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A Washington National Tax Services (WNTS)
Publication

March 16, 2012

Indiana Supreme Court reverses Tax Court, sets procedure in forced combination cases



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The Indiana Supreme Court upheld the presumption of validity afforded to the Department of Revenue's proposed assessment requiring Rent-A-Center East, Inc. to file a combined return with two affiliated entities for the 2003 tax year. [[*Indiana Department of Revenue v. Rent-A-Center East, Inc.*, No. 49T10-0612-TA-106, 3/9/12](#)]

Background

During the 2003 tax year, Rent-A-Center East, Inc. ("RAC East") operated over 1000 rent-to-own retail stores in the United States, including 106 in Indiana. Rent-A-Center West, Inc. ("RAC West") owned the Rent-A-Center trademarks and other related intellectual property which it licensed to RAC East in exchange for royalty payments. Rent-A-Center Texas, L.P. ("RAC TX") performed all strategic management and related functions for RAC East in exchange for a strategic assistance fee. At all times during the 2003 tax year neither RAC West nor RAC TX operated retail stores in Indiana and did not have any capital, property, or employees within the state.

Following an audit of RAC East for the 2003 tax year, the Department issued a proposed assessment of \$513,272 in additional liability based on a determination that RAC East should have filed a combined return with RAC West and RAC TX. RAC East protested the assessment and filed a motion for summary judgment in the Tax Court.



The Department also moved for summary judgment. The Tax Court granted RAC East's motion and the Department appealed to the Indiana Supreme Court ("Court").

Applicable law and trial rules

Indiana taxes a corporation's adjusted gross income based on the portion of that income derived from sources within the state determined according to the provisions of Indiana Code Sec. 6-3-2-2(a)-(k) (the "standard sourcing rules"), and reported on a separate company basis. Pursuant to Sec. 6-3-2-2(l), if none of the methods available through the standard sourcing rules fairly represent the taxpayer's activity in Indiana, the taxpayer may petition, or the Department may require, alternative sourcing methods. However, pursuant to Sec. 6-3-2-2(p) the Department may only require taxpayers to file a combined income tax return where it is unable to fairly reflect the taxpayer's adjusted gross income for the taxable year through use of the other powers granted to the Department in subsection (l).

In the context of a summary judgment, tax statutes must operate within the statutory framework established by trial rules. Indiana Trial Rule 56(C) states "summary judgment must be rendered as to all or some of the issues or claims when 'the designated evidentiary matter shows that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law.'"

Proposed assessments are presumed valid

The Tax Court construed the tax statutes so as to require the Department to make a Rule 56(C) prima facie showing by designating facts required under Sec. 6-3-2-2(p). The Tax Court had found that the Department did not present any facts that it complied with Sec. 6-3-2-2(p) and therefore failed to prove that it was entitled to judgment as a matter of law. However, on appeal the Court ruled that the Tax Court erred in its application of the rules.

The Court ruled that the tax statutes and trial rules function together in a different way. The Court noted Sec. 6-8.1-5-1(c) provides, in general, that a notice of proposed assessment by the Department is presumed to be valid and that the burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made. Sec. 6-3-2-2(p) does not "trump the presumption of validity given to the proposed assessment," nor does it serve as a means of "vitiating the Department's prime facia showing." Sec. 6-3-2-2(p) serves as an evidentiary bar "at the end of the summary judgment analysis (or trial process), not a threshold over which the Department must pass at the beginning."

Thus, the Court ruled that in this case, and in similar cases, the procedural process is a fairly straightforward one - "[W]hen properly designated, the Department's notice of proposed assessment constitutes a prima facie showing -- sufficient to satisfy Trial Rule 56(C) -- that there is no genuine issue of material fact with respect to the validity of the unpaid tax -- including presuming the Department's compliance with subsection (p)" and with subsection (l) where required. Upon issuance of a notice of proposed assessment, the burden shifts to the taxpayer to demonstrate that a genuine issue of material fact exists with respect to the unpaid tax.

The Court held that the Tax Court improperly applied the applicable law and trial rules and reversed and remanded the case to consider the motions for summary judgment on their merits in light of this ruling.

PwC Observes

"This decision by the Indiana Supreme Court may not be as significant as it might first appear," observes Mike Ralston, PwC SALT Director in Indianapolis, Indiana. "It should be noted that during the oral argument before the Court, the Taxpayer agreed with the state that the case should be remanded to the Indiana Tax Court for a decision on the merits, although for different reasons."

"The more practical takeaway is that subsections (l) and (p) should be read together as part of the same multi-part analysis rather than subsection (p) being read as a separate test. It is possible that the *AE Outfitters* decision will also be remanded back to the Tax Court since that decision was based on a similar analysis, but without the procedural aspects of *Rent-a-Center*. However, it is unclear as to when that might occur since the decision was on a motion for partial summary judgment and is not yet up on appeal."

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