

**Letter of Findings: 01-20232295 and 01-20232297  
Indiana Individual Income Tax For the Years 2019 and 2020**

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

S Corporation's Shareholders, in the business of operating a combination gas station and convenience store, were unable to meet their burden of proof necessary to establish that the Department's proposed assessments of additional income tax were wrong.

**ISSUE****I. Indiana Individual Income Tax - Flow-Through Business Income.**

**Authority:** [IC 6-8.1-5-1](#); [IC 6-8.1-5-4](#); *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); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Letter of Findings 04-20232323 (January 20, 2024).

Taxpayers argue that the Department of Revenue overstated the amount of income attributable to their ownership of a combination gas station/convenience store.

**STATEMENT OF FACTS**

Taxpayers are Indiana residents who routinely file joint IT-40 Resident Individual Income Tax returns. On their 2019 and 2020 returns, Taxpayers reported income received from their combination gas station/convenience store. This business was organized as an S corporation. The S Corporation's income flowed through to Taxpayers. Taxpayers were subject to individual income tax on their distributive shares of their S Corporation business.

The Indiana Department of Revenue conducted an audit of the S Corporation's 2019 and 2020 income and sales tax returns. That audit resulted in an assessment of additional sales tax and consequently affected the amount of income flowing through to Taxpayers. The Department's sales tax audit was conducted in parallel with the Department's review of Taxpayers' own individual returns.

The Department assessed Taxpayers additional income tax for the years under review. The Department did so on the grounds that the S Corporation received additional unreported income and because correcting the S Corporation's original income tax return called for adjustments to the Taxpayers' returns.

Taxpayers disagreed with both the S Corporation's sales tax assessment and the assessment of additional individual income tax. Taxpayers submitted protests challenging both the results of the sales tax audit and the income tax audit. An administrative hearing was conducted in order to permit Taxpayers' representative to explain the basis for their protests.

The S Corporation's sales tax assessment is addressed in a separate Letter of Findings docketed as 04-20232296. This Letter of Findings addresses Taxpayers' income tax assessment.

**I. Indiana Individual Income Tax - Flow-Through Business Income.****DISCUSSION**

The issue is whether Taxpayers have met the burden of proof necessary to establish that the Department's

adjustments to their income statements and tax returns were wrong.

### **A. Summary of Taxpayers' Arguments.**

In general, Taxpayers concede that the S Corporation "[did] not have all the required documents" and that Department's audit relied on "estimates." In opposition, Taxpayers here argue that the Department's reliance on these "estimates" was "unreasonable and unacceptable."

### **B. Burden of Proof.**

In considering both the audit result and Taxpayers' contentions, the Department points out that it is Taxpayers' responsibility to establish that the income tax assessments are 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, including during an action appealed to the tax court under this chapter. 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). Consequently, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong.

In assessing the audit report conclusion, the relevant Indiana law, and Taxpayers' arguments, 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, as well as both original audits, are entitled to deference.

### **C. Record Keeping Responsibility.**

Indiana law requires that "[e]very 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." [IC 6-8.1-5-4\(a\)](#). In addition, [IC 6-8.1-5-4\(c\)](#) provides that, "A person must allow inspection of the books and records and returns by the department or its authorized agents at all reasonable times." *Id.*

In the absence of the required "books and records," [IC 6-8.1-5-4\(e\)](#) provides:

The failure of a person to keep books and records in the ordinary course of business shall be considered for purposes of determining the weight of the evidence as it relates to the person's liability for a listed tax, and not for purposes of the admissibility of the evidence.

[IC 6-8.1-5-1\(b\)](#) requires of the Department as follows:

If the department reasonably believes that a person has not reported the proper amount of tax due, the department *shall make* a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the department. The amount of the assessment is considered a tax payment not made by the due date and is subject to [IC 6-8.1-10](#) concerning the imposition of penalties and interest. (*Emphasis added*).

### **D. S Corporation Audit.**

The Department's audit of S Corporation commenced in October 2021 and was completed April 2023. The audit reviewed the S Corporation's sales returns, income tax returns, and business records. Simultaneously, the Department audited Taxpayers' income tax returns.

The Department's audit concluded that the S Corporation failed in its responsibility to maintain and/or provide all requested books and records and that the documentation that was provided was unreliable. As explained in the audit report:

The [S Corporation] did not keep ledgers during the audit period. The [S Corporation's] sales recap worksheets given to [S Corporation's] representative in order to file their monthly sales tax returns were provided, but only in photo or PDF format.

In addition, the audit informed Taxpayers that "certain columns in the file had bad formats" with the result "that only the taxable sales and tax collected amounts were valid [but] not the total sales column."

Further, the audit report indicates that the S Corporation "was unable to provide Z-Tapes or any information from their . . . Point of Sale system." The S Corporation was also unable to provide invoices detailing purchases from its vendors or copies of the checks used to pay these vendors.

The audit found that the S Corporation had underreported taxable sales by approximately eight hundred and thirty thousand dollars, requiring an assessment of additional sales tax. The sales tax assessment was approximately \$105,000.

#### **E. Taxpayers/Shareholders.**

As noted above, the results of the S Corporation audit adjustments flowed through to Taxpayers' own individual income tax returns because, according to the audit report, Taxpayers had not reported the correct amount of income attributable to their ownership of the S Corporation. In particular, the audit concluded that Taxpayers underreported their S Corporation income by approximately \$510,000.

Taxpayers' arguments essentially parallel the objections submitted in support of the S Corporation's audit. These are the objections raised:

- The combination gas station/convenience store was sold in April 2020.
- The Department's audit personnel did not allow the S Corporation "enough time to gather all the information."
- The S Corporation was unable to provide the requested Z Tapes or the point of sale (cash register) reports because the Taxpayers had closed the business.
- The Department "refused to consider all the missing vendor invoices" with the result that the cost of goods sold amount was not correctly calculated.
- The Department's reliance on bank account deposits was unwarranted because the amount of bank deposits included amounts for "Lottery, ATM & money orders and [Taxpayer] only make[s] a small commission out of [these sales]."

#### **F. Analysis and Conclusion.**

Taxpayers' arguments essentially parallel the objections submitted in support of their S Corporation's protest. As in Letter of Findings 04-20232296 (date), the Department found that the arguments did not support the contention that the assessment should either be abated or modified based on the limited documentation that was provided.

As to the remainder of both the S Corporation's and Taxpayers' argument, this decision quotes from the S Corporation Letter of Findings.

[S Corporation's] argument that the Department did not provide sufficient time in which to provide all the documents requested does not survive scrutiny. The record indicates that the audit took period over approximately 18 months. That record also documents approximately thirty instances in which the Department requested documentation or reminded [S Corporation] that already requested documents had not yet been provided. In some instances, the [S Corporation] responded that the documents requested were unavailable or that the Department should obtain the documents from the convenience store's new owner. The audit notes are replete with instances in which the Department indicated that it had "no response from the POA," that the POA was "having trouble getting ahold of their client," that the POA had "gotten busy and still hasn't gotten in touch with his client," that the POA's client "did not recognize the bank accounts" referred to by the Department, and informing the representative that the information provided was for a different convenience store than the one here under consideration.

The Department is unable to agree that Taxpayers have met their statutory burden under [IC 6-8.1-5-1\(c\)](#) of establishing that the assessment was wrong. The cumulative effect of the two audit reports - and consideration of

both Taxpayers' and S Corporation's arguments - does not lead to a conclusion that that the assessments should be either abated or reduced.

In the face of the S Corporation's failure of maintain the requisite documentation, the Department is required under [IC 6-8.1-5-1](#)(b) to make "a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the department." Taxpayers have not met their statutory burden under [IC 6-8.1-5-1](#)(c) of establishing the assessment of additional income tax was wrong.

### **FINDING**

Taxpayers' protest is denied.

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