

**Letter of Findings Number: 07-0371
Sales and Use Tax
For the Tax Years 2003-2005**

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ISSUES

I. Sales and Use Tax – Press Guards.

Authority: IC § 6-8.1-5-1(b); IC § 6-2.5-2-1(a); IC § 6-2.5-3-2(a); IC § 6-2.5-5-3(b); [45 IAC 2.2-5-8\(c\)\(2\)\(f\)](#); *Indiana Dep't of State Revenue v. Interstate Warehousing*, 783 N.E.2d 248 (Ind. 2003).

The Taxpayer protests the use tax assessment on press guards.

II. Sales and Use Tax – Hoists.

Authority: IC § 6-2.5-3-2(a); IC § 6-2.5-5-3(b); [45 IAC 2.2-5-8\(c\)](#).

The Taxpayer protests the assessment of use tax on hoists.

III. Tax Administration – Negligence Penalty.

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

The Taxpayer protests the imposition of the negligence penalty.

STATEMENT OF FACTS

The Taxpayer is a corporation engaged in the manufacturing of automotive parts in industrial processing. The Indiana Department of Revenue (Department) audited the Taxpayer for the tax years 2003-2005. The audit resulted in an assessment of use tax, interest, and penalty. The Taxpayer protested the use tax assessments on two categories of capital purchases – press guards and hoists – and the penalty. A hearing was held and this Letter of Findings results.

ISSUES

I. Sales and Use Tax – Press Guards.

DISCUSSION

During the audit period, the Taxpayer purchased the materials to build and install press guards. The guards were cages made of fencing materials that attached to the presses. If the door to the guard was opened, the press automatically ceased operation. The Department assessed use tax on the materials used to build the press guards. The Taxpayer protested the assessment contending that the press guards qualified for a manufacturing exemption from the use tax.

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 Dep't of State Revenue v. Interstate Warehousing*, 783 N.E.2d 248 (Ind. 2003).

IC § 6-2.5-2-1(a) imposes sales tax on retail transactions made in Indiana. IC § 6-2.5-3-2(a) imposes a complementary use tax on the storage, use or consumption of tangible personal property in Indiana, if the property was acquired in a retail transaction as defined for sales tax purposes. IC § 6-2.5-5-3(b) provides for an exemption for tangible personal property directly used in the direct production of the Taxpayer's product for sale. This manufacturing exemption is further described at [45 IAC 2.2-5-8\(c\)](#) as follows:

The state gross retail tax does not apply to purchases of manufacturing machinery, tools and equipment to be directly used by the purchaser in the production process, provided such machinery, tools and equipment are directly used in the production process; i.e., they have an immediate effect on the article being produced. Property has an immediate effect on the article being produced if it is an essential and integral part of an integrated process which produces tangible personal property.

The Taxpayer contends that the press guards met the requirements to be exempt from the sales and use tax as property directly used in the direct production of property because the parts had an immediate effect on the product produced. Safety equipment which is required for workers to safely participate in the manufacturing process is an essential and integral part of the production process and has an immediate effect on the article being produced. [45 IAC 2.2-5-8\(c\)\(2\)\(f\)](#). Since the presses were large and used great force in the industrial process to produce the automobile parts, the presses endangered the employees. To protect the Taxpayer's employees from serious injury or death, OSHA and IOSHA required functional press guards for the operation of the machinery. Because of current safety standards, all new presses include the required press guards. The Taxpayer built the guards and integrated them with the presses to meet the OSHA and IOSHA safety standards for the protection of its employees. The Taxpayer sustained its burden of proving that the press guards were an essential and integral part of the Taxpayer's process of producing automotive parts and qualified for the manufacturing exemption pursuant to IC § 6-2.5-5-3(b).

FINDING

The Taxpayer's protest is sustained.

II. Sales and Use Tax – Hoists.

DISCUSSION

The Taxpayer rearranged its manufacturing facility in 2004. As a result, of the rearrangement, some presses had so little space around them that the Taxpayer could no longer use its pull motors to place tools in the presses. Therefore, the Taxpayer purchased and installed hoists to lift and place tools in the presses. The Department assessed use tax on the hoists pursuant to IC § 6-2.5-3-2(a). The Taxpayer protested the assessment contending that the hoists qualified for the manufacturing exemption pursuant to IC § 6-2.5-5-3(b).

To qualify for exemption as directly used in direct production, equipment must be directly used in the production process and have an immediate effect on the Taxpayer's product. [45 IAC 2.2-5-8\(c\)](#). The tools and presses acted on and had an immediate effect on the Taxpayer's production of automobile parts. However, the hoists in question positioned tools in the presses. They did not touch, change, or act on the taxpayer's product. Therefore, the hoists were not exempt from the use tax pursuant to IC § 6-2.5-5-3(b).

FINDING

The Taxpayer's protest is respectfully denied.

III. 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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