

**Supplemental Letter of Findings: 02-20181181
Adjusted Gross Income Tax
For The Tax Years 2014-16**

NOTICE: IC § 4-22-7-7 permits the publication of this document in the Indiana Register. The publication of this document provides the general public with information about the Indiana Department of Revenue's official position concerning a specific set of facts and issues. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Supplemental Letter of Findings.

HOLDING

Business was able to establish that one aspect of the Department's calculations was incorrect. Business was not able to establish that the Department's calculations were incorrect in any other way.

ISSUE

I. Adjusted Gross Income Tax—Calculation.

Authority: IC § 6-3-2-2; 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 the Department's calculation of adjusted gross income tax due.

STATEMENT OF FACTS

Taxpayer operates a restaurant in Indiana. As the result of an audit, the Indiana Department of Revenue ("Department") determined that Taxpayer had under-reported adjusted gross income tax ("AGIT") for the tax years 2014, 2015, and 2016. The Department therefore issued proposed assessments for AGIT, penalties, and interest for those years. Taxpayer filed a protest of the proposed assessments and an administrative hearing was scheduled. Neither Taxpayer nor its representative appeared or called into the scheduled administrative hearing. Following Departmental policy, the protest was deemed withdrawn and the protest file closed without issuing a written decision on Taxpayer's protest. Subsequently, Taxpayer's representative requested and was granted a rehearing. The rehearing was scheduled via telephone and Taxpayer's representative called in at the appropriate time to present Taxpayer's protest. This Supplemental Letter of Findings results. Further facts will be supplied as required.

I. Adjusted Gross Income Tax—Calculation.

DISCUSSION

Taxpayer protests the Department's calculations of AGIT for the tax years 2014-16. The Department based its determinations of AGIT due on its determination in a related audit of Taxpayer's sales tax compliance. In that other audit, the Department used the best information available, since Taxpayer did not keep cash register tapes or other sales records. Rather, Taxpayer kept track of sales in journals, which were supplied to the Department. The Department supplemented the information in the journals with information from Taxpayer's income tax returns, sales tax returns, withholding tax returns, employee W-2s, food and beverage tax returns, and various other financial information from Taxpayer. The Department also used information from Total Systems Services, which provides information regarding businesses and the financial averages in various aspects of those businesses. The Department's calculations resulted in the determination that Taxpayer had additional unreported sales. The Department then concluded that the additional sales resulted in additional income to Taxpayer. Taxpayer protested the results of the sales tax audit. Taxpayer protested that, while there may have been additional sales, those additional sales were not as high as calculated by the Department.

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.

Indiana income tax is established under IC § 6-3-2-2(a), which states:

With regard to corporations and nonresident persons, "adjusted gross income derived from sources within Indiana", for the purposes of this article, shall mean and include:

- (1) income from real or tangible personal property located in this state;
- (2) *income from doing business in this state*;
- (3) income from a trade or profession conducted in this state;
- (4) compensation for labor or services rendered within this state; and
- (5) income from stocks, bonds, notes, bank deposits, patents, copyrights, secret processes and formulas, good will, trademarks, trade brands, franchises, and other intangible personal property to the extent that the income is apportioned to Indiana under this section or if the income is allocated to Indiana or considered to be derived from sources within Indiana under this section.

Income from a pass through entity shall be characterized in a manner consistent with the income's characterization for federal income tax purposes and shall be considered Indiana source income as if the person, corporation, or pass through entity that received the income had directly engaged in the income producing activity. Income that is derived from one (1) pass through entity and is considered to pass through to another pass through entity does not change these characteristics or attribution provisions. In the case of nonbusiness income described in subsection (g), only so much of such income as is allocated to this state under the provisions of subsections (h) through (k) shall be deemed to be derived from sources within Indiana. In the case of business income, only so much of such income as is apportioned to this state under the provision of subsection (b) shall be deemed to be derived from sources within the state of Indiana. In the case of compensation of a team member (as defined in section 2.7 of this chapter), only the portion of income determined to be Indiana income under section 2.7 of this chapter is considered derived from sources within Indiana. In the case of a corporation that is a life insurance company (as defined in Section 816(a) of the Internal Revenue Code) or an insurance company that is subject to tax under Section 831 of the Internal Revenue Code, only so much of the income as is apportioned to Indiana under subsection (r) is considered derived from sources within Indiana.

In this case, Taxpayer was doing business in Indiana and so was subject to AGIT as provided by IC § 6-3-2-2(a). The Department's calculations of additional sales at the restaurant resulted in the determination that Taxpayer also had additional income from those sales.

Taxpayer protests that the Department's sales tax calculations were too high and that the AGIT calculations were correspondingly too high. In the Supplemental Letter of Findings which addressed Taxpayer's sales tax protest, the Department agreed with one point of the protest and disagreed with the other point. The result of that Supplemental Letter of Findings was that the Department agreed to recalculate the amount of additional sales which would result in a lower amount of sales tax due for the tax years. That also means that Taxpayer's protest of the AGIT calculations will be similarly reduced, since there will be a lower amount of additional sales from which additional income could flow. The Department will recalculate the amount of AGIT due after recalculating the amount of additional sales as determined in the related sales tax audit/protest.

FINDING

Taxpayer's protest is sustained in part and denied in part.

May 31, 2018

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