

**Letter of Findings Number: 01-20170094  
Individual Income Tax  
For Tax Years 2013, 2014 & 2015**

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 This document is effective as of its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

Individual Shareholder was responsible for additional individual income tax because he could not deduct hobby activity as S-Corporation's ordinary and necessary business expenses.

### ISSUE

#### **I. Individual Income Tax—Pass-Through Income.**

**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).

Taxpayer protests proposed assessments of additional individual income tax.

### STATEMENT OF FACTS

Taxpayer is the sole shareholder of an Indiana S-corporation in the business of selling lawn mowers and other outdoor power equipment ("S-Corp"). During the audit period, S-Corp also purchased "slot cars" which are miniature, collectable cars that race on electric race tracks. As the result of a corporate income tax audit, the Indiana Department of Revenue ("Department") determined that S-Corp overstated its business expense deductions for the tax years 2013, 2014 and 2015 ("Tax Years"). The audit thus disallowed certain business expense deductions which resulted in the assessment of additional income tax. Because S-Corp is operated as a pass-through entity, the Department issued proposed assessments to Taxpayer for individual income tax for the Tax Years.

S-Corp protested the audit's disallowance of the deductions. Taxpayer also protested the proposed assessments for individual income tax and associated penalties and interest. An administrative hearing was held to address S-Corp's and Taxpayer's protests. A separate Letter of Findings 04-20170095 addresses S-Corp's protest of the income tax audit and a related use tax audit. Further facts will be supplied as necessary.

#### **I. Individual Income Tax—Pass-Through Income.**

### DISCUSSION

Taxpayer protests the Department's finding that S-Corp overstated its deductible business expenses, thus understating its corporate income tax liability. Specifically, the audit found that purchases of slot cars and accessories were not qualified business expenses because they constituted Shareholder's hobby, and were therefore not deductible as S-Corp's business expenses. The audit also found that S-Corp overstated its deduction for fuel expenses and reduced the allowable deduction by fifty-percent. Taxpayer protests the resulting increase in his individual income tax liability for the same reasons S-Corp protested findings made in the corporate income tax audit.

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.

In a separate Letter of Findings, the Department denied S-Corp's protest of the disallowance of certain business expense deductions. The Department found that purchases of slot cars and related accessories constituted Shareholder's personal hobby and were therefore not ordinary and necessary business expenses. The Department further found that S-Corp could not show that the Department's calculation of fuel expenses was incorrect because it failed to sufficiently document actual vehicle expenses. Since Taxpayer's protest is wholly dependent on the outcome of S-Corp's protest of the characterization of its slot car activity and documentation of its vehicle expenses, Taxpayer's protest is also denied.

### **FINDING**

Taxpayer's protest is respectfully denied.

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