DEPARTMENT OF STATE REVENUE

03-20150606.LOF

Letter of Findings Number: 03-20150606
Withholding Tax
For Tax Years 2012-14

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 This document is effective as of its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

Retail business did not prove that the Department's calculations of withholding tax which should have been remitted were incorrect. Therefore, the Department's proposed assessments for withholding tax were proper.

ISSUES

I. Withholding Tax–Calculations.

Authority: IC § 6-8.1-5-1; IC § 6-8.1-5-4; IC § 3-4-8; 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 3.1-1-97.

Taxpayer protests proposed assessments for additional withholding tax.

II. Tax Administration–Penalties and Interest.

Authority: IC § 6-8.1-5-4; IC § 6-8.1-10-1; IC § 6-8.1-10-2.1; 45 IAC 15-11-2.

Taxpayer protests the imposition of penalties and interest.

STATEMENT OF FACTS

Taxpayer is a retail business which was incorporated in February 2012 and which operated a store with gasoline sales with an attached convenience store. Taxpayer filed state and county withholding tax returns. As the result of an audit, the Indiana Department of Revenue ("Department") determined that Taxpayer had underreported state and county withholding taxes the tax years 2012, 2013, and 2014. As explained in the audit report, the Department first contacted Taxpayer in August 2014, to schedule the first meeting of the audit process. One of Taxpayer's shareholders ("Shareholder One") responded to the Department's letter and agreed to meet with the first auditor involved in the audit ("Auditor One") during the first week of August 2014. On the day of the scheduled meeting, no one representing Taxpayer showed up for the scheduled meeting. On September 23, 2014, Auditor One received a call from Shareholder One's business partner/former spouse ("Business Partner") requesting a detailed list of records required for the audit. Business Partner is not a shareholder in Taxpayer. Later that same day, Shareholder One called to request information about the audit of the store. Auditor One and Shareholder One agreed to reschedule the meeting for October 10, 2014. On that day, Auditor One was unable to meet with Shareholder One and arrangements were made for Auditor One's supervisor to meet with Shareholder One and to accept the requested records. The supervisor was also unable to meet with Shareholder One due to unforeseen circumstances. Shareholder One arrived at the Department's District Office and left a message for Auditor One to call him. Shareholder One did not leave any records with the Department at that time.

Later, Shareholder One emailed Auditor One to reschedule the meeting for October 27, 2014. Auditor One agreed and requested that Shareholder One bring records to that meeting. On October 27, 2014, Shareholder One and another person arrived at the Department's District Office, but did not bring any records. Shareholder One explained that his partner did not believe that Taxpayer was being audited and so Shareholder One requested a written statement from the Department explaining that an audit was underway. Auditor One complied with this request despite the fact that several written documents discussing the audit had already been sent to Shareholder One. The Department also gave Taxpayer until October 31, 2014 to provide the requested documents. The Department explained that without those documents the audit would proceed based on the best information

available to it.

On October 31, 2014, Shareholder One had an employee call Auditor One to request additional time to provide records. Auditor One explained that October 31, 2014 was the deadline and that it would not be extended. Auditor One retired before the audit was finished, and on February 20, 2015 the file was assigned to another auditor ("Auditor Two"). On March 3, 2015, Auditor Two sent an email to Shareholder One to advise him that she would be completing the audit. Auditor Two also requested that Shareholder One contact her to discuss the audit and to let him know that he could bring additional records at the time of the meeting. On March 4, 2015, Auditor Two called Shareholder One, but there was no answer and no voicemail option. On March 6, 2015, Auditor Two called again with similar results. Auditor Two sent Shareholder One an email with a complete list of records required to complete the audit and setting a deadline of March 11, 2015 to contact Auditor Two to avoid having the audit completed using the best information available to it. On March 11, 2015, Shareholder One called Auditor Two to set a meeting on March 18, 2015. On March 12, 2015, Auditor Two sent a confirmation email to Shareholder One regarding the new meeting date and repeating the list of required documents.

On March 18, 2015, two managers for the stores arrived at the Department's District Office, explaining that Shareholder One was ill and would not be attending. The two managers did not bring any records with them. They explained that Shareholder One and Taxpayer's other shareholder ("Shareholder Two") were estranged and were not communicating directly with each other. This lack of communication, according to the two managers, caused Shareholder Two to decide not to cooperate with the audit process even though he held most of the relevant records. Also, the two managers stated that they sent a package to the Department through FedEx. Auditor Two informed the managers that no package was received by the Department and requested that they either obtain and send in proof of delivery through FedEx or that they send the records again. During this meeting, the two managers provided the hours of operation for all of the stores operated by Taxpayer.

On March 27, 2015, Auditor Two sent an email to Shareholder One to recap the meeting on March 18 and to advise him that, unless additional records were provided, the audit would be completed using the best information available. No records were provided. On the Department therefore issued proposed assessments for sales tax, penalties, and interest for those years, based on the best information available. On October 2, 2015, Taxpayer protested a portion of the assessments.

On March 1, 2016, the Hearing Officer sent Taxpayer's representative ("Representative") a letter which scheduled the administrative hearing for March 17, 2016. Representative called the Hearing Officer requesting that the hearing be rescheduled to a date in late April 2016. The Hearing Officer explained that the hearing could be moved, but that a six week delay was not possible. The hearing was rescheduled for April 5, 2016. On April 4, 2016, Representative called the Hearing Officer to state that Shareholder One would be unavailable for the April 5 hearing due to a funeral. Representative again requested that the hearing be rescheduled for late April. The Hearing Officer informed Representative that, because the hearing had already been rescheduled once and because Shareholder One's presence was not required since Representative was authorized to represent Taxpayer, the hearing would not be rescheduled a second time. The administrative hearing was held on April 5, 2016, with an extension to April 22, 2016 to allow for the submission of additional documentation and analysis and this Letter of Findings results. Further facts will be supplied as needed.

I. Withholding Tax–Calculations.

DISCUSSION

Taxpayer protests a portion of the Department's proposed assessments of state and county withholding tax for the tax years 2012 through 2014. The Department based its determinations on the best information available to it. As described above, Taxpayer's managers explained the operating hours for the location operated by Taxpayer, which was twenty-four hours a day, 365 days a year. After review of the amount of state and county withholding remitted by Taxpayer, the Department determined that this amount was insufficient to pay employees to operate a convenience for the hours the managers said the store was open. In the absence of any documentation from Taxpayer, the Department referenced BizStats.com ("BizStats") to determine a reasonable estimate of wages for operating a convenience store with gasoline sales. The Department found that BizStats does not have a category for wages in convenience stores. The Department therefore found the BizStats categories for gasoline stations (2.12 percent of total sales) and for food and beverage stores (6.30 percent of total sales) and separately calculated employee wages for gasoline stations and for food and beverage stores, based on total sales for each type of business. Those two amounts were added together to determine total wages for the whole business and then that total was multiplied by 3.4 percent to arrive at total Indiana withholding tax which should have been remitted. Also, the total was multiplied by 1.25 percent to determine the amount of county withholding tax which

should have been remitted. Credit was allowed for the amounts of state and county withholding tax which had previously been remitted. The remaining amount was considered tax due and proposed assessments were issued.

Taxpayer protests that the Department did not use the best information available. First, Taxpayer states that the store in question was not open twenty-four hours a day, 365 days a year. Second, Taxpayer states that other BizStats categories offer more accurate percentages to reflect the amount of wages paid.

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 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.

First, the Department refers to IC § 6-3-4-8(a), which provides:

> Except as provided in subsection (d) or (l), every employer making payments of wages subject to tax under this article, regardless of the place where such payment is made, who is required under the provisions of the Internal Revenue Code to withhold, collect, and pay over income tax on wages paid by such employer to such employee, shall, at the time of payment of such wages, deduct and retain therefrom the amount prescribed in withholding instructions issued by the department. The department shall base its withholding instructions on the adjusted gross income tax rate for persons, on the total rates of any income taxes that the taxpayer is subject to under IC 6-3.5, and on the total amount of exclusions the taxpayer is entitled to under IC 6-3-1-3.5(a)(3) and IC 6-3-1-3.5(a)(4). However, the withholding instructions on the adjusted gross income of a nonresident alien (as defined in Section 7701 of the Internal Revenue Code) are to be based on applying not more than one (1) withholding exclusion, regardless of the total number of exclusions that IC 6-3-1-3.5(a)(3) and IC 6-3-1-3.5(a)(4) permit the taxpayer to apply on the taxpayer's final return for the taxable year. Such employer making payments of any wages:
> (1) shall be liable to the state of Indiana for the payment of the tax required to be deducted and withheld under this section and shall not be liable to any individual for the amount deducted from the individual's wages and paid over in compliance or intended compliance with this section; and
> (2) shall make return of and payment to the department monthly of the amount of tax which under this article and IC 6-3.5 the employer is required to withhold.

The relevant regulation is 45 IAC 3.1-1-97, which states in part:

> Employers who make payments of wages subject to the Adjusted Gross Income Tax Act, and who are required to withhold Federal taxes pursuant to the Internal Revenue Code (USC Title 26), are required to withhold from employees' wages Adjusted Gross and County Adjusted Gross Income Tax.

Therefore, employers such as Taxpayer are required to withhold adjusted gross and county adjusted gross income tax from payments of wages made to its Indiana employees.

Next, the Department refers to IC § 6-8.1-5-1(b), which states:

> If the department reasonably believes that a person has not reported the proper amount of tax due, the department shall make a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the department. The amount of the assessment is considered a tax payment not made by the due date and is subject to IC 6-8.1-10 concerning the imposition of penalties and interest. The department shall send the person a notice of the proposed assessment through the United States mail.
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> (Emphasis added).

Also, the Department refers to IC § 6-8.1-5-4(a), which states:

> Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records. The records referred to in this subsection include all source documents necessary to determine the tax, including invoices, register tapes, receipts, and canceled checks.
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> (Emphasis added).

Therefore, all taxpayers subject to a listed tax must keep books and records such as, but not limited to, invoices, register tapes, receipts, and cancelled checks, as provided by IC § 6-8.1-5-4-(a). If the Department reasonably believes that a person has not reported the proper amount of tax due, the department shall make a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the department, as provided by IC § 6-8.1-5-1(b). In the instant case, the Department had no records to review and so used the best information available in reaching its conclusion that Taxpayer did not report the proper amount of tax due.

In the course of the audit, the Department determined that Taxpayer had not reported sufficient state and withholding taxes to account for enough employees to operate the store twenty-four hours a day, 365 days per year. Taxpayer disagreed with this and protested that the store was only open from 6 a.m. to 11 p.m. seven days a week. In support of this position, Taxpayer offered a hand written, two-sentence letter from an individual claiming to have been a manager at the store. This statement is dated March 15, 2016, which is more than a year after the end of the audit period. The Department notes that the statement does not state that the individual was managing the store during the audit years. Neither does the letter contain any explanation of the signatory's work duties at the store. Neither does the letter state that the hours listed were consistent over the entire three years of the audit period.

Taxpayer also offered several similarly limited letters from other individuals who claim to have been managers at other stores operated by Taxpayer. Those letters address the operating hours of other stores, not the store at issue in this case. The Department is not convinced that, even if taken at face value, those letters have any bearing on the hours of operation at the store which is the subject of the instant protest. Taxpayer was unable to provide any documentation for the Department to review in support of its position that the store was not open twenty-four hours a day, 365 days a year. As previously explained, all taxpayers are required to keep records for the Department to review under IC § 6-8.1-5-4(a). Therefore, since Auditor Two was told during the audit process by two of Taxpayer's managers that the store was operated twenty-four hours a day, 365 days a year, the Department's use of those hours of operation was reasonable. Taxpayer has offered no records or documentation other than extremely limited letters from unverified sources in support of its position regarding the number of employees required to operate the store at issue.

Next, Taxpayer states that the Department erred in its choice of BizStats categories when calculating its best information available estimates of withholding tax due. Specifically, Taxpayer believes that the Department should apply the same 2.12 percent of total sales to determine what wages should have been for the gasoline portion of the store to the total convenience store sales, rather than the 6.30 percent of total sales BizStats recommends for calculating food and beverage stores' wages, as was done in the audit. In the course of the protest process, Taxpayer provided definitions of several different retailers, such as gasoline stations, food and beverage stores, and convenience stores, as defined by the North American Industry Classification System. Taxpayer believes that these definitions are significant and that BizStats relies on these definitions in its own definitions. Therefore, Taxpayer believes that the Department should rely on these definitions as well.

The Department is not convinced by Taxpayer's argument. Taxpayer's references to the North American Industry Classification System's definitions is not a substitute for the documents it was required to keep under IC § 6-8.1-5-4(a). The Department's best information available calculations, as authorized by IC § 6-8.1-5-1(b) were reasonable in light of the absence of documentation from Taxpayer. The Department applied the BizStats percentage for gasoline station wages to gasoline sales and it applied the BizStats percentage for food and beverage store wages to convenience store sales. Taxpayer's suggestion that the Department apply the significantly lower gasoline station wages percentage of 2.12 to convenience store sales is inappropriate. No matter what definition is applied to a convenience store, none of them approach the definition of a gasoline station.

In conclusion, Taxpayer's protest is based on post-audit, vague statements from personnel with unverified credibility stating that at some point the store in question (or two other stores which are not the subject of the audit) was not open twenty-four hours a day, 365 days a year. The Department is unpersuaded by these documents. Neither is the Department persuaded by Taxpayer's references to various definitions of various retail operations. Taxpayer failed in its duties to keep and make available records for the Department to review, as

provided by IC § 6-8.1-5-4(a). The Department therefore was compelled to use the best information available to it to determine whether or not additional tax was due, as provided by IC § 6-8.1-5-1(b). The Department made logical and reasonable efforts to be as accurate as possible, given the total absence of Taxpayer documentation. It is Taxpayer's burden to prove the proposed assessments wrong, as established by IC § 6-8.1-5-1(c). Taxpayer has not met that burden.

FINDING

Taxpayer's protest is denied.

II. Tax Administration–Penalties and Interest.

DISCUSSION

Taxpayer protests the imposition of penalties pursuant to IC § 6-8.1-10-2.1 and the imposition of interest pursuant to IC § 6-8.1-10-1. The Department notes that waiver of interest is not permitted under IC § 6-8.1-10-1(e). Penalty waiver is permitted if the taxpayers show that the failure to pay the full amount of the tax was due to reasonable cause and not due to willful neglect. 45 IAC 15-11-2(b) clarifies the standard for the imposition of the negligence penalty as follows:

> "Negligence", on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The standard for waiving the negligence penalty is given at 45 IAC 15-11-2(c) as follows:

> The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section. Factors which may be considered in determining reasonable cause include, but are not limited to:
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> (1) the nature of the tax involved;
> (2) judicial precedents set by Indiana courts;
> (3) judicial precedents established in jurisdictions outside Indiana;
> (4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc.;
> (5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.
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> Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

Taxpayer protests the Department's assessment of penalties and interest. After review of the documentation and analysis provided in the protest process, the Department may not waive interest, as provided by IC §6-8.1-10-1(e). Taxpayer failed in its duty to keep sales records as required under IC § 6-8.1-5-4(a). Taxpayer has not affirmatively established that it exercised ordinary business care in this case. Therefore, waiver of penalties is not warranted under 45 IAC 15-11-2(c).

FINDING

Taxpayer's protest to the imposition of penalties and interest is denied.

SUMMARY

Taxpayer's Issue I protest regarding the imposition of state and county withholding tax is denied. Taxpayer's Issue

II protest regarding the imposition of penalties and interest is denied.

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