

Letter of Findings: 01-20170142
Individual Income Tax
For the Years 2010, 2011, and 2012

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

Indiana Restaurant Partner failed to establish that the Department's assessment of additional income tax on the flow-through restaurant income was "wrong;" the Department established that Restaurant Partner's restaurant income was underreported, the assessment was not issued outside Indiana's statute of limitations, and the assessment did not violate Restaurant Partner's Due Process Rights.

ISSUE

I. Indiana Individual Income Tax - Flow-Through Business Income.

Authority: U.S. Const. amend. V; IC § 6-3-4-11; IC § 6-3-4-11(a); IC § 6-8.1-5-1(b); IC § 6-8.1-5-1(c); IC § 6-8.1-5-2(b); IC § 6-8.1-5-2(f); *Grady v. Corbin*, 110 S.Ct. 2084 (1990); *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); [45 IAC 3.1-1-106](#); [45 IAC 15-5-7](#)(e).

Taxpayer argues that the Department of Revenue overstated the amount of income attributable to his shared ownership of twenty-four Indiana restaurants, that the assessment of tax was outside the statute of limitations, and that the penalty assessment violates the Double Jeopardy Clause of the United States Constitution.

STATEMENT OF FACTS

Taxpayer is a partner in twenty-four Indiana restaurants. The Indiana Department of Revenue ("Department") along with local law enforcement agencies conducted an audit investigation of the restaurants' books, records, and tax returns. The investigation resulted in the issuance of the Department's "Case Report" dated December 2104. The Case Report concluded that during 2010 through 2012, the restaurants failed to report the full amount of their sales. Accordingly, the Department issued the restaurants assessments of additional tax.

Criminal tax evasion charges were filed against Taxpayer. Taxpayer pled guilty to those charges. As a partner to the restaurants, the Department conducted an audit review of Taxpayer's own income tax returns and tax records resulting in the assessment of additional Indiana income tax.

Taxpayer protested the assessment of income tax. An administrative hearing was conducted during which Taxpayer's representative explained the basis for the protest. This Letter of Findings results.

I. Indiana Individual Income Tax - Flow-Through Business Income.

DISCUSSION

Taxpayer objects to the assessment of additional income tax on the grounds that the assessments are overstated, that the Department acted outside its authority in assessing the tax, that the assessments are barred by the statute of limitations, and that the penalty assessment violates the Double Jeopardy Clause of the United States Constitution.

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, "[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, interpretations of Indiana tax law contained within this decision, as well as the preceding audit and investigative report, are entitled to deference.

Because the restaurants are operated as S-corporations, IC § 6-3-4-11 imposes on the Taxpayer the responsibility for paying Indiana individual income tax on his share of the income earned from two restaurants. The statute provides in part:

A partnership as such shall not be subject to the adjusted gross income tax imposed by [IC 6-3-1](#) through [IC 6-3-7](#). *Persons or corporations carrying on business as partners shall be liable for the adjusted gross income tax only in their separate or individual capacities.* In determining each partner's adjusted gross income, such partner shall take into account his or its distributive share of the adjustments provided for in [IC 6-3-1-3.5](#).

IC § 6-3-4-11(a) (*emphasis added*); see also [45 IAC 3.1-1-106](#).

In the 2014 "Case Report" issued by the Department's "Special Investigation Division," the Department found that Taxpayer's restaurants underreported the amount of sales which occurred at the restaurant locations.

The Department's investigation found that the restaurants failed to maintain "source documents" and that it was the restaurants' practice to destroy "guest check tickets" on a regular basis. In addition, the audit questioned the accuracy of the restaurants' daily summary register tapes ("z-tape") because the cash register daily tapes were not retained. The audit report also indicates that it was the practice of restaurant employees to "register a lesser amount than the actual sales price," use the "no sale" register button to ring up particular transactions, and routinely "left the cash register drawer open between customers." Further, the audit found that a review of the restaurants' bank accounts established "that there were no cash deposits for many months, and often there were no cash deposits for years."

In reviewing the restaurants' general ledgers, the Department found that restaurant "[r]evenues were increased and cash on hand was increased in order to balance [] accounting entries." According to the Department's investigative report, the restaurants' practice of adjusting the general ledger entries "indicates the business was not reporting all their sales" and that restaurant records were incomplete and unreliable.

The Department is unable to agree with Taxpayer that the assessment of additional tax was unfounded or that the Department had no basis upon which to issue the assessment. Instead, the Department acted reasonably in fulfilling the responsibility imposed upon it by IC § 6-8.1-5-1(b) which *mandates* that the Department issue proposed assessments when there is a reasonable belief a taxpayer has not reported the correct amount of tax due. As explained in the audit report, "The Department could not rely on the [T]axpayer's records" Taxpayer has produced no substantive, contemporaneous documents which would directly - or even indirectly - refute the Department's conclusion that the restaurants' record keeping practices were questionable at best and Taxpayer's income from the restaurants was under-reported. Taxpayer raises numerous objections but has proposed no reasonably well-documented alternative to the assessment. If there are records accurately detailing the restaurant's 2010 through 2012 sales and the corresponding income passing through to Taxpayer, Taxpayer has not produced them.

Taxpayer argues that the assessments were issued outside the three-year statute of limitations. Taxpayer is incorrect. IC § 6-8.1-5-2(b) provides as follows:

If a person files a return for the utility receipts tax ([IC 6-2-3](#)), adjusted gross income tax ([IC 6-3](#)), supplemental net income tax ([IC 6-3-8](#)) (repealed), county adjusted gross income tax ([IC 6-3.5-1.1](#)) (repealed), county option income tax ([IC 6-3.5-6](#)) (repealed), local income tax ([IC 6-3.6](#)), or financial institutions tax ([IC 6-5.5](#)) that understates the person's income, as that term is defined in the particular income tax law, by at least twenty-five percent (25[percent]), the proposed assessment limitation is six (6) years instead of the three (3) years provided in subsection (a).

See also [45 IAC 15-5-7\(e\)](#).

Since Taxpayer underreported his income by more than twenty-five percent, the assessments are not barred by the three-year limitation. In addition, IC § 6-8.1-5-2(f) provides:

If a person files a fraudulent, unsigned, or substantially blank return, or if a person does not file a return, there is no time limit within which the department must issue its proposed assessment.

Taxpayer pled guilty in Marion County Superior Court of failing to report tax. It was not unreasonable to impute to Taxpayer the failure to report the income from the restaurants to which he was a partner.

Finally, Taxpayer - having pled guilty to criminal evasion of taxes - argues that the assessment of the tax penalty is barred by the Double Jeopardy Clause of the United States Constitution. Taxpayer relies on U.S. Const. amend. V which provides, "nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb." As stated in *Grady v. Corbin*, 110 S.Ct. 2084, 2087 (1990), "[T]he Double Jeopardy Clause of the Fifth Amendment prohibits successive prosecutions for the same criminal act or transaction under two *criminal statutes*" (*Emphasis added*). In this case, Taxpayer has a routine income tax penalty issued under an Indiana civil tax provision. There is little indication that the Department has imperiled either the "life or limb" of Taxpayer. The penalty imposed by the Department does not stem from a criminal statute but rather is a civil penalty; the principle of Double Jeopardy is not implicated.

The Department is unable to agree that Taxpayer has made a coherent or quantifiably specific objection to the results of the audit. Rather than offering a specific alternative, Taxpayer has simply set forth a litany of complaints and criticisms. The Department does not disagree with Taxpayer's suggestion that there *may* be alternative methods of determining the income from these two restaurant locations, but Taxpayer has done nothing to meet his burden of establishing that the assessments are "wrong" as required by IC § 6-8.1-5-1(c).

The Department acted well within its statutory mandate of issuing assessments when confronted with instances of underreported tax, the issuance of the assessment did not take place outside the statute of limitations, and the assessment does not constitute a violation Taxpayer's Fifth Amendment Due Process rights.

FINDING

Taxpayer's protest is denied.

Posted: 11/29/2017 by Legislative Services Agency
An [html](#) version of this document.