

## LETTER OF FINDINGS NUMBER: 06-0034

Gross Income Tax  
For Tax Year 2002

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## ISSUE

**I. Gross Income Tax—Amortized Gain**

**Authority:** [IC 6-8.1-5-1](#); [45 IAC 1.1-1-5](#)

Taxpayer protests imposition of gross income tax on the amortized gain from a buyout of RUS debt.

**II. Gross Income Tax—Non-Cash Patronage Revenue**

**Authority:** [45 IAC 1.1-1-5](#)

Taxpayer protests the imposition of gross income tax on non-cash patronage revenue.

**III. Tax Administration—Negligence Penalty and Interest**

**Authority:** [IC 6-8.1-5-2](#); [IC 6-8.1-10-1](#)

Taxpayer protests a ten percent negligence penalty and interest.

## STATEMENT OF FACTS

Taxpayer is a Rural Electric Membership Corporation ("REMC") in Indiana. As the result of an audit, the Indiana Department of Revenue ("Department") issued proposed assessments for Gross Income Tax ("GIT") for the tax year 2002. Taxpayer protests the proposed assessments. Further facts will be supplied as required.

**I. Gross Income Tax—Amortized Gain**

## DISCUSSION

Taxpayer protests the imposition of gross income tax on amounts it included in its amortization schedule resulting from a buyout of Rural Utilities Services (RUS) debt in 1988. Taxpayer states that it paid tax on the gain in 1988.

The Department based its decision on [45 IAC 1.1-1-5](#), which states:

(a) "Constructive receipt" means an item of gross income which is not actually received by a taxpayer but is:

- (1) credited to the taxpayer;
- (2) made available for the taxpayer's withdrawal;
- (3) paid to another for the taxpayer's direct benefit; or
- (4) income to which the taxpayer is entitled.

(b) The term includes, but is not limited to, the following:

- (1) The partial or complete forgiveness of a debt.
- (2) Payment of a taxpayer's obligations by a third party for the taxpayer's direct benefit. The assumption of an outstanding lien on equipment sold by the taxpayer is not a payment for the taxpayer's direct benefit.
- (3) The sale, by a lender, of property pledged or assigned by the taxpayer as collateral for a loan.
- (4) Amounts credited to a partner as its distributive share of partnership income.
- (5) The amount of known liabilities discharged as a result of a sale or other disposition of property, and from which the taxpayer receives a direct benefit. For example, if a taxpayer sells a piece of equipment for five hundred thousand dollars (\$500,000) and uses part of the proceeds to pay off a two hundred thousand dollar (\$200,000) lien against the piece of equipment, the amount received by the taxpayer for gross income tax purposes is five hundred thousand dollars (\$500,000).

Taxpayer has provided sufficient documentation to establish that gross income tax was paid in 1988 on the amount of RUS debt it bought back. As [IC 6-8.1-5-1\(b\)](#) explains, the burden of proving a proposed assessment wrong rests with the taxpayer. In this case, taxpayer has met that burden.

## FINDING

Taxpayer's protest is sustained.

**II. Gross Income Tax—Non-Cash Patronage Revenue**

## DISCUSSION

Taxpayer protests the imposition of gross income tax on non-cash patronage revenue (NCPR). Taxpayer states that it has historically and consistently included non-cash patronage received as taxable gross income. The Department referred to [45 IAC 1.1-1-5](#), which states:

(a) "Constructive receipt" means an item of gross income which is not actually received by a taxpayer but is:

- (1) credited to the taxpayer;
- (2) made available for the taxpayer's withdrawal;
- (3) paid to another for the taxpayer's direct benefit; or
- (4) income to which the taxpayer is entitled.

(b) The term includes, but is not limited to, the following:

- (1) The partial or complete forgiveness of a debt.
- (2) Payment of a taxpayer's obligations by a third party for the taxpayer's direct benefit. The assumption of an outstanding lien on equipment sold by the taxpayer is not a payment for the taxpayer's direct benefit.
- (3) The sale, by a lender, of property pledged or assigned by the taxpayer as collateral for a loan.
- (4) Amounts credited to a partner as its distributive share of partnership income.
- (5) The amount of known liabilities discharged as a result of a sale or other disposition of property, and from which the taxpayer receives a direct benefit. For example, if a taxpayer sells a piece of equipment for five hundred thousand dollars (\$500,000) and uses part of the proceeds to pay off a two hundred thousand dollar (\$200,000) lien against the piece of equipment, the amount received by the taxpayer for gross income tax purposes is five hundred thousand dollars (\$500,000).

Taxpayer refers to two Letters of Findings issued by the Department to non-related REMCs which taxpayer believes are directly on point and support its position. The two LOFs in question are from 1993 and 1995 and rely on a regulation which was superseded in 1999. [45 IAC 1.1-1-5](#) is now the relevant regulation. Since [45 IAC 1.1-1-5\(a\)\(1\)](#) and (4) explain that "constructive receipt" of gross income includes income which is credited to a taxpayer or to which a taxpayer is entitled, and since taxpayer here was credited with and/or entitled to the non-cash patronage, the non-cash patronage was properly classified as gross income. Since the non-cash patronage was gross income, the Department was correct to assess gross income tax on that income.

#### **FINDING**

Taxpayer's protest is denied.

### **III. Tax Administration–Negligence Penalty and Interest**

#### **DISCUSSION**

Taxpayer protests the imposition of penalty and interest. A review of the billing statement shows that the Department did not impose penalty on this assessment. The Department refers to [IC 6-8.1-10-1\(e\)](#), which states, "Except as provided by [IC 6-8.1-5-2\(e\)\(2\)](#), the department may not waive the interest imposed under this section." Therefore, the Department may not waive interest.

#### **FINDING**

Taxpayer's protest is denied.

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