DEPARTMENT OF STATE REVENUE

01-20140105.LOF

Letter of Findings: 01-20140105
Individual Income Tax
For the Tax Year 2012

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 requires the publication of this document in the Indiana Register. The document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective on its date of publication and remains in effect until the date it is superseded by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Indiana residents claiming a credit for out-of-state municipal income tax paid by an Indiana limited liability partnership failed to provide sufficient information to support their argument against the Department's income tax assessment. The taxpayers bear the burden of proving that the Department's assessment is incorrect.

I. Individual Income Tax - Imposition.

Authority: IC § 6-3.5-6-23; IC § 6-8.1-5-1; 45 IAC 3.1-1-74; Columbus City Code § 361.03; Columbus City Code § 361.19; Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579 (Ind. 2014); Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Commissioner's Directive 35 (January 2007).

Taxpayers argue that they are entitled to an Indiana tax credit based on the amount of local income taxes paid by a partnership to another state.

II. Tax Administration - Negligence Penalty.

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

Taxpayers protest the imposition of the negligence penalty.

STATEMENT OF FACTS

Taxpayers are married Indiana residents that filed a joint income tax return for the 2012 tax year. The husband's income included income earned as a partner in an Indiana limited liability partnership ("Indiana Partnership"). Based upon the Indiana Partnership's office locations, the Indiana Partnership had income tax filing obligations in several Ohio cities or municipalities.

Taxpayers claimed a credit for a portion of the Ohio municipal taxes paid by the Indiana Partnership. The Indiana Department of Revenue ("Department") denied the credit and issued a proposed assessment for additional Indiana income tax**.** Taxpayers disagreed with the proposed assessment and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayers explained the basis for the protest. This Letter of Findings results.

DISCUSSION

I. Individual Income Tax - Imposition.

Taxpayers assert that they do not owe the additional Indiana income tax because they paid Ohio municipal income tax. Taxpayers state that they are entitled to a credit for the Ohio tax paid. Taxpayers argue that, because the Indiana Partnership filed and paid Ohio municipal income tax on the Indiana Partnership's income, Taxpayers should receive a credit amounting to the Taxpayers' proportionate share of Ohio municipal income tax paid by the Indiana Partnership against Taxpayers' Indiana income tax due. Taxpayers base their argument on communications with an Ohio municipal tax employee regarding an interpretation of Kentucky income tax administration and an interpretation of Commissioner's Directive 35 (January 2007), 20070221 Ind. Reg. 045070134NRA.

As a threshold issue, it is Taxpayers' responsibility to establish that the existing tax assessment is incorrect. IC § 6-8.1-5-1(c) provides that, "The 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." Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007). "[W]hen [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] defer to the agency's reasonable interpretation of [the] statute even over an equally reasonable interpretation by another party.'" Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579, 583 (Ind. 2014). Thus, all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

To the extent that Taxpayers attempt to clarify provisions of Commissioner's Directive 35 with an Ohio municipal taxing authority regarding Kentucky income tax, the Department acknowledges Taxpayers' efforts. However, without providing any interpretation of Kentucky income tax law, the Department states that Taxpayers' attempt to apply the circumstances and provisions given in Commissioner's Directive 35 to resolve Taxpayers' Ohio and Indiana income tax liabilities is unconvincing.

Columbus City Code § 361.19(c)(2) provides that income tax is imposed "[o]n the net profits earned of all unincorporated businesses, professions, or other activities conducted in the city by nonresidents." The same Code also states that:

> [A]n association shall be taxed as an entity, on the net profits of the association derived from work done or services performed or rendered and business or other activities conducted in the city, whether or not such association has its principal or any place of business located in the city . . . .

Columbus City Code § 361.19(c)(3).

Taxpayers asserted to the Department that the husband's employer is not an association, but a limited liability partnership. The Department does not dispute that the Indiana Partnership is a limited liability partnership. However, the Columbus City Code includes "partnership[s], limited partnership[s], and any other form of unincorporated enterprise owned by two or more persons" in its definition of "association." Columbus City Code § 361.03.

Under 45 IAC 3.1-1-74, "[a]n Indiana resident must report income from all sources, including out-of-state income, in calculating Indiana adjusted gross income tax." Therefore, Taxpayers must report the husband's income earned from the Indiana Partnership on Taxpayers' 2012 Indiana income tax return.

IC § 6-3.5-6-23 does not allow a credit for local taxes paid outside Indiana incurred at the partnership level. The out-of-state municipality did not impose the partnership tax on the Taxpayers, nor does the partnership-level tax flow through to the Taxpayers. The information provided by Taxpayers does not show Taxpayers' liability for the Columbus local tax; nor does the information show that the Indiana Partnership paid the Columbus local tax on behalf of Taxpayers. Therefore, Taxpayers have not met their burden of showing that Taxpayers are entitled to a credit for taxes that were neither imposed on, or due from, Taxpayers.

FINDING

Taxpayers' protest is respectfully denied.

II. Tax Administration - Negligence Penalty.

DISCUSSION

Taxpayers requested that the Department abate the negligence penalty.

Pursuant to IC § 6-8.1-10-2.1(a), the Department may assess a negligence penalty if the taxpayer:

(1) fails to file a return for any of the listed taxes;
(2) fails to pay the full amount of tax shown on the person's return on or before the due date for the return or payment;
(3) incurs, upon examination by the department, a deficiency that is due to negligence;
(4) fails to timely remit any tax held in trust for the state; or

(5) is required to make a payment by electronic funds transfer (as defined in IC 4-8.1-2-7), overnight courier, or personal delivery and the payment is not received by the department by the due date in funds acceptable to the department.

45 IAC 15-11-2(b) further 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.

The Department may waive a negligence penalty when "the taxpayer affirmatively establishes that the failure . . . was due to reasonable cause and not due to negligence." 45 IAC 15-11-2(c). 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." Id. The Department is mindful that "[r]easonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case."

In this instance, Taxpayers displayed efforts and communications that lead them to reasonably believe they could claim a credit for out-of-state municipal income tax paid. Given the totality of the circumstances, the Department is prepared to agree that Taxpayers affirmatively demonstrated that their failure to pay the full amount of tax due for 2012 was due to reasonable cause and not due to negligence.

FINDING

Taxpayers' protest of the negligence penalty is sustained.

SUMMARY

For the reasons discussed above, Taxpayers' protest of the Department's proposed assessment for the 2012 tax year is denied. Taxpayers' protest of the negligence penalty is sustained.

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