

**Final Order Denying Refund: 01-20182238R
Individual Income Tax
For Tax Year 2017**

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 is provided for the convenience of the reader and is not part of the analysis contained in this document.

HOLDING

Married couple did not establish that out-of-state local taxes were paid by them or paid by the couples' LLC on behalf of the couple.

ISSUE

I. Individual Income Tax--Refund.

Authority: IC § 6-8.1-9-1; IC § 6-3.5-1.1-6; KRS 91.260; *Dept. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); Louisville, Kentucky Metro Code § 110.02; Information Bulletin 115.

Taxpayers protest the denial of their claim for refund.

STATEMENT OF FACTS

Taxpayers, husband and wife, filed a Claim for Refund via an amended Indiana IT-40X with the Indiana Department of Revenue ("Department") for the tax year 2017. Taxpayers claimed a refund of local taxes paid to Kentucky. The Department denied Taxpayers' refund claim in a letter dated August 31, 2017 stating that "Taxes paid by your [Limited Liability Companies ("LLC")] are not pass-through deductions. They are business expenses and reduce your pass-through income." Taxpayers in turn filed a protest with the Department requesting a final determination without a hearing. Further facts will be presented as required.

I. Individual Income Tax--Refund.

DISCUSSION

Taxpayers filed an amended return for tax year 2017 requesting a refund. The Department denied the refund since the Taxpayers' LLC paid the income tax in Kentucky, and therefore the individual shareholders could not claim credit on Kentucky local taxes paid.

The Department initially notes that, "[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 all the Department's previous decisions, shall be entitled to deference. Taxpayers' refund claim was filed pursuant to IC § 6-8.1-9-1.

Taxpayers protest letter states:

Due to recent court case, *Comptroller of Maryland v. Wynne*, and a change in policy via Commissioner's Directive [number]57 by the Indiana Department of Revenue, we believe [Taxpayers] . . . [are] entitled to the refund we have requested on their amended 2017 return. The directive, influenced by the Supreme Court's decision in *Comptroller of Maryland v. Wynne*, allows a credit on an individual's Indiana tax return for taxes paid to another state's local, county, and/or city taxes to reduce the individual's county taxes paid to Indiana.

Taxpayers, to substantiate their protest, provided their 2017 Indiana amended return, Commissioner's Directive 57 July 2016, Indiana 2017 original IT-40, their 2017 Kentucky Individual income tax return for nonresident or part-year resident, their Kentucky Occupational License Tax Return for the LLC, several Kentucky county Net Profits Occupational License Tax Returns for the LLC, and K-1s.

Indiana law includes IC § 6-3.5-1.1-6, prior Indiana Information Bulletins, and various published written decisions by the Department.

Before its repeal in 2017, IC § 6-3.5-1.1-6 stated:

(a) Except as provided in subsection (b), if for a particular taxable year a county taxpayer *is liable for an income tax imposed by a county, city, town, or other local governmental entity located outside of Indiana, that county taxpayer is entitled to a credit against his county adjusted gross income tax liability for that same taxable year.* The amount of the credit equals the amount of tax imposed by the other governmental entity on income derived from sources outside Indiana and subject to the county adjusted gross income tax. However, the credit provided by this section may not reduce a county taxpayer's county adjusted gross income tax liability to an amount less than would have been owed if the income subject to taxation by the other governmental entity had been ignored.

(b) The credit provided by this section does not apply to a county taxpayer to the extent that the other governmental entity provides for a credit to the taxpayer for the amount of county adjusted gross income taxes owed under this chapter.

(c) *To claim the credit provided by this section, a county taxpayer must provide the department with satisfactory evidence that he is entitled to the credit.*

(Emphasis added).

Based on the statute above Taxpayers must be directly responsible for the tax. The Kentucky statute at issue, KRS 91.260, states in relevant part, "Each city of the first class shall raise a revenue from ad valorem taxes and from taxes based on *income, licenses and franchises.*" *(Emphasis added).* Information Bulletin 115, 20180131 Ind. Reg. 045180053NRA, November 2017 (replaced Commission's Directive 57) states in relevant part:

The tax regimes of Maryland and Indiana differ in several key respects. Like Maryland, Indiana imposes a state income tax, taxes residents on income earned elsewhere, and taxes non-residents on income earned in Indiana.

Unlike Maryland, however, Indiana allows credit for out-of-state taxes at both the state and local levels. Indiana allows a credit for out-of-state income taxes against Indiana's state income tax and a credit for out-of-state local income taxes against local income taxes owed in Indiana.

However in this instance it is not a *Wynne* issue per se, but a preliminary issue of local tax that is per Kentucky law, that is an entity level tax. There is no Indiana corollary. In the present case, Taxpayers have not established that the tax at issue was imposed on the husband and/or wife personally and not on the LLC itself. Taxpayers have not provided the Department with a copy of a Louisville/Jefferson County return that shows that the husband and/or wife paid the tax at issue as an individual (that is to say, Taxpayers have not established that the husband or wife was directly responsible for the tax, and not the LLC). In fact, Chapter 110, Section 110.02(D) of the Louisville/Jefferson County Metro Code of Ordinances states in relevant part, "The occupational license taxes imposed in this chapter are **assessed against business income at the entity level** and before it is passed through to the partners, members, shareholders or owners." **(Emphasis added)**. In other words, it is the entity—viz., the LLC—that the occupational license tax is imposed upon. Thus, since Kentucky taxes local taxes at the entity level the Department was correct in denying Taxpayers' individual income tax refund claim.

FINDING

Taxpayers' protest is denied.

May 2, 2019

Posted: 07/31/2019 by Legislative Services Agency
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