

**Letter of Findings: 04-20210111**  
**Tax Administration**  
**For the Years 2014-2019**

**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 Indiana Department of Revenue'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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

Taxpayer failed to provide sufficient documentation and analysis to establish that the penalties and interest should be abated.

### ISSUE

#### I. Tax Administration - Penalties and Interest.

**Authority:** [IC 6-2.5-2-1](#); [IC 6-2.5-9-3](#); [IC 6-8.1-5-1](#); [IC 6-8.1-5-4](#); [IC 6-8.1-10-1](#); [IC 6-8.1-10-2.1](#); [IC 6-8.1-10-4](#); [IC 6-8.1-10-7](#); *Dept. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Dept. of Treas. v. Ice Serv.*, 41 N.E.2d 201 (Ind. 1942); *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); *Indiana Dept. of State Revenue v. Safayan*, 654 N.E.2d 270 (Ind. 1995); *Universal Group Ltd. v. Indiana Dept. of State Revenue*, 642 N.E.2d 553 (Ind. T.C. 1994); [45 IAC 15-5-7](#); [45 IAC 15-11-2](#); [45 IAC 15-11-4](#); Black's Law Dictionary (11th ed. 2019); Restatement (First) of Agency § 1 (1933); Restatement (Third) of Agency § 1.01 (2006).

Taxpayer protests the penalty and interest in the Department's assessment.

### STATEMENT OF FACTS

Taxpayer is an Indiana-based retailer. The Indiana Department of Revenue ("Department") audited Taxpayer's sales records for tax years 2017-2019. During the audit, the Department determined that Taxpayer did not file sales tax returns or remit sales tax for several months of 2014 and all of 2016-2019. Furthermore, the Department determined that Taxpayer underreported sales tax for 2015.

The Department issued proposed assessments adjusting the amount of sales tax due for 2014-2019. Taxpayer disagreed with the proposed assessment and submitted a protest. An administrative hearing was held, and this Letter of Findings results. Additional facts will be provided below, as necessary.

#### I. Tax Administration - Penalties and Interest.

### DISCUSSION

The Department audited Taxpayer for tax years 2017-2019. The audit revealed that Taxpayer had collected sales tax but not filed sales tax returns for or remitted Indiana sales tax from March to December in 2014, as well as for 2016-2019. However, Taxpayer filed returns for and remitted both Indiana income tax and federal excise tax for 2014-2019. Furthermore, Taxpayer underreported Indiana sales tax for 2015. Taxpayer reported \$23,691 in total sales and a \$1,658.37 tax liability. As determined in the Department's audit, Taxpayer had \$561,931 in total sales and a \$31,927.49 tax liability in 2015. The Department adjusted Taxpayer's sales tax accordingly for 2014-2019.

Taxpayer stated in its protest letter that the reason for both underreporting and not filing Indiana sales tax for the tax years of 2014-2019 was due to an error with the business' QuickBooks point of sale system. Taxpayer provided limited documentation to support its reasoning. Taxpayer conceded that it owes the unremitted sales tax. Taxpayer protests the penalty and interest claiming financial hardship. Regarding Taxpayer's protest on the imposition of interest, under [IC 6-8.1-10-1](#)(e) the Department is prohibited from waiving interest.

As a threshold issue, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect. A proposed assessment is prima facie evidence that the Department's claim for the unpaid tax is valid. [IC 6-8.1-5-1\(c\)](#). The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made. *Id.*; See e.g., *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). An assessment, including Taxpayer's penalty assessment, is therefore presumed valid. A taxpayer must provide documentation explaining and supporting that the Department's position is wrong. Additionally, "[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).

[IC 6-2.5-2-1\(b\)](#) provides:

The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. *The retail merchant shall collect the tax as agent for the state.* (Emphasis added).

The Indiana Tax Court, in *Universal Group Ltd. v. Indiana Dept. of State Revenue*, 642 N.E.2d 553, 556 (Ind. T.C. 1994), explained:

Section 1 of the Restatement (First) of Agency defines agency as "the relationship which results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act." Our supreme court adopted this definition in full in *Dept. of Treas. v. Ice Serv.*, 41 N.E.2d 201, 203 (Ind. 1942), and in the more than half a century since, Indiana courts have adhered to it. (Internal notation and emphasis omitted).

§ 1.01 of the Restatement (Third) of Agency states:

Agency is the *fiduciary relationship* that arises when one person (a "principal") manifests assent to another person (an "agent") that the agent shall act on the principal's behalf and subject to the principal's control, and the agent manifests assent or otherwise consents so to act. (Emphasis added).

"Fiduciary" is defined in Black's Law Dictionary (11th ed. 2019) as:

1. Someone who is required to act for the benefit of another person on all matters within the scope of their relationship; *one who owes to another the duties of good faith, loyalty, due care, and disclosure* (the corporate officer is a fiduciary to the corporation). 2. *Someone who must exercise a high standard of care in managing another's money or property* (the beneficiary sued the fiduciary for investing in speculative securities). (Emphasis added).

Therefore, when a retail merchant is acting as an agent for the state, as provided by [IC 6-2.5-2-1\(b\)](#), Indiana uses the definition of "agent" provided in the Restatement of Agency, as confirmed by the court in *Universal Group Ltd.* Agents have a fiduciary relationship with Indiana, as defined by the Restatement (Third) of Agency § 1.01. That fiduciary relationship means that the retail merchant acts as Indiana's agent and owes Indiana the duties of good faith, loyalty, due care, and disclosure and must exercise a high standard of care in managing Indiana's money, as defined by *Black's*.

Next, [IC 6-2.5-9-3](#) states that an individual who:

(1) is an individual retail merchant or is an employee, officer, or member of a corporate or partnership retail merchant; and  
(2) *has a duty to remit state gross retail or use taxes to the [D]epartment; holds those taxes in trust* for the state and is personally liable for the payment of those taxes, plus any penalties and interest attributable to those taxes, to the state. (Emphasis added).

The Indiana Supreme Court provided further explanation in *Indiana Dept. of State Revenue v. Safayan*, 654

The taxes at issue in this case are the gross retail tax, Ind.Code Ann. § 6-2.5-3-2 (West 1989 & Supp.1990), and the withholding tax on employee wages, Ind.Code Ann. § 6-3-4-8 (West 1989). *These are termed "trust taxes" because the obligors pay them to third parties designated by statute to collect, hold, and remit the money to the State. These third parties hold the funds in trust for the State and thus may be held personally liable when the funds are not remitted.*  
(Emphasis added).

Next, the Department refers to [IC 6-8.1-10-7](#), which provides, "[T]he maximum total penalty that may be assessed against a person . . . is one hundred percent (100 percent) of the unpaid tax. . . ." Regarding liability for penalties, [IC 6-8.1-10-2.1\(a\)](#) states, a person that:

- (1) fails to file a return for any of the listed taxes;
  - (2) fails to pay the full amount of tax shown on the person's return on or before the due date for the return or payment;
  - (3) incurs, upon examination by the department, a deficiency that is due to negligence;
  - (4) fails to timely remit any tax held in trust for the state; or
  - (5) fails to file a return in the electronic manner required by the department if such return is required to be filed electronically;
- is subject to a penalty.

According to [IC 6-8.1-5-4\(a\)](#), "Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records. The records referred to in this subsection include all source documents necessary to determine the tax, including invoices, register tapes, receipts, and canceled checks."

As a starting point, the Department refers to [45 IAC 15-11-2](#), which describes the negligence penalty as:

(a) "Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or *inattention to duties* placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer. (Emphasis added).

(b) The department shall waive the negligence penalty imposed under [IC 6-8.1-10-1](#) if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under [\[45 IAC 15-11-2\]](#). . . .

Subsequently, the Department refers to [IC 6-8.1-10-4](#), which states:

(a) If a person fails to file a return or to make a full tax payment with that return with the fraudulent intent of evading the tax, the person is subject to a penalty.

(b) *The amount of the penalty imposed for a fraudulent failure described in subsection (a) is one hundred percent (100[percent]) multiplied by:*

- (1) the full amount of the tax, if the person failed to file a return; or
- (2) *the amount of the tax that is not paid, if the person failed to pay the full amount of the tax.*

(c) In addition to the civil penalty imposed under this section, a person who knowingly fails to file a return with the department or fails to pay the tax due under [IC 6-6-5](#), [IC 6-6-5.1](#), or [IC 6-6-5.5](#) commits a Class A misdemeanor.

(d) The penalty imposed under this section is imposed in place of and not in addition to the penalty imposed under section 2.1 of this chapter.  
(Emphasis added).

Further, the Department refers to [45 IAC 15-11-4](#), which states:

The penalty for failure to file a return or to make full payment with that return with the fraudulent intent of evading the tax is one hundred percent (100[percent]) of the tax owing. Fraudulent intent encompasses the making of a misrepresentation of a material fact (See [45 IAC 15-5-7\(f\)\(3\)](#)) which is known (See [45 IAC 15-5-7\(f\)\(3\)\(B\)](#)) to be false, or believed not to be true, in order to evade taxes. Negligence, whether slight or great, is not equivalent to the intent required. An act is fraudulent if it is an actual, intentional wrongdoing, and the intent required is the specific purpose of evading tax believed to be owing.

Also, [45 IAC 15-5-7\(f\)\(3\)](#) provides:

(3) *A person who files a return which makes a false representation(s) with knowledge or reckless ignorance of the falsity will be deemed to have filed a fraudulent return. There are five elements to fraud.*

(A) *Misrepresentation of a material fact:* A person must truthfully and correctly report all information required by the Indiana Code and the department's regulations. Any failure to correctly report such information is a misrepresentation of a material fact. Failure to file a return may be a misrepresentation.

(B) *Scienter:* This is a legal term meaning guilty knowledge or previous knowledge of a state of facts, such as evasion of tax, which it was a person's duty to guard against. A person must have actual knowledge of the responsibility of reporting the information under contention. However, the reckless making of statements without regard to their truth or falsity may serve as an imputation of scienter for purpose of proving fraud.

(C) *Deception:* Deception operates on the mind of the victim of the fraud. If a person's actions or failure to act causes the department to believe a given set of facts which are not true, the person has deceived the department.

(D) *Reliance:* Reliance also concerns the state of mind of the victim and is generally considered along with deception. If the person's actions, failure to act, or misrepresentations cause the department to rely on these acts to the detriment or injury of the department, the reliance requirement of fraud will be met.

(E) *Injury:* The fraud instituted upon the department must cause an injury. This can be satisfied simply by the fact that the misrepresentation(s) caused the department not to have collected the money which properly belongs to the state of Indiana.

In order to demonstrate fraud, the department is required to prove all of the above elements are present. This must be shown by clear and convincing evidence. *(Emphasis added).*

Taxpayer collected but failed to file returns for and remit sales tax in Indiana for part of 2014, as well as 2016-2019, but successfully filed its federal returns and remitted excise tax each year during that same period. Additionally, Taxpayer underreported Indiana sales tax for 2015. Taxpayer acknowledged that it was at fault because it did not file and remit Indiana sales tax. Per [IC 6-8.1-10-2.1](#) and [IC 6-8.1-10-1](#), failure to file a return for sales tax, subjects Taxpayer to penalties and interest. Taxpayer reasoned that it was QuickBooks that failed and caused this situation. Yet, Taxpayer filed an annual sales tax return for 2020 and monthly sales tax returns starting in 2021 upon receiving the letter from the Department explaining that an audit was scheduled. Taxpayer's actions and inactions plainly go beyond mere negligence, as defined by [45 IAC 15-11-2](#). Therefore, the Department imposed the fraud penalty provided under [IC 6-8.1-10-4](#).

In reviewing the imposition of the fraud penalty in the instant case, the Department will review the five elements of fraud, as provided under [45 IAC 15-5-7\(f\)](#). The first element of fraud is misrepresentation. As failure to file a return may be a misrepresentation, this element is satisfied by the fact that Taxpayer did not file returns for sales tax and remit sales tax required by the Indiana Code and the Department's regulations. From 2014-2019, Taxpayer failed to file Indiana sales tax for 58 out of 72 months. Furthermore, Taxpayer underreported Indiana sales tax for an additional 12 months.

The second element of fraud is scienter, which states that a person must have actual knowledge of the responsibility of reporting the information under contention. This element is satisfied by the fact that Taxpayer had actual knowledge of the responsibility of filing and remitting Indiana sales tax. This is confirmed by the fact that Taxpayer knowingly filed sales tax returns and remitted Indiana sales tax in previous years, including part of 2014 and all of 2015 as well as subsequent years after notification of a scheduled audit. Furthermore, Taxpayer was aware that filing and remitting sales tax was necessary because he did so prior to 2014 and after notification of the impending audit in 2021 and did file returns for Indiana income tax and for federal excise tax for 2014-2019.

The third and fourth elements are deception and reliance, which are considered together. Taxpayer did deceive

the Department as Taxpayer's actions caused the Department to believe that the Taxpayer's Indiana tax returns were accurate and true when they were not. Furthermore, the reliance element is satisfied as confirmed by the fact that Taxpayer's actions caused the Department to rely on Taxpayer's misrepresentations to the detriment of the Department and the State of Indiana.

The fifth element of fraud is injury, which is satisfied by the fact that Taxpayer's misrepresentations caused the Department to not collect the money which properly belonged to the state of Indiana.

All five elements of fraud, as provided by [45 IAC 15-5-7\(f\)](#), have been satisfied. The consistent and constant collection of and underreporting and nonreporting of sales tax confirms that Taxpayer's actions rise above mere negligence as defined by [45 IAC 15-11-2\(b\)](#).

In conclusion, Taxpayer was acting as an agent of the State of Indiana, as provided by [IC 6-2.5-2-1](#) and collected but failed to fulfil its duty as the State's agent to remit a trust tax, as explained by the Indiana Supreme Court in *Safayan*. Taxpayer was acting as an agent for the state, as provided by [IC 6-2.5-2-1\(b\)](#), as a fiduciary, as established by the court in *Universal Group Ltd.*, and had a fiduciary relationship with Indiana, as defined by the Restatement (Third) of Agency § 1.01. Taxpayer owed Indiana the duties of good faith, loyalty, due care, and disclosure and of exercising a high standard of care in managing Indiana's tax revenue. Taxpayer failed to fulfil these duties. All five elements of fraud, as provided by [45 IAC 15-5-7\(f\)](#), have been satisfied. The consistent and constant underreporting and non-reporting of sales tax, combined with Taxpayer's prior and subsequent record of filing, confirms that Taxpayer's actions rise above mere negligence as defined by [45 IAC 15-11-2\(b\)](#) and that the imposition of the 100 percent fraud penalty was appropriate. As explained above, under [IC 6-8.1-10-1\(e\)](#) the Department is prohibited from waiving interest.

### FINDING

Taxpayer's protest is denied.

May 19, 2023

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An [html](#) version of this document.