

**Letter of Findings Number: 07-0017**  
**Use Tax**  
**For Tax Years 2003-05**

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**ISSUES**

**I. Use Tax–Utility Exemption.**

**Authority:** IC § 6-2.5-5-5.1; IC § 6-8.1-5-1; [45 IAC 2.2-4-13](#).

Taxpayer protests the assessment of use tax.

**II. Tax Administration–Negligence Penalty.**

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

Taxpayer protests the imposition of a ten percent negligence penalty.

**STATEMENT OF FACTS**

Taxpayer operates restaurants in Indiana. As the result of an audit, the Indiana Department of Revenue ("Department") issued proposed assessments for use tax for the tax years 2003, 2004, and 2005, as well as a ten percent negligence penalty. Taxpayer protests the Department's determination that Taxpayer did not qualify for the predominant use exemption for utilities. Taxpayer also protests the imposition of negligence penalty. Further facts will be supplied as required.

**I. Use Tax–Utility Exemption.**

**DISCUSSION**

Taxpayer protests the Department's determination that two of taxpayer's restaurants did not qualify for the predominant use exemption for utilities. The Department concluded that Taxpayer's restaurants used utilities in an exempt manner less than fifty percent of the time and imposed use tax on Taxpayer's purchases of utilities which were not used in an exempt manner. Taxpayer disagrees and believes that its restaurants do predominantly use the utilities it purchases in an exempt manner. The Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

The relevant statute is IC § 6-2.5-5-5.1, which states:

(a) As used in this section, "tangible personal property" includes electrical energy, natural or artificial gas, water, steam, and steam heat.

(b) Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for direct consumption as a material to be consumed in the direct production of other tangible personal property in the person's business of manufacturing, processing, refining, repairing, mining, agriculture, horticulture, floriculture, or arboriculture. This exemption includes transactions involving acquisitions of tangible personal property used in commercial printing.

Also, [45 IAC 2.2-4-13](#) explains:

(a) In general, the furnishing of electricity, gas, water, steam, or steam heating services by public utilities to consumers is subject to tax.

(b) The gross receipt of every person engaged as a power subsidiary or a public utility derived from selling electrical energy gas, water, or steam to consumers for direct use in direct manufacturing, mining, production, refining, oil or mineral extraction, irrigation, agriculture, horticulture, or another public utility or power subsidiary described in [IC 6-2.5-4-5](#) shall not constitute gross retail income of a retail merchant received from a retail transaction. Electrical energy, gas, water, or steam will only be considered directly used in direct production, manufacturing, mining, refining, oil or mineral extraction, irrigation, agriculture, or horticulture if the utilities would be exempt under [IC 6-2.5-5-5.1](#).

(c) Sales of public utility services or commodities to consumers engaged in manufacturing, mining, production, refining, oil or mineral extraction, irrigation, agriculture, horticulture, or another public utility or power subsidiary described in [IC 6-2.5-4-5](#), based on a single meter charge, flat rate charge, or other charge, are excepted if such services are separately metered or billed and will be used predominantly for the excepted purposes.

(d) Sales of public utility services and commodities to consumers engaged in manufacturing, mining, production, refining, oil or mineral extraction, irrigation, agriculture, or horticulture, based on a single meter charge, flat rate charge, or other charge, which will be used for both excepted and nonexcepted purposes are taxable unless such services and commodities are used predominantly for excepted purposes.

(e) *Where public utility services are sold from a single meter and the services or commodities are utilized for both exempt and nonexempt uses, the entire gross receipts will be subject to tax unless the services or*

*commodities are used predominantly for excepted purposes. Predominant use shall mean that more than fifty percent (50 [percent]) of the utility services and commodities are consumed for excepted uses. (Emphasis added.)*

In the instant case, Taxpayer's restaurants purchased their electricity from a single meter at each location. In the course of its protest, Taxpayer has provided sufficient documentation to establish that it satisfies the requirements of [45 IAC 2.2-4-13\(e\)](#). Since Taxpayer has established that it predominantly used the electricity from these meters for excepted purposes, as required by [45 IAC 2.2-4-13\(e\)](#), Taxpayer has met the burden imposed by IC § 6-8.1-5-1(c).

**FINDING**

Taxpayer's protest is sustained.

**II. Tax Administration–Negligence Penalty.**

**DISCUSSION**

The Department issued proposed assessments and the ten percent negligence penalty for the tax years in question. Taxpayer protests the imposition of penalty. The Department refers to IC § 6-8.1-10-2.1(a), which states in relevant part:

If a person:

...

(3) incurs, upon examination by the department, a deficiency that is due to negligence;

...

the person is subject to a penalty.

The Department refers to [45 IAC 15-11-2\(b\)](#), which states:

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.

[45 IAC 15-11-2\(c\)](#) provides in pertinent part:

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.

In this case, taxpayer incurred a deficiency which the Department determined was due to negligence under [45 IAC 15-11-2\(b\)](#), and so was subject to a penalty under IC § 6-8.1-10-2.1(a). While Taxpayer has been sustained on the utilities discussed in Issue I, Taxpayer had other use tax assessments resulting from this audit. Taxpayer has not affirmatively established that its failure to pay the remaining deficiency was due to reasonable cause and not due to negligence, as required by [45 IAC 15-11-2\(c\)](#). The amount of base tax subject to penalty will be reduced as a result of the finding in Issue I, but the remaining amount of use tax will still be subject to penalty.

**FINDING**

Taxpayer's protest is denied.

*Posted: 02/27/2008 by Legislative Services Agency*

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