

Letter of Findings Number: 06-0461
Sales and Use Tax
For the Tax Period 2005

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ISSUE

I. Sales and Use Tax - Imposition

Authority: IC § 6-8.1-5-1(b); IC § 6-2.5-2-1; IC § 6-2.5-3-2(a); [IC 6-2.5-2\(c\)\(1\)](#); IC § 6-6-6.5-8(d); [45 IAC 2.2-5-15](#); [45 IAC 2.2-4-27](#)(d); *Indiana Department of State Revenue v. Interstate Warehousing*, 783 N.E.2d 248 (Ind. 2003).

The Taxpayer protests the assessment of use tax on an airplane.

II. Tax Administration - Ten Percent Negligence Penalty

Authority: IC § 6-8.1-10-2.1; [45 IAC 15-11-2\(b\)\(c\)](#).

The Taxpayer protests the imposition of the ten percent negligence penalty.

STATEMENT OF FACTS

The Taxpayer is a limited liability corporation which bought an airplane in 2005. The Indiana Department of Revenue, hereinafter referred to as the "Department," assessed Indiana use tax, interest, and penalty on the airplane. The Taxpayer protested the assessment of use tax. A hearing was held and this Letter of Findings results.

I. Sales and Use Tax - Imposition

DISCUSSION

All tax assessments are presumed to be valid. IC § 6-8.1-5-1(b). The Taxpayer bears the burden of proving that any assessment is incorrect. *Id.* Exemption statutes are to be strictly construed against the Taxpayer. *Indiana Department of State Revenue v. Interstate Warehousing*, 783 N.E.2d 248 (Ind. 2003).

Indiana imposes a sales tax on the transfer of tangible personal property in a retail transaction. IC § 6-2.5-2-1. Indiana imposes a complementary excise tax, the use tax, on tangible personal property purchased in a retail transaction and stored, used, or consumed in Indiana. IC § 6-2.5-3-2(a). Payment of sales tax at the time of purchase exempts the use of tangible personal property from the use tax. IC § 6-2.5-2(c)(1).

IC § 6-6-6.5-8(d) provides for the payment of sales or use tax on an airplane as follows:

A person shall pay the gross retail tax or use tax to the department on the earlier of:

- (1) the time the aircraft is registered; or
- (2) not later than thirty-one (31) days after the purchase date;

unless the person presents proof to the department that the gross retail tax or use tax has already been paid with respect to the purchase of the aircraft or proof that the taxes are inapplicable because of an exemption.

The Taxpayer bases its claim for exemption on the following provisions of IC § 6-2.5-5-8 which states as follows:

Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for resale, rental, or leasing in the ordinary course of his business without changing the form of the property....

The law concerning the exemption for rental to others is further explained at [45 IAC 2.2-5-15](#) as follows:

(a) The state gross retail tax shall not apply to sales of any tangible personal property to a purchaser who purchases the same for the purpose of reselling, renting or leasing, in the regular course of the purchaser's business, such tangible personal property in the form in which it is sold to such purchaser.

(b) General rule. Sales of tangible personal property for resale, renting or leasing are exempt from tax if all of the following conditions are satisfied:

- (1) The tangible personal property is sold to a purchaser who purchases this property to resell, rent or lease it;
- (2) The purchaser is occupationally engaged in reselling, renting or leasing such property in the regular course of his business; and
- (3) The property is resold, rented or leased in the same form in which it was purchased.

(c) Application of general rule.

(1) The tangible personal property must be sold to a purchaser who makes the purchase with the intention of reselling, renting or leasing the property. This exemption does not apply to purchasers who intend to consume or use the property or add value to the property through the rendition of services or value to the property through the rendition of services or performance of work with respect to such property.

(2) The purchaser must be occupationally engaged in reselling, renting or leasing such property in the regular course of his business. Occasional sales and sales by servicemen in the course of rendering

services shall be conclusive evidence that the purchaser is not occupationally engaged in reselling the purchased property in the regular course of his business.

(3) The property must be resold, rented or leased in the same form in which it was purchased.

The Taxpayer states that it was in the business of renting the aircraft and therefore qualifies for the rental exemption on the airplane. This exemption requires compliance with three elements. One of these requirements is that the Taxpayer must be engaged in the reselling, renting, or leasing of such property in its regular course of business. The Taxpayer rented the airplane to a related corporation. Both the Taxpayer and the related corporation had the same key people. The key people in the Taxpayer corporation rented the aircraft to one of their own key people – the other corporation's managing member. Essentially the key people in the first corporation rented the airplane to themselves.

The rental rates charged were below the fair market rental rate of comparable airplanes available to the public. The Taxpayer argued that the rental rates were so low due to circumstances beyond the Taxpayer's control. Had it been able to, the Taxpayer argued, it would have charged market rates. The other circumstances do not, however, control in determining the sales taxability of the transaction selling the airplane to the Taxpayer. At the time of the hearing, the Taxpayer had not yet begun its anticipated rental business.

The Department is unable to agree that this arrangement constitutes an arms length transaction.

Although the Taxpayer may have initially intended to use the airplane as a rental in its ordinary course of business, the Taxpayer did not use it in this manner. Rather, the Taxpayer converted the airplane to its own use. The Taxpayer is properly subject to the use tax on its use of the airplane.

FINDING

The taxpayer's protest to the assessment of use tax on its airplane is respectfully denied.

II. Tax Administration - Ten Percent Negligence Penalty

DISCUSSION

The Taxpayer protests the imposition of the ten percent negligence penalty pursuant to IC § 6-8.1-10-2.1. Indiana Regulation [45 IAC 15-11-2\(b\)](#) clarifies the standard for the imposition of the negligence penalty as follows:

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.

The standard for waiving the negligence penalty is given at [45 IAC 15-11-2\(c\)](#) as follows:

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 this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

- (1) the nature of the tax involved;
- (2) judicial precedents set by Indiana courts;
- (3) judicial precedents established in jurisdictions outside Indiana;
- (4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc;
- (5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

The Taxpayer provided substantial documentation to indicate that its failure to pay the assessed use tax was due to reasonable cause rather than negligence.

FINDING

The Taxpayer's protest to the imposition of the penalty is sustained.

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