DEPARTMENT OF STATE REVENUE

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Letter of Findings Number: 08-0374
Indiana Corporation Income Tax
For the Tax Years 2003 and 2004

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ISSUES

I. Adjusted Gross Income Tax–Unitary Filing.

Authority: IC § 6-3-2-2; IC § 6-3-2-2.4; IC § 6-8.1-5-1; 45 IAC 3.1-1-62; Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Bethlehem Steel Corp. v. Ind. Dept. of State Revenue, 597 N.E.2d 1327 (Ind. Tax Ct. 1992); Allied-Signal Corp. v. Director, Division of Taxation, 504 U.S. 768 (1992); Gregory v. Helvering 293 U.S. 465 (1935); Lee v. Comm'r of Internal Revenue, 155 F.3d 584 (2d Cir. 1998); Horn v. Comm'r, 968 F.2d 1229 (D.C. Cir. 1992); Comm'r v. Transp. Trading and Terminal Corp., 176 F.2d 570 (2nd Cir. 1949), cert denied, 338 U.S. 955 (1950); Zebra Technologies Corp. v. Topinka, 799 N.E.2d 725 (Ill. Ct. App. 2003).

Taxpayer maintains that the Department of Revenue erred when it recomputed Taxpayer's adjusted gross income to include affiliated companies on a unitary combined-filing basis.

II. Adjusted Gross Income Tax–Calculation Errors.

Authority: IC § 6-8.1-5-1.

Taxpayer maintains that the Department of Revenue made certain calculation errors in preparing the proposed assessment.

III. Tax Administration–Penalties.

Authority: IC § 6-3-4-4.1; IC § 6-8.1-10-2.1; 45 IAC 15-11-2.

Taxpayer protests the imposition of penalties.

STATEMENT OF FACTS

Taxpayer is a multi-entity company–consisting of a parent corporation and over forty subsidiaries–that designs, produces, markets, and delivers products to customers. Taxpayer operates in three business areas–as a retailer selling directly to individuals, as a wholesaler selling to retail stores, and as a wholesaler selling to the service industry. Taxpayer has operations throughout countries in Europe and throughout most of the United States, including Indiana. Taxpayer reorganized its business structure in 2000 and again in 2003. After the 2000 reorganization, Taxpayer's corporate structure consisted of a parent corporation and several subsidiaries, including sales corporations, a manufacturing corporation, technology corporations, a research and development corporation, an intellectual property disregarded LLC (hereafter "IP LLC"), a financial services disregarded LLC (hereafter "Financing LLC").

The manufacturing corporation subsidiary (hereafter "Mfg. Corp."), which is owned by affiliate-subsidiaries that are also Mfg. Corp's customers, manufactures products for the affiliate-subsidiaries to sell. Mfg. Corp. makes wholesale sales to the other subsidiaries and then pays "patronage dividends" back to the subsidiaries according to the volume of purchases that the subsidiaries make. Taxpayer did not include Mfg. Corp. in its Indiana corporate income tax returns for the years in question. However, the subsidiaries that Taxpayer included in its Indiana corporate income tax returns were all affiliate-subsidiaries of Mfg. Corp. that made purchases and received "patronage dividends" back from Mfg. Corp.

IP LLC licenses trademarks to the subsidiaries. In turn, royalties are transferred from the subsidiaries to IP LLC. IP LLC then transfers the royalties to Financing LLC. Financing LLC uses the transferred royalties to make loans to the subsidiaries (including the subsidiaries paying the royalties). The loans are supported by loan contracts that are open ended with no stated amounts due and with no set maturity dates. IP LLC and Financing LLC have no employees or property of their own. IP LLC and Financing LLC, through their holding corporation ("Holding Subsidiary"), pay a dividend to another corporation, which then pays the precisely same amount of a dividend to another corporation (hereafter "Corp. F"), which is one of the corporations Taxpayer included in its Indiana corporate income tax returns for the tax years in question.

Effective for the 2003 tax year, Taxpayer's sales corporation was reorganized into two corporations, one for the retail operations and one for the wholesale operations (hereafter "Retail Corp." and "Wholesale Corp."). Also effective for the 2003 tax year, Taxpayer formed an LLC (hereafter "Admin. Services LLC") to provide the administrative services–human resources, accounting, legal, and information technology services–to the subsidiaries pursuant to administrative services agreements. Admin. Services LLC is owned 94 percent by Retail Corp., two percent by Wholesale Corp., two percent by another corporation (hereafter "Corp. T") and two percent by another manufacturing corporation ("hereafter Corp. B"). Taxpayer included the four corporations that own Admin. Services LLC in its Indiana corporate income tax returns for the tax years in question.

For the tax years in question, Taxpayer filed consolidated Indiana corporate income tax returns that included five of its subsidiaries, Retail Corp., Wholesale Corp., Corp. F, Corp. T, and Corp. B. Taxpayer's consolidated Indiana corporate income tax returns reported large net operating losses for each year. The Department audited Taxpayer's Indiana corporate income tax returns for the 2000 through 2004 tax years. As a result of the audit, the Department assessed additional adjusted gross income tax, interest, the negligence penalty, and the underpayment of estimated tax penalty for the 2003 and 2004 tax years. The Department's audit determined that additional tax was due for the 2002 tax year, but did not issue a tax assessment because the statute of limitations had expired. The Department concluded that Taxpayer's adjusted gross income should be calculated using a unitary combined-filing basis. Taxpayer protested the assessments. An administrative hearing was held, and this Letter of Findings results. Further facts will be supplied as necessary.

I. Adjusted Gross Income Tax–Unitary Filing.

DISCUSSION

Pursuant to IC § 6-8.1-5-1(c), all tax assessments are presumed accurate, and the taxpayer bears the burden of proving that an assessment is incorrect. Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

Taxpayer asserts that the Department failed to go through the proper steps before calculating Taxpayer's adjusted gross income under the unitary combined-filing method and that Holding Subsidiary cannot be included in the combined filing.

A. Unitary Filing.

IC § 6-3-2-2, provides, in relevant parts:

...

(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) for a taxable year beginning before January 1, 2011, the exclusion of any one (1) or more of the factors, except the sales factor;

(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.

...

(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).

....

In addition, 45 IAC 3.1-1-62, states:

All corporations doing business in more than one state shall use the allocation and apportionment provisions described in Regulations 6-3-2-2(b)-(k) [45 IAC 3.1-1-37–45 IAC 3.1-1-61] unless such provisions do not result in a division of income which fairly represents the taxpayer's income from Indiana sources. In such case the taxpayer must request in writing or the Department may require the use of a more equitable formula for determining Indiana income. However, the Department will depart from use of the standard formula only if the use of such formula works a hardship or injustice upon the taxpayer, results in an arbitrary division of income, or in other respects does not fairly attribute income to this state or other states. It is anticipated that these situations will arise only in limited and unusual circumstances (which ordinarily will be unique and nonrecurring) when the standard apportionment provisions produce incongruous results.

Accordingly, when a taxpayer's method of filing individual Indiana adjusted gross income tax returns for related corporations distorts the taxpayer's Indiana source income, the Department may require that the related entities file a combined return. The purpose of the combined return would be to fairly reflect the taxpayer's and related entities' actual Indiana income and expenses. In order to do so, the Department must find the entities form a unitary group. The second step is that the Department must make a finding that the taxpayer's own method of filing the adjusted gross income tax distorts the taxpayer's Indiana income and/or expenses. Lastly, the Department must be unable to fairly reflect Indiana income using other methods before requiring the combined-filing method.

In this situation, the Taxpayer agrees with the Department that it and the related corporations form a unitary group. However, Taxpayer disputes the Department's determination that its original filing did not fairly reflect Indiana source income and disputes the Department determination that only a unitary filing can fairly reflect its income.

1. Fairly Reflect.

Taxpayer maintains that the Department's audit report did not provide evidence to support its finding of an unfair reflection, but only provides "conclusory statements." Taxpayer illustrated its point by asserting that the audit report does not show "economies of scale," but only states that the economies exist. Notwithstanding that the audit report begins by providing various facts about Taxpayer business operations which support its later conclusions, even if Taxpayer's assertion about the "economies of scale" were correct, Taxpayer's argument is not supported by the "economies of scale" example. Since "economies of scale" are used to demonstrate that a business is unitary and Taxpayer admits it operates as a unitary business, the Department declines to address this illustration. See Allied-Signal Corp. v. Director, Division of Taxation, 504 U.S. 768, 781 (1992) (citing F.W. Woolworth Co. v. Taxation and Revenue Dep't. of New Mexico, 458 U.S 354, 364 (1982) (explaining that one must look at the (1) functional integration; (2) centralization of management; and (3) economies of scale of the entities to determine whether the taxpayer and subsidiary comprise a unitary business).

The Department's audit report provides the following facts about Taxpayer after its restructuring. Taxpayer's subsidiaries paid IP LLC royalties for the right to use trademarks. IP LLC transferred the royalty payments to Financing LLC, which loaned the money back to the subsidiaries. The subsidiaries took interest expense deductions on these loans. These royalties and interest payments were used to pay dividends back to the subsidiaries. Mfg. Corp. made wholesale sales to the other subsidiaries and then paid "patronage dividends" back to the subsidiaries according to the volume of purchases that the subsidiaries made. While nothing changed with respect to the Taxpayer's overall business after entering into the royalties, interest, and manufacturing transactions, Taxpayer received a substantial profit from its sales of products only to have it greatly reduced by these intercompany transactions.

For illustrative purposes, Taxpayer's reported pre-apportioned adjusted gross income ("Pre-apportioned AGI") and Taxpayer's reported apportioned adjusted gross income ("IN AGI') prior to and after Taxpayer's 2000 restructuring have been provided, with the numbers rounded to the nearest million dollars, below:

Tax Year	Pre–Apportioned AGI	IN AGI (Apportioned)
1996	Not available	3,000,000
1997	141,000,000	4,000,000
1998	114,000,000	3,000,000
1999	28,000,000	000,000
2000	125,000,000	3,000,000
2001	(71,000,000)	(2,000,000)
2002	(51,000,000)	(1,000,000)
2003	(62,000,000)	(1,000,000)
2004	(48,000,000)	(1,000,000)

Here, based on numerous intercompany transactions and excluding certain entities from the return, Taxpayer sought to shield virtually all of the income of its Indiana operations from Indiana's taxation. Taxpayer's method of reporting the transactions can only be described as not fairly representing Taxpayer's Indiana income. Taxpayer received a substantial profit from its sales of products, only to have the profit greatly reduced by several intercompany transactions, including the subsidiaries' use of their own names for a substantial sum of money, taking interest expense deductions when this royalty money was "loaned" back to the subsidiaries, and taking "cost of goods sold" deductions for goods that were "bought" from a related entity that in turn paid those subsidiaries purchasing the goods tax-exempt dividends in relation to the amounts that were purchased. These businesses, if respected as businesses, constituted an integrated enterprise. Thus, to state that only a portion of the income due to Taxpayer's primary products sales was taxable, without recognizing the whole of the enterprise to overall profitability, was to not fairly represent Taxpayer's income in Indiana.

2. Alternate Methods.

Taxpayer maintains that the Department's audit report did not show how every other method failed and, therefore, does not meet the prerequisite for a mandatory combined-filing. However, the Department notes that IC § 6-3-2-2(p) does not require that the Department provide explanations of why every other method does not fairly reflect Indiana income. The requirement is that the Department be unable to fairly reflect Indiana income using other methods before requiring a combined filing. The Department provided an explanation in the audit report concerning the interwoven nature of the entities' activities and demonstrated at least three circular flows of monies. The Department requested that Taxpayer suggest alternative methods that could be used, and Taxpayer said that it had no suggestions other than using the standard filing method. The Department explained that it tried

alternatives methods and was unable to otherwise fairly reflect Taxpayer's Indiana income and required combined filing, as allowed under IC § 6-3-2-2(l). Thus, the Department considered combined filing as a last resort, as required by 45 IAC 3.1-1-62.

Therefore, Taxpayer's protest to the Department's use of the unitary combined-filing method is denied.

B. Holding Subsidiary.

Alternatively, Taxpayer maintains that if the Department uses the unitary combined-filing method, Holding Subsidiary cannot be included because it is a "foreign operating corporation." IC § 6-3-2-2(o) provides that a foreign corporation or foreign operating corporation cannot be combined under subsections (l) and (m). A foreign operating corporation is defined by IC § 6-3-2-2.4(a) as a corporation which has 80 percent or more of its business activity occur outside the United States. IC § 6-3-2-2.4(b) provides a method to determine the percentage by using the taxpayer's U.S. property factor (defined as United States property over worldwide property) and the taxpayer's U.S. payroll factor (defined as United States payroll over worldwide payroll), added together, divided by two.

Only one court has dealt with the situation presented by the Taxpayer with respect to an intangibles holding corporation located in a foreign country. In Zebra Technologies Corp. v. Topinka, 799 N.E.2d 725 (Ill. Ct. App. 2003), a company engaged in the business of manufacturing bar-coding equipment, formed another corporation, which it incorporated in Bermuda and to which it transferred its intellectual property. Taxpayer maintained that the corporation was not subject to forced unitary filing based on an Illinois statute similar to IC § 6-3-2-2(o). In particular, the taxpayer argued that the company had no payroll or property in the United States, and therefore was precluded from forced unitary filing. The court, however, noted that much of the work related to the intellectual property actually occurred in the United States and held that the company in question was not a foreign operating company, and therefore subject to unitary filing. Id. at 732-34.

Taxpayer was presented with an opportunity to address this issue during hearing. In the period after the hearing, Taxpayer was presented an additional opportunity to gather information. Taxpayer has presented only internal documents and mere assertions claiming that Holding Subsidiary was a foreign operating corporation. Taxpayer asserts that Holding Subsidiary is a foreign operating corporation based upon another disregarded LLC, operating as a division of Holding Subsidiary, which has a small number of employees and small amount of property in the United Kingdom. However, Taxpayer makes these assertions without demonstrating what those employees do in regards to business activity, for what the property is used in regards to business activity, and how this activity would relate to the financing and intellectual property royalty income. Moreover, Taxpayer makes these assertions in an attempt to show that Holding Subsidiary was a foreign operating corporation without providing any further information regarding the exploitation of the intellectual property and financing activities either in the United States or elsewhere. Accordingly, Taxpayer failed to meet its burden.

Notwithstanding, even if Taxpayer had met its burden, Taxpayer arrangements constitute "sham transactions." The "sham transaction" doctrine is well established both in state and federal tax jurisprudence dating back to Gregory v. Helvering 293 U.S. 465 (1935). In that case, the Court held that in order to qualify for a favorable tax treatment, a corporate reorganization must be motivated by the furtherance of a legitimate corporate business purpose. Id. at 469. A corporate business activity undertaken merely for the purpose of avoiding taxes was 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." Id. at 470. The courts have subsequently held that "in construing words of a tax statute which describe [any] commercial transactions [the court is] to understand them to refer to transactions entered upon for commercial or industrial purposes and not to include transactions entered upon for no other motive but to escape taxation." Comm'r v. Transp. Trading and Terminal Corp., 176 F.2d 570, 572 (2nd Cir. 1949), cert denied, 338 U.S. 955 (1950). "Transactions that are invalidated by the [sham transaction] doctrine are those motivated by nothing other than the taxpayer's desire to secure the attached tax benefit" but are devoid of any economic substance. Horn v. Comm'r, 968 F.2d 1229, 1236-37 (D.C. Cir. 1992). In determining whether a business transaction was an economic sham, two factors can be considered; "(1) did the transaction have a reasonable prospect, ex ante, for economic gain (profit), and (2) was the transaction undertaken for a business purpose other than the tax benefits?" Id. at 1237.

The question of whether or not a transaction is a sham, for purposes of the doctrine, is primarily a factual one. Lee v. Comm'r of Internal Revenue, 155 F.3d 584, 586 (2d Cir. 1998). The taxpayer has the burden of demonstrating that the subject transaction was entered into for a legitimate business purpose. IC § 6-8.1-5-1(c).

The Department is unable to discern a business purpose for the arrangement between Taxpayer, IP LLC, Financing LLC, and Holding Subsidiary. Taxpayer transferred the intellectual property to IP LLC, which licensed that property only to Taxpayer's subsidiaries. Taxpayer had, at most, a relatively modest profit from its operations from products sales, but IP LLC and Financing LLC generated substantial profits from licensing names and logos to nobody but their prior owners and loaning these monies back to the subsidiaries. IP LLC had no employees or property of its own, and its balance sheet reports a minimum amount of intangible property held (approximately $33,000 in 2002, $11,000 in 2004, and $1,500 in 2005), which Taxpayer claims is an oversight in its record keeping. Moreover, Financing LLC also had no payroll or property of its own. Taxpayer states that the "day to day administration" of the trademarks and financing activities is performed by Admin. Services LLC. Thus, the "day to

day administration," if any, would be performed by a U.S. entity operating one hundred percent in the U.S. that is owned by five corporations all of which also operated one hundred percent in the U.S and all of which were included by Taxpayer in its Indiana returns.

Furthermore, Holding Subsidiary, the U.S. tax reporting entity for IP LLC and Financing LLC, also had no payroll or property of its own, but–conveniently enough–owned another disregarded LLC that maintained only a small office in the United Kingdom and had no employees until 2003 when it started reporting the wage expenses of eight people. While Holding Subsidiary did file a tax return with the United Kingdom reporting little to no activity, Taxpayer states that the United Kingdom's tax code does not require it to report the income received by the disregarded LLCs, which is why no royalty or interest income is reflected on the United Kingdom returns. In effect, Taxpayer has attempted to create through a series of transactions employed with three "shell entities," the means to transfer and isolate a substantial amount of income in the United Kingdom, which is non-reportable to the United Kingdom, and take large expense deductions for state tax purposes. However, for purposes of Taxpayer's shareholders, the bottom line and the companies' operating performance remained unchanged.

Taxpayer is, of course, entitled to structure its business affairs in any manner its sees fit and to vigorously pursue any tax advantage attendant upon the management of those affairs. However, in determining the nature of business transactions and the resultant tax consequences, the Department is required to look at "the substance rather than the form of the transaction." Bethlehem Steel Corp. v. Ind. Dept. of State Revenue, 597 N.E.2d 1327, 1331 (Ind. Tax Ct. 1992). The transfer of the intellectual property, the royalty payments, and interest payments were purely matters of "form" and lack any business "substance."

Taxpayer's protest of the Department's inclusion of Holding Subsidiary is denied.

FINDING

Taxpayer's protest is denied.

II. Adjusted Gross Income Tax–Calculation Errors.

DISCUSSION

Taxpayer maintains that the Department made certain calculation errors in preparing the proposed assessment and asks that those errors be corrected. As noted above, all tax assessments are presumed to be accurate, and the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c).

Taxpayer asserts that the Department's audit report made two errors on page 31 of the audit report overstating its federal taxable income by improperly reporting its cost of goods sold for two entities. Essentially, Taxpayer states that the audit erroneously included a negative adjustment for the parent corporation, of approximately $36,000, and that Wholesale Corp.'s cost of goods sold was understated by approximately $2,000,000. Taxpayer has done nothing to conclusively demonstrate that the amount of contributions should be corrected. Nonetheless, the Audit Division is requested to conduct a supplemental review of Taxpayer's records and its cost of goods sold.

FINDING

The Audit Division is requested to review Taxpayer's assertion that the audit report contained the errors cited above and to make whatever corrections it deems appropriate. Taxpayer's protest is sustained subject to that supplemental audit review.

III. Tax Administration–Penalties.

DISCUSSION

The Department determined that Taxpayer incurred an assessment that was due to negligence as found under 45 IAC 15-11-2(b) and imposed the penalty under IC § 6-8.1-10-2.1(a). Also, the Department found that based upon Taxpayer's failure to make sufficient estimate payments, Taxpayer was subject to the penalty under IC § 6-3-4-4.1. Taxpayer protests the imposition of the negligence penalty and the underpayment of estimated tax penalty.

A. Negligence Penalty.

Taxpayer argues that it is not subject to a negligence penalty with respect to the additional taxes assessed against it. In particular, Taxpayer maintains that it had reasonable cause not to originally file a unitary/combined return because by statute it could not have filed the combined return without requesting and receiving the Department's permission. Accordingly, Taxpayer argues that it was not negligent in its tax return filings for the years in question.

The Department refers to IC § 6-8.1-10-2.1(a)(3), which provides "if a person... incurs, upon examination by the department, a deficiency that is due to negligence... the person is subject to a penalty." Penalty waiver is only 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(d).

Further, the Indiana Administrative Code, 45 IAC 15-11-2(b) provides:

> 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 may waive the negligence penalty as provided in 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.

Taxpayer has acted in a manner the review of which confirms the Department's conclusion that its actions were negligent. Accordingly, the penalty must stand.

Therefore, Taxpayer's protest to the imposition of the negligence penalty is denied.

B. Estimated Tax Penalty.

Taxpayer protests the imposition of the underpayment of estimated tax penalty. IC § 6-3-4-4.1, in relevant part, provides:

(d) Every corporation subject to the adjusted gross income tax liability imposed by this article shall be required to report and pay an estimated tax equal to twenty-five percent (25 [percent]) of such corporation's estimated adjusted gross income tax liability for the taxable year. A taxpayer who uses a taxable year that ends on December 31 shall file the taxpayer's estimated adjusted gross income tax returns and pay the tax to the department on or before April 20, June 20, September 20, and December 20 of the taxable year. If a taxpayer uses a taxable year that does not end on December 31, the due dates for filing estimated adjusted gross income tax returns and paying the tax are on or before the twentieth day of the fourth, sixth, ninth, and twelfth months of the taxpayer's taxable year. The department shall prescribe the manner and forms for such reporting and payment.

(e) The penalty prescribed by IC 6-8.1-10-2.1(b) shall be assessed by the department on corporations failing to make payments as required in subsection (d) or (g). However, no penalty shall be assessed as to any estimated payments of adjusted gross income tax which equal or exceed:

(1) twenty percent (20 [percent]) of the final tax liability for such taxable year; or

(2) twenty-five percent (25 [percent]) of the final tax liability for the taxpayer's previous taxable year.

In addition, the penalty as to any underpayment of tax on an estimated return shall only be assessed on the difference between the actual amount paid by the corporation on such estimated return and twenty-five percent (25%) of the corporation's final adjusted gross income tax liability for such taxable year.

A penalty is imposed under IC § 6-3-4-4.1(d) for the underpayment of estimated tax when a taxpayer fails to make the required estimated payments. Under IC § 6-3-4-4.1(e), the penalty is assessed on the amount by which the taxpayer underestimated its tax liability. IC § 6-3-4-4.1 does not contain a negligence standard. Rather, IC § 6-3-4-4.1(e) simply states that the penalty "shall be assessed by the department on corporations failing to make payments as required...." Since Taxpayer failed to make the required estimated payments, Taxpayer is subject to penalty. Taxpayer invites the Department to abate the underpayment of estimated tax penalty, but has not provided an equitable or statutory basis upon which to do so. Therefore, the Department must decline the invitation.

Therefore, Taxpayer's protest to the imposition of the underpayment of estimated tax penalty is denied.

FINDING

Taxpayer's protest to the imposition of penalties is denied.

CONCLUSION

Taxpayer's protest to the Department's imposition of tax based upon the unitary combined-filing method, as discussed in Issue I, is denied. Taxpayer's protest to the imposition of penalties, as discussed in Issue III, is denied. Taxpayer's protest that calculation errors due to its cost of goods sold should be corrected, as discussed in Issue II, is sustained subject to the results of a supplemental audit.

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