

Letter of Findings Number: 07-0558
Income 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 It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register.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.

ISSUES

I. Income Tax–Net Operating Losses.

Authority: IC § 6-3-2-2.6; IC § 6-8.1-5-1.

Taxpayer protests the determination that claimed net operating losses were unavailable for 2004.

II. Tax Administration–Negligence Penalty.

Authority: 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 is an Indiana corporation. As the result of an audit, the Indiana Department of Revenue ("Department") determined that Taxpayer had additional liabilities for the tax year 2004. The Department issued proposed assessments for adjusted gross income tax, interest, and a ten percent negligence penalty. Taxpayer protests these assessments and the Department's determination that Taxpayer misapplied net operating losses ("NOL"). An administrative hearing was conducted and this Letter of Findings results. Further facts will be supplied as required.

I. Income Tax–Net Operating Losses.

DISCUSSION

Taxpayer protests that the Department incorrectly adjusted Taxpayer's application of a NOL for the tax year 2004. Taxpayer states that the Department misunderstood Taxpayer's application of the NOL from 1999 and 2000. The Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

The Department audited Taxpayer and determined that it had applied the NOL from 1999 as carrybacks to 1997 and 1998 for federal purposes and as a carryover to 2004 for Indiana purposes. Taxpayers are required to treat NOLs the same way for Indiana purposes as for federal purposes. When it determined that Taxpayer had applied the 1999 NOL differently for federal and Indiana purposes, the Department disallowed the carryover on Taxpayer's 2004 Indiana return. This resulted in additional Indiana adjusted gross income tax for 2004.

IC § 6-3-2-2.6 states in relevant part:

- (a) This section applies to a corporation or a nonresident person.
- (b) Corporations and nonresident persons are entitled to a net operating loss deduction. The amount of the deduction taken in a taxable year may not exceed the taxpayer's unused Indiana net operating losses carried back or carried over to that year.
- (c) An Indiana net operating loss equals the taxpayer's federal net operating loss for a taxable year as calculated under Section 172 of the Internal Revenue Code, derived from sources within Indiana and adjusted for the modifications required by [IC 6-3-1-3.5](#).
- (d) The following provisions apply for purposes of subsection (c):
 - (1) The modifications that are to be applied are those modifications required under [IC 6-3-1-3.5](#) for the same taxable year in which each net operating loss was incurred.
 - (2) The amount of the taxpayer's net operating loss that is derived from sources within Indiana shall be determined in the same manner that the amount of the taxpayer's adjusted income derived from sources within Indiana is determined under section 2 of this chapter for the same taxable year during which each loss was incurred.
 - (3) An Indiana net operating loss includes a net operating loss that arises when the modifications required by [IC 6-3-1-3.5](#) exceed the taxpayer's federal taxable income (as defined in Section 63 of the Internal Revenue Code), if the taxpayer is a corporation, or when the modifications required by [IC 6-3-1-3.5](#) exceed the taxpayer's federal adjusted gross income (as defined by Section 62 of the Internal Revenue Code), if the taxpayer is a nonresident person, for the taxable year in which the Indiana net operating loss is determined.
- (e) Subject to the limitations contained in subsection (g), an Indiana net operating loss carryback or carryover shall be available as a deduction from the taxpayer's adjusted gross income derived from sources within Indiana (as defined in section 2 of this chapter) in the carryback or carryover year provided in subsection (f).
- (f) Carrybacks and carryovers shall be determined under this subsection as follows:
 - (1) An Indiana net operating loss shall be an Indiana net operating loss carryback to each of the carryback

years preceding the taxable year of the loss.

(2) An Indiana net operating loss shall be an Indiana net operating loss carryover to each of the carryover years following the taxable year of the loss.

(3) Carryback years shall be determined by reference to the number of years allowed for carrying back a net operating loss under Section 172(b) of the Internal Revenue Code.

(4) *Carryover years shall be determined by reference to the number of years allowed for carrying over net operating losses under Section 172(b) of the Internal Revenue Code.*

(5) *A taxpayer who makes an election under Section 172(b)(3) of the Internal Revenue Code to relinquish the carryback period with respect to a net operating loss for any taxable year shall be considered to have also relinquished the carryback of the Indiana net operating loss for purposes of this section.*

....
(*Emphasis added.*)

Taxpayer protests that the carrybacks to 1997 and 1998 were from a NOL incurred in 2000, not from 1999. Taxpayer provided documentation showing that it elected on its federal return to carryover the 1999 NOL. Therefore, under IC § 6-3-2-2.6(f)(5) Taxpayer's federal election to relinquishment of the carryback period with respect to the NOL from 1999 shall be considered to be the relinquishment of the carryback of the Indiana NOL from 1999. Since the federal government approved refunds for 1997 and 1998, and since Taxpayer had relinquished its right to carryback the 1999 NOL, the NOLs applied to those years must logically have come from a year or years other than 1999.

Since Taxpayer relinquished the carryback of NOL from 1999, that NOL was available for carryover to future years, as provided by IC § 6-3-2-2.6(f)(4). Taxpayer applied a portion of the 1999 NOL on its 2004 Indiana adjusted gross income tax return. The 1999 NOL was available for application in 2004. Taxpayer has met its burden under IC § 6-8.1-5-1(c).

FINDING

Taxpayer's protest is sustained.

II. Tax Administration—Negligence Penalty.

DISCUSSION

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

If a person:

....

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

....

the person is subject to a penalty.

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

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to 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 explained that there was no deficiency as the Department had previously determined, and so Taxpayer was not subject to a penalty under IC § 6-8.1-10-2.1(a). Taxpayer has affirmatively established that there was no failure to pay a deficiency, as required by [45 IAC 15-11-2\(c\)](#).

FINDING

Taxpayer's protest is sustained.

CONCLUSION

Taxpayer is sustained on Issue I regarding application of the 1999 NOL on its 2004 Indiana adjusted gross income tax return. Taxpayer is sustained on Issue II regarding imposition of negligence penalty.

Posted: 10/01/2008 by Legislative Services Agency

An [html](#) version of this document.