

Letter of Findings Number: 01-20150219
Individual Income Tax
For Tax Years 2011-12

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 This document is effective as of its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Individuals are the sole shareholders of their S Corporation, and the corporation's income flows to them. The corporation is liable for additional adjusted gross income tax, thus; Individuals are properly liable for additional individual income tax.

ISSUE

I. Individual Income Tax–S Corporation Receipts.

Authority: IC § 6-8.1-5-1; Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579 (Ind. 2014); Indiana Dept. of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dept. of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); [45 IAC 3.1-1-66](#).

Taxpayers protest proposed assessments for additional individual income tax.

STATEMENT OF FACTS

Taxpayers are shareholders of an Indiana S Corporation ("S-Corp"). The Indiana Department of Revenue ("Department") audited S-Corp for sales and use tax and corporate income tax as well as Taxpayers for individual income tax. Taxpayers protested the results of all of these audits. This Letter of Findings addresses Taxpayers' protest of proposed individual income tax assessments. As the result of an audit, the Department determined that S-Corp had under-reported sales for the tax years 2011 and 2012. The Department examined S-Corp's income tax returns and bank statements, which showed the cash and credit card deposits totaled more than the amount of gross sales reported on the income tax returns. The Department made adjustments to S-Corp's gross income for the years 2011 and 2012. The adjustments resulted in an increase in Taxpayers' taxable income. The Department therefore issued proposed assessments for individual income taxes for years 2011 and 2012. Taxpayers protested the proposed assessments. An administrative hearing was held and this Letter of Findings results. Further facts will be supplied as required.

I. Individual Income Tax–S Corporation Receipts.

DISCUSSION

Taxpayers protest the Department's proposed assessments of additional individual income tax. In the companion Letter of Findings (02-20140609) addressing the assessment of adjusted gross income tax for S-Corp, the Department found the business had underreported its sales and improperly deducted some of its expenses during the audited tax years. This resulted in additional adjusted gross income for the business. Since the business is an S Corporation, the tax liability flows to Taxpayers because they are the sole shareholders of the business.

As a threshold issue, it is Taxpayers' 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 Dept. of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dept. 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, "[W]hen [courts] examine a statute that an agency is 'charged with enforcing. . . [courts] defer to the agency's reasonable interpretation of [the]

statute even over an equally reasonable interpretation by another party." Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579, 583 (Ind. 2014). Thus, all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

The Department refers to [45 IAC 3.1-1-66](#), which provides in part:

Subchapter S corporation shareholders are taxed on their distributive shares of income at the individual income tax rate. The character of the income (as capital gains or ordinary income) also passes through to the shareholders.

Therefore, income from an S Corporation flows through to the individual shareholders' personal income, and is reported by the shareholders on their personal income tax returns. In this case, Taxpayers are the sole shareholders of S-Corp, which requires them to report S-Corp's income on their individual income tax returns pursuant to [45 IAC 3.1-1-66](#). In the companion LOF (02-20140609), the Department found that S-Corp had additional income from sales that it did not report. Taxpayers did meet their burden of establishing that some of their business' expenses were properly deducted. However, Taxpayers did not meet their burden of establishing that the remainder of the Department's proposed assessments of additional income tax for S-Corp were wrong as required IC § 6-8.1-5-1(c). Therefore, the Department will re-determine the business' adjusted gross income minus the properly deducted expenses. Taxpayers will then be liable for the amount of additional income that the Department determines flows through to them from S-Corp, pursuant to [45 IAC 3.1-1-66](#).

FINDING

Taxpayer's protest is respectfully denied.

Posted: 09/30/2015 by Legislative Services Agency
An [html](#) version of this document.