DEPARTMENT OF STATE REVENUE

Letter of Findings: 02-20130675
Corporate Income Tax
For Tax Years 2008 through 2010

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This 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 This document is effective as of its date of publication and remains in effect until the date it is superseded by the publication of another document in the Indiana Register.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 conveniences of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Out-of-State Holding Corporation could not use the activities of its subsidiaries that had Indiana activities to claim an Indiana connection for its interest and other investment income receipts that were properly attributed to a place outside of Indiana under Indiana law. Holding Corporation could not include non-income items in its receipts factor. Holding Corporation must redetermine its net operating loss special limitation for non-life subgroup loss based upon the members of its Indiana consolidated return. Holding Corporation could not include net operating losses incurred when filing financial institutions tax in its net operating loss deduction on its adjusted gross income tax return.

ISSUES

I. Corporate Income Tax-Taxable Nexus.

Authority: I.R.C. § 338; IC § 6-3-1-15; IC § 6-3-1-22; IC § 6-3-2-1; IC § 6-3-2-2; IC § 6-3-2-2.2; IC § 6-3-2-2.6; IC § 6-3-4-1; IC § 6-8.1-5-1; 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); Hunt Corp. v. Department of State Revenue, 709 N.E.2d 766 (Ind. Tax Ct. 1999); 45 IAC 3.1-1-32; 45 IAC 3.1-1-55; 28 TAC § 7.7; IRM 4.42.6.1.1 (May 29, 2002); Black's Law Dictionary (8th ed. 2004).

Taxpayer protests the Department's disallowance of Taxpayer's 2010 net operating loss deduction for net operating losses incurred in 2004 and 2005 based upon Taxpayer not having "taxable nexus" with Indiana in 2004 and 2005.

II. Corporate Income Tax-Apportionment Factor: Sales Factor.

Authority: I.R.C. § 338; I.R.C. § 1504; IC § 6-3-1-20; IC § 6-3-1-21; IC § 6-3-1-22; IC § 6-3-1-24; IC § 6-3-2-1; IC § 6-3-2-2; IC § 6-3-2-2.2; IC § 6-3-4-14; IC § 6-8.1-5-1; United States v. New Mexico, 455 U.S. 720 (1982); Kern-Limerick, Inc. v. Scurlock, 347 U.S. 110 (1954); Alabama v. King & Boozer, 314 U.S. 1 (1941); Metcalf & Eddy v. Mitchell, 269 U.S. 514 (1926); Cochrane v. C.I.R, 23 B.T.A. 202 (1931); Burnett v. C.I.R., 356 F.2d 755 (5th Cir. 1966); Levy v. Commissioner, 212 F.2d 552 (5th Cir. 1954); Elick v. CIR, T.C. Memo 2013-139, 2013 WL 2394860 (U.S. Tax Ct. 2013); Fuhrman v. CIR, T.C. Memo 2011-236, 2011 WL 4502290 (U.S. Tax Ct. 2011); Weekend Warrier Trailers v. CIR,. T.C. Memo 2011-105, 2011 WL 1900159 (U.S. Tax Ct. 2011); 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); Treas. Reg. § 1.1502-47; 45 IAC 3.1-1-32; 45 IAC 3.1-1-34; 45 IAC 3.1-1-50; 45 IAC 3.1-1-51; 45 IAC 3.1-1-52; 45 IAC 3.1-1-55.

Taxpayer protests that the Department's adjustments resulted in an understatement of its sales factor for the Short Year Dec 2007, 2008, 2009, and 2010 tax years.

III. Corporate Income Tax-Net Operating Loss: Limitation.

Authority: I.R.C. § 1501; I.R.C. § 1503; I.R.C. § 1504; IC § 6-3-1-15; IC § 6-3-2-2.6; IC § 6-.5-9-4; 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); Treas. Reg. § 1.1502-47; 45 IAC 3.1-1-111.

Taxpayer protests the Department's redetermination of Taxpayer's net operating loss limitation for its consolidated "life" and "non-life" subgroups.

IV. Corporate Income Tax-Net Operating Loss Deduction: Entities Subject to FIT.

Authority: IC § 6-3-1-15; IC § 6-3-2-2.6; IC § 6-5.5-9-4; 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).

Taxpayer protests the disallowance of Taxpayer's 2010 net operating loss deduction from net operating losses incurred in periods when Taxpayer and its bank holding company subsidiary were subject to Indiana's financial institutions tax ("FIT").

STATEMENT OF FACTS

Taxpayer, a parent holding company, is a corporation that was incorporated in Delaware. Taxpayer owns all of the stock of the group of companies, consisting of life insurance companies, non-life insurance companies, and other corporations. Taxpayer first registered to do business in Indiana in 2006. Taxpayer was no longer registered to do business in Indiana by 2008.

For the 2004 and 2005 tax years, Taxpayer filed Indiana adjusted gross income tax returns. For these years, Taxpayer was a holding company. Taxpayer was the holding company for a Texas domestic life insurance company ("Texas Insurance Subsidiary"), which was the parent company of a group of at least three life insurance companies. These three life insurance companies for purposes of this Letter of Findings are designated as Texas Sub 1, Texas Sub 2, and Texas Sub 3. Texas Sub 1 had Indiana direct premiums and filed an Indiana adjusted gross income tax return for 2004 and 2005. Texas Sub 1 had operating authority in two United States territories and in every state except New York. Texas Sub 2 was domiciled outside of Indiana and did not have Indiana direct premiums. Texas Sub 2 had operating authority in five states (Arkansas, Louisiana, Ohio, Oklahoma, and Texas). Texas Sub 3 was an assurance company that did not have direct premiums. Texas Sub 3 had operating authority in two United States territories and in every state except New York. Texas Insurance Subsidiary acquired the stock of Texas Sub 1, Texas Sub 2, and Texas Sub 3 during 2004. Texas Insurance Subsidiary financed the acquisition of these three entities by issuing a surplus debenture to Taxpayer. Texas Insurance Subsidiary's surplus debenture was filed with and accepted by the Texas Department of Insurance. Taxpayer began receiving interest payments from its Texas Insurance Subsidiary's surplus debenture in 2005 and continued to receive interest payments throughout the tax years at issue.

During the 2006 tax year, Taxpayer acquired a bank that was operating in Indiana. Taxpayer as the upper-tier holding company of the bank filed a combined financial institutions tax return with the bank and one other subsidiary, its bank holding subsidiary ("Holding Subsidiary"). During 2007, Taxpayer transferred all of its stock in the bank to its stockholders and, thus, no longer filed a combined financial institutions tax return after the transfer. For the short year January 1, 2007, to June 30, 2007 ("Short Year June 2007"), Taxpayer as the upper-tier holding company filed the combined financial institutions tax return with the bank and Holding Subsidiary. After Taxpayer's transfer of the stock to its shareholders, the bank filed an Indiana financial institutions tax return on a separate return basis. After the transfer, for the short year July 1, 2007, to December 31, 2007 ("Short Year Dec 2007"), Taxpayer filed an Indiana adjusted gross income tax return on a separate company basis. Texas Sub 1, Texas Insurance Subsidiary's only life insurance subsidiary with Indiana direct premiums, continued to file an Indiana adjusted gross income tax return separate from Taxpayer.

For the 2008 tax year, Taxpayer and its subsidiaries filed consolidated federal income tax returns. Taxpayer and its subsidiaries filed their Indiana adjusted gross income tax returns on a separate return basis. The bank filed a separate Indiana financial institutions tax return. Texas Sub 1, Texas Insurance Subsidiary's only life insurance subsidiary with Indiana direct premiums, continued to file an Indiana adjusted gross income tax return separate from Taxpayer.

For the 2009 tax year, Taxpayer filed a consolidated federal adjusted gross income tax return for its non-insurance subsidiaries ("non-life group"). Taxpayer also filed a life insurance company federal consolidated return for its life insurance subsidiaries ("life-group"). For Indiana purposes, Taxpayer filed on a consolidated Indiana adjusted gross income tax return basis for the non-life group entities that did business in Indiana excluding the bank. The bank was subject to and filed a separate Indiana financial institutions tax return. Texas Sub 1, Texas Insurance Subsidiary's only life insurance subsidiary with Indiana direct premiums, continued to file

an Indiana adjusted gross income tax return separate from Taxpayer.

Beginning with the 2010 tax year, Taxpayer filed a joint-consolidated federal adjusted gross income tax return to report Taxpayer and its subsidiaries' income from all of its activities for its two consolidated groups, the life group and the non-life group. For Indiana purposes, Taxpayer also filed a joint-consolidated Indiana adjusted gross income tax return which included its life group and non-life group entities that did business in Indiana excluding the bank. The bank was subject to and filed a separate Indiana financial institutions tax return.

The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayer's business records and tax returns for the 2008 to 2010 tax years. Taxpayer's 2008 and 2009 Indiana adjusted gross income tax returns reported net operating losses that Taxpayer carried forward as a net operating loss deduction in the 2010 tax year. Taxpayer's 2010 return also reported as part of the net operating losses deduction an amount of net operating losses that were incurred in the tax years 2004, 2005, 2006, Short Year June 2007, and Short Year Dec 2007. The Department issued two audit reports (control number ending in 5-08 and control number ending in 9-03). In the reports, the Department made adjustments to Taxpayer's returns which increased Taxpayer's Indiana adjusted gross income and adjusted Taxpayer's apportionment for the 2010 tax year. The Department made adjustments to Taxpayer's Short Year Dec 2007, 2008 and 2009 tax years returns which reduced Taxpayer's 2010 net operating loss deduction as to those net operating losses that Taxpayer reported it incurred in the Short Year Dec 2007, 2008 and 2009 tax years. The Department also disallowed Taxpayer's 2010 net operating loss deduction in full for the net operating losses that Taxpayer reported it incurred in the 2004, 2005, 2006, and Short Year June 2007 tax years. The Department applied what remained of Taxpayer's net operating loss deduction to the 2010 tax year. The Department's adjustments resulted in the Department issuing a proposed assessment of additional adjusted gross income tax and interest for tax year 2010. Taxpayer protested the assessment. An administrative hearing was held, and this Letter of Findings results. Additional information will be provided as necessary.

I. Corporate Income Tax-Taxable Nexus.

DISCUSSION

Taxpayer protests the Department's disallowance of its 2010 net operating loss deduction as to Taxpayer's net operating losses that it reported were incurred in the 2004 and 2005 tax years.

A. Audit Results.

The Department disallowed Taxpayer's net operating losses deductions as to the net operating losses that Taxpayer reported it incurred in the 2004 and 2005 tax years. During 2004 and 2005, the Department determined that Taxpayer had no Indiana property, payroll, or sales and, therefore, had an Indiana apportionment factor of zero for these years. Since Taxpayer's Indiana apportionment factor was zero, Taxpayer lacked taxable nexus in Indiana and did not incur Indiana net operating losses during 2004 or 2005.

1. 2004 Tax Year.

Specifically, the audit made the following findings (on page 8 of the audit report ending in 5-08) as to the 2004 tax year:

> [Taxpayer] reported a [$]4 million dollar Indiana net operating loss in this year. There was no Indiana property and no total property. There was no Indiana payroll or total payroll. There was $26,000 in gross income, which was interest. [Taxpayer] attributed this interest to Indiana in the sales factor of its reported apportionment schedule. This initial Indiana tax return was signed by [a New York Management Company representative, who listed himself as Taxpayer's] secretary/treasurer. The net operating loss resulted primarily from $3.4 million in interest expense that was interest expense on a note payable that was generated as part of the acquisition [of Texas Sub 1, Texas Sub 2, and Texas Sub 3 by Texas Insurance Subsidiary and others entities by Taxpayer]. Interest income was minimal and was attributable to the checking account and investments. The interest expense and over $400,000 in travel expenses, some of the larger corporate expenses, resulted from the acquisition transactions[.] [The acquisition transactions] were controlled by the [New York Management Company], the out of state investor and originator of [Taxpayer]. [Taxpayer] attributed the 4 million dollar loss 100[percent] to Indiana based on its apportionment calculation, which due to [Taxpayer reporting it has] no property or payroll, was calculated on sales/gross income. The [$26,000] of gross income reported by [Taxpayer] in the sales factor was not from Indiana operations, but resulted from interest on investment/bank account[(s)] from the investment and acquisition [that was

> administered and controlled by the New York Management Company]. [Taxpayer's] operating subsidiaries were not filing a consolidated return with [Taxpayer] at this time, and [Taxpayer] was operating solely as an acquisition entity and stock holding company. [Taxpayer] was not registered to do business in the state of Indiana. The tax return was signed by a representative of [New York Management Company] and the travel expense deduction is presumably attributable to the travel of the investors. [Taxpayer] had no property or payroll in Indiana [or anywhere] and the only income generated was investment income which should be attributed to the state of commercial domicile, which in this year would be the commercial domicile of the investors. [Taxpayer's] gross income is reclassified as non-Indiana per audit resulting in 0[percent] apportionment for the total sales factor.

In summary, the Department's audit removed the $26,000 of receipts from the sales factor numerator leaving Taxpayer with no Indiana property, payroll, or sales and, therefore, an Indiana apportionment factor of zero. Without an Indiana apportionment factor, Taxpayer does not have taxable nexus in Indiana. Thus, the Department disallowed the amount of Taxpayer's 2010 net operating loss deduction taken for a net operating loss incurred in Indiana for the 2004 tax year.

2. 2005 Tax Year.

Specifically, the audit made the following findings (on pages 8-9 of the audit report ending 5-08) as to the 2005 tax year:

> [Taxpayer] reported a [$]1.8 million dollar Indiana net operating loss in this year. There was no Indiana property and no total property. There was no Indiana payroll, but there was total payroll reported of $147,149. There was approximately $8.6 million in gross income. Interest income from the surplus debentures issued as part of the acquisition [of Texas Sub 1, Texas Sub 2, and Texas Sub 3 by Texas Insurance Subsidiary] account for [$8.4 million]. The balance of the remaining reported income was from investments and interest on checking. The taxpayer reported that the entire gross income was attributed 100[percent] to Indiana in the sales factor of its reported apportionment. This yielded a reported apportionment percentage of [over 60] percent. Primary expenses included $7.4 million in interest expense related of the acquisition and a $3.5 million . . . management fee paid to [New York Management Company], the out of state investors and corporate managers. The [$]8.6 million in income reported as Indiana gross income in the apportionment sales factor by [Taxpayer] is reclassified as non-Indiana per audit. The 8.4 million in interest from the surplus debenture was attributable to the acquisition transaction and was originated, controlled and managed by the out of state management group, [New York Management Company]. The investment income and interest on the checking should be allocable to the state of commercial domicile and with no Indiana property or payroll; Indiana was not a commercial headquarters for the taxpayer. [New York Management Company] received [$]3.5 million in management fees as compensation for management services in this year when the total payroll for [Taxpayer] was only $147,000. Based on the dollars, [New York Management Company], domiciled outside of Indiana was in control. Additionally, the payroll that [Taxpayer] did incur was outside of Indiana and [Taxpayer] was not registered to do business in Indiana. Based on the [Taxpayer's] filing election the operating subsidiaries were not filing a consolidated return with [Taxpayer] at this time and [Taxpayer] was operating solely as an acquisition entity and stock holding company. The reclassification of the gross income of $8.6 million results in a 0[percent] Indiana apportionment for this year.

In summary, the Department's audit removed the $8.6 million of interest income from the sales factor numerator leaving Taxpayer with no Indiana property, payroll, or sales and, therefore, an Indiana apportionment factor of zero. Without an Indiana apportionment factor, Taxpayer did not have taxable nexus in Indiana for 2005. Thus, the Department disallowed the amount of Taxpayer's 2010 net operating loss deduction taken for a net operating loss incurred in Indiana for the 2005 tax year.

B. Taxpayer's Response.

Taxpayer protests the Department's determination that it did not incur Indiana net operating losses during 2004 and 2005. Taxpayer argues that its apportionment factor is not zero because all of its interest income receipts were properly attributed to Indiana and belong in its sales factor numerator. Therefore, Taxpayer asserts that its Indiana apportionment factor was not zero, it had taxable nexus in Indiana in 2004 and 2005, and it incurred Indiana net operating losses during 2004 or 2005.

As to Taxpayer's 2004 and 2005 investment/bank accounts interest income receipts, Taxpayer states that the auditor incorrectly attributed those receipts based upon its commercial domicile and asserts that instead those receipts are properly attributed under 45 IAC 3.1-1-55 to the "receipt's business situs," which was Indiana.

Taxpayer maintains that the receipts have an Indiana business situs "because the investment activity that gave rise to those receipts was performed in Indiana." Alternatively, Taxpayer claims that even if the receipts are attributed to Taxpayer's place of commercial domicile, its commercial domicile was in Indiana for 2004 and 2005. Taxpayer claims that when it responded to the auditor's original request for information and told the auditor that its commercial domicile was in Texas, this was only true for the 2008, 2009, and 2010 tax years. Taxpayer further states that the "Auditor assumes that [Taxpayer] was managed by the members of the [New York Management Company] . . . [and] [h]er assumption is not supported by fact." Taxpayer claims that Indiana is its place of its commercial domicile because the "executive authority of [Taxpayer] was not centralized in one state in 2004 and 2005" and Indiana is the "place where the majority of [Taxpayer's] daily operational decisions were made." Taxpayer states that on "the application for approval filed with the Indiana Department of Insurance on June 24, 2004, [Taxpayer stated that it] was 'formed with the sole purpose of entering into a Purchase Agreement with [seller, an Indiana corporation,] to acquire [Texas Sub 1, Texas Sub 2, Texas Sub 3, and the other companies]' [and] [a]ll of these subsidiaries were domiciled in and/or managed from [Indiana] at the time of the acquisition." Taxpayer further states that "[a]fter the acquisition, the day to day operations of [Taxpayer] and the [acquired subsidiaries] continued to be managed from [Indiana]." In support of this statement, Taxpayer's protest letter provides "five facts" that, other than its bare assertions, were not supported with documentation and were contrary to publically available information and the relevant findings of fact in the audit report and, therefore, will not be restated here.

Additionally, as to the surplus debenture interest income it received in 2005, Taxpayer asserts that the auditor improperly attributed the receipts based upon its commercial domicile. Taxpayer states that those receipts are properly attributed to Indiana under IC § 6-3-2-2.2(c). Taxpayer maintains the surplus debenture receipts are attributed to Indiana under IC § 6-3-2-2.2(c) because "(1) the Surplus Debenture is an installment loan not secured by real or tangible personal property and (2) the proceeds of such loan were applied in Indiana when [Taxpayer's Texas Insurance Subsidiary] paid the loan proceeds to [the seller, an Indiana Corporation,] in [Indiana]."

C. Hearing Analysis.

As a threshold issue, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "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). Consequently, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Further, "when [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) (internal citation omitted). Thus, all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

A corporation's Indiana net operating loss deduction is determined under IC § 6-3-2-2.6(c) as "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." (Emphasis added). Thus, a net operating loss must be incurred by an entity that is a taxpayer for that taxable year.

A "taxpayer" is defined in IC § 6-3-1-15 as "any person or any corporation subject to taxation under this article." Corporations that are subject to tax under IC 6-3 – i.e., that have taxable nexus in Indiana–are those corporations that have "adjusted gross income from sources within Indiana." IC § 6-3-2-1(b); IC § 6-3-4-1(3). For a corporation to have "adjusted gross income from sources within Indiana," the corporation must have either Indiana apportionment factors resulting in deemed Indiana business income/loss or nonbusiness income/loss that is allocated to Indiana. IC § 6-3-2-2. See Hunt Corp. v. Department of State Revenue, 709 N.E.2d 766, 781 (Ind. Tax Ct. 1999) (explaining that a corporation that has neither apportionment factors in Indiana nor nonbusiness income that is allocated to Indiana does not have adjusted gross income from Indiana sources).

Indiana imposes an adjusted gross income tax on "income derived from sources within Indiana of every corporation." IC § 6-3-2-1(b). IC § 6-3-2-2(a)(2) provides that "income derived from sources in Indiana" includes "income from doing business in this state." If a corporation's income "is derived from sources within the state of Indiana and from sources without the state of Indiana," the income apportioned to Indiana for tax purposes is calculated by multiplying the corporation's total income by the Indiana apportionment factor. IC § 6-3-2-2(b). For the years at issue, the Indiana apportionment factor formula was based upon three factors one of which was a

"sales factor." IC § 6-3-2-2(b). "The sales factor is a fraction, the numerator of which is the total sales of the taxpayer in this state during the taxable year, and the denominator of which is the total sales of the taxpayer everywhere during the taxable year." IC § 6-3-2-2(e).

Taxpayer's "sales" receipts, at issue, consist of interest income receipts from its investment bank account(s) and from its surplus debenture.

1. Interest Income: Investment/Bank Account(s).

Taxpayer received interest income receipts from its investment/bank account(s) during the 2004 and 2005 tax years. The Department determined that Taxpayer's investment/bank accounts receipts were attributable to a place outside of Indiana. Taxpayer maintains that the auditor incorrectly attributed these receipts. Taxpayer states that the auditor improperly attributed the receipts based upon its commercial domicile and asserts that instead those receipts are properly attributed under IC § 6-3-2-2(f)(1) and 45 IAC 3.1-1-55 to the "receipt's business situs," which was Indiana.

For sales factor apportionment purposes, receipts from intangible property that are not specifically attributed under IC § 6-3-2-2.2, giving rise to a corporation's income, are attributed to Indiana if "the income-producing activity is performed in this state." IC § 6-3-2-2(f)(1). Therefore, the receipts from the intangible property are Indiana receipts to the extent that the "income-producing activity is performed in this state" and are included in the sales factor numerator. IC § 6-3-2-2(f)(1). When the "income-producing activity" for a transaction is performed in Indiana, the receipts from the transaction are included in the numerator under IC § 6-3-2-2(f)(1). Thus, to the extent that the transaction's "income producing activity" is performed in Indiana, the income from the transaction is included in the Indiana numerator. Conversely, to the extent that an "income producing activity" for a transaction is performed outside Indiana, then the income from the transaction is generally excluded from the Indiana numerator.

"Income producing activity" is defined as "the act or acts directly engaged in by the taxpayer for the ultimate purpose of obtaining gains or profit." 45 IAC 3.1-1-55. Income producing activity is "deemed performed at the situs of . . . intangible personal property. . . ." Id. "The situs of intangible personal property is the commercial domicile of the taxpayer (i.e., the principal place from which trade or business of the taxpayer is directed or managed), unless the property has acquired a 'business situs' elsewhere." Id. "'Business situs' is the place at which intangible personal property is employed as capital; or the place where the property is located if possession and control of the property is localized in connection with a trade or business so that substantial use or value attaches to the property." Id.

Accordingly, the receipts from the intangible property not specifically attributed under IC § 6-3-2-2.2 are attributed to Indiana based upon the "business situs" of the intangible property and the commercial domicile of the Taxpayer. IC § 6-3-2-2(f)(1) and 45 IAC 3.1-1-55. When the intangible property has not "acquired a business situs" outside of Indiana and the commercial domicile of the taxpayer is in Indiana, the receipts are attributed to Indiana. 45 IAC 3.1-1-55. In addition, when the intangible property has "acquired a business situs" in Indiana and the commercial domicile of the taxpayer is outside of Indiana, the receipts from the intangible property are attributed to Indiana. Id. However, when neither the taxpayer's commercial domicile nor the "acquired business situs" of the intangible property are in Indiana, the receipts from the intangible property are attributed to a place outside of Indiana.

During the 2004 and 2005 tax years, Taxpayer received interest income from its investment/bank account(s). The Department removed the interest income from Taxpayer's sales factor numerator and attributed these receipts to Taxpayer's commercial domicile that was outside of Indiana. Taxpayer maintains that it properly included these receipts in the sales factor numerator under IC § 6-3-2-2(f)(1) and 45 IAC 3.1-1-55 because the "receipts have a business situs in Indiana" and are attributed to Indiana.

Taxpayer is mistaken in its application of the law. Taxpayer suggests that 45 IAC 3.1-1-55 would determine the attribution of the receipts from the intangible property based upon the "receipt hav[ing] a business situs" in a particular location. However, as provided above, pursuant to 45 IAC 3.1-1-55, it is when the "intangible property" from which the receipts are derived has "acquired a business situs" in Indiana and the commercial domicile of the taxpayer is outside of Indiana that the receipts from the intangible property are attributed to Indiana. Therefore, Taxpayer must demonstrate that 1) the intangible property from which Taxpayer received the interest income has "acquired a business situs" at a place other than Taxpayer's Texas commercial domicile and 2) that intangible property has "acquired a business situs" in Indiana.

"Business situs" is explained in 45 IAC 3.1-1-55, which states, in relevant part:

> "Business situs" is the place at which intangible personal property is employed as capital; or the place where the property is located if possession and control of the property is localized in connection with a trade or business so that substantial use or value attaches to the property. Example: Taxpayer, a corporation whose principal business activity is the manufacture and sale of hot water heaters, obtains notes for the sale of such water heaters in connection with its Indiana business activity. The property has a business situs in this state, therefore, interest income derived from such notes is attributable to this state.

Based upon the facts presented, Taxpayer received interest income from its investment/bank account(s). Taxpayer's business is that of a traditional holding company formed by a group of investors. Taxpayer holds these investment/bank accounts to perform its business as a traditional holding company. Taxpayer failed to present documentation/information that demonstrated that Taxpayer's investment/bank account(s) had a business situs away from its commercial domicile. Specifically, Taxpayer has failed to present documentation/information that demonstrated the investment/bank account(s) were "employed as capital" by Taxpayer or that Taxpayer's "possession and control of the [investment/bank account(s)] [were] localized in connection with [Taxpayer's holding company] business so that substantial use or value attache[d] to the [investment/bank account(s)]" in any specific place. Moreover, based on the facts presented, the Department presumes if Taxpayer's investment/bank account(s) were "employed as capital" in Taxpayer's holding company business or were "localize[d] in connection with Taxpayer's holding company business," these happenstances would not occur at any place other than Taxpayer's commercial domicile.

Therefore, Taxpayer's intangible property–i.e. its investment/bank account(s)–has not acquired a "business situs" away from its commercial domicile. Taxpayer's business is that of a traditional holding company formed by a group of investors. During 2004, Taxpayer had no employees and owned no property other than intangible property–i.e., the stock of the subsidiaries and its investment/bank account(s). During 2005, Taxpayer had only $147,000 of employee expense(s) and owned no property other intangible property–i.e., the stock of the subsidiaries and its investment/bank account(s). Taxpayer states it was formed for "the sole purpose of entering into a Purchase Agreement with [seller, an Indiana corporation,] to acquire [of Texas Sub 1, Texas Sub 2, and Texas Sub 3 for its Texas Insurance Subsidiary and the other companies for itself]."

IC § 6-3-1-22 provides that "'commercial domicile' means the principal place from which the trade or business of the taxpayer is directed or managed." Further, 45 IAC 3.1-1-32, states:

> The term "commercial domicile" is defined in the Act as "the principal place from which the trade or business of the taxpayer is directed or managed." Commercial domicile is not necessarily in the state of incorporation. A corporation that is incorporated in a state, but that has little or no activity in that state, has not established a commercial domicile there.
>
> Each corporation has one, and only one, commercial domicile. Generally, it is where the executive authority of the business is concentrated. However, if such authority is not centralized in one state, then the commercial domicile is the place where the majority of the corporation's daily operational decisions are made. There are several factors to be considered in determining the commercial domicile of a corporation. These factors include, but are not limited to:
> (a) The relative amount of revenue from sales in the various states
> (b) The relative value of fixed assets in the various states
> (c) The principal place of work of a majority of the employees
> (d) The place where the corporate records are kept
> (e) The principal place of work of the corporate executives
> (f) The place where policy and investment decisions are made
> (g) The relative amount of decision-making power held by various executives and employees
> (h) The place where payments are made on intangibles held by the corporation
> (i) Whether income from intangibles held by the corporation is taxable elsewhere
> (j) The office from which the Federal income tax return is filed
> (k) Information contained in the corporation's annual and quarterly reports
> (l) The place where the board of directors meets.

While this regulation provides that generally a taxpayer's commercial domicile "is where the executive authority of the business is concentrated" or "the place where the majority of the corporation's daily operational decisions are made." The regulation provides a nonexclusive list of factors that are weighed to help determine the "commercial domicile of the taxpayer"–i.e. "the principal place from which the trade or business of the taxpayer is directed or

managed." Therefore, the determination of the taxpayer's commercial domicile is a fact sensitive question based upon weighing the particular circumstances of the taxpayer.

Taxpayer maintains its "executive authority (i.e. its board of directors and executive officers)" is not centralized or concentrated in one state because Taxpayer's directors/officers reside in different states (New York, Connecticut, and Texas). Additionally, Taxpayer argues that the auditor has incorrectly imputed the activities /domicile of New York Management Company as Taxpayer's activities/domicile. Lastly, Taxpayer maintains that both Taxpayer's "daily operations" are conducted in Indiana and its domicile was in Indiana for the 2004 and 2005 tax years.

However, the Department disagrees. Based upon the facts presented, Taxpayer's executive authority was concentrated in one state, New York, and Taxpayer's documentation presented during the hearing affirms that it was managed and controlled by New York Management Company during 2004 and 2005. During 2004 and 2005, Taxpayer's trade of business is that of a traditional holding company. During 2004, Taxpayer had no employees and in 2005 reported a de minimis, non-Indiana total payroll expense of $147,000. Taxpayer had a board of directors that were also Taxpayer's executive officers. Thus, it was only Taxpayer's board of directors/executive officers who were available to direct or manage Taxpayer's holding company activities.

Taxpayer presented the minutes for Taxpayer's board of directors meetings. During 2004, all of the board meetings were held in New York. During 2005, Taxpayer's board meetings were held or scheduled to be held in New York, except one that was rescheduled from its New York location to be held in Maine at the home of a recently deceased, former board member within days of his funeral. Taxpayer's protest letter states that in 2004 and 2005 Taxpayer had five officers–of which four were Taxpayer's shareholders and the fifth was the son of one of the shareholders. Taxpayer's four shareholder-officers were also members of New York Management Company that is headquartered in New York.

Additionally, during the protest, Taxpayer presented a "purchase agreement" for the July 1, 2004, acquisition of Texas Sub 1, Texas Sub 2, and Texas Sub 3 by Taxpayer's Texas Insurance Subsidiary and the acquisition of other entities by Taxpayer and/or one of its other subsidiaries from an Indiana corporation ("July 1, 2004, Purchase Agreement"). The July 1, 2004, Purchase Agreement provides, in Schedule A, these relevant facts in the recitals "[Seller, an Indiana corporation,] is currently negotiating with [New York Management Company] relating to the purchase by **a company formed and controlled by [New York Management Company]** and/or its principals ("Purchaser"), [–i.e., Taxpayer,] . . . ." (**Emphasis added**). During the protest, Taxpayer also presented a "management fee agreement" between Taxpayer and New York Management Company, effective as of May 16, 2006, for the continued management services to be performed by New York Management Company for Taxpayer after that date ("Management Fee Agreement"). The Management Fee Agreement provides these relevant facts in the recitals of the agreement:

> 1) "Members of [New York Management Company] were instrumental in the formation and organization of [Taxpayer], as well as the acquisition of [Texas Sub 1, Texas Sub 2, Texas Sub 3, other entities from the Indiana corporation] in July 2004 (the 'Acquisition') . . . .
>
> 2) "Members of [New York Management Company] were instrumental in arranging the financing of the Acquisition . . . ."
>
> 3) During the financing of the Acquisition, "restrictions were negotiated regarding three types of fees (transaction, management, and transaction advisory fees) that Taxpayer could pay to Affiliates, with the [New York Management Company] in mind . . . ."
>
> 4) "Members of [New York Management Company] have served as officers and continue to serve in certain positions as advisors of [Taxpayer] . . . ."
>
> 5) "[Taxpayer] does not yet separately maintain the full internal capability to perform all necessary management, financial and administrative functions which [Taxpayer] requires . . . ."
>
> 6) "[Taxpayer, in January 2006,] hired an executive to serve as the new President and CEO . . . ."
>
> 7) "[T]he new executive has assumed some of the duties previously carried out by Members of [New York Management Company] . . . ."
>
> 8) "[Taxpayer] desires to continue receiving some of the management, financial and administrative services provided by [New York Management Company], if, as and when requested by the CEO of [Taxpayer], for a

set period of time until the entire new management team is trained and integrated."

Based upon the recitals in the Management Fee Agreement and July 1, 2004, Purchase Agreement, Taxpayer lacked the capacity to manage itself during 2004 and 2005 and was directly managed and controlled by the members of the New York Management Company during this time. Taxpayer's four shareholder-officers were also members of this New York Management Company, which Taxpayer, the publically available information, and the audit report all affirm was headquartered in New York. Taxpayer's board of directors meeting minutes provide that its 2004 board meetings were held in New York. Taxpayer's board of directors meeting minutes provide that its 2005 board meetings were held or were scheduled to be held in New York, except one that was rescheduled from its New York location to be held at the home of a recently deceased, former board member within days of his funeral. During the protest, Taxpayer also presented a promissory note that was issued by Taxpayer on July 1, 2004, to Indiana Corporation. This promissory note attested that Taxpayer's principal executive office was in Maine, designated New York as the place for all litigation, and designated New York law as the governing law. Taxpayer did not register to do business in Indiana until 2006. During 2004, Taxpayer reported it had no employees. During 2005, Taxpayer reported $147,000 in total payroll expenses, none of which was attributed to employee(s) located in Indiana. During 2004 and 2005, Taxpayer reported that it had no property other than intangible property–i.e., the stock of the subsidiaries and its investment/bank account(s).

Upon review the facts presented, Taxpayer had a domicile outside of Indiana. Based upon the facts presented, the place from which Taxpayer's board of directors/executive officers directed or managed was not in Indiana. Based upon the facts presented, Taxpayer did not have any employees or property in Indiana, did not have a concentration of board of directors/officers that directed or managed from a place in Indiana, did not have a principal executive office in Indiana, did not have daily operational activities that were conducted by Taxpayer's director/officers or employees in Indiana. Moreover, based upon the facts presented, Taxpayer did not have bank/investment account(s) which acquired a business situs in Indiana. Since Taxpayer neither had bank/investment account(s) which acquired a business situs in Indiana nor a commercial domicile in Indiana, Taxpayer did not have income from an intangible with "income-producing activity" in Indiana. Thus, the only conclusion available is that the "income-producing activity" for Taxpayer's interest income from its investment/bank account(s) is attributed to a place outside of Indiana.

Therefore, Taxpayer has not met its burden of proving that the audit's determination–that the $26,000 of investment/bank account(s) interest income receipts from the 2004 tax year and the $200,000 of investment/bank account(s) interest income receipts from the 2005 tax year should be attributed to a place outside of Indiana–was incorrect as prescribed under IC § 6-8.1-5-1(c). Given the totality of the circumstances, in the absence of other supporting documentation, the Department's audit properly excluded the investment/bank account(s) interest income from the sales factor numerator. Taxpayer's protest of the Department's adjustment to remove its investment/bank account(s) interest income from the numerator of the sales factor in the 2004 and 2005 tax years is denied.

2. Interest Income: Surplus Debenture.

Taxpayer received surplus debenture interest income receipts during the 2005 tax year. The Department determined that Taxpayer's surplus debenture interest income receipts were attributable to a place outside of Indiana. Taxpayer maintains that the auditor incorrectly attributed these receipts. Taxpayer maintains the surplus debenture receipts are attributed to Indiana under IC §6-3-2-2.2(c) because "(1) the Surplus Debenture is an installment loan not secured by real or tangible personal property and (2) the proceeds of such loan were applied in Indiana when [Taxpayer's Texas Insurance Subsidiary] paid the loan proceeds to [the seller, an Indiana Corporation,] in [Indiana]."

For sales factor apportionment purposes, receipts from intangible property that are specifically attributed to Indiana under IC § 6-3-2-2.2 are receipts derived from sources within Indiana for the sales factor numerator. IC § 6-3-2-2(e). IC § 6-3-2-2.2(c) provides the attribution of interest income from unsecured commercial loans and installment obligations.

Taxpayer maintains that the surplus debenture is an unsecured installment loan. Taxpayer asserts that, pursuant to the surplus debenture, Taxpayer "loaned" Texas Insurance Subsidiary over $100 million dollars that was required to be repaid in "annual installments of principle and interest each year from 2006 to 2012." Texas Insurance Subsidiary started repayment early making its first payment in 2005 and repaid the entire surplus debenture early making its last payment in 2010.

An "installment loan" is "[a] loan that is to be repaid in usu. equal portions over a specific period of time." Black's

Law Dictionary 955 (8th ed. 2004). Additionally, a "debenture" is "[a] debt secured only by the debtor's earning power, not by a lien on any specific assert." Id. 430. The Internal Revenue Manual, in relevant part, states that a "surplus debenture" is:

> Generally, an unsecured interest-bearing note carried as an equity contribution (normally made by shareholders or affiliates) to prevent a surplus deficiency by the borrowing company. The debenture is normally worded to require repayment only from future earnings of the company and this repayment generally requires the approval of the state insurance commissioner.

IRM 4.42.6.1.1 (May 29, 2002). Lastly, the Texas regulations under which Taxpayer's Texas Insurance Subsidiary applied for and received approval for this surplus debenture defines a "surplus debenture" as "[a]ny contingent indebtedness issued by an insurer for which such insurer assumes a subordinated liability for repayment of principal and payment of interest pursuant to a written agreement providing for payment only out of that portion of an insurer's surplus that exceeds a minimum surplus stated in such agreement." 28 TAC § 7.7(a)(3).

Therefore, the Department agrees that Taxpayer correctly states that its surplus debenture is an unsecured commercial loan or installment obligation, and the receipts from its surplus debenture are properly attributed under IC § 6-3-2-2.2(c).

Taxpayer maintains that when IC § 6-3-2-2.2(c) is applied to the receipts in question, the receipts are attributed to Indiana because the entity from which Texas Insurance Subsidiary bought the stock of Texas Sub 1, Texas Sub 2, and Texas Sub 3 was a corporation that was domiciled in Indiana. However, Taxpayer is mistaken in its results of its application of IC § 6-3-2-2.2(c) to the receipts in question. When IC § 6-3-2-2.2(c) is applied to the receipts in question, Taxpayer's receipts are not attributed to Indiana.

IC § 6-3-2-2.2(c) provides, as follows:

> Interest income and other receipts from commercial loans and installment obligations not secured by real or tangible personal property are attributable to this state if the proceeds of the loan are to be applied in Indiana. If it cannot be determined where the funds are to be applied, the income and receipts are attributable to the state in which the business applied for the loan. As used in this section, "applied for" means initial inquiry (including customer assistance in preparing the loan application) or submission of a completed loan application, whichever occurs first.

Accordingly, the interest income from the unsecured commercial loans and installment will be attributed to Indiana when the place where the funds are to be applied can be determined and that place is in Indiana. However, if the place where the funds are to be applied is indeterminable, then the interest income is attributed to the place where the "business applied for the loan." Therefore, the question becomes if the place where the funds/proceeds of the loan are to be applied can be determined by the lender. In other words, the facts and circumstances must be examined to establish whether the lender could determine how the borrower planned to use the borrowed funds–i.e., was it known by the lender at the time of the loan what the borrower planned to buy with the loan proceeds, and if so, where was it located. If the lender could not determine how the borrower planned to use the funds at the time of the loan, then the place where the borrower applied for loan with the lender is the place where the lender is to attribute the income from the loan.

In the instant case, Taxpayer "loaned" Texas Insurance Subsidiary "funds" when Texas Insurance Subsidiary issued a surplus debenture to Taxpayer. The surplus debenture provided that the funds will be used to buy the stock of Texas Sub 1, Texas Sub 2, and Texas Sub 3 pursuant to the July 1, 2004, Purchase Agreement. The July 1, 2004, Purchase Agreement required that the acquisition transaction be reported as an acquisition of assets under an I.R.C. § 338(h)(10) election. Therefore, the loan proceeds of the surplus debenture were "to be applied" on the purchase of Texas Sub 1's, Texas Sub 2's, and Texas Sub 3's assets.

However, neither the July 1, 2004, Purchase Agreement nor the surplus debenture provided how much of the funds borrowed were to be applied generally to each of Texas Sub 1, Texas Sub 2, and Texas Sub 3 let alone to each of the assets of Texas Sub 1, Texas Sub 2, and Texas Sub 3. Moreover, Texas Sub 1, Texas Sub 2, and Texas Sub 3 are life insurance companies that are domesticated in different states, have certificates of operating authority in multiple states, and have assets in multiple states. Specifically, Texas Sub 1 was registered as an Indiana domestic life insurance company with certificates of authority in 49 states, the District of Columbia, and Puerto Rico, and had assets in multiple states including Indiana. Texas Sub 2 was registered as an Arkansas domestic life insurance company with certificates of authority in five states–none of which is Indiana–and had assets in multiple states. Texas Sub 3 was registered as an Indiana domestic life assurance company with

certificates of authority in 49 states, the District of Columbia, and Puerto Rico and had assets in multiple states. Therefore, the loan proceeds of the surplus debenture were "to be applied" on the purchase of Texas Sub 1's, Texas Sub 2's, and Texas Sub 3's assets that were located in multiple states. Since neither the July 1, 2004, Purchase Agreement nor the surplus debenture provided how much of the funds borrowed were to be applied to each of the assets that were located in multiple states, neither the amount nor the place where the surplus debenture proceeds were applied could be determined from the surplus debenture or the July 1, 2004, Purchase Agreement.

As provided above, pursuant to IC § 6-3-2-2.2(c), when the lender cannot determine where the borrower would apply the funds, the lender's income and receipts are attributed to the state where its customer applied for the loan. Thus, the issue is determining the location where Texas Insurance Subsidiary "applied" for its surplus debenture with Taxpayer.

Taxpayer, under the control and management of the New York Management Company, agreed to "loan" Taxpayer's Texas Insurance Subsidiary the financing under a surplus debenture that was required to be approved by, was approved by, and was registered with the Texas Department of Insurance. As provided above in the recitals of the Management Fee Agreement and the July 1, 2004, Purchase Agreement, Taxpayer did not have the capacity to manage itself during 2004 and 2005 and was managed and controlled by the members of the New York Management Company who "were instrumental in arranging the financing of the [acquisition of Texas Sub 1, Texas Sub 2, and Texas Sub 3]." Based upon the facts presented, the place where Taxpayer's Insurance Subsidiary applied for the surplus debenture would be either in New York–where the New York Management Company planned the acquisition–or in Texas–where the surplus debenture was registered with and approved by the Texas Department of Insurance. Thus, the only conclusion possible is that the place where Taxpayer's Insurance Subsidiary applied for the surplus debenture was a place outside of Indiana and the interest income from the surplus debenture is not attributed to Indiana under IC § 6-3-2-2.2(c). Therefore, Taxpayer has not met its burden of proving that the audit's determination–that the over $8 million of interest income receipts from the surplus debenture should be attributed to a place outside of Indiana–was incorrect as prescribed under IC § 6-8.1-5-1(c). Given the totality of the circumstances, in the absence of other supporting documentation, the Department's audit properly excluded the surplus debenture interest income from the sales factor numerator. Taxpayer's protest of the Department's adjustment–to remove its over $8 million of interest income from the surplus debenture from the numerator of the sales factor in the 2005 tax year–is denied.

In summary, based upon the facts presented, Taxpayer has not met its burden of proving that the audit's determination–that the interest income receipts from the bank/investment account(s) from the 2004 and 2005 tax year should be attributed to a place outside of Indiana–is incorrect. Based on the facts presented, Taxpayer has not met its burden of proving that the audit's determination–that the over $8 million of interest income receipts from the surplus debenture should be attributed to a place outside of Indiana–was incorrect. Accordingly, Taxpayer's protest to the removal of its interest income receipts from the numerator of the sales factor resulting in the disallowance of the net operating loss deduction for the net operating losses incurred in the 2004 and 2005 tax year is denied.

FINDING

Taxpayer's protest of the Department's disallowance of Taxpayer's net operating loss deductions for net operating losses incurred in 2004 and 2005 is respectfully denied.

II. Corporate Income Tax-Apportionment Factor: Sales Factor.

DISCUSSION

Taxpayer protests the Department's adjustments to its sales factor that resulted in the reduction of Taxpayer's net operating loss deduction and the assessment of tax in the 2010 tax year. Taxpayer asserts that the Department's exclusion of its short term investment interest income, capital gains, other investment income, dividends, surplus debenture interest income, and "rebill receipts" from Taxpayer's sales factor numerator and/or denominator for the Short Year Dec 2007, 2008, 2009, and 2010 tax years was improper.

A. Audit Results.

For the 2010 tax year, the audit made the following findings (on pages 12-13 of the audit report ending in 9-03), provided in relevant part:

Numerator [Adjustments]

. . .

3.) [Taxpayer's subsidiary] performed services and paid bills for affiliates and billed the affiliates the actual cost of performing the services of paying the bills plus a mark-up to compensate it for its administrative services. The gross income of these intercompany charges was included in the numerator by the taxpayer. Intercompany income of affiliates included in the consolidated return is not included in the numerator of the sales factor. The intercompany income is eliminated from the numerator of the sales factor per audit.

4.) . . . [Taxpayer's] income that was included in the numerator of the sales factor was composed of investment interest and other investment income that was not intercompany in nature. In CY 2010 the [Taxpayer's] executive officers and commercial domicile were Texas and the interest income and other income are considered intangible income attributable to Texas. An adjustment is made per audit to remove [Taxpayer's] income from the numerator.

5.) [Taxpayer's subsidiary's] interest income was included in the numerator of the sales factor. . . . That income is removed from the numerator per audit.

Denominator [Adjustments]

1) [Taxpayer] received intercompany dividend income of $5,000,000, but erroneously eliminated $500,000 when determining its intercompany eliminations for the denominator of the sales factor. The remaining $4,500,000 was eliminated per audit.

. . .

3.) [Taxpayer's Subsidiary's] intercompany income from billing its administrative services to its affiliates that was eliminated from the numerator also needs to be eliminated from the denominator of the sales factor.

4.) [Taxpayer's Subsidiary's] intercompany interest income removed from the numerator of the sales factor also needs to be removed from the denominator of the sales factor.

In summary, the Department's audit removed approximately $54 million of receipts from the sales factor numerator and $57 million of receipts from the sales factor denominator. The Department's total audit adjustments resulted in over a 16 percent reduction to Taxpayer's Indiana apportionment factor for the 2010 tax year.

For the 2009 tax year, the audit made the following findings (pages 7-9 of the audit report ending in 9-03), which are provided in relevant part:

Total gross income received by [Taxpayer] in CY 2009 was approximately [$]17.3 million. Components of this income were [$]7.5 million in interest income, [$]1.2 million in capital gains, [$]2.7 million in dividends, and [$]5.7 million in rebill income. A review of [Taxpayer's] apportionment workpapers revealed that these receipts were classified as 100 [percent] Indiana. The audit proposes to adjust the [Taxpayer's] Indiana gross income for apportionment purposes from Indiana to out of state sources. An adjustment is also proposed to exclude non-income items from the sales factor calculation.

. . .

The interest income from the surplus debenture is not attributable to the state of Indiana. It originates from a transaction that was devised by [New York Management Company] as part of the acquisition of [Texas Sub 1, Texas Sub 2, Texas Sub 3 for Texas Insurance Company]. [Taxpayer's] management agreement with [New York Management Company] (agreement active from 2006-2010) acknowledges [New York Management Company's] role in the financing of the acquisition and specifies the ongoing services provided by [New York Management Company] as providing consultation and assistance with business strategies, assistance in corporate affairs and governance, consultation and maintenance of financial records and controls, consultation and assistance in cash management, tax management, internal audits and potential acquisitions.

. . .

> The [$]1.2 million in capital gains reported was reported from investment income in the stock of nonrelated companies. This capital gain investment income is attributed to [Taxpayer's] state of commercial domicile which was Texas in 2009. As a result this income is removed from the Indiana sales factor per audit.
>
> [Taxpayer's] dividend income was primarily intercompany and was not included in the numerator or denominator accordingly since [Taxpayer] was filing a consolidated return and intercompany dividends among affiliates are not included in the apportionment calculation.
>
> In CY 2009, [Taxpayer's] rebill income resulted from billings to [Texas Sub 1] and [Texas Insurance Subsidiary], companies not included in the Indiana consolidated filing. Upon inquiry [Taxpayer] indicated that [Taxpayer's] rebill income was a straight cost allocation with no profit mark-up. As the holding company of the affiliated group, some expenditures were paid or assumed by the holding company and then recouped from the subsidiaries accordingly. The largest of these billings was for incentive compensation and employee stock option expense. The reimbursement of these expenses without a mark-up is a reduction of expense and not a gross income receipt. The allocations of these expenses by [Taxpayer] were made to properly match the expense to the appropriate entity and to include the credits used to facilitate these allocations as income for the sales factor would be a misrepresentation of their nature. These receipts were removed from both the Indiana sales factor and total sales factor per audit. . . .

In summary, the Department's audit removed approximately $14 million of receipts from the sales factor numerator and $5.7 million of receipts from the sales factor denominator. The Department's total audit adjustments resulted in over a 12 percent reduction to Taxpayer's Indiana apportionment factor for the 2009 tax year.

For the 2008 tax year, the audit made the following findings (pages 6-7 of the audit report ending 5-08), which are provided in relevant part:

> In CY 2008 [Taxpayer] reported . . . gross receipts of [over $8.7 million] . . . [T]his income is sourced primarily from interest income from the surplus debenture, capital gain from the preferred stock redemption and loan interest income from a loan to [Funding Subsidiary]. [Taxpayer] has treated all its gross income as attributable to Indiana. The audit has adjusted this classification such that none of the income is treated as Indiana gross income [resulting] in a zero sales factor for apportionment purposes. . . .
>
> [Taxpayer] was incorporated in Delaware and has commercial domicile in Texas. In written responses [Taxpayer] affirmed that [Taxpayer's] commercial domicile was Texas. [Taxpayer] is not currently and was not registered in CY 2008 with the Indiana Secretary of State as doing business in the state of Indiana. [Taxpayer's] primary corporate officers, such as CEO, CFO, and General Counsel, were located in Texas. . . . [T]he interest income from the surplus debenture is not attributable to the state of Indiana. The issuance of the surplus debenture was part of a capital transaction that was regulated by the Texas Department of Insurance and overseen by [Taxpayer's] Texas officers and outside investors, [New York Management Company]. . . . The fact that a [$]3 million dollar management fee was paid to [New York Management Company] would indicate that [New York Management Company] performed substantial services for this entity. The fact that [nearly 90 percent] of [Taxpayer's] payroll dollars were outside of Indiana would indicate that the management of this entity was being conducted outside the state of Indiana . . . .
>
> The other gross income reported by [Taxpayer] was the capital gain from the redemption of the preferred stock issue to [Indiana Corporation] as part of the 2004 acquisition. It is also treated as gross income attributed outside of Indiana, since this income was also part of the acquisition and structure engineered by [New York Management Company] and overseen by the corporate office in Texas.
>
> The balance of the gross income [receipts] reported by [Taxpayer], including loan interest from [Funding Corp.] and some miscellaneous income, are attributable to [Taxpayer's] state of commercial domicile . . . .

In summary, the Department's audit removed approximately $8.7 million of receipts from the sales factor numerator and $57 million of receipts from the sales factor denominator. This adjustment changed Taxpayer's reported 100 percent Indiana sales factor to a zero percent Indiana sales factor. The Department's total audit adjustments resulted in over a 70 percent reduction to Taxpayer's Indiana apportionment factor for the 2008 tax year.

For the Short Year Dec 2007, the audit made the following findings (on pages 11-12 of the audit report ending in 5-08), provided in relevant part:

> [Taxpayer reported] approximately $5.5 million in gross income, which was interest income from the surplus debentures issued as part of the acquisition and income from short term investments and checking account interest. Additionally the taxpayer reported $40 million in dividend income from affiliates and [$9,000] in other income. All gross income was attributed 100[percent] to Indiana by the taxpayer in the sales factor of [Taxpayer's] reported apportionment schedule. This resulted in an overall apportionment percentage reported by [Taxpayer] of 85.30[percent]. There are no audit adjustments proposed to the property and payroll factors, but the Indiana sales factor and total sales factor are reduced per audit. The interest income from the surplus debentures is attributed outside Indiana for reasons previously detailed under the CY 2008 adjustments. . . . Like 2008, [Taxpayer] was paying management fees to [New York Management Company] under the provisions of a [Management Fee Agreement]. Based on the management fees and the 73[percent] non-Indiana payroll factor, [Taxpayer's] commercial domicile was not Indiana. As a result the interest income from the debentures, the investment income and the other income should be removed from the Indiana sales factor and attributed to [Taxpayer's] commercial domicile outside the state. . . .
>
> Under a similar rationale the dividend income, if considered a gross receipt, should be allocated to [Taxpayer's] state of commercial domicile and therefore not included in [Taxpayer's] Indiana numerator. . . .
>
> The audit calculation attributed all gross income outside the state of Indiana for the sales factor which resulted in the total apportionment percentage being 25.30[percent].

In summary, the Department's audit removed approximately $8.7 million of receipts from the sales factor numerator and $57 million of receipts from the sales factor denominator. This adjustment changed Taxpayer's reported 100 percent Indiana sales factor to a zero percent Indiana sales factor. The Department's total audit adjustments resulted in a 60 percent reduction to Taxpayer's Indiana apportionment factor for the Short Year Dec 2007 tax year.

Accordingly, the Department's audit removed the short term investment interest income, capital gains, other investment income, "rebill receipts," dividends, and surplus debenture interest income from Taxpayer's sales factor numerator and/or denominator reducing Taxpayer's Indiana apportionment for the Short Year Dec 2007, 2008, 2009, and 2010 tax years. These adjustments reduced Taxpayer's reported net operating losses it occurred in the Short Year Dec 2007, 2008, and 2009 tax years and resulted in an assessment of adjusted gross income tax for the 2010 tax year.

B. Taxpayer's Response.

Taxpayer protests that the Department understated its sales factor numerator because the Department's audit improperly excluded the short-term investment interest income, capital gains, other investment income, "rebill receipts," dividends, and surplus debenture interest income from its sales factor numerator and/or denominator. The Department determined that these receipts were not attributable to Indiana and were attributable to Texas, its commercial domicile.

As to the surplus debenture interest income received in 2008 and 2009, Taxpayer asserts that the auditor improperly attributed the receipts based upon its commercial domicile. Taxpayer states that those receipts are properly attributed to Indiana under IC § 6-3-2-2.2(c). Taxpayer maintains the surplus debenture receipts are attributed to Indiana under IC § 6-3-2-2.2(c) because "(1) the Surplus Debenture is an installment loan not secured by real or tangible personal property and (2) the proceeds of such loan were applied in Indiana when [Taxpayer's Texas Insurance Subsidiary] paid the loan proceeds to [the seller, an Indiana Corporation,] in [Indiana]." Taxpayer states that it "properly included such receipts in the numerator of its sales factor for the 2008 and 2009 Taxable Years, as required by under IC §§ 6-3-2-2(e) and 2.2(c)."

For the short term investment interest income received in the 2008, 2009, and 2010 tax years, Taxpayer asserts that the auditor improperly attributed the receipts based upon its commercial domicile. Taxpayer maintains these receipts are properly attributed under 45 IAC 3.1-1-55 to the receipt's Indiana business situs. Taxpayer argues that the receipts have an "Indiana business situs" because "[a]ll of these intangibles are held to support other capital needs of [Taxpayer] and its Subsidiaries, e.g. servicing of debt, business expenses, capital requirements, insurance regulatory requirements, etc. in Indiana." Taxpayer maintains that the employees of Taxpayer's subsidiary, Funding Subsidiary, that are located in Indiana control the investment operations and the "investments and proceeds thereof are employed as capital by [Taxpayer] in Indiana to support its operations, which are conducted from Indiana."

As to the capital gains and other investment income received in the 2008, 2009, and 2010 tax years, Taxpayer asserts that the auditor improperly attributed the receipts based upon its commercial domicile. Taxpayer maintains these receipts are properly attributed under 45 IAC 3.1-1-55 to the "receipt's business situs," which was Indiana. Taxpayer argues that the receipts have an Indiana business situs "because the gain and other income resulted from sales of liquid assets held by [Taxpayer] as reserves to cover its operational expenses and obligations and, accordingly, the proceeds from disposition of such liquid assets were employed as working capital in Indiana." Taxpayer maintains that "[its] purpose for acquiring, holding, and disposing of the assets that gave rise to the capital gain and other income was to generate cash for its business operations and such activities were frequent, occurring each of the Taxable Years."

For the "income from the Surplus Debenture, checking accounts, and other short term investments" received in the Short Year Dec 2007, Taxpayer asserts that the auditor improperly attributed the receipts to Texas. Taxpayer maintains that during this period its commercial domicile was in Indiana and not in Texas. Taxpayer claims that when it responded to the auditor's original request for information and told the auditor that its commercial domicile was in Texas, this was only true for the 2008, 2009, and 2010 tax years. Taxpayer maintains that "[i]n 2007, the majority of [Taxpayer's] officers were from Indiana along with one each from Connecticut and Florida." Taxpayer maintains that its new chief executive officer who was hired in January 2006 "did not move to Texas until the end of this short year and did not open a Texas office until 2008. Also, in the short year, [Taxpayer's] daily operations were conducted from Indiana in the same manner as [discussed in the section of the protest letter addressing the 2004 and 2005 tax years]." Taxpayer further asserts that the Department audit improperly "excluded dividend income from the numerator and denominator of [Taxpayer's] sales factor." However, the Department notes that the adjustment [on page 18 of the audit report ending in 5-08] made by the auditor was the removal of these intercompany dividends from only the sales factor numerator as sourced to its commercial domicile in Texas.

As to the "rebill receipts" Taxpayer received in the 2009 and 2010 tax years, Taxpayer asserts that the auditor erroneously removed the receipts from the numerator and denominator of Taxpayer's sales factor. Taxpayer states, "Pursuant to a Cost Allocation Agreement among [Taxpayer] and [its subsidiaries] . . ., [Taxpayer] charged [Texas Sub 1] for the cost of certain services that [it] performed" for Texas Sub 1 for which Taxpayer was reimbursed. Taxpayer has labeled these reimbursements as "rebill receipts." Taxpayer states, "The Cost Allocation Agreement provides a list of services for which a charge can be made based on the actual cost plus an amount of up to ten percent of such amount. The Cost Allocation Agreement does not require that an amount greater than the cost has to be charged."

Taxpayer maintains that the "rebill receipts" belong in the sales factor based upon Indiana law and refers to the definition of sales in IC § 6-3-1-24 and example three in 45 IAC 3.1-1-50, which states, "If the taxpayer is working under a cost plus fixed fee contract, such as the operation of a government owned plant for a fee, gross receipts includes the entire reimbursed cost plus the fee." For the 2010 tax year, Taxpayer maintains that the Department's audit erroneously excluded these receipts as eliminated intercompany receipts. Taxpayer claims that the auditor incorrectly determined that the receipts–paid by Texas Sub 1, which is a member of its life insurance company subgroup, to Taxpayer, which is a member of the non-life subgroup–are included among the intercompany transactions that are eliminated. Taxpayer states that these receipts are not eliminated because "[t]he consolidated income of each subgroup and the apportionment of such consolidated income is determined separately at the subgroup level and thereafter the consolidated income of each subgroup is added together."

C. Hearing Analysis.

Again, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "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). Consequently, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Further, "when [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] deter *[sic]* 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) (internal citation omitted). Thus, all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

Indiana imposes an adjusted gross income tax on "income derived from sources within Indiana of every corporation." IC § 6-3-2-1(b). IC § 6-3-2-2(a)(2) provides that "income derived from sources in Indiana" includes "income from doing business in this state." If a corporation's income "is derived from sources within the state of

Indiana and from sources without the state of Indiana," the income apportioned to Indiana for tax purposes is calculated by multiplying the corporation's total income by the apportionment factor. IC § 6-3-2-2(b). For the years at issue, the apportionment factor formula included a "sales factor." IC § 6-3-2-2(b). "The sales factor is a fraction, the numerator of which is the total sales of the taxpayer in this state during the taxable year, and the denominator of which is the total sales of the taxpayer everywhere during the taxable year." IC § 6-3-2-2(e).

1. Surplus Debenture Interest Income.

As explained previously in Issue I, Texas Insurance Subsidiary issued a surplus debenture to Taxpayer in July 2004. Taxpayer received interest income from the surplus debenture in the 2007, 2008, and 2009 tax years. Taxpayer maintains that these receipts belong in the sales factor numerator because the receipts are attributed to Indiana under IC § 6-3-2-2.2(c).

However, Taxpayer is mistaken. As explained in Issue I, Subpart C, above, when the surplus debenture interest income receipts are attributed under IC § 6-3-2-2.2(c), the receipts are not attributed to Indiana. As provided above, pursuant to IC § 6-3-2-2.2(c), the interest income from the unsecured commercial loans and installment will be attributed to Indiana when the place where the funds are to be applied can be determined and that place is Indiana. If the place where the funds are to be applied is indeterminable, then the interest income is attributed to the place where the "business applied for the loan." Therefore, the issues is if the place where the funds/proceeds of the loan are to be applied could be determined by the lender. In other words, the facts and circumstances must be examined to establish whether the lender could determine how the borrower planned to use the funds borrowed; did the lender's documentation at the time of the loan detail what the borrower planned to buy with the loan proceeds, and if so, where it was located. If the lender could not determine how the borrower planned to use the funds at the time of the loan, then the place where the borrower applied for loan is the place where the lender attributes the income from the loan.

In the instant case, Taxpayer "loaned" Texas Insurance Subsidiary "funds" when Texas Insurance Subsidiary issued a surplus debenture to Taxpayer. The surplus debenture provided that the funds will be used to buy the stock of Texas Sub 1, Texas Sub 2, and Texas Sub 3 pursuant to the July 1, 2004, Purchase Agreement. The July 1, 2004, Purchase Agreement required that the acquisition transaction be reported as an acquisition of assets under the I.R.C. § 338(h)(10) election. Therefore, the loan proceeds of the surplus debenture were "to be applied" on the purchase of Texas Sub 1's, Texas Sub 2's, and Texas Sub 3's assets.

However, neither the July 1, 2004, Purchase Agreement nor the surplus debenture provided how much of the funds borrowed were to be applied generally to each of Texas Sub 1, Texas Sub 2, and Texas Sub 3 let alone to each of the assets of Texas Sub 1, Texas Sub 2, and Texas Sub 3. Moreover, Texas Sub 1, Texas Sub 2, and Texas Sub 3 are life insurance companies that are domesticated in different states, have certificates of operating authority in multiple states, and have assets in multiple states. Specifically, Texas Sub 1 was registered as an Indiana domestic life insurance company with certificates of authority in 49 states, the District of Columbia, and Puerto Rico, and had assets in multiple states including Indiana. Texas Sub 2 was registered as an Arkansas domestic life insurance company with certificates of authority in five states–none of which is Indiana–and had assets in multiple states. Texas Sub 3 was registered as an Indiana domestic life assurance company with certificates of authority in 49 states, the District of Columbia, and Puerto Rico and had assets in multiple states. Therefore, the loan proceeds of the surplus debenture were "to be applied" on the purchase of Texas Sub 1's, Texas Sub 2's, and Texas Sub 3's assets that were located in multiple states. Since neither the July 1, 2004, Purchase Agreement nor the surplus debenture provided how much of the funds borrowed were to be applied to each of the assets that were located in multiple states, neither the amount nor the place where the surplus debenture proceeds were applied could be determined from the surplus debenture or the July 1, 2004, Purchase Agreement.

As provided above, pursuant to IC § 6-3-2-2.2(c), when the lender cannot determine where the borrower would apply the funds, the lender's income and receipts are attributed to the state where its customer applied for the loan. Thus, the issue becomes the location where Texas Insurance Subsidiary "applied" for its surplus debenture with Taxpayer.

Taxpayer, under the control and management of the New York Management Company, agreed to "loan" Taxpayer's Texas Insurance Subsidiary the financing under a surplus debenture that was required to be approved by, was approved by, and was registered with the Texas Department of Insurance. As provided above in the recitals of the Management Fee Agreement and the July 1, 2004, Purchase Agreement, Taxpayer did not have the capacity to manage itself during 2004 and 2005 and was managed and controlled by the members of the New York Management Company who "were instrumental in arranging the financing of the [acquisition of Texas Sub 1,

Texas Sub 2, and Texas Sub 3]." Based upon the facts presented, the place where Taxpayer's Insurance Subsidiary applied for the surplus debenture would be either in New York where the New York Management Company planned the acquisition or in Texas where the surplus debenture was registered with and approved by the Texas Department of Insurance. Thus, the only conclusion possible is that the place where Taxpayer's Insurance Subsidiary applied for the surplus debenture was a place outside of Indiana and the interest income from the surplus debenture is not attributed to Indiana under IC § 6-3-2-2.2(c). Therefore, Taxpayer has not met its burden of proving that the audit's determination–that the interest income receipts from the surplus debenture should be attributed to a place outside of Indiana–was incorrect as prescribed under IC § 6-8.1-5-1(c). Given the totality of the circumstances, in the absence of other supporting documentation, the Department's audit properly excluded the surplus debenture interest income from the sales factor numerator. Taxpayer's protest of the Department's adjustment–to remove its interest income from the surplus debenture from the numerator of the sales factor in the Short Year Dec 2007, 2008, 2009 tax years–is denied.

2. Other Interest and Investment Income.

The Department determined that Taxpayer's receipts from other investment and interest income such as capital gains, short-term investment interest income, and dividends were attributable to a place outside of Indiana for the Short Year 2007, 2008, 2009, and 2010 tax years. Taxpayer maintains that the auditor incorrectly attributed these receipts outside Indiana. Taxpayer states that the auditor improperly attributed the receipts based upon its commercial domicile and asserts that instead those receipts are properly attributed to Indiana under IC § 6-3-2-2(f)(1) and 45 IAC 3.1-1-55.

For sales factor apportionment purposes, receipts from intangible property that are not specifically attributed under IC § 6-3-2-2.2, giving rise to a corporation's income, are attributed to Indiana if "the income-producing activity is performed in this state." IC § 6-3-2-2(f)(1). Therefore, the receipts from the intangible property are Indiana receipts to the extent that "income-producing activity is performed in this state" and are included in the sales factor numerator. IC § 6-3-2-2(f)(1). When the "income producing activity" for a transaction is performed in Indiana, the receipts from the transaction are included in the numerator under IC § 6-3-2-2(f)(1). Thus, to the extent that the transaction's "income producing activity" is performed in Indiana, the income from the transaction is included in the Indiana numerator. Conversely, to the extent that an "income producing activity" for a transaction is performed outside Indiana, then the income from the transaction is generally excluded from the Indiana numerator.

"Income producing activity" is defined as "the act or acts directly engaged in by the taxpayer for the ultimate purpose of obtaining gains or profit." 45 IAC 3.1-1-55. Income producing activity is "deemed performed at the situs of . . . intangible personal property. . . . " Id. "The situs of intangible personal property is the commercial domicile of the taxpayer (i.e., the principal place from which trade or business of the taxpayer is directed or managed), unless the property has acquired a 'business situs' elsewhere." Id.

Accordingly, the receipts from the intangible property not specifically attributed under IC § 6-3-2-2.2 are attributed to Indiana based upon the "business situs" of the intangible property and the commercial domicile of the Taxpayer. IC § 6-3-2-2(f)(1) and 45 IAC 3.1-1-55. When the intangible property has not "acquired a business situs" outside of Indiana and the commercial domicile of the taxpayer is in Indiana, the receipts are attributed to Indiana. 45 IAC 3.1-1-55. In addition, when the intangible property has "acquired a business situs" in Indiana and the commercial domicile of the taxpayer is outside of Indiana, the receipts from the intangible property are attributed to Indiana. Id. However, when neither the taxpayer's commercial domicile nor the "acquired business situs" of the intangible property are in Indiana, the receipts from the intangible property are attributed outside of Indiana.

a). Business Situs: 2008, 2009, and 2010

During the 2008, 2009, and 2010 tax years, Taxpayer received short-term investments interest income, capital gains, and other investment income. The Department removed the interest, capital gains, and other investment income from Taxpayer's sales factor numerator and attributed these receipts to Taxpayer's Texas commercial domicile. Taxpayer maintains that it properly included these receipts in the sales factor numerator under IC § 6-3-2-2(f)(1) and 45 IAC 3.1-1-55 because the "receipts have a business situs in Indiana" and are attributed to Indiana regardless of its Texas domicile during these years.

Taxpayer argues that the "receipts have an Indiana business situs" because "[a]ll of these intangibles are held to support other capital needs of [Taxpayer] and its Subsidiaries, e.g. servicing of debt, business expenses, capital requirements, insurance regulatory requirements, etc. in Indiana." Taxpayer maintains that the Indiana employees

of one of its subsidiary control the investment operations and, therefore, the "investments and proceeds thereof are employed as capital by [Taxpayer] in Indiana to support its operations, which are conducted from Indiana." However, Taxpayer has not provided any information other than its bare assertions about how the receipts that Taxpayer received from the intangible property were used by Taxpayer and its subsidiaries or about the rights or activities of the employees of its subsidiary.

Notwithstanding Taxpayer not providing documentation to support its assertions, Taxpayer is also mistaken in its application of the law. Taxpayer states that 45 IAC 3.1-1-55 would determine the attribution of the receipts from the intangible property based upon the "receipt hav[ing] a business situs" in a particular location. However, Taxpayer has mischaracterized 45 IAC 3.1-1-55. As provided above, 45 IAC 3.1-1-55 states that it is when the "intangible property has acquired a business situs" in Indiana and the commercial domicile of the taxpayer is outside of Indiana that the receipts from the intangible property are attributed to Indiana. Therefore, Taxpayer must demonstrate that 1) the intangible property from which Taxpayer received the interest, investment income, capital gains, and dividends has "acquired a business situs" away from Taxpayer's Texas commercial domicile and 2) that the intangible property "acquired a business situs" in Indiana.

"Business situs" is explained in 45 IAC 3.1-1-55, which states, in relevant part:

> "Business situs" is the place at which intangible personal property is employed as capital; or the place where the property is located if possession and control of the property is localized in connection with a trade or business so that substantial use or value attaches to the property." Example: Taxpayer, a corporation whose principal business activity is the manufacture and sale of hot water heaters, obtains notes for the sale of such water heaters in connection with its Indiana business activity. The property has a business situs in this state, therefore, interest income derived from such notes is attributable to this state.

Based upon the facts presented, Taxpayer received interest income, other investment income, and capital gains from its stocks and short-term investment accounts. Taxpayer's business is that of a traditional holding company formed by a group of investors. Taxpayer holds these stocks and short-term investment accounts to perform its business of a traditional holding company. Three of Taxpayer's board of directors/executive officers were designated as the three authorized signatories that would control Taxpayer's investment/bank accounts in Taxpayer's board of director minutes. Taxpayer failed to present documentation that demonstrated that Taxpayer's stocks and short-term investment accounts had a business situs away from its Texas commercial domicile. Specifically, Taxpayer has failed to present documentation that demonstrated the stock and short-term investment accounts were either "employed as capital" by Taxpayer in any specific place or that Taxpayer's "possession and control of the [stock and short-term investment accounts] [were] localized in connection with [Taxpayer's holding company business] so that substantial use or value attache[d] to the [stocks and short-term investment accounts]" in any specific place. Based on the facts presented, the Department presumes if Taxpayer's stock and short term investment accounts were "employed as capital" or were "localize[d] in connection with Taxpayer's holding company business," this would not occur at any place other than Taxpayer's Texas commercial domicile.

Therefore, Taxpayer has not met its burden of proving that the audit's determination–that Taxpayer's interest income, dividends, capital gains, and other investment income should be attributed to a place outside of Indiana–was incorrect as prescribed under IC § 6-8.1-5-1(c). Given the totality of the circumstances, in the absence of other supporting documentation, the Department's audit properly excluded Taxpayer's interest income, capital gains, and other investment income from the sales factor numerator. Taxpayer's protest of the Department's adjustment to remove its interest income, capital gains, and other investment income from the numerator of the sales factor in the 2008, 2009, and 2010 tax years is denied.

b). Domicile: Short Year Dec 2007

During the Short Year Dec 2007, Taxpayer received interest income from its checking accounts and short-term investments. Taxpayer also received approximately $45 million of intercompany dividends that were not eliminated as intercompany transactions, because Taxpayer filed its Indiana and federal income tax returns on a separate return basis. The intercompany dividends were included in Taxpayer's gross income and were deducted by Taxpayer as part of its dividend received deduction. The Department removed the interest income and the dividends from Taxpayer's sales factor numerator and attributed these receipts to Taxpayer's commercial domicile in Texas.

Taxpayer asserts that it properly included these receipts in the sales factor numerator under IC § 6-3-2-2(f)(1) and 45 IAC 3.1-1-55 because its domicile for the Short Year Dec 2007 tax year was in Indiana and not in Texas.

IC § 6-3-1-22 provides that "'commercial domicile' means the principal place from which the trade or business of the taxpayer is directed or managed." Further, 45 IAC 3.1-1-32, states:

> The term "commercial domicile" is defined in the Act as "the principal place from which the trade or business of the taxpayer is directed or managed." Commercial domicile is not necessarily in the state of incorporation. A corporation that is incorporated in a state, but that has little or no activity in that state, has not established a commercial domicile there.
>
> Each corporation has one, and only one, commercial domicile. Generally, it is where the executive authority of the business is concentrated. However, if such authority is not centralized in one state, then the commercial domicile is the place where the majority of the corporation's daily operational decisions are made. There are several factors to be considered in determining the commercial domicile of a corporation. These factors include, but are not limited to:
> (a) The relative amount of revenue from sales in the various states
> (b) The relative value of fixed assets in the various states
> (c) The principal place of work of a majority of the employees
> (d) The place where the corporate records are kept
> (e) The principal place of work of the corporate executives
> (f) The place where policy and investment decisions are made
> (g) The relative amount of decision-making power held by various executives and employees
> (h) The place where payments are made on intangibles held by the corporation
> (i) Whether income from intangibles held by the corporation is taxable elsewhere
> (j) The office from which the Federal income tax return is filed
> (k) Information contained in the corporation's annual and quarterly reports
> (l) The place where the board of directors meets.

While this regulation provides that generally a taxpayer's commercial domicile "is where the executive authority of the business is concentrated" or "the place where the majority of the corporation's daily operational decisions are made." The regulation provides a nonexclusive list of factors that are evaluated to help determine the "commercial domicile of the taxpayer"–i.e., "the principal place from which the trade or business of the taxpayer is directed or managed." Therefore, the determination of the taxpayer's commercial domicile is a fact sensitive question based upon weighing the particular circumstances of the taxpayer.

Taxpayer asserts that its commercial domicile was in Indiana. Taxpayer claims that when it responded to the auditor's original request for information and told the auditor that its commercial domicile was in Texas, this was only true for the 2008, 2009, and 2010 tax years. Taxpayer maintains that "[i]n 2007, the majority of [Taxpayer's] officers were from Indiana along with one each from Connecticut and Florida." Taxpayer states that its new chief executive officer hired in January 2006 "did not move to Texas until the end of this short year and did not open a Texas office until 2008. Taxpayer further maintains that "its daily operations were conducted from Indiana in the same manner as [discussed in the section of the protest letter addressing the 2004 and 2005 tax years]." However, as provided in Issue I, Subpart B, as to Taxpayer's statement that "[a]fter the acquisition, the day to day operations of [Taxpayer] and the [acquired subsidiaries] continued to be managed from [Indiana]," was based upon bare assertions that were not supported with documentation and were contrary to publically available information and the findings of fact in the audit report.

During Short Year Dec 2007, Taxpayer's trade of business is that of a traditional holding company formed by a group of investors. During the Short Year Dec 2007, Taxpayer reported approximately $600,000 of employee expense(s) in Indiana and $2.3 million outside Indiana. Since Taxpayer's payroll allocation reports that the majority of the payroll expenses–which would include Taxpayer's executive officer compensation–occurred outside of Indiana, presumably the majority of the executive officers were located outside of Indiana. Taxpayer's board members were also executive officers. Taxpayer's protest letter states that its board members resided in at least three states other than Indiana during 2007. Taxpayer presented the minutes for Taxpayer's board of directors meetings. During 2006, the first of Taxpayer's board meetings was held in January by conference call where the new chief executive officer was hired and appointed. The remainder of Taxpayer's 2006 board meetings were held in New York and the new chief executive officer was in attendance. During 2007, the first three of Taxpayer's board meetings were held by conference call and last two were held in Indiana with some members attending by telephone.

Additionally, as discussed in Issue I, Subpart C, during the protest, Taxpayer presented a July 1, 2004, Purchase Agreement. The July 1, 2004, Purchase Agreement provided, in Schedule A, these relevant facts in the recitals

"[Seller, an Indiana corporation,] is currently negotiating with [New York Management Company] relating to the purchase by **a company formed and controlled by [New York Management Company]** and/or its principals ("Purchaser"), [–i.e., Taxpayer,] . . . ." (**Emphasis added**). During the protest, as discussed in Issue I, Subpart C, Taxpayer also presented a Management Fee Agreement between Taxpayer and New York Management Company. The Management Fee Agreement provided these relevant facts in the recitals of the agreement:

1) "Members of [New York Management Company] were instrumental in the formation and organization of [Taxpayer], as well as the acquisition of [Texas Sub 1, Texas Sub 2, Texas Sub 3, other entities from the Indiana corporation] in July 2004 (the 'Acquisition') . . . .

2) "Members of [New York Management Company] were instrumental in arranging the financing of the Acquisition . . . ."

3) During the financing of the Acquisition, "restrictions were negotiated regarding three types of fees (transaction, management, and transaction advisory fees) that Taxpayer could pay to Affiliates, with the [New York Management Company] in mind . . . ."

4) "Members of [New York Management Company] have served as officers and continue to serve in certain positions as advisors of [Taxpayer] . . . ."

5) "[Taxpayer] does not yet separately maintain the full internal capability to perform all necessary management, financial and administrative functions which [Taxpayer] requires . . . ."

6) "[Taxpayer, in January 2006,] hired an executive to serve as the new President and CEO . . . ."

7) "[T]he new executive has assumed some of the duties previously carried out by Members of [New York Management Company] . . . ."

8) "[Taxpayer] desires to continue receiving some of the management, financial and administrative services provided by [New York Management Company], if, as and when requested by the CEO of [Taxpayer], for a set period of time until the entire new management team is trained and integrated."

Based upon the recitals in the Management Fee Agreement and July 1, 2004, Purchase Agreement, Taxpayer did not have the capacity to manage itself as of May 16, 2006, was managed and controlled by the members of the New York Management Company, and would continue to pay for such management services it received from New York Management Company until it acquired the capacity to manage itself. Taxpayer reported, as an ordinary and necessary business expense deductions, on its federal tax returns millions of dollars in management fees it paid to the New York Management Company for the management services that Taxpayer incurred during 2007, 2008, and 2009 tax years. See Elick v. CIR, T.C. Memo 2013-139, 2013 WL 2394860, at *3 (U.S. Tax Ct. 2013) (citing to Treas. Reg. §1.162-7 and explaining that fees due under a management service agreement must be "actually rendered" for a taxpayer to take a deduction for management services fees for the management fees to be incurred as ordinary and necessary business expenses for purposes of I.R.C. § 162); See also Fuhrman v. CIR, T.C. Memo 2011-236, 2011 WL 4502290, at *3 (U.S. Tax Ct. 2011) (explaining that to take a deduction for management fees the taxpayer must have detailed records of the management services that were provided); See also Weekend Warrier Trailers v. CIR,. T.C. Memo 2011-105, 2011 WL 1900159, at *19-20 (U.S. Tax Ct. 2011) (explaining that to report a business expense deduction for management fees the taxpayer must be able to demonstrate that specific services were performed). During 2007, at least three of Taxpayer's shareholder-officers were also members of this New York Management Company, which Taxpayer, the publically available information, and the audit report all affirm is headquartered in New York.

Based upon the facts presented, the place from which Taxpayer's board of directors/executive officers directed or managed was not in Indiana. Moreover, based upon the facts presented, Taxpayer employed the majority of its employees outside of Indiana, did not have a "concentration" of board of directors/officers that "directed or managed" from a place in Indiana, did not have a principal executive office in Indiana, did not have daily operational activities that were conducted by Taxpayer's officers or employees from Indiana. Thus, based upon the facts presented, Taxpayer had a domicile outside of Indiana for the Short Year Dec 2007.

Therefore, Taxpayer has not met its burden of proving that the audit's determination–that Taxpayer's interest income from its checking accounts and short-term investments and its dividends should be attributed to a place outside of Indiana–was incorrect as prescribed under IC § 6-8.1-5-1(c). Given the totality of the circumstances, in the absence of other supporting documentation, the Department's audit properly excluded Taxpayer's interest

income from its checking accounts and short-term investments and its dividends income from the sales factor numerator. Taxpayer's protest of the Department's adjustment to remove its interest income from its checking accounts and short-term investments and its dividends from the numerator of the sales factor in the Short Year Dec 2007 tax years is denied.

3. "Rebill Receipts."

As explained above, Texas Sub 1 reimbursed Taxpayer for the cost of certain services that Taxpayer performed for Texas Sub 1. Taxpayer labeled these reimbursements received from "Texas Sub 1" as "rebill receipts." Taxpayer included the "rebill receipts" in its sales factor numerator and denominator for the 2009 and 2010 tax years. The Department's audit determined that the "rebill receipts" should be excluded from the sales factor. The Department's audit found that "reimbursement of these expenses without a mark-up is a reduction of expense and not a gross income receipt" and, therefore, did not represent income included in the apportionment factor. Additionally, as to the 2010 tax year, the Department's audit determined that the "rebill receipts" should also be excluded from the sales factor on the basis that the "rebill receipts" were eliminated intercompany receipts and therefore did not represent income included in the apportionment factor.

Taxpayer maintains that it properly included the "rebill receipts" in the sales factor and the receipts should not be excluded from the factor based upon their classification as non-income expense reimbursements or intercompany eliminations.

a). Expense Reimbursement

IC § 6-3-2-2(a) explains that for nonbusiness income "only so much of such income that is allocated to this state under the provision of subsections (h) through (k) shall be deemed to be derived from sources within the state of Indiana" and for business income "only so much of such income as is apportioned to this state under the provision of subsection (b) shall be deemed to be derived from sources within the state of Indiana." IC § 6-3-2-2(b) provides that a corporation with "business income . . . from sources within the state of Indiana and from sources without the state of Indiana, [determines its] business income derived from sources within this state . . . by multiplying its business income derived from sources within and without the state of Indiana by [an apportionment factor]." For the tax years at issue, the apportionment factor formula included a "sales factor." IC § 6-3-2-2(b).

At issue is the computation of Taxpayer's sales factor. Taxpayer's computation of its sales factor included its "rebill receipts" from two of its subsidiaries. The "rebill receipts" are cost reimbursements paid to Taxpayer by these subsidiaries for expenditures for incentive compensation and employee stock option expenses that Taxpayer, as the holding company, paid or assumed on behalf of its subsidiaries. The Department excluded these "cost reimbursements" from Taxpayer's sales factor because the items of cost reimbursement without any mark-up are not considered gross income and are instead treated and reported as reductions to Taxpayer's expenses. Taxpayer asserts that the "rebill receipts" are items that are included in its sales factor regardless of the cost recovery nature of the items because the items meet the definition of "sales" under IC § 6-3-1-24 and cites to example three in 45 IAC 3.1-1-50 as support for this assertion.

However, Taxpayer is mistaken. "The sales factor is a fraction, the numerator of which is the total sales of the taxpayer in this state during the taxable year, and the denominator of which is the total sales of the taxpayer everywhere during the taxable year." IC § 6-3-2-2(e) (Emphasis added). "Sales" are defined as "all gross receipts of the taxpayer not allocated under IC 6-3-2-2(g) through IC 6-3-2-2(k) other than compensation . . . ." IC § 6-3-1-24. IC § 6-3-2-2(g) provides, "[R]ents and royalties from real or tangible property, capital gains, interest, dividends, or patent or copyright royalties, to the extent that they constitute nonbusiness income, shall be allocated as provided in subsections (h) through (k)." (Emphasis added). "'[N]onbusiness income' means all income other than business income." IC § 6-3-1-21. "'[B]usiness income' means income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property . . . ." IC § 6-3-1-20. Additionally, 45 IAC 3.1-1-34 explains that "sales" are defined as "all gross receipts of the taxpayer not allocated under IC 6-3-2-2(g)-(k)" and that "any business income of a corporate taxpayer is considered to be from 'sales' under this definition, regardless of its actual source." (Emphasis added).

Moreover, 45 IAC 3.1-1-52 explains that "[t]he numerator of the sales factor generally includes gross receipts from sales attributable to this state, and includes all interest income, service charges, carrying charges, or time-price differential charges incidental to such sales regardless of the place where the accounting records are maintained or the location of the contract or other evidence of indebtedness." (Emphasis added). Consistently, 45 IAC 3.1-1-51 states that "[t]he denominator of the sales factor includes all gross receipts from the taxpayer's sales, except as noted in [45 IAC 3.1-1-62]." (Emphasis added).

Accordingly, the numerator and the denominator of the sales factor include the "gross receipts from the taxpayer's sales." 45 IAC 3.1-1-51 and 45 IAC 3.1-1-52. The taxpayer's "sales" are all items of the taxpayer's "business income." IC § 6-3-1-24 and 45 IAC 3.1-1-34. Therefore, the items that are "sales" that are included in the taxpayer's sales factor are those items that are income items, specifically the "business income" items.

Taxpayer attempts to include in its sales factor numerator and denominator items that are not income on its federal income tax return, but are items that are expense reductions. Taxpayer, in support of its assertion, cites to example three in 45 IAC 3.1-1-50, which states, "If the taxpayer is working under a cost plus fixed fee contract, such as the operation of a government owned plant for a fee, gross receipts includes the entire reimbursed cost plus the fee." However, this example does not support Taxpayer's attempt because it refers to an item that is an item of federal income and, therefore, would be included in the sales factor. See generally Metcalf & Eddy v. Mitchell, 269 U.S. 514 (1926) (finding that contractors for the government are not agents of the government and their receipts do not qualify as exempt income of the federal government). This example relates to the general rule from Supreme Court decisions that in contracting with the government, using a cost plus contract on a non-agency or non-employee basis, all the fees received are most likely taxable income. See generally Alabama v. King & Boozer, 314 U.S. 1 (1941); Kern-Limerick, Inc. v. Scurlock, 347 U.S. 110 (1954); United States v. New Mexico, 455 U.S. 720, 736 (1982).

Mere cost reimbursement transactions are not income and are subtracted from taxable gross receipts because taxpayers are not allowed a business expense deduction under I.R.C. § 162 for an item for which it will receive reimbursement. See generally Cochrane v. C.I.R, 23 B.T.A. 202, *208 (1931) (referring to Albright v. C.I.R., 16 B.T.A. 1228 (1929) and Grelck Condensed Buttermilk Co. v. C.I.R., 7 B.T.A. 79 (1927) finding that expenditures made with the expectation of reimbursement are not deductable *[sic]* business expense and, therefore, the receipt of the reimbursement is not a taxable gross receipt); See also Levy v. Commissioner, 212 F.2d 552 (5th Cir. 1954) (referring to Glendinning, McLeish & Co. v. Commissioner, 61 F.2d 950 (2nd Cir. 1932); All Russian Textile Syndicate v. Commissioner, 62 F.2d 614 (2nd Cir. 1933); Universal Oil Products v. Campbell, 181 F.2d 451 (7th Cir. 1950) explaining that "[i]t is well settled that expenses for which there exists a right of reimbursement are not ordinary and necessary business expenses within the meaning of Section 23(a)(1) of the Internal Revenue Code, 26 U.S.C.A."); See also Burnett v. C.I.R., 356 F.2d 755, 759 (5th Cir. 1966) (citing to Levy v. Commissioner, 212 F.2d 552 (5th Cir. 1954) and explaining that "it is well settled that an expenditure for which there is an unconditional right of reimbursement is not deductible as a business expense[.]").

Accordingly, Taxpayer has not met its burden of proving that the audit's determination–that the "rebill receipts" were non-income items that should be removed from the apportionment factor–was incorrect as prescribed under IC § 6-8.1-5-1(c). Given the totality of the circumstances, in the absence of other supporting documentation, the Department's audit properly excluded from the sales factor numerator and denominator the "rebill receipts" Taxpayer received from Texas Sub 1. Taxpayer's protest of the Department's adjustment–to remove its "rebill receipts" from the numerator and the denominator of the sales factor in the 2009 tax year–is denied.

b). Intercompany Eliminations

During 2010, Texas Sub 1 was included in Taxpayer's federal and Indiana consolidated return filing. Taxpayer maintains that the Department's audit erroneously excluded these receipts from the sales factor on the basis that the "rebill receipts" were eliminated intercompany receipts. Taxpayer asserts that the auditor incorrectly determined that the receipts–paid by Texas Sub 1, a member of its life insurance subgroup, to Taxpayer, a member of the non-life subgroup–are included among the intercompany transactions that are eliminated. Taxpayer maintains that these receipts were not eliminated intercompany transactions because "[t]he consolidated income of each subgroup and the apportionment of such consolidated income is determined separately at the subgroup level and thereafter the consolidated income of each subgroup is added together." In effect, Taxpayer suggests that the elimination of intercompany transactions generally takes place at the subgroup level and when transactions occur between members of the different subgroups the transactions are not eliminated.

However, Taxpayer is mistaken. Pursuant to IC § 6-3-4-14(a), an "affiliated group" of taxpayers are allowed "the privilege of making a consolidated return with respect to the taxes imposed by IC 6-3" as long as certain conditions are met. All corporations in the "affiliated group" must "consent" to follow the filing requirements specified in IC § 6-3-4-14. Id. An Indiana consolidated return "affiliated group" is an "'affiliated group' as defined in Section 1504 of the Internal Revenue Code with the exception that the affiliated group shall not include any corporation which does not have adjusted gross income derived from sources within the state of Indiana." IC § 6-3-4-14(b). Additionally, IC § 6-3-4-14(c) prescribes that "the determination of 'taxable income,' as defined in

Section 63 of the Internal Revenue Code, of any affiliated group of corporations making a consolidated return and of each corporation in the group, both during and after the period of affiliation, shall be determined pursuant to the regulations prescribed under Section 1502 of the Internal Revenue Code."

An "affiliate group" is a group of "includible corporations." I.R.C. § 1504. Generally, life insurance companies are not "includible corporations" for federal consolidated return purposes. I.R.C. § 1504(b). However, a parent company with non-life insurance and life insurance affiliates can make an election for its consolidated group filing to include the life insurance companies in certain circumstances. I.R.C. § 1504(c). These consolidated returns report the income and losses of the parent's affiliated subsidiaries in two subgroups: one group for the life insurance companies and one group for the non-life insurance companies. See Treas. Reg. § 1.1502-47(a)(2). However, Treas. Reg. § 1.1502-47(a)(4), states that "[t]he provisions of §§ 1.1502-1 through 1.1502-80 apply unless this section provides otherwise." Moreover, Treas. Reg. § 1.1502-47(r) specifically, states:

> The fact that this section treats the life and nonlife members as separate groups in computing, respectively, consolidated partial LICTI (or LO) and nonlife consolidated taxable income (or loss) does not affect the usual rules in §§ 1.1502-0--1.1502-80 unless this section provides otherwise. **Thus, the usual rules in § 1.1502-13 (relating to intercompany transactions) apply to both the life and nonlife members by treating them as members of one affiliated group**. (**Emphasis added**).

As provided in Treas. Reg. § 1.1502-47(a)(2), Taxpayer is correct that for purposes of making a consolidated return consisting of a group of life insurance companies and non-life insurance companies, the income of the consolidated group will be calculated separately for its life-insurance and non-life subgroups. However, contrary to Taxpayer's suggestion that its intercompany eliminations will also be based upon the transactions between members of each subgroup, pursuant to Treas. Reg. § 1.1502-47, the general consolidated return rules, including the elimination of intercompany transactions, will be applied and the life and nonlife members are treated as members of one affiliated group for such rules, unless Treas. Reg. § 1.1502-47 specifically states otherwise. Treas. Reg. §§ 1.1502-47(a)(2) and (r). Taxpayer has not cited to any provision in the regulation that would suggest that its own situation is treated differently than the general rule of eliminating the intercompany transaction. Moreover, the Department could not find any provision in the regulation that would suggest that this situation is treated differently than the general rule of eliminating the intercompany transaction. Therefore, these "rebill receipts" transactions, if they were income items, would be eliminated at the federal level as intercompany transactions and did not represent income to be included in the apportionment factor. See 45 IAC 3.1-1-51 and 45 IAC 3.1-1-52 (explaining that neither the sales factor denominator nor the sales factor numerator "shall not include sales made between members of an affiliated group filing consolidated returns under IC 6-3-4-14").

Accordingly, Taxpayer has not met its burden of proving that the audit's determination–that the "rebill receipts" were also eliminated intercompany transactions that should be removed from the apportionment factor for the 2010 tax year–was incorrect as prescribed under IC § 6-8.1-5-1(c). Given the totality of the circumstances, in the absence of other supporting documentation, the Department's audit properly excluded the "rebill receipts" that Taxpayer received in the 2010 tax year from Texas Sub 1 from the sales factor numerator and denominator. Taxpayer's protest of the Department's adjustment–removing its "rebill receipts" from the numerator and the denominator of the sales factor in the 2010 tax year–is denied.

In summary, Taxpayer has not met its burden of proving that the Department's adjustments to its sales factor were incorrect as prescribed under IC § 6-8.1-5-1(c). Given the totality of the circumstances, in the absence of other supporting documentation, the Department's adjustments–excluding the receipts from Taxpayer's short-term investment interest income, capital gains, other investment income, dividends, surplus debenture interest income, and "rebill receipts" from Taxpayer's sales factor numerator and/or denominator for the Short Year Dec 2007, 2008, 2009, and 2010 tax years resulting in the reduction of Taxpayer's net operating loss deduction and the assessment of tax in the 2010 tax year–were proper. Taxpayer's protest of the Department's adjustments to its sales factor is denied.

FINDING

Taxpayer's protest of the Department's removal of Taxpayer's receipts from its short-term investment interest income, capital gains, other investment income, dividends, "rebill receipts," and surplus debenture interest income from the sales factor numerator and/or denominator is respectfully denied.

III. Corporate Income Tax-Net Operating Loss: Limitation.

DISCUSSION

Taxpayer protests the Department's redetermination of its net operating loss limitation for the loss incurred by its non-life insurance companies.

A. Audit Results.

The Department determined that Taxpayer incorrectly calculated the thirty-five percent limitation that applies to offsetting a loss incurred by its non-life insurance companies group against the income of its life insurance company group. The Department found that Taxpayer incorrectly included Taxpayer's bank's income–which is excluded from Indiana's adjusted gross income tax–in the thirty-five percent limitation equation.

Specifically, the audit made the following findings (page 10 of the audit report ending in 9-03):

> Provisions exist pursuant to IRC Section 1503 that allow a deduction of non-life insurance company losses of non-life members of an affiliate group against life insurance taxable income of life insurance affiliates when they are part of the same affiliated group. When computing a life insurance company's taxable income (LICTI), losses from non-life insurance companies are limited to the smaller of 35[percent] of the loss or 35[percent] of LICTI excluding any non-life insurance losses used in determining LICTI. The taxpayer performed this computation on a federal basis which included all entities included in its federal return including [its bank subsidiary]. The bank was not included in the Indiana consolidated return due to Financial Institutions Tax filing requirements. As a result the loss limitation that has been allowed per audit has been recomputed eliminating the bank's taxable income from the calculation which resulted in an increased loss and loss limitation. This resulted in less non-life insurance company loss available to offset the insurance company income and increase in consolidated Indiana income. This adjustment was made pursuant to 45 IAC 3.1-1-111 which defines membership of affiliated group for Indiana income tax returns and states that if any bank is a member of an affiliated group for Federal income tax purposes then it cannot be included as an affiliated member for adjusted gross income tax purposes since banks are not subject to adjusted gross income tax. Since the bank is not a member of [Taxpayer's] Indiana income tax return, the loss limitation for Indiana filing purposes should be computed excluding [Taxpayer's bank subsidiary]. . . .

B. Taxpayer's Response.

Taxpayer protests the Department's determination excluding its bank subsidiary from the calculation of its net operating loss deduction. Taxpayer asserts that it correctly included the income of its bank subsidiary in the calculation because the bank subsidiary is included in the federal calculation of its non-life insurance company group. Taxpayer maintains that the Department is unfairly "requiring a recomputation of the Section 1503(c)(1) federal deduction [limitation]" based upon the members of its Indiana consolidated group as opposed to its federal consolidated group "creating a situation where [Taxpayer's] federal taxable income is no longer the starting point for Indiana tax purposes" for this tax year and the years after.

C. Hearing Analysis.

Again, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "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). Consequently, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Further, "when [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] deter *[sic]* 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) (internal citation omitted). Thus, all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

For federal tax purposes, an "affiliate group" of corporations "shall . . . have the privilege of making a consolidated return." I.R.C. § 1501. The affiliated group's federal consolidated income tax is calculated as provided under the regulations prescribed under section 1502. I.R.C. § 1503(a). An "affiliate group" is defined as a group of "includible corporations." I.R.C. § 1504. Generally, life insurance companies are not "includible corporations" for federal consolidated return purposes. I.R.C. § 1504(b). However, a parent company with non-life insurance and life insurance affiliates can make an election for its consolidated group filing to include the life insurance companies in certain circumstances. I.R.C. § 1504(c). These consolidated returns report the income and losses of

the parent's affiliated subsidiaries in two subgroups, one group for the life insurance companies and one group for the non-life insurance companies. See Treas. Reg. § 1.1502-47(a)(2).

When this election for the consolidation of life insurance and non-life insurance companies is made, special rules exist for applying the amount of the losses earned by the life insurance companies group against the income earned by non-life insurance companies group and vice versa. See I.R.C. § 1503(c); Treas. Reg. § 1.1502-47(a)(2). The losses earned by one subgroup must first be applied to income of that same subgroup in the preceding years before the losses is applied to the income of the other subgroup in the year in which the loss occurred. Treas. Reg. § 1.1502-47(a)(2)(ii). Then, any subgroup losses that are carried forward to a future year must also first be applied against the same subgroup's income before it is applied to the other subgroup's income. Treas. Reg. § 1.1502-47(a)(2)(iii). However, these losses that are available for use against the other subgroup's income are subject to an additional limitation. I.R.C. § 1503(c). The non-insurance companies group's loss that can be applied against the life insurance group's income is limited to "[thirty-five] percent of such loss or [thirty-five] percent of the taxable income of the [life insurance companies group], whichever is less." I.R.C. § 1503(c)(1). This thirty-five percent limitation applies for the year in which the non-life insurance companies group incurred the loss as well as for the subsequent carry-forward years. Id.

For the 2010 tax year, Taxpayer made the election under I.R.C. § 1504(c) to include its life insurance companies in its federal consolidated return filings. There is no question that for federal tax purposes, Taxpayer's bank subsidiary is allowed to file as a part of this federal consolidated return. Thus, Taxpayer correctly determined that its bank subsidiary was to be included in its federal consolidated filing as part of its non-life insurance company group when determining its federal net operating loss limitation under I.R.C. § 1503(c)(1) for its federal consolidated filing group.

However, for Indiana adjusted gross income tax purposes, Taxpayer's bank subsidiary is not included as part of its Indiana consolidated filing. As explained in 45 IAC 3.1-1-111, "[i]f any bank is a member of an affiliated group for Federal income tax purposes, it cannot be included as an affiliated member for Indiana adjusted gross income tax purposes, since the banking entity is not subject to the adjusted gross income tax." Pursuant to IC § 6-5.5-9-4, a corporation that is subject to FIT in Indiana under IC 6-5.5 "is not . . . subject to the income taxes imposed under IC 6-3." IC § 6-3-1-15 defines a "taxpayer" as "any person or any corporation subject to taxation under this article." Thus, any corporation that is subject to FIT for a taxable period is not subject to income tax under IC 6-3 and is not a taxpayer under IC 6-3. An Indiana consolidated return filing is made by an affiliated group of taxpayers to report the taxes imposed by IC 6-3. IC § 6-3-4-14.

Pursuant to IC § 6-3-4-14(a), an "affiliated group" of corporations are allowed "the privilege of making a consolidated return with respect to the taxes imposed by IC 6-3" as long as certain conditions are met. All corporations in the "affiliated group" must "consent" to the filing requirements specified in IC § 6-3-4-14. An Indiana consolidated return "affiliated group" is an "'affiliated group' as defined in Section 1504 of the Internal Revenue Code with the exception that the affiliated group shall not include any corporation which does not have adjusted gross income derived from sources within the state of Indiana." IC § 6-3-4-14(b). Thus, for those taxpayers filing an Indiana consolidated return, an affiliated group for purposes of I.R.C. §1504 has been redefined to include only those corporation's that have "adjusted gross income derived from sources within in Indiana." Lastly, IC § 6-3-4-14(c) prescribes that "the determination of 'taxable income,' as defined in Section 63 of the Internal Revenue Code, of any affiliated group of corporations making a consolidated return and of each corporation in the group, both during and after the period of affiliation, shall be determined pursuant to the regulations prescribed under Section 1502 of the Internal Revenue Code." In effect, federal "taxable income" is calculated for this newly defined Indiana affiliated group and for each of the corporation's in the Indiana affiliated group under the federal consolidated return regulations. Therefore, IC § 6-3-4-14(b)-(c) specifically provides for the redetermination of federal taxable income for each corporation in the Indiana affiliated group as well as for the Indiana affiliated group itself under the federal consolidated return regulations.

For the taxable periods at issue, Taxpayer's bank subsidiary was subject to FIT in Indiana under IC § 6-5.5. Since Taxpayer's bank subsidiary was subject to FIT for those periods, Taxpayer's bank subsidiary was, pursuant to IC § 6-5.5-9-4, not subject to tax under IC § 6-3 for those periods. Therefore, Taxpayer's bank subsidiary was not a taxpayer for IC § 6-3 purposes and not part of the Taxpayer's Indiana affiliated group.

Accordingly, the Department redetermination of Taxpayer's net operating loss limitation under I.R.C § 1503(c) for its Indiana affiliated group–that excluded the income from Taxpayer's bank subsidiary that was subject to FIT from the calculation–was proper under IC § 6-3-4-14.

FINDING

Taxpayer's protest of the imposition of adjusted gross income tax as a result of the Department's calculation of Taxpayer's non-life group's net operating loss limitation is respectfully denied.

IV. Corporate Income Tax-Net Operating Loss Deductions: Entities Subject to FIT.

DISCUSSION

Taxpayer protests the Department's disallowance of its net operating loss deduction for losses incurred by Taxpayer during the tax years 2006 and the short year January 1, 2007, to June 30, 2007. During these tax periods, Taxpayer, its bank, and Holding Subsidiary were subject to financial institution's tax ("FIT") under IC § 6-5.5.

A. Audit Results.

Taxpayer included in its calculation of its 2010 Indiana net operating loss deduction the losses that were incurred by Taxpayer during taxable periods when Taxpayer was subject to FIT. The Department determined that Taxpayer had incorrectly calculated its net operating loss deduction as allowed under IC § 6-3-2-2.6 and disallowed the losses that were incurred by Taxpayer and its subsidiaries while they were subject to FIT.

Specifically, the audit made the following findings (pages 9-10 of the audit report ending in 5-08):

> Net operating losses were incurred in both [the 2006 tax year] and [the short year January 1, 2007, to June 30, 2007] that were filed on a combined basis. [Taxpayer's] reported position is that the net operating losses sustained by [Taxpayer] from these FIT filing years should be carried forward to years when [Taxpayer] is again subject to Indiana Adjusted Gross Income Tax (AGIT). In determining [Taxpayer's] portion of the combined group loss, [Taxpayer] allocated based on Indiana receipts and prorated for shortened reporting periods. The position per audit is that [Taxpayer] is not allowed to carry forward a net operating loss determined under the FIT statutes into a year where [Taxpayer] is subject to AGIT. These two taxes are mutually exclusive in that [Taxpayer] is never subject to both at the same time. Different statutes, regulations and definitions govern these two different tax types. Adjusted gross income and ultimately taxable income are computed in separate and unique ways. . . .

B. Taxpayer's Response.

Taxpayer asserts that the losses incurred by Taxpayer and its subsidiaries during periods when they were subject to FIT are allowed. Taxpayer maintains that they "had no choice in how they were taxed in Indiana once they became subject to supervision by banking regulators." Taxpayer states that "[n]owhere in the Indiana Code or the Department's regulations does it state that this deduction [under IC § 6-3-2-2.6] is denied if the [net operating loss] happens to related to a year that a corporation was subject to FIT."

C. Hearing Analysis.

Again, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "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). Consequently, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Further, "when [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] deter *[sic]* 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) (internal citation omitted). Thus, all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

A corporation's Indiana net operating loss deduction is determined under IC § 6-3-2-2.6(c), which provides a computation that starts with "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." (Emphasis added). Thus, the net operating loss deduction calculation would include only the federal net operating loss for a taxable year of an entity that is a taxpayer for that taxable year.

A "taxpayer" is defined in IC § 6-3-1-15 as "any person or any corporation subject to taxation under this article." Therefore, for an entity's federal taxable income to be included in the equation in IC § 6-3-2-2.6(c), the entity must meet the definition of taxpayer in IC § 6-3-1-15 for that taxable year and, therefore, must be a corporation subject to taxation under IC 6-3 for that taxable year.

Pursuant to IC § 6-5.5-9-4, a corporation that is subject to FIT in Indiana under IC 6-5.5 "is not . . . subject to the income taxes imposed under IC 6-3." Thus, any corporation that is subject to FIT for a taxable period is not subject to income tax under IC 6-3 for that taxable period and, therefore, is not a taxpayer under IC 6-3 for that taxable period.

For the taxable periods as issue, Taxpayer and its subsidiaries were subject to FIT in Indiana under IC 6-5.5. Since Taxpayer and its subsidiaries were subject to FIT for those periods, Taxpayer and its subsidiaries were, pursuant to IC § 6-5.5-9-4, not subject to tax under IC 6-3 for those periods. Therefore, Taxpayer and its subsidiaries were not taxpayers for purposes of IC § 6-3-2-2.6 for those taxable periods.

Accordingly, the Department disallowance of Taxpayer's net operating loss deduction–that Taxpayer claimed for net operating losses incurred during taxable periods for which Taxpayer and its subsidiaries were subject to FIT and were not taxpayer's for purposes of IC § 6-3-2-2.6–was proper.

FINDING

Taxpayer's protest to the imposition of tax from the Department's disallowance of its net operating loss deduction–that Taxpayer claimed for net operating losses incurred during periods for which Taxpayer and its subsidiaries were subject to financial institution's tax–is respectfully denied.

SUMMARY

Taxpayer's protest is respectfully denied.

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