penalties—Audit Deficiencies—Lack of Proof of Intent to Defraud

A. TAXPAYER'S ARGUMENT

The taxpayer submits that the other reason the Department should waive the negligence penalties is that the taxpayer had no intent to defraud.

B. ANALYSIS

This argument, like the one regarding consistent payment of tax, does not address the reason why the Audit Division proposed the penalties, and in particular the kind of penalties, it did. The Audit Division propose those penalties under IC § 6-8.1-10-2.1 for negligence, not under IC § 6-8.1-10-4 (2004) for civil fraud. Both statutes set their respective penalties as a percentage of the tax in question. IC § 6-8.1-10-2.1(b) sets the negligence penalty at only 10 percent. In contrast, IC § 6-8.1-10-4(b) sets the civil fraud penalty at 100 percent, the maximum penalty the Department can assess. IC § 6-8.1-10-7. In addition, the civil fraud penalty "is imposed in place of and not in addition to the penalty imposed under section 2.1 of this chapter[i.e., IC § 6-8.1-10-2.1]." IC § 6-8.1-10-4(d) (alteration added).

The two penalties also differ in several other important ways, the first and most important of which for present purposes is the state of mind required to support each penalty. The statute imposing the penalty in question, a regulation implementing that statute, or both, explicitly defines the mental state required for that penalty. Comparing these definitions makes the difference between these states of mind clear. To be liable for the civil fraud penalty of IC § 6-8.1-10-4, a taxpayer must have failed to file a return, or failed to pay in full the tax reported on any filed return, "with the fraudulent intent of evading the tax[.]" *Id.*(a) (alteration added). One of the implementing regulations, 45 IAC § 15-11-4 (2004), describes "the [kind of] intent required [to constitute fraud as having] the

specific purpose of evading tax believed to be owing." *Id.* (Alterations added.)

Civil tax fraud in Indiana is thus what lawyers who practice criminal law call a "specific intent" offense. *Cf.* IC § 6-8-1-24 (requiring intent to defraud the state or to evade payment of tax for certain actions described therein to be criminal tax offenses). In contrast, as previously noted, under IC § 6-8.1-10-2.1 "[n]egligence would result [merely] from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations." 45 IAC § 15-11-2(b) (alterations added). Thus, negligence requires the person penalized to have a less guilty (and more common) mental state than, and does not require proof of, intent to defraud. Conversely, fraud requires a guiltier (and hopefully rarer) state of mind than negligence does. Neither mental state is a component of the other. Each state of mind excludes the other.

Thus, negligence does not require intent to defraud, the taxpayer's implied assertion to the contrary notwithstanding. However, absence of intent to defraud is not the same as proof that a taxpayer had reasonable cause for failing to meet its compliance responsibilities. The taxpayer has failed to submit any evidence showing, or make any argument, that it had reasonable cause for incurring the audit deficiencies. Indiana law is settled that this state's taxation hearing officers, and by extension the state-level taxing authorities of which they are agents, "do not have the duty to make a taxpayer's case." *Hoogenboom-Nofziger v. State Bd. of Tax Comm'rs*, 715 N.E.2d 1018, 1024 (Ind. Tax Ct. 1999), *cited with approval in State Bd. of Tax Comm'rs v. New Castle Lodge # 147, L.O.O.M.*, 765 N.E.2d 1257, 1264 (Ind. 2002). The Tax Court stated the rationale for this rule in *Hoogenboom-Nofziger* as follows:

> [T]o allow [a taxpayer] to prevail after it made such a cursory showing at the administrative level would result in a tremendous workload increase for [the Department and] the State Board [now the Indiana Board of Tax Review], … administrative agenc[ies] that already bear[ ] … difficult burden[s] in administering this State's [listed and] property tax system[s]. If taxpayers could make a de minimis showing and then force [the Department or] the State Board to support its decisions with detailed factual findings, the [Indiana taxing authorities] would be overwhelmed with cases such as this one. This would be patently unfair to other taxpayers who do make detailed presentations to the [taxing authorities] because resolution of their appeals would necessarily be delayed.
>
> 715 N.E.2d at 1024-25 (alterations added).

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20050025P.LOF

LETTER OF FINDINGS NUMBER 05-0025P
TAX ADMINISTRATION (USE TAX)—
NEGLIGENCE PENALTIES FOR THE REPORTING PERIODS
COVERING CALENDAR 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

I. Tax Administration—Negligence Penalties—Audit Deficiencies--Good Filing History

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); *State Bd. of Tax Comm'rs v. New Castle Lodge # 147, L.O.O.M.*, 765 N.E.2d 1257, 1264 (Ind. 2002); *Hoogenboom-Nofziger v. State Bd. of Tax Comm'rs*, 715 N.E.2d 1018, 1024 and 1024-25 (Ind. Tax Ct. 1999); 45 IAC §§ 15-5-3(b)(8) and -11-2 (2004)

The taxpayer protests the Audit Division's proposed assessment of negligence penalties.

STATEMENT OF FACTS

The Department's Audit Division conducted a field audit of the taxpayer for the tax type and reporting periods set out in the heading of this Letter of Findings. As a result of the audit, the taxpayer incurred tax deficiencies. The Audit Division proposed assessing, and the taxpayer has only protested the proposed, negligence penalties. The Department will provide additional information as needed.

I. Tax Administration—Negligence Penalties—Audit Deficiencies--Good Filing History

DISCUSSION

A. TAXPAYER'S PROTEST

The taxpayer argues that the Department should waive the negligence penalties because the taxpayer files its returns on time and reports and remits the proper amount of tax due.

B. ANALYSIS

IC § 6-8.1-10-2.1 (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 and alterations 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.* (Alterations added.) 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 and alteration 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.*….
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> …
>
> 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 and alterations added.)

Under IC § 6-8.1-5-1(b) (2004) and 45 IAC § 15-5-3(b)(8) (2004), 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 and alterations added). 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's argument is in effect that it exercised ordinary care and prudence in filing its returns with and remitting tax to this Department, thereby implying that it had "reasonable cause," as 45 IAC § 15-11-2(c) defines that term, for incurring the audit deficiencies. That argument does not support the taxpayer's protest because it does not address the basis on which the negligence penalties were proposed against it. The taxpayer was not penalized by the Compliance Division under IC § 6-8.1-10-2.1(a)(1) or (2) for failing to file returns, for failing to file returns on time, or for failing to pay the full amount of tax shown on those returns. It was penalized by the Audit Division 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.* (Alterations added.) 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.

The taxpayer has failed to make any argument that it had reasonable cause for incurring the audit deficiencies. Indiana law is settled that this state's taxation hearing officers, and by extension the state-level taxing authorities of which they are agents, "do not have the duty to make a taxpayer's case." *Hoogenboom-Nofziger v. State Bd. of Tax Comm'rs*, 715 N.E.2d 1018, 1024 (Ind. Tax Ct. 1999), *cited with approval in State Bd. of Tax Comm'rs v. New Castle Lodge # 147, L.O.O.M.*, 765 N.E.2d 1257, 1264 (Ind. 2002). The Tax Court stated the rationale for this rule in *Hoogenboom-Nofziger* as follows:

> [T]o allow [a taxpayer] to prevail after it made such a cursory showing at the administrative level would result in a tremendous workload increase for [the Department and] the State Board [now the Indiana Board of Tax Review], … administrative agenc[ies] that already bear[ ] … difficult burden[s] in administering this State's [listed and] property tax system[s]. If taxpayers could make a de minimis showing and then force [the Department or] the State Board to support its decisions with detailed factual findings, the [Indiana taxing authorities] would be overwhelmed with cases such as this one. This would be patently

unfair to other taxpayers who do make detailed presentations to the [taxing authorities] because resolution of their appeals would necessarily be delayed.
715 N.E.2d at 1024-25 (alterations added).

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20050040P.LOF

LETTER OF FINDINGS NUMBER 05-0040P
TAX ADMINISTRATION (GROSS RETAIL AND USE TAX)—
NEGLIGENCE PENALTIES FOR THE REPORTING PERIODS
COVERING CALENDAR YEARS 2001-03

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. Tax Administration—Negligence Penalties—Audit Deficiencies—Ignorance of Law

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); 45 IAC §§ 15-5-3(b)(8) and -11-2 (2004)

II. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); 45 IAC §§ 15-5-3(b)(8) and -11-2 (2004)

The taxpayer protests the Audit Division's proposed assessment of negligence penalties.

STATEMENT OF FACTS

The Department's Audit Division conducted a field audit of the taxpayer for the tax type and reporting periods set out in the heading of this Letter of Findings. As a result of the audit, the taxpayer incurred tax deficiencies. The Audit Division proposed assessing, and the taxpayer has protested only the proposed assessment of, negligence penalties. The Department will provide additional information as needed.

I. Tax Administration—Negligence Penalties—Audit Deficiencies—Ignorance of Law

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer failed to accrue and remit use tax on equipment and supplies on which its vendors did not charge it gross retail (sales) tax. The taxpayer submits that one reason the Department should waive the negligence penalties is that these failures occurred due to an incorrect understanding of what uses of these items were subject to use tax and which ones were not so subject. The Department notes that the taxpayer is engaged in a service, not a production, business.

B. ANALYSIS

IC § 6-8.1-10-2.1 (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 and alterations 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 … of:… (4) the amount of deficiency as finally determined by the department[.]" *Id.* (Alterations added.) 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 and alteration 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 and alterations added.)

Under IC § 6-8.1-5-1(b) (2004) and 45 IAC § 15-5-3(b)(8) (2004), 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 and alterations added). 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's argument is in effect that it did not know it was liable for use tax on the equipment and supplies on which the Audit Division ultimately proposed to assess the audit deficiencies against it. The taxpayer thus has admitted that it was "ignoran[t] of the listed tax laws, rules and/or regulations[,][which] is treated as negligence. " 45 IAC § 15-11-2(b) (alterations added). Such ignorance is not an exercise of "ordinary business care and prudence[,]" *id.*(c) (alteration added), and therefore does not establish reasonable cause under IC § 6-8.1-10-2.1(d) and 45 IAC § 15-11-2(c) to waive the proposed negligence penalties.

FINDING

The taxpayer's protest is denied to the extent it is based on this issue.

II. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer submits that the other reason the Department should waive the negligence penalties is that it files all of its returns on time.

B. ANALYSIS

The taxpayer's argument is in effect that it exercised ordinary care and prudence in filing its returns with this Department, thereby implying that it had "reasonable cause," as 45 IAC § 15-11-2(c) defines that term, for its incurring audit deficiencies. That argument does not support the taxpayer's protest because it does not address the basis on which the negligence penalties were proposed against it. The taxpayer was not penalized by the Compliance Division under IC § 6-8.1-10-2.1(a)(1) or (2) for failing to file returns, for failing to file returns on time, or for failing to pay the full amount of tax shown on those returns. It was penalized by the Audit Division 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.* (Alterations added.) 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. The taxpayer has therefore failed to sustain its burden of proof concerning the proposal of the negligence penalties to the extent it has based its protest on this ground.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20050041P.LOF

LETTER OF FINDINGS NUMBER 05-0041P
TAX ADMINISTRATION (GROSS RETAIL AND USE TAX)—
NEGLIGENCE PENALTIES FOR THE REPORTING PERIODS
COVERING CALENDAR YEARS 2001-03

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. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); 45 IAC §§ 15-5-3(b)(8) and -11-2 (2004)

II. Tax Administration—Negligence Penalties—Audit Deficiencies—Ignorance of Law

Authority: IC §§ 6-8.1-5-1(b) and -10-2.1 (2004); 45 IAC §§ 15-5-3(b)(8) and -11-2 (2004)

The taxpayer protests the Audit Division's proposed assessment of negligence penalties.

STATEMENT OF FACTS

The Department's Audit Division conducted a field audit of the taxpayer for the tax type and reporting periods set out in the heading of this Letter of Findings. As a result of the audit, the taxpayer incurred tax deficiencies. The Audit Division proposed assessing, and the taxpayer has protested only proposed assessment of, negligence penalties. The Department will provide additional information as needed.

I. Tax Administration—Negligence Penalties—Audit Deficiencies—Good Filing History

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer submits that one reason the Department should waive the negligence penalties is that it is a "good corporate citizen" and files all of its returns on time.

B. ANALYSIS

IC § 6-8.1-10-2.1 (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 and alterations 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 … of:… (4) the amount of deficiency as finally determined by the department[.]" *Id.* (Alterations added.) 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 and alteration 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 and alterations added.)

Under IC § 6-8.1-5-1(b) (2004) and 45 IAC § 15-5-3(b)(8) (2004), 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 and alterations added). 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's argument is in effect that it exercised ordinary care and prudence in filing its returns with this Department, thereby implying that it had "reasonable cause," as 45 IAC § 15-11-2(c) defines that term, for its incurring audit deficiencies. That argument does not support the taxpayer's protest because it does not address the basis on which the negligence penalties were

proposed against it. The taxpayer was not penalized by the Compliance Division under IC § 6-8.1-10-2.1(a)(1) or (2) for failing to file returns, for failing to file returns on time, or for failing to pay the full amount of tax shown on those returns. It was penalized by the Audit Division 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.* (Alterations added.) 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. The taxpayer has therefore failed to sustain its burden of proof concerning the proposal of the negligence penalties to the extent it has based its protest on this ground.

FINDING

The taxpayer's protest is denied to the extent it is based on this issue.

II. Tax Administration—Negligence Penalties—Audit Deficiencies—Ignorance of Law

DISCUSSION

A. TAXPAYER'S ARGUMENT

The taxpayer failed to accrue and remit use tax on licenses for new software on which its licensors/vendors did not charge it gross retail (sales) tax. The taxpayer submits that the other reason the Department should waive the negligence penalties is that these failures were unintentional. The protest letter implies that the taxpayer did not previously know that such licenses were subject to sales and use tax.

B. ANALYSIS

The taxpayer's argument is in effect that it did not know that it was liable for tax on the largest single category of retail transactions on which the Audit Division ultimately proposed to assess the audit deficiencies against it. The taxpayer thus has admitted that it was "ignoran[t] of the listed tax laws, rules and/or regulations[,][which] is treated as negligence. " 45 IAC § 15-11-2(b) (alterations added). Such ignorance is not an exercise of "ordinary business care and prudence[,]" *id.*(c) (alteration added), and therefore does not establish reasonable cause under IC § 6-8.1-10-2.1(d) and 45 IAC § 15-11-2(c) to waive the proposed negligence penalties.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420050053.LOF

LETTER OF FINDINGS: 05-0053
GROSS RETAIL TAX
For 2001 through 2003

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. Purchase of Asphalt from Illinois Vendors – Sales Tax.

Authority: IC 6-2.5-2-1; IC 6-2.5-3-2; IC 6-2.5-3-5(a); 45 IAC 2.2-3-16; Ill. Admin. Code tit. 86, § 130.605(a)(1)-(2); Ill. Admin. Code tit. 86, § 130.605(b); Ill. Admin. Code tit. 86, § 130.605(d).

The taxpayer protests the Department's decision to assess use tax on asphalt material purchased in Illinois, transported to Indiana, and used within Indiana construction projects.

II. Use Tax Assessments.

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

Taxpayer maintains that it is not required to pay Indiana use tax on the purchase of capital assets, vehicles, and various tools and other equipment on the ground that taxpayer paid Illinois sales tax at the time it purchased the items.

STATEMENT OF FACTS

Taxpayer is an in-state asphalt contractor providing commercial and residential asphalt construction and paving services.

The Indiana Department of Revenue (Department) conducted an audit review of taxpayer's business records for 2001 through 2003. The audit concluded that taxpayer owed additional Indiana use tax. Accordingly, the Department sent taxpayer notices of "Proposed Assessment." Taxpayer disagreed with the proposed assessments and submitted a protest to that effect. An administrative hearing was conducted during which taxpayer explained the basis for its protest. This Letter of Findings results.

DISCUSSION

I. Purchase of Asphalt from Illinois Vendors – Sales Tax.

Indiana imposes a use tax on the "storage, use, or consumption of tangible personal property in Indiana... regardless of the

location of that transaction or of the retail merchant making that transaction." IC 6-2.5-3-2. The tax is imposed on transactions that occur outside of Indiana that would be taxable if they occurred within Indiana but only if property is stored, used or consumed in Indiana. IC 6-2.5-2-1.

The imposition of the use tax, on purchases occurring outside the state, is qualified pursuant to 45 IAC 2.2-3-16 which allows an Indiana credit for "the amount of any sale, purchase, or use tax paid to any other state... with respect to the tangible personal property on which Indiana use tax applies." *See* IC 6-2.5-3-5(a).

Taxpayer bought liquid asphalt from two Illinois vendors. The liquid asphalt was transported from Illinois to taxpayer's Indiana location by common carrier. The vendors stipulated which common carriers were permitted to pick up the liquid asphalt and transport the material into Indiana. When the vendors sent taxpayer a bill for the asphalt, the vendors charged Illinois sales tax. The vendors' bill states that the F.O.B. point was at the site of the Illinois vendors. The common carriers sent taxpayer a separate bill for the transportation services.

The audit found the taxpayer purchased tangible personal property (the asphalt) which was subject to Indiana use tax because, "Indiana state gross retail tax [had] not been collected at the point of these purchases and use tax was not remitted upon disposition of the material."

Taxpayer apparently agrees that it owed the Indiana use tax but argues that it should be permitted a credit for the Illinois sales tax paid to the Illinois vendors. In support, taxpayer cites to IC 6-2.5-3-5(a) which states that, "A person is entitled to a credit against the use tax imposed on the use, storage, or consumption of a particular item of tangible personal property equal to the amount, if any, of sales tax, purchase tax, or use tax paid to another state... for the acquisition of that property." *See* 45 IAC 2.2-3-16.

The taxpayer has provided information purporting to establish that the Illinois sales tax (Retailers' Occupation Tax) was due and payable for taxpayer's purchase of liquid asphalt. Pursuant to Ill. Admin. Code tit. 86, § 130.605 (2000), "Where tangible personal property is located in this State at the time of its sale... and then delivered in Illinois to the purchaser, the seller is taxable if the sale is at retail: 1) the sale is not deemed to be in interstate commerce if the purchaser or his representative receives the physical possession of such property in this State. 2) This is so notwithstanding the fact that the purchaser may, after receiving physical possession of the property in this state, transport or send the property out of the state for use outside the State or for use in the conduct of interstate commerce." Ill. Admin. Code tit. 86, § 130.605(a)(1)-(2).

However, the administrative code also makes exceptions for certain purchases made within Illinois. Pursuant to Ill. Admin. Code tit. 86, § 130.605(b), "The tax does not extend to gross receipts from sales in which the seller is obligated, under the terms of his agreement with the purchaser, to make physical delivery of the goods from a point in [Illinois] to a point outside [Illinois], not to be returned to a point within [Illinois]." Under the terms of taxpayer's agreement, the liquid asphalt was not delivered to taxpayer; the liquid asphalt was transferred to a common carrier – paid for by taxpayer but selected by the vendors – for eventual delivery to taxpayer. The parties did not enter into a contract for delivery of hot asphalt in Illinois, and the taxpayer did not 'receive[] physical possession of the such property in [Illinois]." Ill. Admin. Code tit. 86, § 130.605(a)(1). The vendors and taxpayer entered into an arrangement "to make physical delivery of the goods from a point in [Illinois] to a point outside [Illinois], not to be returned to a point within [Illinois]." Ill. Admin. Code tit. 86, § 130.605(b). The fact that the parties designated Illinois as the F.O.B. point is irrelevant in this analysis because, under Ill. Admin. Code tit. 86, § 130.605(d), "[t]he place at which title to the property passes to the purchaser is immaterial" Accordingly, taxpayer's purchase of liquid asphalt, designated for delivery and ultimate consumption within the state of Indiana, was not subject to the Illinois sales tax because "[s]ales of the type described in [Ill. Admin. Code tit. 86, § 130.605(b)] are deemed to be within the protection of the Commerce Clause of the Constitution of the United States." Ill. Admin. Code tit. 86, § 130.605(d).

Therefore, because Illinois sales tax was not due and payable on taxpayer's purchase of the liquid asphalt destined for Indiana, taxpayer is not entitled to an Indiana credit under 45 IAC 2.2-3-16. Instead, the purchase of the liquid asphalt is subject to Indiana use tax under IC 6-2.5-3-2 because the liquid asphalt constituted tangible personal property used or consumed in Indiana.

FINDING

Taxpayer's protest is respectfully denied.

II. Use Tax Assessments.

The audit assessed use tax on the purchase of "capital assets," vehicles, tools, supplies, and equipment because "sales tax was not paid at the time of purchase nor the use tax remitted to the Department of Revenue." Taxpayer challenges the assessments on the ground that it can now produce documentation establishing that it paid sales tax on the purchase of certain of these items and because it "is in the process of obtaining contemporaneous written documentation that the tax was paid [and] these documents will be available shortly."

IC 6-8.1-5-1(b) states 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 the person against whom the proposed assessment is wrong."

The specific issue raised by taxpayer is not one amenable to resolution in a Letter of Findings. Nonetheless, taxpayer has met its threshold burden of demonstrating that it is entitled to have the documents presented reviewed by the audit division. The audit

division is requested to review the documents which taxpayer has presented and to make whatever adjustments to the specific use tax assessments the audit division deems appropriate and justified. However, taxpayer is cautioned that the request to the audit division does not extend indefinitely to include whatever documents taxpayer deems to be "available shortly." Both taxpayer and the Department are entitled to a *timely and final* resolution of the issue.

FINDING

Subject to audit review of the documents taxpayer has presented within 30 days of the issuance of this Letter of Findings, taxpayer's protest is sustained to the extent that it paid sales tax at the time it purchased the various items at issue.

DEPARTMENT OF STATE REVENUE

0120050236.LOF

LETTER OF FINDINGS NUMBER: 05-0236
Adjusted Gross Income Tax
Tax Period 1999-2003

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-Imposition of Tax on Construction Income

Authority: IC § 6-3-2-1; IC § 6-8.1-5-1(b); IC § 6-8.1-5-4.

The taxpayer protests the imposition of adjusted gross income tax on construction income.

II. Adjusted Gross Income Tax-Imposition of Tax on Unexplained Income

Authority: IC § 6-3-1-3.5(a); 26 U.S.C.A. § 62.

The taxpayer protests the imposition of adjusted gross income tax on unexplained income.

III. Adjusted Gross Income Tax-Disallowance of Expense Deductions

Authority: IC § 6-3-1-3.5; Webster's II New Riverside University Dictionary 81 1984.

The taxpayer protests the disallowance of several expense deductions.

IV. Tax Administration-Ten Percent Negligence Penalty

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

The taxpayer protests the imposition of the penalty.

STATEMENT OF FACTS

The taxpayers are a married couple. After an investigation, the Indiana Department of Revenue (department) assessed additional adjusted gross income tax, penalty, and interest against them for the tax period 1999-2003. The taxpayers protested the assessment and a hearing was held. This Letter of Findings results.

I. Adjusted Gross Income Tax-Imposition of Tax on Construction Income

DISCUSSION

The audit assessed adjusted gross income tax on the taxpayers' income from the husband's construction activities. The taxpayers argued that the husband did not operate a construction business since he did not charge for his services. Rather, he donated his construction services to others.

Notices of Proposed Assessment are prima facie evidence that the tax assessment is correct. IC § 6-8.1-5-1(b). The taxpayers bear the burden of proving that any assessment is incorrect. Id. Taxpayers are required to keep adequate books and records so that the department can determine the proper tax owed to the state. IC § 6-8.1-5-4.

An adjusted gross income tax is imposed upon the income of Indiana residents. IC § 6-3-2-1. If the husband never charged for his construction services, he would not have had any construction income on which to impose the tax. Court documents indicated that a dissatisfied customer had previously sued the taxpayer. In his defense of that lawsuit, the taxpayer submitted letters from satisfied customers stating that he had charged a fair price. The lawsuit and letters indicate that the husband actually operated a construction business and did not always donate his services.

The taxpayers' books and records were not adequate to allow the department to determine the correct amount of income earned in the husband's construction business. Therefore, the department had no option but to prepare an estimate based upon the best information available. The taxpayers did not produce adequate documentation to substantiate their contention that the department's estimate was inaccurate.

FINDING

The taxpayer's protest to the assessment of tax on the construction income is denied.

II. Adjusted Gross Income Tax-Imposition of Tax on Unexplained Income

DISCUSSION

The taxpayers had unexplained deposits in their bank accounts. The department assessed income tax on these deposits. The taxpayers protested this assessment contending that the deposits did not represent taxable income. Rather, the taxpayer argued that the deposits represented reimbursals of monies advanced for motivational tapes and seminar tickets.

Indiana adjusted gross income is calculated by starting with the federal adjusted gross income and making certain modifications. IC § 6-3-1-3.5(a). The federal adjusted gross income calculation begins with the inclusion of all of the taxpayers' income. 26 U.S.C.A. § 62.

The taxpayers offered no documentation to substantiate that the unexplained deposits into their bank accounts were anything other than income. Therefore, they failed to sustain their burden of proving that the unexplained deposits were not subject to the Indiana adjusted gross income tax.

FINDING

The taxpayers' protest to the assessment of Indiana adjusted gross income tax on unexplained deposits is denied.

III. Adjusted Gross Income Tax-Disallowance of Expense Deductions

DISCUSSION

The taxpayers also operated a part-time business that involved two types of activities. First, the taxpayers sold items over the internet. Second, the taxpayers recruited and developed other sales people. The taxpayer took deductions for expenses incurred in the operation of the businesses. These deductions included mileage, internet usage, training and education, advertising and promotions, wages, supplies, postage, travel, meals, and lodging. Each year of the audit, the deductions exceeded the income the taxpayers received from this business. This resulted in losses that were taken against the taxpayers' income from the husband's construction business and wages received as a teacher. The department disallowed the deductions taken.

The Indiana adjusted gross income tax is calculated by starting with the taxpayers' federal adjusted gross income and making certain adjustments. IC § 6-3-1-3.5. Since the Indiana adjusted gross income tax is calculated by starting with the federal adjusted gross income, federal deductions are a part of the initial computation.

The taxpayers deducted the total cost of their internet usage claiming that it was used for business purposes only. There were six people in their household during the audit period. It is unknown if any of those people ever e-mailed a friend, checked the weather, or looked up a recipe on the internet. There were indications that the taxpayers ordered many of their goods for personal use over the internet. These are not business uses. The taxpayers were not entitled to deduct the entire amount of the internet charges. The taxpayers did not provide documentation of a reasonable estimate of the business use of the internet. They did not sustain their burden of proving that the internet usage was totally devoted to the business.

The taxpayers also took deductions for wages paid to their children. They provided no documentation substantiating that the payments to their children were actually wages for services rendered. The taxpayers did not sustain their burden of proving that the payments to their children were actually deductible wages.

The taxpayers claimed deductions for advertising expenses. Most of the advertising expenses claimed were gifts for family and friends ordered by the taxpayers through their internet sales business. Webster's II New Riverside University Dictionary 81 (1984) defines "advertise" as:

1. To make public announcement of, esp. to proclaim the qualities or advantages of so as to increase sale, *advertise* a new product.

Gifts to family and friend do not constitute public announcements about the qualities or advantages of a product. They do not have the effect of increasing sales. Therefore, gifts to family and friends do not qualify as advertising expenses. The taxpayers did not sustain their burden of proving that these gifts for family and friends were actually used for advertising. Therefore, these deductions cannot be taken against the taxpayers' income.

The taxpayers also claimed deductions for "tools" distributed to related dealers in the internet sales system. These tools were motivational tapes and books. The sales invoices they provided were postdated. The taxpayers did not substantiate *what* they paid for these items *even* if the expenses qualified as legitimate deductions.

The taxpayers took deductions for fees paid to attend seminars and the travel expenses associated with the seminars. The taxpayers submitted sheets of paper with handwritten statements of expenses on them and seminar programs to substantiate these deductions. There were no receipts or any other original documentation of a financial nature to substantiate their claims. The taxpayers did not sustain their burden of proving that they actually paid the amounts deducted for their travel, food, and seminars even if these expenses qualified as business deductions.

Finally, the taxpayers claimed deductions for office expenses and postage. Again, the taxpayers provided no original records substantiating their payments or whether the expenses they claimed were used for postage or office supplies.

FINDING

The taxpayers' protest to the denial of the expenses taken as deductions on their federal adjusted gross income tax is denied.

IV. Tax Administration-Ten Percent Negligence Penalty

DISCUSSION

The taxpayers protested the imposition of the ten percent 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 taxpayers did not keep the books and records necessary to determine the proper amount of tax due. Their disregard of their duty to keep accurate records constituted negligence.

FINDING

The taxpayers' protest to the imposition of the penalty is denied.

DEPARTMENT OF STATE REVENUE

05-20050254.LOF

LETTER OF FINDINGS NUMBER: 05-0254
Cigarette Tax
For Tax Year 2004

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.

I. Cigarette Tax--Imposition

Authority: IC 6-8.1-5-1; 45 IAC 15-5-3(b); IC 6-7-1-1; 15 U.S.C. §§ 375-378

Taxpayer protests the imposition of cigarette tax.

II. Tax Administration—Negligence Penalty and Interest

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

Taxpayer protests the imposition of a ten percent negligence penalty and interest.

STATEMENT OF FACTS

Taxpayer is an individual. As the result of an investigation, the Indiana Department of Revenue determined that taxpayer owed cigarette tax on cigarettes ordered via the internet/telephone and delivered in Indiana. Taxpayer protests that she does not owe these taxes. Further facts will be supplied as required.

I. Cigarette Tax--Imposition

DISCUSSION

Before examining the taxpayer's protest, it should be noted that the *taxpayer* bears the burden of proof. IC 6-8.1-5-1(b) states in pertinent 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 Indiana Administrative Code also states "[t]he burden of proving that a proposed assessment is incorrect rests with the taxpayer…." 45 IAC 15-5-3(b).

The taxpayer's protest consisted of the following single sentence (the taxpayer neither attended, nor telephoned, for the scheduled hearing):

> I would like to protest this tax. What law (I.C.) Indiana Code is being used to collect this tax?

The cigarette tax is found at IC 6-7-1-1, which states:

> *It is the intent and purpose of this chapter to levy a tax on all cigarettes sold, used, consumed, handled, or distributed within this state*, and to collect the tax from the person who first sells, uses, consumes, handles, or distributes the cigarettes. It is further the intent and purpose of this chapter that whenever any cigarettes are given for advertising or any purpose whatsoever, they shall be taxed in the same manner as if they were sold, used, consumed, handled, or distributed in this state. *Notwithstanding any other provisions contained in this chapter, the liability for the excise taxes imposed by this chapter shall be conclusively presumed to be on the retail purchaser or ultimate consumer, precollected for convenience and facility only.* When such taxes are paid by any other person, such payment shall be considered as an advance payment and shall be added to the price of the cigarettes and recovered from the ultimate consumer or user. Distributors, wholesalers, or retailers may state the amount of the tax separately from the price of such cigarettes on all price display signs, sales or delivery slips, bills, and statements which

advertise or indicate the price of such cigarettes.

(*Emphasis* added) As this statute makes clear, this tax applies to all purchases of cigarettes. It does not make a difference if the purchase is over the counter, via the internet/telephone, or in any other manner. Just as every person who purchases cigarettes in a store owes cigarette tax, so does the person who purchases cigarettes from an internet vendor.

The Department's assessment is based on information received pursuant to the Jenkins Act, 15 U.S.C. §§ 375-378, which is an enforcement mechanism for states to prevent evasion of state cigarette taxes.

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.

The Department received information from the vendor naming taxpayer as the purchaser of cigarettes. The Department proposed assessments based on the best information available to it, as provided by IC 6-8.1-5-1(a).

In conclusion, the Department received information under the Jenkins Act which named taxpayer as the purchaser of cigarettes in Indiana. The cigarette tax is imposed on all purchases of cigarettes in Indiana, including those purchases which are delivered into Indiana, as provided by IC 6-7-1-1. The burden of proving the assessment wrong rests with the taxpayer, as provided in IC 6-8.1-5-1(b). Taxpayer has not met this burden.

FINDING

Taxpayer's protest is denied.

II. Tax Administration—Negligence Penalty and Interest

DISCUSSION

The Department issued proposed assessments and the ten percent negligence penalty and interest for the tax years in question. Taxpayer (apparently) protests the imposition of penalty and interest. With regard to interest, the Department refers to IC 6-8.1-10-1, which states in relevant part:

> (a) If a person fails to file a return for any of the listed taxes, fails to pay the full amount of tax shown on his return by the due date for the return or the payment, or incurs a deficiency upon a determination by the department, the person is subject to interest on the nonpayment.
>
> …
>
> (e) The department may not waive the interest imposed under this section.

Since taxpayer incurred a deficiency upon a determination by the Department, as explained in Issue I., the Department may not waive interest under IC 6-8.1-10-1.

With regard to the 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 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.

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). Taxpayer has not affirmatively established that her 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

05-20050329.LOF
05-20050330.LOF

LETTER OF FINDINGS NUMBER: 05-0329; 05-0330
Cigarette Tax & Use Tax
For Tax Years 2003 and 2004

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.

I. Cigarette Tax--Imposition

Authority: 15 U.S.C. §§ 375-378; IC 6-7-1-1; IC 6-8.1-5-1; 45 IAC 15-5-3

Taxpayer protests the imposition of cigarette tax.

II. Use Tax--Imposition

Authority: IC 6-2.5-3-2; IC 6-2.5-1-5; IC 6-2.5-3-7; IC 6-8.1-5-1; 45 IAC 2.2-3-4

Taxpayer protests the imposition of use tax.

III. Tax Administration—Negligence Penalty and Interest

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

Taxpayer protests the imposition of a ten percent negligence penalty and interest.

STATEMENT OF FACTS

Taxpayer is an individual. As the result of an investigation, the Indiana Department of Revenue determined that taxpayer owed cigarette tax, use tax, and penalty on cigarettes ordered and delivered into Indiana. Taxpayer protests that he does not owe these taxes. Taxpayer also mentioned during the telephone hearing that he was protesting cigarette tax assessments for the year 2005. No protest information for 2005 is included in the file. Thus this Letter of Finding only addresses the period prior to the year 2005. Further facts will be supplied as required.

I. Cigarette Tax--Imposition

DISCUSSION

Before examining the taxpayer's protest, it should be noted that the *taxpayer* bears the burden of proof. IC 6-8.1-5-1(b) states in pertinent 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 Indiana Administrative Code also states "[t]he burden of proving that a proposed assessment is incorrect rests with the taxpayer…." 45 IAC 15-5-3(b).

The Department's proposed assessment is based on information received pursuant to the Jenkins Act, 15 U.S.C. §§ 375-378, which is an enforcement mechanism for states to prevent evasion of state cigarette taxes.

Taxpayer did not file a return with the Department which included the cigarette taxes. 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.

The Department received information from the vendor naming taxpayer as the purchaser of cigarettes. The Department made proposed assessments based on the best information available to it, as provided by IC 6-8.1-5-1(a).

Taxpayer protests the imposition of cigarette tax. Taxpayer argues that he does not owe cigarette tax. Taxpayer states in correspondence:

> [T]his is double taxation, which I do not believe is Federally Legal unless you give me an avenue to seek a refund from Kentucky for the tax collected. Kentucky tax stamps are on the cigarette packs, so a cigarette tax was already paid on these packs.

Regarding the taxpayer's "double taxation" argument, the Indiana cigarette tax (found at IC 6-7-1-1) states:

> *It is the intent and purpose of this chapter to levy a tax on all cigarettes sold, used, consumed, handled, or distributed within this state, and to collect the tax from the person who first sells, uses, consumes, handles, or distributes the cigarettes*. It is further the intent and purpose of this chapter that whenever any cigarettes are given for advertising or any purpose whatsoever, they shall be taxed in the same manner as if they were sold, used, consumed, handled, or distributed in this state. *Notwithstanding any other provisions contained in this chapter, the liability for the excise taxes imposed by this chapter shall*

be conclusively presumed to be on the retail purchaser or ultimate consumer, precollected for convenience and facility only. When such taxes are paid by any other person, such payment shall be considered as an advance payment and shall be added to the price of the cigarettes and recovered from the ultimate consumer or user. Distributors, wholesalers, or retailers may state the amount of the tax separately from the price of such cigarettes on all price display signs, sales or delivery slips, bills, and statements which advertise or indicate the price of such cigarettes.

(*Emphasis* added). As this statute makes clear, this tax applies to all purchases of cigarettes. It does not make a difference if the purchase is over the counter, via the internet, telephone, or in any other manner. Just as every person who purchases cigarettes in a store owes cigarette tax, so does the person who purchases cigarettes from an internet vendor.

Returning to the taxpayer's argument, as IC 6-7-1-1 makes clear, the taxpayer's cigarettes were taxable in Indiana. The taxpayer does not develop his "double taxation" argument beyond the assertion quoted above. As already indicated, the taxpayer has the burden of proof, and has failed to meet it regarding the "double taxation" argument. If the taxpayer did in fact pay a cigarette tax to Kentucky on the cigarettes at issue (the taxpayer did not supply any documentation to that effect), any remedy (if there is one) would have to be sought with Kentucky.

Taxpayer also argues the number of cigarettes purchased in 2004. Taxpayer states:

According to my recorders [*sic*], which I have provided a report from my Quicken, I received 11 orders from [Company X] in 2004 totaling 108 cartons/1080 pack of cigarettes. We consumed 1000 of these packs, 80 packs were given as gifts to relatives in Ill. and TN. Not sure the gifts are taxable either.

Dealing with this in reverse order, regarding the (purported) gifts argument, taxpayer does not develop this argument, but it should be recalled that IC 6-7-1-1 states (*Emphasis* added):

It is the intent and purpose of this chapter to levy a tax on *all* cigarettes sold, used, consumed, *handled*, or *distributed* within this state, and to collect the tax from the person who first sells, uses, consumes, handles, or distributes the cigarettes….

Turning to the number of cigarettes purchased, taxpayer seems to be arguing that he was billed for purchases he did not make. However, what the taxpayer fails to note is the fact that he also made purchases in 2003. The taxpayer has been billed for 2003 *and* 2004.

In conclusion, the Department received information under the Jenkins Act which named taxpayer as the purchaser of cigarettes in Indiana. The cigarette tax is imposed on all purchases of cigarettes in Indiana, including those purchases which are delivered into Indiana, as provided by IC 6-7-1-1. The burden of proving the assessment wrong rests with the taxpayer, as provided in IC 6-8.1-5-1(b). Taxpayer has not met this burden.

FINDING

Taxpayer's protest is denied.

II. Use Tax--Imposition

DISCUSSION

Taxpayer protests the imposition of use tax on his purchase of cigarettes ordered and delivered into Indiana. The use tax is complementary to the sales tax and is found at IC 6-2.5-3-2(a), which states:

An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

Also of relevance is 45 IAC 2.2-3-4, which states:

Tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used, or otherwise consumed in Indiana is subject to Indiana use tax for such property, unless the Indiana state gross retail tax has been collected at the point of purchase.

This means that Indiana use tax is due when Indiana sales tax is not collected. The Department has received no documentation to indicate, let alone establish, that sales tax was collected on the purchase of the cigarettes at issue.

Taxpayer challenges the number of cigarettes purchased and "shipping which is not taxable." Regarding the number of cigarettes purchased, that was dealt with already in Issue I. It should be noted that shipping is in fact taxable under IC 6-2.5-1-5. (It should also be noted that taxpayer provided one receipt for a 2005 purchase—not a 2003 or 2004 purchase. However, if this receipt is indicative of the cost of the cigarettes for 2003 and 2004, it goes against the taxpayer's argument, since if it truly is representative of 2003 and 2004 then it appears the Department may have *under* billed the taxpayer for use tax).

As explained in Issue I, under IC 6-8.1-5-1(b) the burden of proving the assessment wrong rests with the taxpayer. Beyond this general burden is IC 6-2.5-3-7(a), which states:

A person who acquires tangible personal property from a retail merchant for delivery in Indiana is presumed to have acquired the property for storage, use, or consumption in Indiana, unless the person or the retail merchant can produce evidence to rebut that presumption.

Taxpayer has not produced sufficient evidence to rebut the presumption that the cigarettes were acquired for storage, use, or consumption in Indiana. Since Indiana sales tax was not collected on the purchase of the cigarettes, under IC 6-2.5-3-2(a) and 45 IAC

2.2-3-4, Indiana use tax is due on the purchase of the cigarettes. Taxpayer has not met the burden of proving the proposed assessment wrong, as explained under IC 6-8.1-5-1(b).

FINDING

Taxpayer's protest is denied.

III. Tax Administration—Negligence Penalty and Interest

DISCUSSION

The Department issued proposed assessments and the ten percent negligence penalty and interest for the tax years in question. Taxpayer protests the imposition of penalty and interest. With regard to interest, the Department refers to IC 6-8.1-10-1, which states in relevant part:

(a) If a person fails to file a return for any of the listed taxes, fails to pay the full amount of tax shown on his return by the due date for the return or the payment, or incurs a deficiency upon a determination by the department, the person is subject to interest on the nonpayment.

…

(e) The department may not waive the interest imposed under this section.

Since taxpayer incurred a deficiency upon a determination by the Department, as explained in Issues I and II, the Department may not waive interest under IC 6-8.1-10-1.

With regard to the 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 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.

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). Taxpayer has not affirmatively established that his 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

0420050354.LOF

LETTER OF FINDINGS NUMBER: 05-0354
Sales and Use Tax
Tax Period 2002-2004

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-Imposition

Authority: IC § 6-8.1-5-1(b); IC § 6-2.5-2-1(a); IC § 6-2.5-2-2; IC § 6-8.1-5-4.

The taxpayer protested the imposition of sales tax.

II. Tax Administration- Ten Percent Negligence Penalty

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

The taxpayer protested the imposition of the ten percent negligence penalty.

STATEMENT OF FACTS

The taxpayer is a vendor of food and drinks at an annual festival. After an audit, the Indiana Department of Revenue (department) assessed additional sales tax, penalty, and interest against the taxpayer for the tax period 2002-2004. The taxpayer protested this assessment. A hearing was held and this Letter of Findings results.

I. Sales and Use Tax-Imposition

DISCUSSION

Indiana imposes a sales tax on the transfer of tangible personal property in a retail transaction. IC § 6-2.5-2-1(a). The sales tax to be remitted to the state is computed by multiplying the total sales by the sales tax rate. IC § 6-2.5-2-2.

Notices of proposed assessments are prima facie evidence that the department's claim for unpaid taxes is valid**.** The taxpayer has the burden of proving that the department incorrectly imposed the assessment. IC § 6-8.1-5-1(b). Taxpayers are required to keep adequate books and records so that the department can determine the proper tax owed to the state. IC § 6-8.1-5-4.

The taxpayers' books and records were not adequate to allow the department to determine the correct amount of tax. Therefore, the department had no option but to prepare an estimate based upon the best information available. The department estimated the total gross amount of sales in the following manner:

The taxpayer did not have invoices from all vendors, and the dates from invoices provided were not consecutive. Invoices were only provided for the audit periods of 2003 and 2004. For the years of 2003 and 2004 the amount of ham purchased from each invoice (which was sixty pounds) was applied every day of the festival with the exception of the weekends. Observations of the festival prove that the weekends have approximately twice as many customers. Therefore, the amounts for weekend operations were doubled.

An approximate amount of ham purchased allowed for conversion of pounds to ounces. Next, the total amount of ham in ounces was divided by four, which is an approximate amount of meat per the average sandwich. The result gave an approximate number of sandwiches. Per observations and taxpayer the sandwiches are sold at six dollars a sandwich. The approximate number of sandwiches was multiplied by the six dollar cost to result in the total dollar amount of sandwiches.

Observations concluded sandwiches were approximately one half of the gross receipts; therefore the total dollar amount of sandwiches was multiplied by two. This resulted in total amount of sales. The amounts were consistent for each year. Therefore, the amount of gross receipts for 2003 and 2004 was applied to 2002.

The total amount of sales less amounts reported gave additional sales subject to the gross retail tax.

The department notes that, aside from poor record keeping, the audit found evidence of unreported sales and transactions. The taxpayer now argues that the amount originally assessed was too great. The taxpayer suggested that the department could make a better estimate by applying the 2005 total sales amounts to the three years covered by the audit. The taxpayer did maintain 2005 records; the amount of 2005 sales is approximately 40 percent lower than the estimated sales for the tax period. While the Department agrees that the 2005 records *could* provide a reasonable basis for projecting the estimated periods, the department declines to make such a factual determination. The administrative review process is not the forum for making such a numerical determination based solely on taxpayer's unexamined, unchallenged assertion. However, the taxpayer has met its burden of demonstrating that the estimated sales amounts should be reconsidered.

FINDING

Subject to a supplementary audit review of the taxpayer's 2005 records and a comparison of those records with the estimated periods, the taxpayer's protest is sustained.

II. Tax Administration- Ten Percent Negligence Penalty

DISCUSSION

The taxpayer protested the imposition of the ten percent (10[percent]) 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.

During the period of the audit, the taxpayer ignored the law and the department's` instructions for the payment of sales tax and maintenance of adequate records. The taxpayer's inattention to these duties resulted in the tax assessment. These breaches of the taxpayer's duty constituted negligence.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0320050355P.LOF

LETTER OF FINDINGS NUMBER: 05-0355P
Withholding Tax
For the month of December 2004

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 period December 2004. The taxpayer is an Indiana company.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the late penalty be abated as the taxpayer says (1) the liability qualifies for the Tax Amnesty program, (2) the taxpayer has a good payment record, and (3) the taxpayer was too busy to complete the return.

With regard to the Tax Amnesty program, only liabilities that end before July 1, 2004, qualify for Tax Amnesty. As this liability period ended after July 1, 2004, this liability does not qualify for Tax Amnesty.

With regard to the compliance record, the taxpayer has had a couple of errors in the past few years. The Department does not feel the taxpayer's compliance record would be a factor in the abatement of penalty.

The taxpayer states he was too busy with work during the holiday season to complete the return on time. This is a situation that would be inattention and inattention is negligence.

The regulation which provides the guideline for penalty is as follows:

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

0520050357.LOF

LETTER OF FINDINGS NUMBER: 05-0357
Cigarette Tax
For Tax Years 2004

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.

I. Cigarette Tax--Imposition

Authority: 15 U.S.C. §§ 375-378; IC 6-7-1-1; IC 6-8.1-5-1; 45 IAC 15-5-3

Taxpayer protests the imposition of cigarette tax.

II. Use Tax--Imposition

Authority: IC 6-2.5-3-2; IC 6-2.5-3-7; IC 6-8.1-5-1; 45 IAC 2.2-3-4

Taxpayer protests the imposition of use tax.

III. Tax Administration—Negligence Penalty and Interest

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

Taxpayer protests the imposition of a ten percent negligence penalty and interest.

STATEMENT OF FACTS

Taxpayer is an individual. As the result of an investigation, the Indiana Department of Revenue determined that taxpayer owed cigarette tax, use tax and penalty on cigarettes ordered via the internet and telephone and delivered in Indiana. Taxpayer protests that he does not owe these taxes. Further facts will be supplied as required.

I. Cigarette Tax--Imposition

DISCUSSION

Before examining the taxpayer's protest, it should be noted that the *taxpayer* bears the burden of proof. IC 6-8.1-5-1(b) states in pertinent 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 Indiana Administrative Code also states "[t]he burden of proving that a proposed assessment is incorrect rests with the taxpayer…." 45 IAC 15-5-3(b).

Taxpayer protests the imposition of cigarette tax. Taxpayer argues that he does not owe cigarette tax. Taxpayer states that there were no warnings about possible tax liabilities on the website and that he had no way of knowing about the taxes.

The cigarette tax is found at IC 6-7-1-1, which states:

> It is the intent and purpose of this chapter to levy a tax on all cigarettes sold, used, consumed, handled, or distributed within this state, and to collect the tax from the person who first sells, uses, consumes, handles, or distributes the cigarettes. It is further the intent and purpose of this chapter that whenever any cigarettes are given for advertising or any purpose whatsoever, they shall be taxed in the same manner as if they were sold, used, consumed, handled, or distributed in this state. Notwithstanding any other provisions contained in this chapter, the liability for the excise taxes imposed by this chapter shall be conclusively presumed to be on the retail purchaser or ultimate consumer, precollected for convenience and facility only. When such taxes are paid by any other person, such payment shall be considered as an advance payment and shall be added to the price of the cigarettes and recovered from the ultimate consumer or user. Distributors, wholesalers, or retailers may state the amount of the tax separately from the price of such cigarettes on all price display signs, sales or delivery slips, bills, and statements which advertise or indicate the price of such cigarettes.

As this statute makes clear, this tax applies to all purchases of cigarettes. It does not make a difference if the purchase is over the counter, via the internet, by telephone or in any other manner. Just as every person who purchases cigarettes in a store owes cigarette tax, so does the person who purchases cigarettes from an internet vendor.

The Department was informed that taxpayer had purchased cigarettes due to the provisions of the Jenkins Act, 15 U.S.C. §§ 375-378. The Jenkins Act states in relevant part:

> (a) Contents. Any person who sells or transfers for profit cigarettes in interstate commerce, whereby such cigarettes are shipped into a State taxing the sale or use of cigarettes to other than a distributor licensed by or located in such State, or who advertises or offers cigarettes for such sale or transfer and shipment, shall--
>
> (1) first file with the tobacco tax administrator of the State into which such shipment is made or in which such advertisement or offer is disseminated a statement setting forth his name and trade name (if any), and the address of his principal place of business and of any other place of business; and
>
> (2) not later than the 10th day of each calendar month, file with the tobacco tax administrator of the State into which such shipment is made, a memorandum or a copy of the invoice covering each and every shipment of cigarettes made during the previous calendar month into such State; the memorandum or invoice in each case to include the name and address of the person to whom the shipment was made, the brand, and the quantity thereof.
>
> (b) Presumptive evidence. The fact that any person ships or delivers for shipment any cigarettes shall, if such shipment is into a State in which such person has filed a statement with the tobacco tax administrator under subsection (a) (1) of this section, be presumptive evidence (1) that such cigarettes were sold, or transferred for profit, by such person, and (2) that such sale or transfer was to other than a distributor licensed by or located in such State.
>
> 15 U.S.C. § 376

Also of relevance, a distributor is defined by 15 U.S.C. § 375(3) as:

> (A) in the case of any State which by State statute or regulation authorizes the distribution of cigarettes at wholesale or retail,

any person so authorized, or

(B) in the case of any other State, any person located in such State who distributes cigarettes at wholesale or retail;

but such term in no case includes a person who acquires cigarettes for purposes other than resale.

15 U.S.C. § 376 provides that a seller of cigarettes that sells cigarettes from one state to consumers for delivery in another state must provide the tobacco tax administrator of the state into which the cigarettes are distributed certain information. This information includes the name of the person to whom the cigarettes were sold, the brand of cigarettes sold, and the quantity of cigarettes sold. The Department's current assessment was based on information received pursuant to the Jenkins Act. The internet distributor was required by law to provide the names, brands, and quantities of all Indiana purchasers of its cigarettes. The internet distributor provided those names, and the Department sought to collect the tax from the persons to whom the distributor shipped its cigarettes.

In conclusion, the Department received information under the Jenkins Act which named taxpayer as the purchaser of cigarettes in Indiana. The cigarette tax is imposed on all purchases of cigarettes in Indiana, including those purchases which are delivered into Indiana, as provided by IC 6-7-1-1. The burden of proving the assessment wrong rests with the taxpayer, as provided in IC 6-8.1-5-1(b). Taxpayer has not met this burden.

FINDING

Taxpayer's protest is denied.

II. Use Tax--Imposition

DISCUSSION

Taxpayer protests the imposition of use tax on its purchase of cigarettes ordered via the internet and delivered in Indiana. Taxpayer offers the same arguments as in Issue I. The use tax is complementary to the sales tax and is found at IC 6-2.5-3-2(a), which states:

An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

Also of relevance is 45 IAC 2.2-3-4, which states:

Tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used, or otherwise consumed in Indiana is subject to Indiana use tax for such property, unless the Indiana state gross retail tax has been collected at the point of purchase.

This means that Indiana use tax is due when Indiana sales tax is not collected. The Department has received no documentation to indicate, let alone establish, that sales tax was collected on the purchase of the cigarettes at issue.

As explained in Issue I, under IC 6-8.1-5-1(b) the burden of proving the assessment wrong rests with the taxpayer. Beyond this general burden is IC 6-2.5-3-7(a), which states:

A person who acquires tangible personal property from a retail merchant for delivery in Indiana is presumed to have acquired the property for storage, use, or consumption in Indiana, unless the person or the retail merchant can produce evidence to rebut that presumption.

Taxpayer has not produced sufficient evidence to rebut the presumption that the cigarettes were acquired for storage, use or consumption in Indiana. Since Indiana sales tax was not collected on the purchase of the cigarettes, under IC 6-2.5-3-2(a) and 45 IAC 2.2-3-4, Indiana use tax is due on the purchase of the cigarettes. Taxpayer has not met the burden of proving the proposed assessment wrong, as explained under IC 6-8.1-5-1(b).

FINDING

Taxpayer's protest is denied.

III. Tax Administration—Negligence Penalty and Interest

DISCUSSION

The Department issued proposed assessments and the ten percent negligence penalty and interest for the tax years in question. Taxpayer protests the imposition of penalty and interest. With regard to interest, the Department refers to IC 6-8.1-10-1, which states in relevant part:

(a) If a person fails to file a return for any of the listed taxes, fails to pay the full amount of tax shown on his return by the due date for the return or the payment, or incurs a deficiency upon a determination by the department, the person is subject to interest on the nonpayment.

…

(e) The department may not waive the interest imposed under this section.

Since taxpayer incurred a deficiency upon a determination by the Department, as explained in Issues I and II, the Department may not waive interest under IC 6-8.1-10-1.

With regard to the 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 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.

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). Taxpayer has not affirmatively established by documentation and explanation that his failure to pay the deficiency was due to reasonable cause and not due to negligence, as required by 45 IAC 15-11-2(c). The interest cannot be waived, under IC 6-8.1-10-1. The negligence penalty shall be waived.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420050358.LOF

LETTER OF FINDINGS NUMBER: 05-0358
Cigarette Tax
For Tax Years 2004

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.

I. Cigarette Tax--Imposition

Authority: 15 U.S.C. §§ 375-378; IC 6-7-1-1; IC 6-8.1-5-1; 45 IAC 15-5-3

Taxpayer protests the imposition of cigarette tax.

II. Use Tax--Imposition

Authority: IC 6-2.5-3-2; IC 6-2.5-3-7; IC 6-8.1-5-1; 45 IAC 2.2-3-4

Taxpayer protests the imposition of use tax.

III. Tax Administration—Negligence Penalty and Interest

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

Taxpayer protests the imposition of a ten percent negligence penalty and interest.

STATEMENT OF FACTS

Taxpayer is an individual. As the result of an investigation, the Indiana Department of Revenue determined that taxpayer owed cigarette tax, use tax and penalty on cigarettes ordered via the internet and telephone and delivered in Indiana. Taxpayer protests that he does not owe these taxes. Further facts will be supplied as required.

I. Cigarette Tax--Imposition

DISCUSSION

Before examining the taxpayer's protest, it should be noted that the *taxpayer* bears the burden of proof. IC 6-8.1-5-1(b) states in pertinent 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 Indiana Administrative Code also states "[t]he burden of proving that a proposed assessment is incorrect rests with the taxpayer…." 45 IAC 15-5-3(b).

Taxpayer protests the imposition of cigarette tax. Taxpayer argues that he does not owe cigarette tax. Taxpayer states that there were no warnings about possible tax liabilities on the website and that he had no way of knowing about the taxes.

The cigarette tax is found at IC 6-7-1-1, which states:

> It is the intent and purpose of this chapter to levy a tax on all cigarettes sold, used, consumed, handled, or distributed within this state, and to collect the tax from the person who first sells, uses, consumes, handles, or distributes the cigarettes. It is further the intent and purpose of this chapter that whenever any cigarettes are given for advertising or any purpose whatsoever, they shall be taxed in the same manner as if they were sold, used, consumed, handled, or distributed in this state. Notwithstanding any other provisions contained in this chapter, the liability for the excise taxes imposed by this chapter shall be conclusively presumed to be on the retail purchaser or ultimate consumer, precollected for convenience and facility only. When such taxes are paid by any other person, such payment shall be considered as an advance payment and shall be added to the price of the cigarettes and recovered from the ultimate consumer or user. Distributors, wholesalers, or retailers may state the amount of the tax separately from the price of such cigarettes on all price display signs, sales or delivery slips, bills, and statements which advertise or indicate the price of such cigarettes.

As this statute makes clear, this tax applies to all purchases of cigarettes. It does not make a difference if the purchase is over the counter, via the internet, by telephone or in any other manner. Just as every person who purchases cigarettes in a store owes cigarette tax, so does the person who purchases cigarettes from an internet vendor.

The Department was informed that taxpayer had purchased cigarettes due to the provisions of the Jenkins Act, 15 U.S.C. §§ 375-378. The Jenkins Act states in relevant part:

> (a) Contents. Any person who sells or transfers for profit cigarettes in interstate commerce, whereby such cigarettes are shipped into a State taxing the sale or use of cigarettes to other than a distributor licensed by or located in such State, or who advertises or offers cigarettes for such sale or transfer and shipment, shall--
>
> > (1) first file with the tobacco tax administrator of the State into which such shipment is made or in which such advertisement or offer is disseminated a statement setting forth his name and trade name (if any), and the address of his principal place of business and of any other place of business; and
> >
> > (2) not later than the 10th day of each calendar month, file with the tobacco tax administrator of the State into which such shipment is made, a memorandum or a copy of the invoice covering each and every shipment of cigarettes made during the previous calendar month into such State; the memorandum or invoice in each case to include the name and address of the person to whom the shipment was made, the brand, and the quantity thereof.
>
> (b) Presumptive evidence. The fact that any person ships or delivers for shipment any cigarettes shall, if such shipment is into a State in which such person has filed a statement with the tobacco tax administrator under subsection (a) (1) of this section, be presumptive evidence (1) that such cigarettes were sold, or transferred for profit, by such person, and (2) that such sale or transfer was to other than a distributor licensed by or located in such State.
>
> 15 U.S.C. § 376

Also of relevance, a distributor is defined by 15 U.S.C. § 375(3) as:

> (A) in the case of any State which by State statute or regulation authorizes the distribution of cigarettes at wholesale or retail, any person so authorized, or
>
> (B) in the case of any other State, any person located in such State who distributes cigarettes at wholesale or retail;

but such term in no case includes a person who acquires cigarettes for purposes other than resale.

15 U.S.C. § 376 provides that a seller of cigarettes that sells cigarettes from one state to consumers for delivery in another state must provide the tobacco tax administrator of the state into which the cigarettes are distributed certain information. This information includes the name of the person to whom the cigarettes were sold, the brand of cigarettes sold, and the quantity of cigarettes sold. The Department's current assessment was based on information received pursuant to the Jenkins Act. The internet distributor was required by law to provide the names, brands, and quantities of all Indiana purchasers of its cigarettes. The internet distributor provided those names, and the Department sought to collect the tax from the persons to whom the distributor shipped its cigarettes

In conclusion, the Department received information under the Jenkins Act which named taxpayer as the purchaser of cigarettes in Indiana. The cigarette tax is imposed on all purchases of cigarettes in Indiana, including those purchases which are delivered into Indiana, as provided by IC 6-7-1-1. The burden of proving the assessment wrong rests with the taxpayer, as provided in IC 6-8.1-5-1(b). Taxpayer has not met this burden.

FINDING

Taxpayer's protest is denied.

II. Use Tax--Imposition

DISCUSSION

Taxpayer protests the imposition of use tax on its purchase of cigarettes ordered via the internet and delivered in Indiana. Taxpayer offers the same arguments as in Issue I. The use tax is complementary to the sales tax and is found at IC 6-2.5-3-2(a), which states:

An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

Also of relevance is 45 IAC 2.2-3-4, which states:

Tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used, or otherwise consumed in Indiana is subject to Indiana use tax for such property, unless the Indiana state gross retail tax has been collected at the point of purchase.

This means that Indiana use tax is due when Indiana sales tax is not collected. The Department has received no documentation to indicate, let alone establish, that sales tax was collected on the purchase of the cigarettes at issue.

As explained in Issue I, under IC 6-8.1-5-1(b) the burden of proving the assessment wrong rests with the taxpayer. Beyond this general burden is IC 6-2.5-3-7(a), which states:

A person who acquires tangible personal property from a retail merchant for delivery in Indiana is presumed to have acquired the property for storage, use, or consumption in Indiana, unless the person or the retail merchant can produce evidence to rebut that presumption.

Taxpayer has not produced sufficient evidence to rebut the presumption that the cigarettes were acquired for storage, use or consumption in Indiana. Since Indiana sales tax was not collected on the purchase of the cigarettes, under IC 6-2.5-3-2(a) and 45 IAC 2.2-3-4, Indiana use tax is due on the purchase of the cigarettes. Taxpayer has not met the burden of proving the proposed assessment wrong, as explained under IC 6-8.1-5-1(b).

FINDING

Taxpayer's protest is denied.

III. Tax Administration—Negligence Penalty and Interest

DISCUSSION

The Department issued proposed assessments and the ten percent negligence penalty and interest for the tax years in question. Taxpayer protests the imposition of penalty and interest. With regard to interest, the Department refers to IC 6-8.1-10-1, which states in relevant part:

(a) If a person fails to file a return for any of the listed taxes, fails to pay the full amount of tax shown on his return by the due date for the return or the payment, or incurs a deficiency upon a determination by the department, the person is subject to interest on the nonpayment.

…

(e) The department may not waive the interest imposed under this section.

Since taxpayer incurred a deficiency upon a determination by the Department, as explained in Issues I and II, the Department may not waive interest under IC 6-8.1-10-1.

With regard to the 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 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.

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). Taxpayer has not affirmatively established by documentation and explanation that his failure to pay the deficiency was due to reasonable cause and not due to negligence, as required by 45 IAC 15-11-2(c). The interest cannot be waived, under IC 6-8.1-10-1. The negligence penalty shall be waived.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0120050373P.LOF

LETTER OF FINDINGS NUMBER: 05-0373P
Income Tax
For the Calendar Year 2004

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 filing of an annual income tax return for the calendar year 2004. The taxpayer is an out-of-state resident.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty be abated as the taxpayer did not receive the needed K-1 information to complete the income tax return until after the April 15th due date.

The Department takes the position that the taxpayer could have submitted an estimate by filing an extension before the April 15th due date. This estimated extension would have been calculated from information included in the 3rd quarterly report or the annual statement of the limited partnership. Then, when the taxpayer received the actual K-1, the taxpayer could file the individual tax return requesting a refund.

The regulation which controls the application of penalty is 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 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 as the taxpayer did not pay 90 percent of the tax due by the April 15th due date. 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

0120050394.LOF

LETTER OF FINDINGS NUMBER 05-0394
ADJUSTED GROSS INCOME TAX
For Tax Period 2002-2004

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.

ISSUE

I. Adjusted Gross Income Tax - Imposition

Authority: IC § 6-3-2-1(a); IC § 6-8.1-5-1(b); IC § 6-8.1-5-4.

The taxpayers protest the imposition of adjusted gross income tax.

STATEMENT OF FACTS

The taxpayers are a married couple who were residents of Georgia. The husband received income as a managing partner of a hotel and restaurant in Indiana. The taxpayers did not remit Indiana adjusted gross income taxes on their income from the hotel and restaurant during the years 2002-2004. The Indiana Department of Revenue (department) assessed the taxpayers adjusted gross income tax, interest, and penalty against the taxpayers for the tax period. The taxpayers protested the assessment and a hearing was scheduled. The taxpayers failed to participate. This Letter of Findings is based upon the documentation in the file.

I. Adjusted Gross Income Tax - Imposition

DISCUSSION

An adjusted gross income tax is imposed upon the Indiana source income of nonresidents. IC § 6-3-2-1(a). Income from managing an Indiana hotel and restaurant is Indiana source income subject to the Indiana adjusted gross income tax. The taxpayers protested the amount of the assessment.

Notices of proposed assessments are prima facie evidence that the department's claim for unpaid taxes is valid**.** The taxpayer has the burden of proving that the department incorrectly imposed the assessment. IC § 6-8.1-5-1(b). Taxpayers are required to keep adequate books and records so that the department can determine the proper tax owed to the state. IC § 6-8.1-5-4.

The taxpayers' books and records were not adequate to allow the department to determine the correct amount of tax. Therefore, the department had no option but to prepare an estimate based upon the best information available. The taxpayers did not produce any documentation to substantiate their contention that the department's estimate was inaccurate.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420050395.LOF

LETTER OF FINDINGS NUMBER 05-0395
RESPONSIBLE OFFICER
SALES TAX
For Tax Period 2002-2004

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.

ISSUE

I. Sales Tax -Responsible Officer Liability

Authority: IC § 6-2.5-9-3; IC § 6-8.1-5-1(b).

The taxpayer protests the assessment of corporate sales taxes against him as a responsible officer.

STATEMENT OF FACTS

The taxpayer was a member of a limited liability corporation that operated a hotel and did not remit sales taxes to Indiana for the tax period 2002-2004. The Indiana Department of Revenue assessed the outstanding corporate sales taxes, interest, and penalty against the taxpayer personally. The taxpayer protested the assessment and a hearing was scheduled. The taxpayer failed to participate. This Letter of Findings is based upon the documentation in the file.

I. Sales Tax -Responsible Officer Liability

DISCUSSION

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.

Indiana Department of Revenue assessments are prima facie evidence that the tax assessment is correct. The taxpayer bears the burden of proving that the assessment is incorrect. IC § 6-8.1-5-1(b).

The taxpayer first argued in his protest letter that he could not be held responsible because the business was organized as a

limited liability corporation. The taxpayer errs in this conclusion pursuant to the statute assigning personal liability for unpaid corporate sales tax trust taxes to members of a business who had the duty to remit the taxes. The taxpayer was listed in the "Articles of Organization" filed with the Indiana Secretary of State as a managing partner of the limited liability corporation. As a managing partner, he was one of the persons responsible for the payment of the trust taxes to the state.

Secondly, the taxpayer argued that there were other persons with the responsibility to remit the trust taxes to the state. Responsible parties are jointly and severally liable for the trust taxes that were not remitted to the state. Therefore, even if there might have been others who were also responsible officers, the department has the authority to impose the corporate trust taxes against one responsible party.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0120050400P.LOF

LETTER OF FINDINGS NUMBER: 05-0400P
Individual Income Tax
For the Calendar Year 2004

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on the 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. Tax Administration – Penalty

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

The taxpayers protest the penalty assessed for failure to file their individual income tax return and remit the tax due by the appropriate date.

STATEMENT OF FACTS

The taxpayers filed their individual income tax return for the calendar year 2004 after the due date. A portion of the calculated amount of tax due was remitted with the return. Accordingly, the department assessed a penalty for the taxpayer's failure to timely remit the full amount of tax due. In the letter of protest, the taxpayer requested that the penalty be abated due to reasonable cause.

I. Tax Administration – Penalty

The return in question was due on April 15, 2005. It was filed on August 31, 2005. The taxpayer asserts that the penalty should be waived because he was unemployed for five months during 2005 due to the dissolution of his corporation. The department acknowledges the hardship created by the dissolution of one's employer. However, the department also notes that the taxpayer failed to have an adequate amount of Indiana income tax withheld from his salary and failed to remit estimated tax during 2004. Had the taxpayers remitted an appropriate amount of estimated tax, this matter could likely have been avoided.

Administrative Rule 45 IAC 15-11-2 (b) states the following:

"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 taxpayers have not established that their failure to timely file the return in question and pay the appropriate tax was due to reasonable cause and not due to negligence.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

05-20050401.LOF

LETTER OF FINDINGS NUMBER: 05-0401
Cigarette Tax
For Tax Year 2005

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.

I. Cigarette Tax--Imposition

Authority: IC 6-8.1-5-1(b); 45 IAC 15-5-3(b); IC 6-7-1-1; 15 U.S.C. §§ 375-378; IC 6-8.1-5-1(a)

Taxpayer protests the imposition of cigarette tax.

STATEMENT OF FACTS

Taxpayer is an individual. As the result of an investigation, the Indiana Department of Revenue determined that taxpayer owed cigarette tax on cigarettes ordered via the internet/telephone and delivered in Indiana. Taxpayer protests that the taxpayer does not owe these taxes. Further facts will be supplied as required.

I. Cigarette Tax--Imposition

DISCUSSION

Before examining the taxpayer's protest, it should be noted that the *taxpayer* bears the burden of proof. IC 6-8.1-5-1(b) states in pertinent 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 Indiana Administrative Code also states "[t]he burden of proving that a proposed assessment is incorrect rests with the taxpayer…." 45 IAC 15-5-3(b).

Regarding the cigarettes at issue, the taxpayer states in correspondence:

> I bought these cigarettes from [Company X] …. They told me they didn't have a carrier to ship direct to California. They asked if I had a relative in Indiana they could ship them to and my relative could ship them on to me.
>
> These cigarettes were NEVER opened in Indiana only addressed and shipped. There is no PROFIT whatsoever only for PERSONAL use.

And further, the taxpayer states that, "They [Company X] had told me that all Taxes had been paid on these cigarettes or I sure wouldn't have ordered them."

The cigarette tax is found at IC 6-7-1-1, which states:

> *It is the intent and purpose of this chapter to levy a tax on all cigarettes sold, used, consumed, handled, or distributed within this state*, and to collect the tax from the person who first sells, uses, consumes, handles, or distributes the cigarettes. It is further the intent and purpose of this chapter that whenever any cigarettes are given for advertising or any purpose whatsoever, they shall be taxed in the same manner as if they were sold, used, consumed, handled, or distributed in this state. *Notwithstanding any other provisions contained in this chapter, the liability for the excise taxes imposed by this chapter shall be conclusively presumed to be on the retail purchaser or ultimate consumer, precollected for convenience and facility only.* When such taxes are paid by any other person, such payment shall be considered as an advance payment and shall be added to the price of the cigarettes and recovered from the ultimate consumer or user. Distributors, wholesalers, or retailers may state the amount of the tax separately from the price of such cigarettes on all price display signs, sales or delivery slips, bills, and statements which advertise or indicate the price of such cigarettes.

(*Emphasis* added) As this statute makes clear, this tax applies to all purchases of cigarettes. It does not make a difference if the purchase is over the counter, via the internet/telephone, or in any other manner. Just as every person who purchases cigarettes in a store owes cigarette tax, so does the person who purchases cigarettes from an internet vendor.

The Department's assessment is based on information received pursuant to the Jenkins Act, 15 U.S.C. §§ 375-378, which is an enforcement mechanism for states to prevent evasion of state cigarette taxes.

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.

The Department received information from the vendor naming taxpayer as the purchaser of cigarettes. The Department made proposed assessments based on the best information available to it, as provided by IC 6-8.1-5-1(a).

In conclusion, the Department received information under the Jenkins Act which named taxpayer as the purchaser of cigarettes in Indiana. The cigarette tax is imposed on all purchases of cigarettes in Indiana, including those purchases which are delivered into Indiana, as provided by IC 6-7-1-1. The burden of proving the assessment wrong rests with the taxpayer, as provided in IC 6-8.1-5-1(b). Taxpayer has not met this burden.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420050413.LOF

LETTER OF FINDINGS NUMBER: 05-0413
Sales and Use Tax
For the Years 2004-2005

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- Imposition

Authority: IC 6-8.1-5-1(b), IC 6-2.5-2-1

The taxpayer protests the imposition of sales tax.

II. Tax Administration- Ten Percent Negligence Penalty

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

The taxpayer protests the imposition of the ten percent negligence penalty.

STATEMENT OF FACTS

The taxpayer became a corporation in 2003 and was formerly a sole proprietorship for 2001 and 2002. The taxpayer's sales are primarily marketing signs for realty agents, apartment complexes, contractors, property managers, and retail establishments. At issue are the signs, banners, monuments, etc. that are custom made for each customer. The Department conducted an audit covering the period January 1, 2004, through June 30, 2005. The audit brought the taxpayer up to date for the reporting of sales tax. No records were provided at the time of the audit so the audit was completed based upon the best information available. After an audit, the Indiana Department of Revenue, hereinafter referred to as the "department," assessed additional sales tax, interest, and penalty. The taxpayer protested the assessment. At the taxpayer's request, this Letter of Findings is based upon the documentation contained in the file and additional documentation supplied prior to hearing.

I. Sales and Use Tax-Imposition

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

Indiana imposes a sales tax on retail sales of tangible personal property in Indiana. The sellers of the property are required to collect the sales tax from the purchasers and remit that tax to the state unless the sale qualifies for a statutory exemption. IC 6-2.5-2-1.

The taxpayer states that the Department used invoices mailed in each period rather than the actual invoices that customers paid. The taxpayer's representative argues that the taxpayer is a cash basis taxpayer, and therefore the taxpayer does not collect the sales tax until the customer pays the invoice. The taxpayer contends the audit shows total amounts billed and not collected. Taxpayer provided computer printed invoices for 2004 through June of 2005. The invoices according to the taxpayer have been "printed as they have been issued." Taxpayer was careful to note that the Department should only "assess tax in the correct period when the moneys are collected."

A careful review of taxpayer's records reveals that none of the computer generated invoices contain sales tax. Also the computer generated invoices appear at times to be numbered out of sequence when compared with the date they were issued. Taxpayer has not accounted for, nor established the reason, for the missing computer generated invoices.

IC 6-2.5-2-1 states, "(a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana. (b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state."

The taxpayer's records show that they are not using a true cash basis. If they were, then over time the amount of sales tax collected and remitted would reconcile. In this case, this does not happen.

The taxpayer stated that some of their sales were to exempt entities. In the transactions that were not allowed in the audit, the taxpayer failed to provide any exemption certificates for the transactions that were made. The taxpayer provided an exemption certificated dated four months after the audit was completed. The Indiana General Sales Tax Exemption Certificate did not indicate why the transaction was exempt from taxation.

FINDING

The taxpayer's protest is denied.

II. Tax Administration- Ten Percent Negligence Penalty

DISCUSSION

The taxpayer protests the imposition of the ten percent 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 department has the authority to waive the negligence penalty pursuant to the provisions of 45 IAC 15-11-2(c) as follows:

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 this case, the taxpayer has not submitted substantial documentation to indicate that its failure to collect and remit Indiana sales tax was due to reasonable cause.

FINDING

The taxpayer's protest of the penalty is denied.

DEPARTMENT OF STATE REVENUE

0420050414.LOF

LETTER OF FINDINGS NUMBER: 05-0414
Sales and Use Tax
For the Periods Ending12/31/01, 11/30/02, and 12/31/02

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- Imposition

Authority: IC 6-8.1-5-1(b), IC 6-2.5-2-1

The taxpayer protests the imposition of sales tax.

II. Tax Administration- Ten Percent Negligence Penalty

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

The taxpayer protests the imposition of the ten percent negligence penalty.

STATEMENT OF FACTS

The taxpayer became a corporation in 2003 and was formerly a sole proprietorship for 2001 and 2002. The taxpayer's sales are primarily marketing signs for realty agents, apartment complexes, contractors, property managers, and retail establishments. At issue are the signs, banners, monuments, etc. that are custom made for each customer. The Department conducted an audit covering the periods ending December 31, 2001, November 30, 2002, and December 31, 2002. The audit brought the taxpayer up to date for the reporting of sales tax. Incomplete records were provided at the time of the audit so the audit was completed based upon the best information available. After an audit, the Indiana Department of Revenue, hereinafter referred to as the "department," assessed additional sales tax, interest, and penalty. The taxpayer protested the assessment. At the taxpayer's request, this Letter of Findings is based upon the documentation contained in the file and additional documentation supplied prior to hearing.

I. Sales and Use Tax-Imposition

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

Indiana imposes a sales tax on retail sales of tangible personal property in Indiana. The sellers of the property are required to collect the sales tax from the purchasers and remit that tax to the state unless the sale qualifies for a statutory exemption. IC 6-2.5-2-1.

The taxpayer states that the Department used invoices mailed in each period rather than the actual invoices that customers paid. The taxpayer's representative argues that the taxpayer is a cash basis taxpayer, and therefore the taxpayer does not collect the sales tax until the customer pays the invoice. The taxpayer contends the audit shows total amounts billed and not collected. Taxpayer provided computer printed invoices for 2004 through June of 2005. The invoices according to the taxpayer have been "printed as they have been issued." Taxpayer was careful to note that the Department should only "assess tax in the correct period when the moneys are collected."

A careful review of taxpayer's records reveals that none of the computer generated invoices contain sales tax. Also the computer generated invoices appear at times to be numbered out of sequence when compared with the date they were issued. Taxpayer has not accounted for, nor established the reason, for the missing computer generated invoices.

IC 6-2.5-2-1 states, "(a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana. (b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state."

The taxpayer's records show that they are not using a true cash basis. If they were, then over time the amount of sales tax collected and remitted would reconcile. In this case, this does not happen.

The taxpayer stated that some of their sales were to exempt entities. In the transactions that were not allowed in the audit, the taxpayer failed to provide any exemption certificates for the transactions that were made. The taxpayer provided an exemption certificated dated four months after the audit was completed. The Indiana General Sales Tax Exemption Certificate did not indicate why the transaction was exempt from taxation.

FINDING

The taxpayer's protest is denied.

II. Tax Administration- Ten Percent Negligence Penalty

DISCUSSION

The taxpayer protests the imposition of the ten percent 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 department has the authority to waive the negligence penalty pursuant to the provisions of 45 IAC 15-11-2(c) as follows:
>
> 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 this case, the taxpayer has not submitted substantial documentation to indicate that its failure to collect and remit Indiana sales tax was due to reasonable cause.

FINDING

The taxpayer's protest of the penalty is denied.

DEPARTMENT OF STATE REVENUE

0420050416.LOF

LETTER OF FINDINGS NUMBER: 05-0416
Sales and Use Tax
For the Period 12/31/03

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- Imposition

Authority: IC 6-8.1-5-1(b), IC 6-2.5-2-1

The taxpayer protests the imposition of sales tax.

II. Tax Administration- Ten Percent Negligence Penalty

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

The taxpayer protests the imposition of the ten percent negligence penalty.

STATEMENT OF FACTS

The taxpayer became a corporation in 2003 and was formerly a sole proprietorship for 2001 and 2002. The taxpayer's sales are primarily marketing signs for realty agents, apartment complexes, contractors, property managers, and retail establishments. At

issue are the signs, banners, monuments, etc. that are custom made for each customer. The Department conducted an audit covering the period ending December 31, 2003. The audit brought the taxpayer up to date for the reporting of sales tax. Incomplete records were provided at the time of the audit so the audit was completed based upon the best information available. After an audit, the Indiana Department of Revenue, hereinafter referred to as the "department," assessed additional sales tax, interest, and penalty. The taxpayer protested the assessment. At the taxpayer's request, this Letter of Findings is based upon the documentation contained in the file and additional documentation supplied prior to hearing.

I. Sales and Use Tax-Imposition

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

Indiana imposes a sales tax on retail sales of tangible personal property in Indiana. The sellers of the property are required to collect the sales tax from the purchasers and remit that tax to the state unless the sale qualifies for a statutory exemption. IC 6-2.5-2-1.

The taxpayer states that the Department used invoices mailed in each period rather than the actual invoices that customers paid. The taxpayer's representative argues that the taxpayer is a cash basis taxpayer, and therefore the taxpayer does not collect the sales tax until the customer pays the invoice. The taxpayer contends the audit shows total amounts billed and not collected. Taxpayer provided computer printed invoices for 2004 through June of 2005. The invoices according to the taxpayer have been "printed as they have been issued." Taxpayer was careful to note that the Department should only "assess tax in the correct period when the moneys are collected."

A careful review of taxpayer's records reveals that none of the computer generated invoices contain sales tax. Also the computer generated invoices appear at times to be numbered out of sequence when compared with the date they were issued. Taxpayer has not accounted for, nor established the reason for the missing computer generated invoices.

IC 6-2.5-2-1 states, "(a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana. (b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state."

The taxpayer's records show that they are not using a true cash basis. If it were, then over time the amount of sales tax collected and remitted would reconcile. In this case, this does not happen.

The taxpayer stated that some of their sales were to exempt entities. In the transactions that were not allowed in the audit, the taxpayer failed to provide any exemption certificates for the transactions that were made. The taxpayer provided an exemption certificated dated four months after the audit was completed. The Indiana General Sales Tax Exemption Certificate did not indicate why the transaction was exempt from taxation.

FINDING

The taxpayer's protest is denied.

II. Tax Administration- Ten Percent Negligence Penalty

DISCUSSION

The taxpayer protests the imposition of the ten percent 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 department has the authority to waive the negligence penalty pursuant to the provisions of 45 IAC 15-11-2(c) as follows:
>
> 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 this case, the taxpayer has not submitted substantial documentation to indicate that its failure to collect and remit Indiana sales tax was due to reasonable cause.

FINDING

The taxpayer's protest of the penalty is denied.

DEPARTMENT OF STATE REVENUE

0420050452.LOF

LETTER OF FINDINGS NUMBER: 05-0452
Sales and Withholding Tax
Responsible Officer
For the Tax Period 1990-1993

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 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); IC § 6-8.1-5-4; 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.

II. Tax Administration- Ten Percent Negligence Penalty

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2(b); 45 IAC 5-11-2(c).

The taxpayer protests the imposition of the ten percent negligence penalty.

STATEMENT OF FACTS

The taxpayer was the secretary/treasurer of a corporation that sold and serviced computers. The corporation did not remit sales taxes and withholding taxes to the state during the tax period 1990-1993. The Indiana Department of Revenue (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 tax assessment. A hearing was held and this Letter of Findings results.

I. Sales Tax and Withholding Tax-Responsible Officer Liability

DISCUSSION

Notices of proposed assessments are prima facie evidence that the department's claim for unpaid taxes is valid**.** IC § 6-8.1-5-1(b). The taxpayer has the burden of proving that the department incorrectly imposed the assessment. Id. Taxpayers are required to keep adequate books and records so that the department can determine the proper tax owed to the state. IC § 6-8.1-5-4.

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 under authority of 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 sales and withholding taxes are paid has the statutory duty to remit those trust taxes to the state. The taxpayer submitted substantial documentation indicating that during most of the tax period he was primarily involved in selling and servicing computers rather than handling the financial affairs of the corporation. During this period, the submitted documentation indicated that the business manager and president managed the daily financial affairs of the corporation and determined which creditors would be paid. The taxpayer was, however, the secretary/treasurer. Whether or not he availed himself of the opportunity to assert such authority, the taxpayer had the authority to be involved in the financial dealings of the corporation and determine which creditors would be paid. After the death of the president, the taxpayer became more involved in the daily finances of the corporation. At that time, he could have seen that the tax arrearage was satisfied. The taxpayer, business manager, and president were jointly and severally liable for the remittance of the sales and withholding trust taxes to the state.

Alternatively, the taxpayer argued that the corporate tax liability was calculated incorrectly resulting in an artificially high assessment. There were not adequate records for the department to determine the actual corporate tax liability at the time of the investigation. Therefore, the department estimated the corporate sales and withholding tax liability. The taxpayer provided substantial documentation indicating that the department's calculation was flawed. The taxpayer sustained his burden of proving that the assessed corporate sales and withholding tax liability for 1990-1993 was too high.

FINDING

The taxpayer's protest is denied as to his responsibility to remit corporate trust taxes to the state. The taxpayer's protest as to

the method of calculating the amount of tax due is sustained. The audit division is requested to review the proposed alternative calculation and make whatever adjustment it deems warranted.

II. Tax Administration- Ten Per Cent Negligence Penalty

DISCUSSION

The taxpayer protested the imposition of the ten percent 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 standard for waiving the negligence penalty is given at 45 IAC 15-11-2(c) as follows:

> 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.

The taxpayer affirmatively established that its failure to pay the proper amount of sales and use tax was due to reasonable cause rather than negligence in this particular situation.

FINDING

The taxpayer's protest to the imposition of penalty is sustained.

DEPARTMENT OF STATE REVENUE

04-20050496.LOF

LETTER OF FINDINGS NUMBER: 05-0496
USE TAX
FOR TAX YEAR 2004

NOTICE: IC 4-22-7-7 requires the publication of this document 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. Use Tax: Exemption

Authority: IC 6-8.1-5-1(b); IC 6-2.5-3-2; IC 6-2.5-3-4(a)(2); IC 6-2.5-5-8(b); IC 6-2.5-4-10(a); Indiana Dept. of Revenue v. Interstate Warehousing, 783 N.E.2d 248 (Ind. 2003); Tri-States Double Cola Bottling Co. v. Indiana Dep't of State Revenue, 706 N.E.2d 282 (Ind. Tax Ct. 1999).

Taxpayer protests disallowance of use tax exemption.

STATEMENT OF FACTS

Taxpayer, a non-resident corporation, purchased an aircraft for $2,248,000. On June 24, 2004, taxpayer moved the aircraft to an Indiana hanger. The Indiana Department of Revenue ("Department") notified the taxpayer the Department's records indicated the taxpayer did not properly register the aircraft with the State. Taxpayer submitted an application for the aircraft registration and claimed an exemption for renting and leasing. The Department denied the exemption claim and issued a notice of proposed assessment for consumer use tax. Taxpayer submitted a protest challenging the assessment. The Department held a hearing and now presents this Letter of Findings, with additional facts to follow.

I. Use Tax: Exemption

DISCUSSION

The taxpayer explains it consists of two shareholders. One shareholder is the owner of a property company and the other shareholder is the owner of a holding company. Both companies needed an aircraft to utilize in connection with their businesses. Specifically, both companies needed the aircraft to visit properties located in multiple states. However, neither company needed an aircraft on a full-time basis. Instead, each needed the use of the aircraft for particular trips at various times. Therefore, the two owners formed the entity referred to as "taxpayer" and entered into lease agreements where the property company would operate the aircraft out of Indiana and the holding company would operate the aircraft out of Illinois. The taxpayer concedes its delay in arranging for the aircraft registration, merchant certificate, and collection of taxes. However, the taxpayer maintains at all times it engaged in the business of leasing an aircraft.

Nevertheless, the Department's aircraft compliance division assessed use tax on the grounds the taxpayer failed to remit either sales tax on the subject aircraft since the date of purchase. The aircraft compliance division contends that in order to claim an exemption from sales and use tax, the taxpayer must predominantly engage in the business of renting and leasing the aircraft and file a "Form ST 103" that lists all use of the aircraft in the State of Indiana.

A presumption exists that all tax assessments are accurate. IC 6-8.1-5-1(b). IC 6-2.5-3-2 provides:

(a) An excise tax, know as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

(b) The use tax is also imposed on the storage, use, or consumption of a vehicle, an aircraft, or a watercraft, if the vehicle, aircraft, or watercraft:

(1) is acquired in a transaction that is an isolated or occasional sale; and

(2) is required to be titled, licensed, or registered by this state for use in Indiana.

IC 6-2.5-3-4(a)(2) allows for a use tax exemption if:

[T]he property is acquired in a transaction that is wholly or partially exempt from state gross retail under any part of IC 6-2.5-5, except IC 6-2.5-5-24(b), and the property is being used, stored, or consumed for the purpose for which it was exempted.

The burden of establishing entitlement to an exemption lies on the taxpayer claiming the exemption. Indiana Dept. of Revenue v. Interstate Warehousing, 783 N.E.2d 248, 250 (Ind. 2003). The Department will strictly construe the exemption statutes against the taxpayer claiming the exemption. Id.

The taxpayer argues it is exempt from use tax under IC 6-2.5-5-8(b). IC 6-2.5-5-8(b) provides:

Transactions involving tangible personal property…are exempt from the state gross retail tax if the person acquiring the property acquires it for resale, rental, or leasing in the ordinary course of his business without changing the form of the property.

To support its IC 6-2.5-5-8(b) claim, the taxpayer supplied the Department with: copies of two lease agreements; an Indiana permit to collect and remit out-of-state use tax; a certificate of authority; an 1120S tax return form; a North Carolina Department of Revenue notice of adjustment for sales and use; flight logs; and an insurance policy.

However, to engage in the business of renting and leasing tangible personal property, Indiana requires a taxpayer be a retail merchant. IC 6-2.5-4-10(a). According to Tri-States Double Cola Bottling Co. v. Indiana Dep't of State Revenue, 706 N.E.2d 282, 285 (Ind. Tax Ct. 1999),

With respect to leases of tangible personal property, section 6-2.5-5-8 and subsection 6-2.5-4-10(a) work together. Subsection 6-2.5-4-10(a) imposes a tax on the leasing of tangible personal property. Section 6-2.5-5-8 exempts, inter alia, tangible personal property acquired for the purpose of leasing that property to others. This means that either… [Taxpayers'] purchase of… [Tangible personal property] is taxable or each transaction between … [taxpayer] and the… [Parties to the lease agreements] is taxable. They cannot both be subject to taxation nor can they both escape taxation because taxation of one depends on the lack of taxation of the other.

Using this analysis, to claim an exemption from use tax under IC 6-2.5-5-8(b), the taxpayer must show more than their intent to lease tangible personal property. The taxpayer must show that it actually did lease the tangible personal property. Particularly, the taxpayer must show that it taxed each lease transaction and remitted those amounts to the state.

The taxpayer has provided the Department with no invoices showing it billed for the aircraft usage, added sales tax to those amounts, nor any cancelled checks showing payments made by the parties for the usage. Taxpayer's federal tax return indicate the taxpayer made $117,023 of gross sales in 2004, yet again the Departments records do not indicate the taxpayer's remittance of any sales tax to the State for the amount. The taxpayer did not begin remitting sales tax to the state for usage of its aircraft until after the Department issued the proposed assessment. Even more so, the taxpayer has provided the Department with no documentation showing where it paid sales tax on the aircraft purchase price. It appears on its face the taxpayer wants to escape taxation on both the aircraft purchase and the lease payments, which clearly runs contrary to the intent of the statutes. Therefore, because the taxpayer has not shown that the taxpayer taxed the lease transactions, the Department's aircraft compliance division was correct to deny the taxpayer's exemption claim.

FINDING

For the reasons stated above, the Department denies the taxpayer's protest.

DEPARTMENT OF STATE REVENUE

04-20050498.LOF

LETTER OF FINDINGS NUMBER: 05-0498
USE TAX
FOR TAX YEAR 2004

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. Use Tax: Exemption

Authority: IC 6-8.1-5-1(b); IC 6-2.5-3-2; IC 6-2.5-3-4(a)(2); IC 6-2.5-5-8(b); IC 6-2.5-1-21(a); IC 6-2.5-5-27; 45 IAC 2.2-3-4; Indiana Dept. of Revenue v. Interstate Warehousing, 783 N.E.2d 248 (Ind. 2003).

Taxpayer protests disallowance of a use tax exemption.

II. Tax Administration – Penalty

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

Taxpayer protests the imposition of the negligence penalty.

STATEMENT OF FACTS

The Indiana Department of Revenue ("Department") notified the taxpayer that the Department's records indicated the taxpayer did not properly register its aircraft with the State. Taxpayer submitted an application for aircraft registration and claimed an exemption from sales and uses tax. The Department denied the exemption claim and issued a notice of proposed assessment for use tax. Taxpayer submitted a protest challenging the assessment. The Department held a hearing and now presents this Letter of Findings, with additional facts to follow.

I. Sales and Use Tax: Aircraft Exemption

DISCUSSION

Taxpayer purchased an aircraft on June 30, 2004, for $247,500. From June of 2004 to September of 2004, the taxpayer's owner used the aircraft for twenty-five flight hours. On October 29, 2004, taxpayer registered the aircraft with the State. On taxpayer's application for registration, the taxpayer claimed an exemption from sales and use tax based on engaging in the business of renting and leasing to others. The Department's aircraft compliance division denied the exemption claim. The aircraft compliance division determined that since the taxpayer did not use the aircraft in an exempt manner after purchasing the aircraft, the taxpayer was not entitled to an exemption from sales and use tax.

A presumption exists that all tax assessments are accurate. IC 6-8.1-5-1(b). IC 6-2.5-3-2 provides:

(a) An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

(b) The use tax is also imposed on the storage, use, or consumption of a vehicle, an aircraft, or a watercraft, if the vehicle, aircraft, or watercraft:

(1) is acquired in a transaction that is an isolated or occasional sale; and

(2) is required to be titled, licensed, or registered by this state for use in Indiana.

45 IAC 2.2-3-4 further clarifies IC 6-2.5-3-2 and states:

Tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used or otherwise consumed in Indiana is subject to Indiana use tax for such property, unless the Indiana state gross retail tax has been collected at the point of purchase.

IC 6-2.5-3-4(a)(2) allows for a use tax exemption if:

[T]he property is acquired in a transaction that is wholly or partially exempt from state gross retail under any part of IC 6-2.5-5, except IC 6-2.5-5-24(b), and the property is being used, stored, or consumed for the purpose for which it was exempted.

The burden of establishing entitlement to an exemption lies on the taxpayer claiming the exemption. Indiana Dept. of Revenue v. Interstate Warehousing, 783 N.E.2d 248, 250 (Ind. 2003). The Department will strictly construe the exemption statutes against the taxpayer claiming the exemption. Id.

Taxpayer offers several arguments to establish its entitlement to a use tax exemption. First, the taxpayer argues the aircraft was exempt from use tax pursuant to IC 6-2.5-5-8(b). IC 6-2.5-5-8(b) provides:

Transactions involving tangible personal property… are exempt from the state gross retail tax if the person acquiring the

property acquires it for resale, rental, or leasing in the ordinary course of his business without changing the form of the property.

The taxpayer insists its sole purpose for acquiring the aircraft was to expand its aircraft leasing operations. However, the sole lease agreement the taxpayer provided to substantiate its IC 6-2.5-5-8(b) exemption claim lacked consideration. To have a valid lease agreement, IC 6-2.5-1-21(a) requires that the lease have a "transfer of possession or control of tangible personal property for a fixed or indeterminate term for consideration…." Thus, since the only lease agreement entered into by the taxpayer was not valid, the Department was correct to deny the taxpayer's exemption claim for renting and leasing to others.

The taxpayer further argues the aircraft was exempt from use tax under IC 6-2.5-5-27. IC 6-2.5-5-27 provides:

Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property.

To satisfy the provisions of IC 6-2.5-5-27, the taxpayer must provide evidence that the taxpayer had the authority to transport individuals or property. A taxpayer can prove its authority to render those types of services by obtaining a FAR Part 121 or a FAR Part 135 certificate. The FAA only allows an aircraft operator with a FAR Part 121 or FAR Part 135 certificate to operate an aircraft for compensation or hire in carrying people or property. The taxpayer provided the Department with no evidence to support whether it could operate the aircraft in question under either a Part 121 or a Part 135 certificate. Moreover, during the hearing, the taxpayer explained it leased the aircraft to another business, which in turn used the aircraft for commercial operations. Thus, if IC 6-2.5-5-27 is applicable at all, the statute would apply to the party that directly engaged in the business of using the aircraft for public transportation. Therefore, the exemption found in IC 6-2.5-5-27 is not applicable to the taxpayer.

As a final point, the taxpayer argues that in denying its exemption claim the Department's determination is contrary to the provisions and requirements of the United States Constitution, the Commerce Clause, the Due Process Clause, and the Indiana Constitution. But, the taxpayer fails to address or analyze exactly how the determination runs contrary to those provisions. Thus, the taxpayer's constitutional challenge does not provide a foundation for the Department to address the issue.

In summation, the aircraft compliance division was correct to deny the taxpayer's use tax exemption. The taxpayer failed to sufficiently establish its entitlement to a use tax exemption under the provisions of IC 6-2.5-3-4(a)(2).

FINDING

For the reasons stated above, the Department denies the taxpayer's protest.

II. Tax Administration – Penalty

DISCUSSION

Taxpayer argues the Department should not impose a negligence penalty on the proposed tax deficiency. The taxpayer asserts that any such deficiency the Department identified was not due to "carelessness, thoughtlessness, disregard or inattention to duties" on the part of the taxpayer.

IC 6-8.1-10-2.1(a)(3) provides in part that "if a person… incurs, upon examination by the department, a deficiency that is due to negligence…, the person is subject to a penalty." Negligence is defined "as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer…." 45 IAC 15-11-2(b). Negligence is "determined on a case-by-case basis according to the facts and circumstances of each taxpayer." Id.

The Department may waive the penalty upon a showing that the failure to pay the deficiency was due to reasonable cause and not due to willful neglect. IC 6-8.1-10-2.1(d). However, in order to establish reasonable cause, the taxpayer must demonstrate that the taxpayer "exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed…." 45 IAC 15-11-2(c).

The taxpayer stated it engaged in the business of renting and leasing aircraft to the general public for the last seven years. The taxpayer conceded that it knew it needed to register the aircraft with the State within thirty-one days of purchasing the aircraft. However, the taxpayer did not register the aircraft with the state until after the Department's aircraft compliance division notified the taxpayer. The Department can properly impose the negligence penalty when the taxpayer is inattentive to its duties. 45 IAC 15-11-2(b). The taxpayer provided the Department with no evidence to establish that the taxpayer's inattention was due to reasonable cause. Thus, the Department was correct in imposing a negligence penalty given that the taxpayer's inattention to its duties constituted negligence.

FINDING

The Department denies the taxpayer's protest.

DEPARTMENT OF STATE REVENUE

0320060012P.LOF

LETTER OF FINDINGS NUMBER: 06-0012P
Withholding Tax
For the Calendar Year 2004

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 filing of W2s for the calendar year 2004. The W2s were received by the Department fifteen days late. The taxpayer is an Indiana company.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty be abated as the W2s were mailed timely.

The Department did not receive the W2s until March 15, 2005, fifteen days late. State tax regulations state the burden of proof is on the taxpayer as to why the W2s were received late by the Department. As the taxpayer has given no explanation, the taxpayer is deemed to be inattentive in the mailing of the W2s.

The regulation which controls the application of penalty is 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 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

0220060066P.LOF

LETTER OF FINDINGS NUMBER: 06-0066P
Income Tax
For the Short Period ended December 31, 2004

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 and filing of the corporate income tax return for the short period ending December 31, 2004.

The taxpayer needed a valuation study completed on the "spin-off" transaction between the taxpayer and the taxpayer's former corporate parent. This valuation study was needed to complete the corporate income tax return. This valuation study was not completed until May 2005, six weeks after the due date of the corporate income tax return. Because of this, the taxpayer was not able to accurately calculate the extension payment, and therefore, the taxpayer erroneously underpaid the extension payment.

The taxpayer is an Indiana company.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests abatement of the penalty as the information necessary to file the corporate income tax return was not available until after the due date.

The Department points out that the error is the result of a planned income transaction, and therefore, is a case of inattention. The regulation which controls the application of penalty is 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 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

0420060078.LOF

LETTER OF FINDINGS NUMBER 06-0078
RESPONSIBLE OFFICER
SALES TAX
For Tax Period July 2004-March 2005

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.

ISSUE

I. Sales Tax -Responsible Officer Liability

Authority: IC § 6-2.5-9-3; IC § 6-8.1-5-1(b).

The taxpayer protests the assessment of corporate sales taxes against him as a responsible officer.

STATEMENT OF FACTS

The taxpayer was an officer of a corporation that sold recreational vehicles. The corporation did not remit sales taxes to Indiana for the tax period July 2004 through March 2005. The Indiana Department of Revenue assessed the outstanding corporate sales taxes, interest, and penalty against the taxpayer personally. The taxpayer protested the assessment and a hearing was held. This Letter of Findings results.

I. Sales Tax -Responsible Officer Liability

DISCUSSION

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.

Indiana Department of Revenue assessments are prima facie evidence that the tax assessment is correct. The taxpayer bears the burden of proving that the assessment is incorrect. IC § 6-8.1-5-1(b).

The taxpayer did not dispute that he was a party responsible for remittance of corporate sales taxes to the state for the period November 2000 – September 1, 2003. The taxpayer argued that he sold his interest in the corporation on September 1, 2003, and was not responsible for the remittance of sales taxes to Indiana after that date. The taxpayer presented substantial documentation indicating that he sold his interest in the corporation on September 1, 2003. The taxpayer sustained his burden of proving that he was not personally responsible for the corporate sales taxes after September 1, 2003.

FINDING

The taxpayer's protest is sustained as to all tax periods after September 1, 2003.

DEPARTMENT OF STATE REVENUE

0120060085.LOF

LETTER OF FINDINGS: 06-0085
INDIANA INCOME TAX
For 2002, 2003, and 2004

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. Proposed Assessments – Indiana Adjusted Gross Income Tax.

Authority: IC 6-8.1-5-1(a); IC 6-8.1-5-1(b)

Taxpayer challenges proposed income tax assessments for 2002, 2003, and 2004 on the ground that taxpayer "was not employed and therefore had no income" during those three years.

STATEMENT OF FACTS

Taxpayer failed to report and pay state adjusted gross income tax for 2002, 2003, and 2004. The Department of Revenue (Department) conducted an investigation to determine if taxpayer owed state income tax for those years.

The examiner sent taxpayer a certified letter and a follow-up letter advising taxpayer of the investigation. However, taxpayer failed to submit the missing tax returns or make available the relevant information.

Faced with the lack of more current information, the examiner reviewed the tax returns taxpayer submitted for 1999 through 2001. Based upon the information contained in those earlier returns, the examiner prepared estimated 2002 through 2004 returns. The examiner concluded that the amounts of income listed on these returns were based upon the "best information available." Thereafter, the Department forwarded taxpayer notices of "Proposed Assessment." Taxpayer disagreed on the ground that he had not received income during 2002, 2003, and 2004 and submitted a protest to that effect.

The protest was assigned to a hearing officer, an administrative hearing was scheduled during which taxpayer would have been provided an opportunity to further explain the basis for his protest. Taxpayer chose not to take part in the hearing. This Letter of Findings was prepared based upon the information contained within taxpayer's file.

DISCUSSION

I. Proposed Assessments – Indiana Adjusted Gross Income Tax.

Taxpayer disagrees with the Department's notices of proposed assessment on the ground that he did not receive taxable income during 2002, 2003, and 2004. In support of that contention, taxpayer has offered three notarized affidavits each of which contains the statement that he "was not employed and therefore had no income for [2002, 2003, and 2004]."

IC 6-8.1-5-1(a) states in part that "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." The statute *requires* the Department to issue proposed assessments when the Department believes that the taxpayer has underpaid his or her state income tax.

Once the notices of proposed assessments are issued, it is up to the taxpayer to provide information demonstrating that the assessments are incorrect. "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." IC 6-8.1-5-1(b).

Based upon the information contained within taxpayer's earlier returns, the Department reasonably believed that taxpayer had underreported his 2002, 2003, and 2004 income because the earlier returns reported yearly adjusted gross income totaling approximately $834,000. IC 6-8.1-5-1(a). Based upon the information contained within those earlier returns the Department was not only correct but was required to issue the notices based upon the best information available to it at the time the investigation report was prepared.

In rebuttal, taxpayer has submitted affidavits which – in effect – declare that taxpayer's 2002, 2003, and 2004 adjusted gross income fell to $0. The Department is unable to conclude that, pursuant to, IC 6-8.1-5-1(b), taxpayer has met his burden of demonstrating that the proposed assessments are wrong. Stripped of the legalese, the affidavits are simply taxpayer's unsupported declarations that taxpayer became unemployed and received no income during 2002, 2003, and 2004. Taxpayer declined the opportunity to provide additional information and chose instead to believe that the affidavits were sufficient to rebut the proposed assessments. Taxpayer erred.

The Department's proposed assessments were based upon the best information available, taxpayer chose to rely solely upon three self-serving affidavits to rebut the assessments, taxpayer failed to meet his burden of demonstrating that the proposed assessments were wrong, and taxpayer's protest must be rejected.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

02-20060099P.LOF

LETTER OF FINDINGS NUMBER: 06-0099P
Gross Income Tax-Penalty
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. 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 negligence penalty.

STATEMENT OF FACTS

Taxpayer is a corporation engaged in the securities brokerage business. During the years in question, Taxpayer had commissions, principal transactions, and margin interest income. The Department and Taxpayer had concluded several years earlier that 60 percent of the amounts attributable to Indiana customers from these sources was subject to Indiana gross income tax. For the years in question, Taxpayer made a computational error that resulted in 60 percent of the 60 percent (i.e., 36 percent) of the amounts being subject to gross income tax.

Before November 15, 2005, during Indiana Tax Amnesty, Taxpayer recomputed its gross income tax liability for the periods at issue. Taxpayer properly included 60 percent of its commissions as being subject to gross income tax; however, Taxpayer only reported 50 percent of its income from principal transactions and margin interest as subject to gross income tax. On December 8, 2005, the Department completed an audit including 60 percent of its income from principal transactions and margin interest as subject to gross income tax. Taxpayer was assessed additional tax, along with interest and penalties on the additional amount of the assessment. Taxpayer only protests the imposition of penalties. Additional facts will be supplied as necessary.

I. Tax Administration—Penalty

DISCUSSION

Taxpayer protests the imposition of the ten percent negligence penalty for the taxes that the Department has imposed.

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.

Taxpayer argues that, had it known about the issues at hand prior to November 15, it would have paid the full amount of the

liability, and would not have been subject to penalty. In review, Taxpayer's return for the years at issue included the incorrect amount of income based on a computational error. Then, Taxpayer sought to correct the error just prior to end of Indiana Tax Amnesty, and made yet another error. By virtue of its initial computational error, Taxpayer was negligent within the meaning of the statute and regulations concerning penalties, notwithstanding Taxpayer's effort to correct this problem prior to November 15, 2005.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0120060105.LOF

LETTER OF FINDINGS NUMBER: 06-0105
Adjusted Gross Income Tax
Tax Period 2002-2003

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 Tax-Imposition

Authority: 26 U.S.C.A. § 62; IC § 6-3-2-1(a); IC § 6-3-1-3.5(a); IC § 6-8.1-5-1(b); IC § 6-8.1-5-4.

The taxpayer protested the imposition of Indiana adjusted gross income tax.

II. Tax Administration- Ten Percent Negligence Penalty

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

The taxpayer protested the imposition of the ten percent negligence penalty.

STATEMENT OF FACTS

The taxpayers are vendors of food and drinks at an annual festival. In a sales tax audit, the Indiana Department of Revenue (department) estimated the total sales of food and drinks at the festival for the years 2002-2004. The department also applied the estimated total sales figures to the taxpayer's 2002-2003 individual income taxes. This resulted in an assessment of additional adjusted gross income tax, interest, and penalty for the 2002-2004 tax period.

The taxpayer protested this assessment. A hearing was held and this Letter of Findings results.

I. Adjusted Gross Income Tax-Imposition

DISCUSSION

Indiana imposes an adjusted gross income tax on the adjusted gross income of Indiana residents. IC § 6-3-2-1(a). Indiana adjusted gross income is calculated by starting with the federal adjusted gross income and making certain modifications. IC § 6-3-1-3.5(a). The federal adjusted gross income calculation begins with the inclusion of all of the taxpayers' income. 26 U.S.C.A. § 62.

Notices of proposed assessments are prima facie evidence that the department's claim for unpaid taxes is valid**.** The taxpayer has the burden of proving that the department incorrectly imposed the assessment. IC § 6-8.1-5-1(b). Taxpayers are required to keep adequate books and records so that the department can determine the proper tax owed to the state. IC § 6-8.1-5-4.

The taxpayers did not have adequate records to support the calculation of their federal gross and adjusted gross income. Since the Indiana calculation flows from the federal calculation, they did not have adequate records to support the calculation of their Indiana adjusted gross income and resulting tax. Therefore, the department's investigation added the sales tax audit's estimated total sales to the taxpayers' Indiana adjusted gross income. This resulted in the assessment of additional Indiana adjusted gross income tax. The taxpayer protested this additional tax.

Concerning the sales and use tax audit, the department notes that, aside from poor record keeping, the audit found evidence of unreported sales and transactions. The taxpayer now argues that the amount originally assessed was too great. The taxpayer suggested that the department could make a better estimate by applying the 2005 total sales amounts to the three years covered by the audit. The taxpayer did maintain 2005 records; the amount of 2005 sales is approximately 40 percent lower than the estimated sales for the tax period. While the Department agrees that the 2005 records *could* provide a reasonable basis for projecting the estimated periods, the department declines to make such a factual determination. The administrative review process is not the forum for making such a numerical determination based solely on taxpayer's unexamined, unchallenged assertion. However, the taxpayer has met its burden of demonstrating that the estimated sales amounts should be reconsidered.

The adjusted gross income tax additional liabilities were based on the sales and use tax audit's proposed assessments. Therefore, the reevaluation of these estimates of total sales during the sales and use tax audit period will impact the taxpayers' adjusted gross income tax liability

FINDING

The taxpayers' protest to the adjusted gross income tax assessment is sustained to the extent that the supplementary audit review adjusts the taxpayers' sales tax assessment.

II. Tax Administration- Ten Percent Negligence Penalty

DISCUSSION

The taxpayer protested the imposition of the ten percent (10[percent]) 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.

During the period of the audit, the taxpayer ignored the law and the department's` instructions for the payment of adjusted gross income tax and maintenance of adequate records. The taxpayer's inattention to these duties resulted in the tax assessment. These breaches of the taxpayer's duty constituted negligence.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0220060111P.LOF

LETTER OF FINDINGS NUMBER: 06-0111P
Income Tax
For the Fiscal Year ended March 31, 2005

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 underpayment penalty was assessed for the filing of the corporate income tax return for the fiscal year ended March 31, 2005

The taxpayer incurred a significant gain from a real estate sale for the fourth quarter. The taxpayer had a significant loss from operations for the fiscal tax year. The resultant tax for the fiscal period was $105,000. The only estimated tax payment was $9,000 for the fourth quarter.

The taxpayer is an Indiana company.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty be abated as the State of Indiana does not have an annualized income tax statute. The taxpayer says that if Indiana did have an annualized income tax statute, there would not have been a penalty.

True, Indiana does not have an annualized income tax statute. However, Indiana does embrace substance over form in tax compliance. The taxpayer had $105,000 in reportable income for the fiscal tax year. This income resulted from the real estate gain in the fourth quarter. The taxpayer would have met its tax compliance duties if (1) the taxpayer paid an estimate equal to 100% of the prior year tax, which in this case was $35,105, or (2) the taxpayer paid 80% of the current year tax, which in this case would be $84,000. The taxpayer paid an estimated tax of $9,000 which is well short of either threshold for abating the penalty.

The regulation which controls the application of penalty is 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 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

0620060113P.LOF

LETTER OF FINDINGS NUMBER: 06-0113P
Motor Fuel Tax
For the Period of November 2005

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on the 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. Gasoline Tax – Disallowance of Gasoline Distributor Deduction

Authority: IC 6-6-1.1-705

The taxpayer protests the disallowance of the gasoline distributor deduction on its consolidated gasoline monthly tax return for November 2005

II. Tax Administration – Penalty

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

The taxpayer protests the penalty assessed for failure to remit its tax due for the month of November 2005 by the due date.

STATEMENT OF FACTS

The taxpayer filed its consolidated gasoline tax return for the month of November 2005 in a timely manner. However, the tax due as determined by the return was remitted after the due date. Accordingly, the department disallowed the gasoline distributor deduction and assessed a penalty for the taxpayer's failure to timely remit its tax. In the letter of protest, the taxpayer requested that the gasoline distributor deduction be restored and the penalty be abated due to reasonable cause.

I. Gasoline Tax – Disallowance of Gasoline Distributor Deduction

Indiana Code 6-6-1.1-705 states:

(a) If a monthly report is filed and the amount due is remitted at or before the time required by this chapter, a distributor is entitled to a deduction equal to one and six-tenths percent (1.6%) of the remainder of:

(1) the number of invoiced gallons of gasoline he received in Indiana during the preceding calendar month; minus

(2) the deductions claimed by the distributor under sections 701 through 704 of this chapter.

This deduction is a flat allowance to cover evaporation, shrinkage, losses (except losses covered by section 301(5) of this chapter), and the distributor's expenses in collecting and timely remitting the tax imposed by this chapter.

(b) If a monthly report is filed or the amount due is remitted later than the time required under this chapter, the distributor shall pay to the administrator all of the gasoline tax the distributor received from the sale of gasoline covered by the late report, reduced by payments made under IC 6-8.1-8-1.

The taxpayer's gasoline distributor deduction was disallowed because the amount of tax due was remitted after the due date. The statute is clear, and there is no basis for allowing the deduction.

FINDING

The taxpayer's protest is denied.

II. Tax Administration – Penalty

The taxpayer asserts that during November 2005 it moved its checking account from one bank to another. The consolidated gasoline tax return was filed on a timely basis, and the payment of tax was "touch toned" on a timely basis. Unfortunately, the payment was linked to the former bank account in which there were insufficient funds to cover the payment.

The taxpayer points out that the company controller was directed to timely file all appropriate documents in order to avoid such a problem. However, the controller failed to perform his duties as assigned. The taxpayer states that as soon as it became aware of the problem, a bank information change form was transmitted to the department by facsimile. The payment was received by the department on December 28, 2005.

The department considers changing bank accounts to be an activity in the usual course of business. The assertion that the

controller failed to fulfill his responsibilities does not establish reasonable cause. The taxpayer is expected to have controls in place to ensure that remittances to the department are made in a timely manner.

Administrative Rule 45 IAC 15-11-2 (b) states the following:

"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 has not established that its failure to timely remit the tax in question was due to reasonable cause.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20060138P.LOF

LETTER OF FINDINGS NUMBER: 06-0138P
Use Tax-Penalty
For the Years 2002-2003

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

Taxpayer protests the imposition of the ten percent negligence penalty.

STATEMENT OF FACTS

Taxpayer is a corporation engaged in retail clothing sales. Taxpayer operated two stores in Indiana during the periods in question.

Taxpayer was audited for sales and use tax for the periods in question. Taxpayer had no changes with respect to sales tax on its retail sales, use tax on its capital purchases, and use tax on its store expenses. However, Taxpayer did not remit use tax on certain promotional items such as catalogs, postcards, and brochures. Taxpayer was assessed use tax, interest, and penalty on the promotional items. Taxpayer protested only the penalty on the assessment.

Taxpayer's letter of protest indicated that Taxpayer waived its right to hearing. Because of the waiver of Taxpayer's hearing, the letter of findings is based on the information in the file. Additional facts will be supplied as necessary.

I. Tax Administration—Penalty

DISCUSSION

Taxpayer protests the imposition of the ten percent negligence penalty for the taxes that the Department has imposed.

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. Ind. Code § 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.

Taxpayer argues that the total assessment represented only a small percentage of Taxpayer's overall sales and use tax liability for the years in question. While the failure to self-assess use tax on a small percentage of a taxpayer's overall liability is not necessarily determinative on the issue of negligence, Taxpayer's compliance with Indiana tax laws in its operations—its minimal failure to remit use tax was in an area of law subject to some difference in interpretation—established that it acted with ordinary business care with respect to its duties.

FINDING

Taxpayer's protest is sustained.