

Letter of Findings: 02-20170365
Corporate Income Tax
For the Year 2016

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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 Partnership was not entitled to claim the Indiana College Credit on its composite Indiana return because the tax reported on the return was merely the individual income tax reported and paid at the partnership level; the tax was that of the non-resident partners and not that of the partnership. However, Indiana Partnership was entitled to "retrospective treatment" of the Department's final determination.

ISSUE

I. Corporate Income Tax - Indiana College Credit.

Authority: IC § 4-22-2-19.1; IC § 6-3-3-5; IC § 6-3-3-5(b); IC § 6-3-3-10(h); IC § 6-3.1-4-7; IC § 6-3-4-12(e); IC § 6-8.1-3-3(b); IC § 6-8.1-5-1(c); *INDOPCO, Inc. v. Comm'r.*, 503 U.S. 79 (1992); *Parker Pen Co. v. O'Day*, 234 F.2d 607 (7th Cir. 1956); *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); *State v. Smith*, 63 N.E. 25 (1902); *Florer v. Sheridan*, 36 N.E. 365 (1893); *Fresenius USA Marketing, Inc. v. Indiana Department of State Revenue*, 56 N.E.3d 734 (Ind. Tax Ct. 2016); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480 (Ind. Tax Ct. 2012); *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138 (Ind. Tax Ct. 2010); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289 (Ind. Tax Ct. 2007); *Ind. Dep't of State Revenue v. Food Marketing Corp.*, 403 N.E.2d 1093 (Ind. Ct. App. 1980); Income Tax Information Bulletin 72 (December 2015).

Taxpayer argues that the Department erred when it disallowed credits on Taxpayer's composite income tax return for contributions made to Indiana colleges and universities made on behalf of Taxpayer's nonresident partners.

STATEMENT OF FACTS

Taxpayer is an Indiana business which files an Indiana "composite" income tax return reporting the income of Taxpayer's non-resident partners. Taxpayer filed its 2016 composite return. On that return, Taxpayer claimed an approximately \$29,000 Indiana College Credit. The Indiana Department of Revenue ("Department") reviewed the return and denied the credit. The denial of the credit resulted in assessment of additional income tax. Taxpayer disagreed with the assessment and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representative explained the basis for the protest. This Letter of Findings results.

I. Corporate Income Tax - Indiana College Credit.

DISCUSSION

The issue is whether Taxpayer is entitled to claim an Indiana College Credit on its Indiana composite income tax return.

As a threshold issue, it is the Taxpayer's responsibility to establish that the assessment of corporate income tax 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). Thus, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Poorly developed and

non-cogent arguments are subject to waiver. *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138, 1145 (Ind. Tax Ct. 2010); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480, 486, fn. 9 (Ind. Tax Ct. 2012). 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 are entitled to deference.

Taxpayer cites to IC § 6-3-3-5(b) as support for its position that it is entitled to claim a credit for the contribution made on behalf of its non-resident partners:

In the case of a taxpayer other than a corporation, the amount allowable as a credit under this section for any taxable year shall not exceed one hundred dollars (\$100) in the case of a single return or two hundred dollars (\$200) in the case of a joint return.

In relevant contrast to IC § 6-3-3-5, the Indiana legislature has specifically provided for "credits" which "flow-through" to non-resident partners. For example, IC § 6-3.1-4-7 provides as follows:

- (a) If a pass through entity does not have state income tax liability against which the research expense tax credit may be applied, a shareholder, partner, or member of the pass through entity is entitled to a research expense tax credit equal to:
 - (1) the research expense tax credit determined *for the pass through entity* for the taxable year; multiplied by
 - (2) the percentage of the pass through entity's distributive income to which the shareholder, partner, or member is entitled.
- (b) The credit provided under subsection (a) is in addition to a research expense tax credit to which a *shareholder, partner, or member of a pass through entity is otherwise entitled under this chapter*. However, a pass through entity and a shareholder, partner, or member of the pass through entity may not claim a credit under this chapter for the same qualified research expenses.

(Emphasis added).

From this - and other examples - it is apparent that the legislature was fully capable of structuring an income tax credit such that the credit could "flow-through" to a "shareholder, partner, or member of the pass through" In the case of the Indiana College Credit, the legislature made no such provision and Taxpayer is not entitled to "read into" the statute a provision which is otherwise entirely absent. See *also* IC § 6-3-3-10(h).

A deduction such as that found in IC § 6-3-3-5 is not an exemption. See *State v. Smith* 158 Ind. 543, 63 N.E. 25 (1902); *Floreer v. Sheridan*, 137 Ind. 28, 36 N.E. 365 (1893). However, the Indiana College Credit has the same result as an exemption and the taxpayer has the burden of establishing that it is entitled to that deduction. "The enlarged deduction has the same end result as the enlarged exemption. In both instances, the tax burden of the individual taxpayer is decreased; but in so doing, the tax burden of all other taxpayers is increased. The allowed or enlarged deduction shifts the tax burden. Thus, like the tax exemption, the tax deduction should be narrowly construed." *Ind. Dep't of State Revenue v. Food Marketing Corp.*, 403 N.E.2d 1093, 1102 (Ind. Ct. App. 1980) (Staton, J. dissenting). The principle that deductions are narrowly construed is well-founded in federal law. "[A]n income tax deduction is a matter of legislative grace and that the burden of clearly showing the right to the claimed deduction is on the taxpayer." *INDOPCO, Inc. v. Comm'r.*, 503 U.S. 79, 84 (1992). "[S]tatutes creating deductions are to be strictly construed against the taxpayer." *Parker Pen Co. v. O'Day*, 234 F.2d 607, 609 (7th Cir. 1956).

In the case of a composite return, the tax reported is merely the individual income tax reported and paid at the partnership (Taxpayer) level. The tax is that of the non-resident partners and not that of the partnership. As stated in IC § 6-3-4-12(e):

Amounts deducted from payments or credits to a nonresident partner during any taxable year of the partnership in accordance with the provisions of this section *shall be considered to be in part payment of the tax imposed on such nonresident partner for the nonresident partner's taxable year* within or with which the partnership's taxable year ends. A return made by the partnership under subsection (b) shall be accepted by the department as evidence in favor of the nonresident partner of the amount so deducted for the nonresident partner's distributive share.

(Emphasis added).

Under IC § 6-3-3-5, the credit does not "flow through because the partnership - and not the partners - made the contributions. Thus the individual could not claim the credit. Because Taxpayer itself does not have a tax liability, Taxpayer cannot claim the credit. Taxpayer has failed to meet its burden of establishing that the Indiana College Credit is a "pass through" credit which the Indiana statute allows to be claimed by Taxpayer on its composite Indiana income tax return.

Nonetheless, Taxpayer cites to Income Tax Information Bulletin 72 (December 2015), 20160127 Ind. Reg. 045160043NRA, which provides as follows:

Any college credit for individual contributions is limited on the composite return to the lower of each shareholder's state tax liability or \$100 (no joint credit with spouse is permitted).

The Information Bulletin is wrong on this particular issue; as did Taxpayer, the Bulletin "reads into" the statute a provision allowing a partnership to claim the credit. That provision is not found in the statute. However, Taxpayer was entitled to rely on the Department's Bulletin when it completed its 2016 composite return and is therefore able to claim the 2016 credit and to avoid paying any additional income liability attributable to the Department's decision disallowing the credit. IC § 6-8.1-3-3(b); IC § 4-22-2-19.1.

However, going forward Taxpayer is on notice that it cannot claim the credit unless there is a statutory change allowing the credit. Pursuant to IC § 4-22-2-19.1, IC § 6-8.1-3-3(b), and *Fresenius USA Marketing, Inc. v. Indiana Department of State Revenue*, 56 N.E.3d 734 (Ind. Tax Ct. 2016), the Department revokes that portion of the Information Bulletin that references the college credit. Beginning on the date this LOF is published in the Indiana Register (the "publication date"), the Department's position on this issue is set forth in this LOF, and not as set forth in the Information Bulletin. Taxpayers may no longer rely on the Information Bulletin.

FINDING

As to the substantive credit issue, Taxpayer's protest is respectfully denied. However, Taxpayer is entitled to "retroactively rely" on the directions contained in Income Tax Information Bulletin 72.

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