Audit Division Statistical Study

The Audit Division Statistical Study addresses the requirements set forth by IC 6-8.1-14-4 (2). The information is based on 100 percent of the audits completed, taxpayers assisted and special projects conducted during fiscal year 2006.

See Page 24 for an index of exhibits and charts included.

Taxpayers Served in District Offices

Taxpayer assistance is available in all district offices. Each office has a taxpayer assistance supervisor and assistant taxpayer supervisor who perform taxpayer-service functions, as well as other office-support responsibilities. Each office has at least one field investigator who supports taxpayer assistance and performs collection functions in the district. Contract employees are available throughout the year to support taxpayer assistance.

The "Taxpayer Assistance Report-Fiscal Year 2006" (Exhibit A) provides the number of taxpayers assisted (in person and by telephone) and the amount of money collected and assessed in each office through the taxpayer-assistance program. Exhibit A reveals that during fiscal year 2006, district offices assisted 154,105 taxpayers in person and 163,073 taxpayers through telephone contact. Total taxpayers served through the district offices were 317,178. The district office in Clarksville served 28,141 taxpayers in person, the highest number of any district office. The Fort Wayne district office served 26,243 taxpayers in person, the second highest total.

The Fort Wayne district office served 27,849 taxpayers by telephone while the Clarksville district office served 25,129 taxpayers by telephone. This was the highest number of telephone contacts among the district offices, totaling 32-percent of total taxpayer telephone contacts. The Fort Wayne district office served a total of 54,092 taxpayers by telephone and walk-in assistance, while Clarksville served 53,270 taxpayers by telephone and walk-in assistance.

"Field Auditors Taxpayer Assistance/Special Projects" (Exhibit B) provides the number of hours field auditors devoted in the district offices to assist taxpayers and conduct special projects. The exhibit reveals that 6,261 auditor hours were channeled in this direction.

Gross Income Tax Violations

The most-frequently violated gross-income-tax rule in the 2006 study is 45 IAC 1.1-2-4. Rule 2-4 defines taxable high-rate income of utilities, display advertising, sale of real estate, rentals and extension of credit. This rule accounted for 26 (16.77 percent) violations of gross-income-tax rules in the 2006 study. Rule 2-4 was the most violated in the 2005 report, with 13.91 percent. Rule 45 IAC 1.1-2-4 and Rule 45 IAC 1.1-2-5 (defined below) were equally rated in the 2004 report, with each rule accounting for 26 (14.69 percent) of violations.

Ranking second in gross-income-tax violations for 2006 was 45 IAC 1.1-2-5. Rule 2-5 defines gross income derived from providing services within Indiana. Violations (19) of Rule 2.5 accounted for 12.26 percent of all violations of the gross income tax rules in the 2006 statistics. Rule 2-2 ranked second in the 2005 study accounting for 11.92 percent of violations. Rule 2-2 defines taxable low-rate gross income of retail and wholesale sales, display advertising, dry cleaning and laundry service, rental of water softening equipment, rental of rooms, lodging, booths and similar accommodations and commercial printing. Rule 2-2 and Rule 3-3 tied for second in violations in the 2004 report with each Rule accounting for 11.30 percent of violations. Rule 3-3 defines the interstate commerce exemption as applied to gross receipts.

Ranking third for the 2006 study with 17 (10.97 percent) infractions of the gross-income-tax rule violations is Rule 45 IAC 1.1-2-2.

(This rule is defined above.) Rule 2-1 was the third-most-frequently violated rule in 2005 and 2004 with 10.60 percent and 5.08 percent respectively. Rule 2-1 defines Indiana source income.

Sales/Use Tax Violations

The most-frequently violated sales and use tax rule was 45 IAC 2.2-3-20. Rule 3-20 states that if the seller of tangible personal property for storage, use or consumption in Indiana fails to collect the appropriate tax, the purchaser of such property must remit tax directly to the Department. This rule produced 777 violations (18.07 percent) of the sales and use tax infractions. In the 2005 study, Rule 3-20 accounted for 16.71 percent of sales and use tax infractions and also ranked first. This rule also ranked first in the 2004 study accounting for 12.28 percent of sales and use tax violations.

The second-most-frequently violated sales and use tax rule was 45 IAC 2.2-3-4. Rule 3-4 imposes use tax on "tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used or otherwise consumed in Indiana…unless the Indiana state gross-retail tax (sales tax) has been collected at the point of purchase." This rule accounted for 557 infractions or 12.95 percent of sales and use tax statute violations. Rule 3-4 ranked second in the 2005 study with 383 infractions (11.64 percent). The second-most violated sales and use rule in 2004 was 45 IAC 2.2-3-4 (11.38 percent).

The third-most violated rule for the 2006 fiscal year was 45 IAC 2.2-5-8. Rule 5-8 clarifies sales and use tax by providing examples of taxable and nontaxable sales of manufacturing machinery, tools and equipment used in direct production and other activities. Failure of taxpayers to comply with this rule accounted for 368 or 8.56 percent of the sales and use tax infractions. Rule 5-8 ranked third in the 2005 study with 308 (9.36 percent) of infractions. Rule 5-8 ranked third in the 2004 study with 195 (9.28 percent) infractions.

Corporate Adjusted Gross Income Tax Violations

Corporate taxpayers violated adjusted gross income Rule 45 IAC 3.1-1-2 more than any other rule. This rule defines gross income for Indiana residents filing individual returns as all income defined by Section 61 of the Internal Revenue Code. Violations (82) of this rule accounted for 17.19 percent of the total violations in the 2006 study. Rule 1-2 ranked first in the 2005 study with 64 (15.27 percent) of total adjusted gross income violations. Rule 1-8 (defined below) was the most violated rule in the 2004 study with 40 (15.81 percent) infractions.

The second-most-frequently violated adjusted gross income rule for 2006 was 45 IAC 3.1-1-8. Rule 1-8 states that taxable income as defined in the Internal Revenue Code is modified in several ways to arrive at Indiana adjusted gross income. Violations (75) of this rule accounted for 15.72 percent of all adjusted gross income tax rules. Rule 1-1 (defined below) ranked second in the 2005 study accounting for 58 (13.84 percent) of total violations. Ranking second in the 2004 report was 45 IAC 3.1-1-9 (net operating loss deduction) comprising 10.67 percent of violations.

Rules 45 IAC 3.1-1-1 and 45 IAC 3.1-1-97 were equally ranked for third with 68 (14.26 percent) infractions in the 2006 study. Rule 1-1 defines adjusted-gross income as noted in Internal Revenue Code Section 62. Rule 1-97 defines withholding agents and their responsibility for remitting tax to Indiana. 45 IAC 3.1-1-8 (defined above) ranked third in the 2005 study with 12.89 percent of infractions. The 2004 study revealed 45 IAC 3.1-1-97 ranked third with 26 (10.28 percent) of violations.

Amounts of Tax Assessed

Exhibits C, D and E display the amount of assessments (refunds) of the gross-income tax, sales tax and adjusted-gross-income tax administrative rules, respectively. "Total assessments" for any tax type represent gross assessments less amounts refunded.

The amount assessed or refunded for each of the most frequent violations and the percentage of the amount to total net assessments are presented as follows:

Gross Income Tax—Exhibit C:

	Amount Assessed	Percentage of All Assessments
45 IAC 1.1-2-4	$2,850,438	10.99%
45 IAC 1.1-2-5	$16,616,716	64.06%
45 IAC 1.1-2-2	$968,441	3.73%

Sales/Use Tax—Exhibit D:

	Amount Assessed	Percentage of All Assessments
45 IAC 2.2-3-20	$2,196,786	16.54%
45 IAC 2.2-3-4	$609,250	4.59%
45 IAC 2.2-5-8	$3,122,478	23.51%

Corporate Adjusted Gross Income Tax—Exhibit E:

	Amount Assessed	Percentage of All Assessments
45 IAC 3.1-1-2	$462,167	1.99%
45 IAC 3.1-1-8	$3,970,518	17.13%
45 IAC 3.1-1-1	$351,603	1.52%
45 IAC 3.1-1-97	$366,796	1.58%

Industry /Business Most Frequently In Violation

Gross Income Tax

Taxpayers engaged in manufacturing most frequently violated the gross-income-tax rules. This group committed 45 violations, or 29.03 percent of the total violations. The gross-income-tax rule most-frequently violated by this group of taxpayers is 45 IAC 1.1-2-4 (eight violations). Rule 2-4 defines high-rate income.

The second-largest number of gross-income-tax violations was committed by taxpayers in information, publishing, telecommunications, finance, rental, insurance, real estate, leasing and professional services group. This group committed 31 infractions, or 20 percent of the total violations for 2006. The most-frequently-violated rules of this group were 45 IAC 1.1-2-1 and 45 IAC 1.1-2-4 (4 infractions each). Rule 2-1 defines Indiana source income and Rule 2-4 defines high-rate income.

Sales and Use Tax

For the 2006 reporting period, wholesale, retail and transportation businesses accounted for the most infractions. They accounted for 750 violations, or 17.44 percent of the total sales and use tax violations. The most-frequently violated rule by these taxpayers was 45 IAC 2.2-3-20 that states if a seller of tangible personal property for storage, use or consumption in Indiana fails to collect the appropriate tax, the purchaser of such property must remit tax directly to the Department.

Repair, personal service and other service businesses had the second-most frequency of violations for the sales and use tax rules. The 690 violations committed by this group represent 16.05 percent of the total violations. The rule most-frequently violated by this group was 45 IAC 2.2-3-20 defined above.

Adjusted Gross Income Tax

Public administration with 128 infractions was the most-frequent violator of adjusted gross-income-tax rules. This figure represents 26.83 percent of the total adjusted gross-income-tax violations. Adjusted gross income for individuals, defined by 45 IAC 3.1-1-2, accounted for the most infractions in this class.

The wholesale, retail and transportation businesses were ranked second in violation of the adjusted gross income rules. They committed 78 infractions, or 16.35 percent of the adjusted gross income tax violations. 45 IAC 3.1-1-8 had the most infractions by this group. Rule 1-8 discusses modifications of federal adjusted gross income in determining Indiana adjusted gross income.

Special Tax Violations

Exhibit G provides the special tax assessments and refunds by citation.

Article VIII (citation R800 on Exhibit G) of the International Fuel Tax Agreement (IFTA) was the most frequently violated special tax item in the study. It specifies the taxable event is the consumption of motor fuels in the propulsion of qualified motor vehicles, except fuel consumed that is exempt from taxation by a jurisdiction. All motor fuel acquired that is normally subject to consumption tax is taxable unless the licensee provides proof to the contrary. Article VIII was violated 296 times and yielded $850,736 in net assessments for the state of Indiana. This represents 26.59 percent of total violations and 20.51 percent of net assessments. Article VIII was the most-violated special-tax citation in the 2005 and 2004 studies. The 2005 study had 235 infractions ($327,854 net assessments) and 2004 had 182 infractions ($487,571 net assessments).

Article X (citation R1000 on Exhibit G) of the International Fuel Tax Agreement (IFTA) was the second-most-frequently violated section of the special tax statutes. This Article discusses how taxpayers can obtain credit for tax previously paid on purchases of fuel at the pump. It also lists the records needed to substantiate the refund request. This article was violated 280 times accounting for 25.16 percent of the total violations. These violations resulted in net refunds of $306,823. Article X had the second most infractions in the 2005 and 2004 special tax citations. The 2005 study showed 221 infractions with $162,948 net assessments while 2004 showed 180 violations with $57,386 net refunds.

The taxpayer group most frequently in violation of the special tax statutes and IFTA Articles for 2006 was the wholesale, retail and transportation industries. This group committed 810 violations accounting for 72.78 percent of the total infractions. Article VIII of the International Fuel Tax Agreement was most frequently violated by the wholesale, retail and transportation industries. The 2005 statistics showed the repair, personal and other services industries with the most violations (432). For 2004, the wholesale, retail and transportation industries ranked first with 360 violations.

Miscellaneous Code Violations

Exhibit F provides the assessment amounts for the following:

- Financial Institutions Tax
- Tax Administration
- Food and Beverage Tax
- Innkeeper's Tax
- Charity Gaming

A review of the miscellaneous code violations data reveals that 45 IAC 15-5-1 was violated 18 (14.06 percent) times in the 2006 study. These violations yielded $805,271 in net assessments. Rule 5-1 discusses issuing notices of assessment. In the 2005 study, 45 IAC 15-9-2 (which discusses statute of limitations for refunds) produced 12 (14.63 percent) infractions. IC 6-8.1-4-2 (discusses examination of taxpayer records) was the most violated rule in the 2004 study with 16 (12.12 percent).

45 IAC 15-4-1 was the second-most violated rule in this category in 2006. It yielded a total of $195,690 in assessments. Rule 4-1 discusses access to records for examination. Eleven rule violations accounted for 8.59 percent of the total infractions in this category. Rule 4-1 was the second-most violated miscellaneous rule in the 2005 study accounting for $47,384 in net refunds. The 2004 study showed Rule 9-2 (statute of limitations for refunds) as having the second most infractions with 15 ($1,369,297 net refunds).

The arts, entertainment, recreation, food service and accommodation industries committed the most infractions under the miscellaneous citations in 2006 with 28 (21.88 percent). The industry ranked second for the 2006 study was the information, publishing, telecommunications, finance, rental, insurance, real estate, leasing and professional services industries with 26 (20.31 percent) infractions.

The information, publishing, telecommunications, finance, rental, insurance, real estate, leasing and professional services industries ranked first in the 2005 study with 26 (31.71 percent) errors. In the 2005 study, repair, personal services and other services industries ranked second with 24 (29.27 percent) errors.

Number of Years in the Audit Period

The audit period averages three years.

Use of Professional Tax Preparation Assistance

The services of professional preparers were used in the preparation of 75 percent of the corporate income tax returns and 11 percent of the sales tax returns. Statistics show that 26 percent of individuals use a professional preparer to complete the returns.

Filing of Appropriate Tax Returns

Rule 45 IAC 3.1-1-92 (Exhibit E) requires qualifying corporations to make estimated tax payments. Taxpayers in violation of this rule either failed to file estimated income tax returns or failed to remit the appropriate amount of tax. For the fiscal years ending in 2004, 2005 and 2006, no activity was recorded. The 2003 study indicated eight violations of this rule, resulting in assessments in the amount of $12,863 and refunds totaling $110,617.

Indiana Code 6-8.1-10-2.1 (Exhibit F) revealed no violations during the 2006 study period. This section specifies the penalty to be imposed if a taxpayer fails to file an appropriate return or pay the full amount of tax due. Violations of this section in the 2005 and 2004 studies were zero.