

**LETTER OF FINDINGS: 06-0486**  
**Sales and Use Tax**  
**For the Years 2003, 2004, 2005**

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**ISSUE**

**I. Use Tax – Imposition - Treatment of Lump Sum Contract.**

**Authority:** IC § 6-2.5-1-1(a); IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-8.1-5-1(b); [45 IAC 2.2-1-1\(a\)](#); [45 IAC 2.2-3-9\(e\)\(3\)](#); [45 IAC 2.2-4-22](#); [45 IAC 2.2-4-26](#).

Taxpayer protests the imposition of use tax on an invoice it characterizes as a lump sum contract for the improvement of realty.

**II. Use Tax – Imposition – Drywall Repairs and Painting.**

**Authority:** IC § 6-2.5-2-1; IC § 6-8.1-5-1(b); IC § 6-2.5-3-2; [45 IAC 2.2-4-2](#).

Taxpayer protests the imposition of use tax on an invoice line item that it characterizes as a service and therefore not subject to the tax.

**STATEMENT OF FACTS**

Taxpayer is an Indiana corporation that operates an inn franchise. The Indiana Department of Revenue (Department) conducted a sales and use tax audit of Taxpayer in 2006 for the years 2003, 2004, and 2005. The Department made no changes to total taxable sales that were reported, but assessed additional use tax for each of the audited three years. Taxpayer protested the assessment of use tax on two 2004 invoices relating to charges for new breakfast service units and to the repair and painting of drywall. A hearing was held and this Letter of Findings ensues. Additional facts will be provided as necessary.

**I. Use Tax – Imposition - Treatment of Lump Sum Contract.**

**DISCUSSION**

Under IC § 6-8.1-5-1(b), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made."

Indiana imposes a gross retail tax on the sales of tangible personal property by retail merchants in Indiana. IC § 6-2.5-2-1. Indiana imposes a complementary tax on the use of tangible personal property purchased in a retail transaction. IC § 6-2.5-3-2.

The taxpayer protests the assessment of use tax on the construction of breakfast units in its breakfast area. The taxpayer argues that this was a lump sum contract for improvement to realty, so, therefore, the contractor was responsible for any tax due. Taxpayer presumably bases its contention on [45 IAC 2.2-3-9\(e\)\(3\)](#), [45 IAC 2.2-4-22](#), and [45 IAC 2.2-4-26\(a\)](#), which deal with construction contracts for the improvement of real estate.

Taxpayer provided the invoice which specifically states that this was a lump sum contract for "NEW BREAKFAST AREA (3) MOBILE SERVING STATIONS." Taxpayer restated this during the hearing. It is clear that this is a "lump sum" contract, in that there is no separate listing of charges for services and materials. The question, therefore, is whether the improvements to Taxpayer's breakfast area constituted an improvement to realty.

The significance of this distinction lies in the fact that Taxpayer is not subject to use tax liability for those transactions, entered into for the purpose of improving Taxpayer's realty, in which the agreement was couched in terms of a lump sum contract. Under [45 IAC 2.2-4-22\(e\)](#), "[w]ith respect to construction material a contractor acquired tax-free, the contractor is liable for the use tax and must remit such tax (measured on the purchase price) to the Department of Revenue when he disposes of such property in the following manner: (1) He converts the construction material into realty on land he owns and then sells the improved real estate; (2) He utilizes the construction material for his own benefit; or (3) Lump sum contract. *He converts the construction material into realty on land he does not own pursuant to a contract that includes all elements of cost in the total contract price.*" (*Emphasis added*). Accordingly, the contractor will either pay the supplier gross retail tax "up-front" when he initially purchases the construction materials or he will self-assess the gross retail tax in the form of use taxes when the materials are incorporated into the construction project. Either upfront or at the point where the materials are incorporated into Taxpayer's realty, in lump sum contracts between the taxpayer and its contractors, it is the contractors who are ultimately responsible for paying the tax on the construction materials. [45 IAC 2.2-4-26\(a\)](#) provides that "[a] person making a contract for the improvement to real estate whereby the material becoming a part of the improvement and the labor are quoted as one price is liable for the payment of sales tax on the purchase price of the all material so used." In other words, the contractor is responsible and liable for the payment of sales tax in a "lump sum" contract.

However, unless Taxpayer can show otherwise, the fact that the units are mobile means they are not fixtures incorporated as improvements to real property. Taxpayer could choose to sell the mobile units, or move them to another facility. Therefore, Taxpayer's characterization of this invoice as one for a lump sum contract for the improvement of realty is incorrect.

Moreover, because the invoice for the mobile breakfast units does not separately break down materials and labor charges, the transaction is deemed to be unitary and therefore the entire charge on the invoice is subject to the gross retail tax. IC § 6-2.5-1-1(a) and [45 IAC 2.2-1-1\(a\)](#).

**FINDING**

Taxpayer's protest is respectfully denied.

**II. Use Tax – Imposition – Drywall Repairs and Painting.**

**DISCUSSION**

Taxpayer protests the imposition of use tax on an invoice line item for drywall repair and painting which it characterizes as a non-taxable provision of a service and not the taxable purchase of tangible personal property.

Again, under IC § 6-8.1-5-1(b), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made."

As previously stated, Indiana imposes a gross retail tax on the sales of tangible personal property by retail merchants in Indiana. IC § 6-2.5-2-1. Indiana imposes a complementary tax on the use of tangible personal property purchased in a retail transaction. IC § 6-2.5-3-2. However, there is no statutory provision imposing a gross retail tax on services. [45 IAC 2.2-4-2](#).

Prior to the hearing, the Department had requested that Taxpayer obtain a letter from its contractor (Contractor) stating the drywall repair and painting were in fact labor. Taxpayer wrote back stating that they had not been able to obtain such a letter because Contractor was no longer in business. Taxpayer reiterated, however, that the invoice itself indicates "repairs and painting" along with the specific amount charged for that line item. Taxpayer argues that the description as well as the relatively small amount charged suggest that the charges were for service and not materials.

Taxpayer provided the invoice which contains four line items, which are: (1) railing at windows, (2) supervision & cleaning, (3) drywall repairs & painting, and (4) 15 [percent] overhead and profit. Audit included the first and third line items in the additional use tax assessment. The first item appears to be for the purchase of tangible personal property, which would explain why Taxpayer did not protest that line item. The issue, therefore, relates to the third line item.

Taxpayer's general manager sent an email, dated August 21, 2007, after the hearing, that described the repairs as follows:

The invoice from [Contractor] for repair of drywall and paint during the installation of the glass enclosure of the Breakfast Area. There was nothing new installed only repair of the existing structure. There was a header in the ceiling that needed additional support to attach the enclosure and also an HVAC unit was installed in that area and they had to paint the area of installation.

Because the invoice lists separate line items for both services and materials, it is reasonable to conclude that the third line item pertains to exactly what it describes – drywall repair and painting. The drywall repair and painting constitute services and it is reasonable to conclude that no materials were used in this instance.

**FINDING**

Taxpayer's protest is sustained.

*Posted: 12/26/2007 by Legislative Services Agency*  
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