

**Letter of Findings Number: 01-20120548**  
**Individual Income Tax**  
**For the Years 2009-2011**

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**ISSUE**

**I. Individual Income Tax – Imposition.**

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

Taxpayers protest the assessment of individual income tax.

**STATEMENT OF FACTS**

Taxpayers are individuals residing outside Indiana. The husband is a partner in a law firm which conducts a portion of its operations in Indiana. The husband received a form WH-18 which reported Indiana income and tax withheld. Taxpayers filed a return reporting zero Indiana source income. The Indiana Department of Revenue ("Department") determined that Taxpayers had Indiana-source income base on the form WH-18. As a result, the Department disallowed Taxpayers' refund claim and assessed additional tax for 2009 and 2010. Taxpayers protested the assessments and refund denials. The Department conducted an administrative hearing by telephone. Additional facts will be supplied as necessary.

**I. Individual Income Tax – Imposition.**

**DISCUSSION**

Taxpayers protest three years of refund denials and two years of assessments for individual income tax. The issue is whether Taxpayers derived income from Indiana sources and, if so, how much income was so derived.

IC § 6-8.1-5-1(c) provides in relevant part that "[t]he 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 § 6-3-2-2(a) provides in relevant part:

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 to the extent that the income is apportioned to Indiana under this section or if the income is allocated to Indiana or considered to be derived from sources within Indiana under this section.

Income from a pass through entity shall be characterized in a manner consistent with the income's characterization for federal income tax purposes and shall be considered Indiana source income as if the person, corporation, or pass through entity that received the income had directly engaged in the income producing activity.

The husband states that his purported Indiana-source income was based on his status as a "non-capital partner." Taxpayers explain that a "non-capital partner" is a partner who has no ownership stake in the firm and does not earn a share of the law firm's profits. Taxpayers have provided copies of the law firm's partnership agreement, including amendments to the agreement, which substantiate Taxpayers' contentions regarding the voting and profit rights from the law firm. Further, Taxpayers provided a listing of the law firms' non-capital partners and salary information; that list of the non-capital partners included the husband. Based on the information provided, Taxpayers have substantiated that their claimed Indiana income was not from Indiana labor or from a trade or business conducted in Indiana. Instead, Taxpayers have established that their income was from salaries derived outside Indiana. Therefore, Taxpayers' income was not derived from Indiana sources and thus Taxpayers' protest is sustained.

**FINDING**

Taxpayer's protest is sustained.

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