

Letter of Findings: 01-20210107
Individual Income Tax
For the Years 2013 through 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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

The Department disagreed with Indiana Business Owners' argument that the assessments of additional income tax were barred by the statute of limitations because Business Owners originally underreported their adjusted gross income by more than 25 percent; the Department also declined to revisit the substantive issues addressed in Business Owners' supplemental audit because their rehearing request was untimely.

ISSUES

I. Individual Income Tax - Statute of Limitations.

Authority: IC § 6-8.1-5-1; Executive Order 20-05 (March 19, 2020) *Indiana Department of Revenue*, <https://www.in.gov/dor/legal-resources/appeals/> (June 26, 2020).

Taxpayers argue that the four individual yearly assessments are barred in whole or in part by Indiana's statute of limitations.

II. Individual Income Tax - Disallowance of Business Deductions.

Authority: IC § 6-8.1-5-1; IC § 6-8.1-5-2; IC § 6-8.1-9-1; *Indiana Dep't of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480 (Ind. Tax Ct. 2012); *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463 (Ind. 2012); *Smith v. Indiana Department of State Revenue*, 122 N.E.3d 484 (Ind. Tax. Ct. 2019); *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); [45 IAC 15-5-7\(a\)](#).

Taxpayers argue that the Department erred in disallowing Schedule C business deductions claimed on their 2013 through 2016 individual income tax returns and assessing additional income tax.

STATEMENT OF FACTS

Taxpayers are Indiana residents who operate an Indiana business. The business provides horse breeding, stabling, and horse training services.

The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayers' individual Indiana income tax returns. The audit found that Taxpayers had improperly deducted expenses stemming from operating their business. Instead, the audit found that Taxpayers were incurring expenses stemming from a "hobby." Those expenses were disallowed because "hobby expenses" were not "ordinary and necessary" costs incurred in "carrying on [a] trade or business." This decision resulted in an assessment of additional income and use tax.

Taxpayers disagreed with the audit assessment and submitted a protest to that effect. An administrative hearing was conducted and Letter of Findings 01-20191483; 04-20191484 (May 19, 2020) was issued. That Letter of Findings ("LOF") sustained Taxpayers on the issue of whether Taxpayers were training, breeding, and stabling horses as a "hobby" and not as a "business."

Since the May 2020 LOF sustained Taxpayers on the business/hobby issue, the matter was referred to the Department's audit division in order to conduct a supplemental audit. The purposes of this supplemental audit was to determine whether Taxpayers were able to verify the amount of expenses originally claimed. That

supplemental audit reduced a portion of the original assessments but found that Taxpayers overstated the amount of eligible expenses. This second audit again found that Taxpayers still owed additional Indiana income tax although that amount is less than the original assessments. Thereafter, the Department issued a "Demand Notice for Payment" for each year and assessment at issue.

Taxpayers disagreed with the results of the supplemental audit and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayers and their representative explained the basis for that protest. This Letter of Findings results.

I. Individual Income Tax - Statute of Limitations.

DISCUSSION

It is important at the outset to explain that the issues raised here are - according to Taxpayers - not one-and-the-same as the issues Taxpayers raised in the May 2020 LOF. Taxpayers maintain that the issues and dollar amounts are entirely distinguished from the original assessments.

The first issue is whether Taxpayers have met their burden of establishing that the four-year assessments are barred in whole or in part by Indiana's statute of limitations' provisions.

As a threshold issue, it is the Taxpayers' responsibility to establish that the existing adjusted gross income 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).

In challenging an assessment, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Further, when an agency is charged with enforcing a statute, the courts defer to the agency's reasonable interpretation of that statute "over an equally reasonable interpretation by another party." *Indiana Dep't 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, are entitled to deference. 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 n.9 (Ind. Tax Ct. 2012).

The Department does not have limitless authority to assess additional tax. Indiana law sets a maximum time within which an additional tax assessment may be imposed.

IC § 6-8.1-5-2(a) provides as follows:

Except as otherwise provided in this section, the department may not issue a proposed assessment under section 1 of this chapter *more than three (3) years after the latest of the date the return is filed*, or either of the following:

- (1) The due date of the return.
- (2) In the case of a return filed for the state gross retail or use tax, the gasoline tax, the special fuel tax, the motor carrier fuel tax, the oil inspection fee, or the petroleum severance tax, the end of the calendar year which contains the taxable period for which the return is filed. (*Emphasis added*).

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

However, IC § 6-8.1-5-2(b) contains a provision extending that assessment period - under limited circumstances - to six years.

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).

The Department refers to *Smith v. Indiana Department of State Revenue*, 122 N.E.3d 484 (Ind. Tax. Ct. 2019) which held that, "The 6-year statute of limitations under Section 2(b) is triggered when a taxpayer understates by more than 25[percent] its 'income' computed under any of the six enumerated income tax schemes." *Id.* at 493. In addition, the court found that the IC § 6-8.1-5-2(b) reference to "income" referred to the petitioners' "adjusted gross income" and not, as petitioners argued, their "gross income." *Id.* At 494.

In this case, the assessment issues trace back to four different periods and four different returns as follows:

- 2013 Indiana income tax return originally filed and postmarked February 20, 2014 and due on April 15, 2014. The Department determined that Taxpayers underreported their adjusted gross income by approximately 53 percent.
- 2014 Indiana income tax return originally filed and postmarked February 11, 2015 and due on April 15, 2015. The Department determined that Taxpayers underreported their adjusted gross income by approximately 53 percent.
- 2015 Indiana income tax return originally filed and postmarked February 9, 2014 and due on April 18, 2016. The Department determined that Taxpayers underreported their adjusted gross income by approximately 39 percent.
- 2016 Indiana income tax return originally filed and postmarked April 7, 2017 and due on April 18, 2017. The Department determined that Taxpayers underreported their adjusted gross income by approximately 39 percent.

Taxpayers are protesting the following assessments all of which were addressed in the supplemental audit review. Those assessments are designated:

- 2013-04110353; this proposed assessment was issued by the Department September 12, 2019, five years, four months, and 28 days after the due date of the original return.
- 2014-04110355; this proposed assessment was issued by the Department September 12, 2019, four years, four months, and 28 days after the due date of the return.
- 2015-04110358; this proposed assessment was issued by the Department September 12, 2019, three years, four months, and 26 days after the due date of the return.
- 2016-04110363; this proposed assessment was issued by the Department September 12, 2019, two years, four months, and 26 days after the due date of the return.

Taxpayers misapprehend the nature of these assessments. None of the designated proposed assessments (2013-04110353, 2014-04110355, 2015-04110358, or 2016-04110363) were issued outside the IC § 6-8.1-5-2(b) six-year statute of limitations because, in each case, The Department determined that Taxpayers underreported their adjusted gross income by at least 25 percent.

FINDING

Taxpayers' protest is respectfully denied.

II. Individual Income Tax - Disallowance of Business Deductions.

DISCUSSION

Taxpayers argue that they are entitled to challenge the supplementary audit's decisions disallowing portions of the originally claimed expenses. Specifically, Taxpayers claim that they are entitled to additional deductions related to: (1) interest expenses; (2) vehicle expenses; (3) utility expenses; and (4) supply and material costs such as gravel and lumber.

As mentioned above, these specific adjustments were the results of the supplemental audit review. However, Taxpayers indicate that they are now prepared to offer "more detailed and voluminous documentation" and point out that Taxpayers have "incurred additional costs associated" with preparing this additional documentation.

Taxpayers argued that the pending liabilities are "entirely new assessments and not the assessments as those determined by the [original] hearing officer." As explained by Taxpayers elsewhere, these are all "new dollars and new issues."

The original Letter of Findings was issued on May 19, 2020. Accompanying the LOF was the boilerplate notice that the recipient was entitled to "request a rehearing under IC § 6-8.1-5-1" which states:

A person that disagrees with a decision in a letter of findings may request a rehearing not more than thirty (30) days after the date on which the letter of findings is issued by the department. The department shall consider the request and may grant the rehearing if the department reasonably believes that a rehearing would be in the best interests of the taxpayer and the state. IC § 6-8.1-5-1(g).

Under a bare reading of IC § 6-8.1-5-1(g), Taxpayers were required to submit their request by Tuesday, May 19, 2020. However, circumstances intervened and Executive Order 20-05 (March 19, 2020) authorized Indiana agencies to extend certain statutory deadlines. In the case of the Department, it concluded that:

Unless the time in which to request a rehearing expired on or before March 19, 2020, any customer wishing to request a rehearing of a final determination, has an additional 60 days from the date the final determination was issued in which to do so. *Indiana Department of Revenue*, <https://www.in.gov/dor/legal-resources/appeals/> (June 26, 2020).

Given the authority granted the Department under the Executive Order, Taxpayers were required to submit their rehearing request by August 17, 2020, which is 90 days after the original Letter of Findings was issued.

Taxpayers submitted their request May 17, 2021 and supplemented that request June 30, 2021. Taxpayers maintain that these are new assessments and new dollars; Taxpayers are wrong. The amounts may be different but the assessments (2013-04110353, 2014-04110355, 2015-04110358, or 2016-04110363) are the same. Taxpayers do not have the right to protest a "Demand Notice for Payment" under IC § 6-8.1-5-1(j)(3), and the Department has no authority to address such a protest. As such, Taxpayers' request to reopen these liabilities for reexamination under the guise of a rehearing request must be denied.

This may seem an inequitable result since the supplemental audit was not issued until May 6, 2021, some 262 days after the date on which Taxpayers were required to request the rehearing. Equitable or not, those are the rules under which Department is required to operate. Under Taxpayer's rationale, a taxpayer would have the right to an administrative hearing each time the Department issued an updated assessment adding additional interest; such a result may also seem inequitable and impractical. Even if the Department were now to issue another written decision addressing the substantive expense issues here raised, it would have no effect and would not alter the assessment amounts one whit.

The only viable option available to Taxpayers is to pay the liability, request a refund under the grounds set forth above, and - if the refund is denied - *timely* submit a protest based on that denial as permitted under IC § 6-8.1-9-1.

FINDING

Taxpayers' protest is denied because the Department lacks the authority to revisit the four assessments.

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