DEPARTMENT OF STATE REVENUE

02-20191011.LOF

Letter of Findings: 02-20191011
Corporate Income Tax
For the Year 2018

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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 again 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, 158 Ind. 543 (1902); *Florer v. Sheridan*, 36 N.E. 365, 137 Ind. 281 (1893); *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); Letter of Findings 02-20170365 (August 18, 2017).

Taxpayer argues that the Department erred when it disallowed credits on Taxpayer's 2018 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 2018 composite return. On that return, Taxpayer claimed an Indiana College Credit amount. The Indiana Department of Revenue ("Department") reviewed the return and denied the credit. The denial of the credit resulted in an assessment of approximately $10,000 in additional income tax. Taxpayer disagreed with the assessment and submitted a protest to that effect. This Letter of Findings results.

I. Corporate Income Tax - Indiana College Credit.

DECISION

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).

In considering Taxpayer's argument, the Department bears in mind that "when [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 apparently relies on IC § 6-3-3-5(b) as support for its position that it is entitled to claim a credit for the college 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 is 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 neither the Department nor Taxpayer are 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); *Florer v. Sheridan*, 137 Ind. 28, 36 N.E. 365 (1893). However, the Indiana College Credit has the same result as an exemption and a 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 such as that submitted by Taxpayer, 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 individuals may not claim the credit. Because Taxpayer - operating as a partnership - 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 Taxpayer to claim on its composite Indiana income tax return.

Nonetheless, Taxpayer relies on 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 Department "reads into" the statute a provision allowing a partnership to claim the credit. That provision is not found in a statute which the law requires be "strictly construed." *Parker Pen*, 234 F.2d at 609. Nonetheless, Taxpayer was entitled to rely on the Department's Bulletin when it completed its 2018 composite return and is therefore able to claim the 2018 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.

Taxpayer is reminded that this identical issue was addressed in a Letter of Findings (Letter of Findings 02-20170365 (August 18, 2017), 20171129-IR-045170526NRA) in which Taxpayer protested an assessment attributable to the filing of its 2016 return. The result in that Letter of Findings is identical. There is (and was) no statutory provision permitting the "flow through" of Indiana college credits to corporate partners.

The result in this 2019 protest is the same as the 2017 decision because the Department did not correct the misinformation contained in the Information Bulletin. Taxpayer - and all Indiana taxpayers - are entitled to rely on the Department's published guidance in determining their tax obligations.

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.

October 30, 2019

Posted: 12/25/2019 by Legislative Services Agency
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