

**Letter of Findings: 01-20100481**  
**Individual Income Tax**  
**For the 2006, 2007, and 2008 Tax Years**

**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 It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register.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. Individual Income Tax—Federal Taxable Income.**

**Authority:** IC § 6-8.1-5-1; Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007).

Taxpayer protests the imposition of adjusted gross income tax resulting from adjustments made to its federal taxable income.

**II. Tax Administration—Statute of Limitations.**

**Authority:** IC § 6-8.1-5-2.

Taxpayer protests the imposition of adjusted gross income tax for the 2006 tax year.

**STATEMENT OF FACTS**

Taxpayer operates an auto repair business as a sole proprietorship. Taxpayer also sells vehicles and used equipment. The Department conducted a review of Taxpayer's business records. After the investigation, the Indiana Department of Revenue ("Department") determined that Taxpayer owed additional individual income tax and assessed tax, interest, and negligence penalties for the 2006, 2007, and 2008 tax years. The Department determined that Taxpayer had under-reported its federal taxable income. Taxpayer protested. An administrative hearing was conducted, and this Letter of Findings results. Further facts will be supplied as required. The hearing officer prepared this Letter of Findings based upon the information contained within the Department's audit report and upon the additional information that taxpayer presented during the protest process.

**I. Individual Income Tax—Federal Taxable Income.**

**DISCUSSION**

As a threshold matter, all tax assessments are prima facie evidence that the Department's claim for the tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

The Department conducted an audit of Taxpayer's business records and tax returns. After reviewing the Taxpayer's documents, the Department determined that Taxpayer had under-reported its gross income and had over reported several expenses resulting in Taxpayer's under-reporting its federal taxable income.

The Department found discrepancies in the information that Taxpayer provided to substantiate the amount of gross sales that were reported on its federal return for its business—i.e., cash sales that were not deposited in the business account, unaccounted for deposits, and evidence that the credit and debit card sales that were deposited into the Taxpayer's personal checking account. The Department determined that the amount of gross sales reported on the federal return was unreliable. The Department derived the additional gross sales by adding the total "business deposits" in the business checking account to the total cash that was received and not deposited to the total credit and debit card sales receipts and then subtracting the reported gross sales. For the 2006 and 2007 tax years, the deposits into the business checking account were categorized into the types of income and only the auto repair income, miscellaneous income, and vehicle and automobile sales income were included as "business deposits." Taxpayer was asked for the deposit information for the business checking account for the 2008 tax year, but did not provide the information to the auditor. Thus, the deposits into the business checking account less loans, balance transfers, and rental receipts were used as the "business deposits" for the 2008 tax year. The Department also requested for Taxpayer to provide its personal checking account information because the credit and debit card receipts were deposited in this account and because of Taxpayer's receipt of cash payments that Taxpayer did not deposit. However, Taxpayer did not provide its personal checking account information.

Additionally, the Department found discrepancies in the information that Taxpayer provided to substantiate the amount of business expenses that Taxpayer claimed on the federal return for the 2006 and 2007 tax years. The 2008 tax year information was not provided. Thus, the Department disallowed any expenses that the Taxpayer could not document. However, the Department included a limited number of additional expenses such as property tax and depreciation that Taxpayer had failed to include. Accordingly, the Department made adjustments to the Taxpayer's business net income for each of the tax years.

Lastly, the Department found discrepancies in the information that Taxpayer provided to substantiate the amount of rental income that Taxpayer reported on the federal returns for the 2006 and 2007 tax years. The 2008 tax year information was not provided. The Department found that Taxpayer had failed to report all of the income

that was deposited into the business checking account and classified as rental income. The Department also found receipts for cash paid for rents that were not deposited into the business checking account. Therefore, for the 2006 and 2007 tax years, additional rental income was added for the properties for which Taxpayer reported either very little or no rental income. For the 2008 tax year, additional rental income was derived based upon the 2006 and 2007 tax year's additional rental income. Additionally, adjustments were made to only allow Taxpayer the rental expense deductions that could be documented. Accordingly, the Department made adjustments to Taxpayer's "rental property net income" for each of the tax years.

Therefore, the Department determined that Taxpayer had under-reported its federal taxable income and made the appropriate adjustments. Taxpayer disagreed with the Department determination that Taxpayer's income was more than Taxpayer reported. During the protest, Taxpayer's representative presented amended Indiana income tax returns for each of the tax years in question to provide revised schedules of income and alleged business-related expenses. While the revised returns attempted to close the gap between Taxpayer's reported income and the income determined by the Department, neither the Taxpayer nor Taxpayer's representative provided the additional documentation to support all of the adjustments proposed on these revised Indiana returns nor to support Taxpayer's position regarding Taxpayer's under-reporting.

Taxpayer has the obligation to prepare a careful, methodical, and detailed factual presentation of the evidence sufficient to refute the conclusions contained within the Department's investigation report. In order to meet its burden, the taxpayer must "walk" the Hearing Officer through each element of the taxpayer's proffered evidence; Taxpayer does not meet its burden by presenting amended returns, without invoices, receipts, daily recaps, or other supporting documentation. Amended returns, without more, only serve as conclusory statements in the hope that those returns or statements will speak for themselves. Taxpayer's amended returns and additional explanation proffered during the hearing do not sufficiently refute the information or the results reached by the Department. Therefore, Taxpayer's protest to the imposition of income tax based upon the general acceptance of the amended returns is denied. However, Taxpayer did provide a limited amount of additional documentation to address specific issues during the protest, and Taxpayer's protest as it relates to each issue raised will now be addressed.

#### **A. "Additional Business Net Income."**

Taxpayer protests the imposition of adjusted gross income tax from the adjustments made to Taxpayer's "business net income." Taxpayer asserts that the certain of its cash deposits that were made into the business checking account were "miscellaneous receipts" that are not receipts of the business. Taxpayer also asserts that the Department incorrectly disallowed expenses that were correctly reported on its income tax returns.

During the course of the protest, Taxpayer presented additional documentation that was not available at the time of audit, which was reviewed by the audit division after the audit during the protest process. Based upon this additional documentation, the Department is in agreement that, during the tax year 2007, Taxpayer received two loans in the amount of \$7,300 and \$3,800. The audit division is requested to perform a supplemental audit to determine if these amounts have been included in "miscellaneous income." Thus, Taxpayer's protest is sustained to the extent that these two loans in the amount of \$7,300 and \$3,800 were included in the calculation of additional business income. However, Taxpayer's protest is denied to the extent that these two loan amounts were not included in the calculation of additional business income.

Additionally, the Department has determined that the additional documentation provided for the 2008 tax year—i.e., additional documentation for the types of revenue deposits and the 2008 depreciation schedule—will be reviewed and taken into account in a supplemental audit. Thus, Taxpayer's protest is sustained to the extent that the supplemental audit adjusts the calculation of additional "business income." However, Taxpayer's protest is denied to extent that the supplemental audit does not adjust the calculation of additional "business income." Lastly, Taxpayer's protest as it relates to any other adjustments for the "business net income" is denied.

Therefore, Taxpayer's protest to the imposition of adjusted gross income tax from the adjustments made to Taxpayer's "business net income" is denied in part and sustained in part subject to the results of a supplemental audit. The file will be returned to the audit division for the completion of a supplemental audit where the audit division will make the adjustments that it deems appropriate.

#### **B. "Additional Rental Property Net Income."**

Taxpayer protests the imposition of tax from the adjustments made to Taxpayer's "rental property net income." Taxpayer makes a general assertion that the Department incorrectly increased the rental income. Taxpayer also asserts that the Department incorrectly disallowed rental property expenses that were correctly reported on its income tax returns.

As stated previously, the Department found discrepancies in the information upon which Taxpayer had reported its rental property income, determined the information was unreliable, and used an alternative calculation to calculate "rental property net income." IC § 6-8.1-5-1(b) provides, "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." Thus, pursuant to this statutory authority, the Department used an alternative audit method to calculate Taxpayer's "rental property income" based upon the "best information available." Therefore, Taxpayer's general protest to the adjustments made for additional "rental

property income' is denied.

During the course of the protest, Taxpayer presented a limited amount of documentation that was not available at the time of audit, which was reviewed by the audit division after the audit during the protest process. Based upon this additional documentation, the Department has determined that the additional documentation provided for the 2008 tax year—i.e., additional documentation for revenue receipts deposits and additional documentation for rental expenses—will be reviewed and taken into account in a supplemental audit. Thus, Taxpayer's protest is sustained to the extent that the supplemental audit adjusts the calculation of additional "rental property net income." However, Taxpayer's protest is denied to the extent that the supplemental audit does not adjust the calculation of additional "rental property net income." Lastly, Taxpayer's protest as it relates to any other adjustments for the "rental property net income" is denied.

Therefore, Taxpayer's protest to the imposition of adjusted gross income tax from the adjustments made to Taxpayer's "rental property net income" is denied in part and sustained in part subject to the results of a supplemental audit. The file will be returned to the audit division for the completion of a supplemental audit where the audit division will make the adjustments that it deems appropriate.

### **C. "Sale of Property."**

Taxpayer protests the imposition of tax from the adjustments made to Taxpayer's gain on a sale of property in 2006. Taxpayer asserts that the Department must take into account the Internal Revenue Service ("IRS") Form 3115 ("Form 3115") to request a change in accounting method for its depreciation that will adjust the basis of the asset.

However, Taxpayer has not filed this form with the IRS. Moreover, it is unlikely that if Taxpayer did file this form that it would be accepted by the IRS. The instructions for Form 3115 state that the form must be "[a]ttach[ed] the original to the filer's **timely filed** (including extensions) federal income tax return for the year of change."

**(Emphasis added).** "In general, a taxpayer that fails to timely file a Form 3115 will not be granted an extension of time to file except in unusual and compelling circumstances. See Regulations section 301.9100-3 for the standards that must be met. For information on the period of limitations, see section 5.03(2) of Rev. Proc. 2010-1." *Id.* (Emphasis added). Thus, the Taxpayer invites the Department to take into consideration the effects of a form that it has not yet filed with the IRS and that would most likely not be accepted by the IRS. The Department declines Taxpayer's invitation.

### **FINDING**

Taxpayer's protest is respectfully denied.

## **II. Tax Administration—Statute of Limitations.**

### **DISCUSSION**

The Department applied the six (6) year statute of limitations for the issuance of the proposed assessment in this matter. Taxpayer protests this extension of the normal three (3) year statute of limitations for the 2006 tax year.

Pursuant to IC § 6-8.1-5-2(a), the statute of limitations for the Department to issue a proposed assessment is three (3) years. However, if the taxpayer understates its income by 25 percent or more for that tax year, the statute of limitations for that tax year is extended to six (6) years. IC § 6-8.1-5-2(b).

### **FINDING**

Taxpayer's protest to the imposition of adjusted gross income tax for the 2006 tax year is respectfully denied.

### **SUMMARY**

Taxpayer's protest to the imposition of adjusted gross income tax from the adjustments made to Taxpayer's "business net income" is denied in part and sustained in part subject to the results of a supplemental audit, as discussed in Issue I(A). Taxpayer's protest to the imposition of adjusted gross income tax from the adjustments made to Taxpayer's "rental property net income" is denied in part and sustained in part subject to the results of a supplemental audit, as discussed in Issue I(B). Taxpayer's protest to the imposition of tax from the adjustments made to Taxpayer's gain on a sale of property in 2006 is denied, as discussed in Issue I(C). Taxpayer's protest to the imposition of adjusted gross income tax for the 2006 tax year as being outside the statute of limitations is respectfully denied, as discussed in Issue II.

As discussed in Issue I(A) and Issue I(B), the file will be returned to the audit division for the completion of a supplemental audit where the audit division will make the adjustments that it deems appropriate.

*Posted: 03/23/2011 by Legislative Services Agency*  
An [html](#) version of this document.