DEPARTMENT OF STATE REVENUE

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Letter of Findings Number: 08-0704
Sales and Use Tax
For the Tax Years 2005-2007

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ISSUE

I. Sales and Use Tax – Taxable Vehicle Rentals.

Authority: IC § 6-8.1-5-1(b)(c); IC § 6-2.5-2-1; IC § 6-2.5-3-2(a); IC § 6-2.5-4-10; 45 IAC 2.2-4-27; Sales Tax Information Bulletin 2 (December 2006).

Taxpayer protests the assessment of use tax on vehicles that it rents and provides to customers who are having their automobiles serviced or repaired.

II. Tax Administration – Ten Percent Negligence Penalty.

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

Taxpayer protests the imposition of the negligence penalty.

III. Tax Administration – Interest.

Authority: IC § 6-8.1-10-1(a); IC § 6-8.1-10-1(e).

Taxpayer protests the interest assessed.

STATEMENT OF FACTS

In the tax years 2005, 2006, and 2007, Taxpayer rented vehicles for customers who had purchased new or used automobiles from Taxpayer in 2002 through 2007. The vehicles were rented for customers when the customer's automobiles were being serviced or repaired by Taxpayer. The vehicles were rented from a national rental car service unaffiliated with Taxpayer. Taxpayer spent $229,000.00 (in 2005), $230,000.00 (2006), and $233,000.00 (2007) in rental fees. Taxpayer did not charge the customers for the rental vehicles, and no sales tax was paid by Taxpayer on the rental of the vehicles.

The Indiana Department of Revenue (Department) conducted a sales and use tax audit of Taxpayer for the years 2005 through 2007. The Department assessed use tax on the vehicle rentals. Taxpayer protested this assessment on the basis that the vehicle rentals were a part of the sales transaction of the customer's automobile because the rentals were covered under the manufacturer warranty and/or the dealer warranty. Taxpayer did not protest the remaining assessments in the audit. An administrative hearing was held, and this Letter of Findings results.

I. Sales and Use Tax – Taxable Vehicle Rentals.

DISCUSSION

Tax assessments are presumed to be accurate. IC § 6-8.1-5-1(c). The taxpayer bears the burden of proving that any assessment is incorrect. Id.

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).

The lease of tangible personal property is considered a retail transaction, subject to the sales and use tax. IC § 6-2.5-4-10. This is further expounded upon in 45 IAC 2.2-4-27, which states that "the gross receipts from renting or leasing tangible personal property are taxable. This regulation only exempts from tax those transactions which would have been exempt in an equivalent sales transaction."

Sales Tax Information Bulletin 2 (December 2006) explains the application of this sales and use tax exemption to rented tangible personal property transferred pursuant to original manufacturer warranties and dealer warranties as follows:

> If the dealer provides a vehicle for the person to use while a car is being repaired under the conditions of a warranty, the furnishing of the vehicle is not considered to be part of the repair or the replacement parts and the charge for the provided vehicle is subject to the sales or use tax. If the warranty explicitly states that a replacement vehicle will be provided while warranty work is being performed, then the rental transaction is considered to be part of the original warranty and is exempt from the sales or use tax. The exemption must be supported by written documentation of payment from the warranty provider.

Taxpayer contends that either the manufacturer's warranty or the dealer's warranty should cause the rental car transactions to be exempt from Indiana's use tax.

A. Manufacturer's Warranty

Taxpayer points to the manufacturer's warranty, which for 2003 through 2006 model year vehicles offered "a customer support program for new vehicles." This customer support program was not offered for model years prior to 2003, and model years after 2006. Since the present audit was for the tax years 2005, 2006, and 2007,

Taxpayer could potentially be servicing cars purchased before 2005 that were still under the manufacturer's warranty, or servicing cars purchased after 2006 when the customer support program was not included in their manufacturer's warranty.

Taxpayer argues that since this customer support program was available to customers for new vehicles from the aforementioned model years, that a majority of the rental vehicle transactions for their customers were covered under the original sales transaction, and thus the transactions were exempt from sales tax. Taxpayer has provided copies of the Owner's Manuals, which state in 2003 through 2006 model year booklets that "[t]he... program is offered to retail purchase/lease customers in conjunction with the Bumper-to-Bumper coverage provided by the New Vehicle Limited Warranty. Several transportation options are available when warranty repairs are required." However, this does not fit within the framework of Sales Tax Information Bulletin 2, as the warranty does not "explicitly state[] that a replacement vehicle will be provided while warranty work is being performed"; instead, it states that the customer has "several transportation options," which does not necessarily mean that a rental car would be provided. This does not guarantee that the customer will be provided a rental car. In fact, according to the manufacturer's website, the customer support program may provide a rental vehicle "if the repair requires the vehicle to stay at the dealership overnight." Finally, the customer support program was only available at "participating dealers," and Taxpayer never stated that they were a participating dealer. In fact, the actual vehicle rentals appear to have been provided pursuant to Taxpayer's Loaner Car Program alone, and independent of the customer support program (as discussed in Section B).

While it is explicit in the 2003 through 2006 model year owner's manuals that the customer support program would be available, the owner's manuals are not explicit in stating what specific services would be provided by the customer support program. In that respect, the manufacturer's warranties are ambiguous, and not explicit, concerning the providing of a replacement vehicle while the dealer performs warranty work. Therefore, according to Sales Tax Information Bulletin 2, the rental cars provided would not be considered part of the manufacturer's warranty. Instead, "the furnishing of the vehicle [would] not [be] considered to be part of the repair or the replacement parts and the charge for the provided vehicle is subject to the sales or use tax."

B. Dealer's Warranty

Taxpayer states that new vehicles that were purchased during the audit period with the model years 2001, 2002, and 2007, and used vehicles that were purchased during the entire audit period, would not be covered by the manufacturer's warranty, but would still be covered by the dealer warranty. Each customer, when purchasing a new or used car from Taxpayer, signed a "Conditional Purchase Order." On the Conditional Purchase Order, there is a section labeled "Loaner Car Program," which states that:

New Vehicle Purchase: 36 months from date of purchase.

Used Car Purchase: 6 months from date of purchase.

Must be 18 years of age, original purchaser and have a valid driver's license. Only on purchase vehicle. Only at [Taxpayer].

There is then an area for the purchaser to sign and date. However, there is nothing else on the Conditional Purchase Area in the Loaner Car Program section stating what the terms and conditions were in order to receive a loaner car.

Taxpayer's president attests that "[t]here was never a specific written black and white policy utilized to determine exactly what circumstances had to exist in order for a customer to be entitled to a loaner vehicle." He goes on to state that the terms of the loaner program were never put into writing because to have a strict policy could end up inconveniencing their customers, which in turn may hurt their business relationship with their customers. Instead, providing a loaner car was discretionary for the manager to provide a loaner vehicle or not based on "whatever was reasonably necessary to meet the needs and/or demands of its customers and to keep the customer happy." There was also a "soft" policy of an estimated two-and-a-half hours waiting time in order for the loaner car to be offered, but this was not strictly followed, as it was possible for the customer to negotiate for a loaner car when the wait time would be less than two-and-a-half hours.

The Loaner Car Program section only states that a loaner vehicle will be available for a certain length of time, depending on whether it is a new or used vehicle, and whether the purchaser is at least 18 years old, has a valid driver's license, and is the original purchaser of the car. As with the manufacturer's warranty, the dealer's warranty does not "explicitly state[] that a replacement vehicle will be provided while warranty work is being performed," and in fact, in the Warranty Information box on the Conditional Purchase Order, it states that for new vehicles or demonstrator vehicles purchased from Taxpayer, the only warranty that is provided to the purchaser is by the manufacturer's warranty. For older vehicles purchased from Taxpayer, there is no warranty provided, only that it is sold "as is – with all faults."

Sales Tax Information Bulletin 2 also states that "[t]he exemption must be supported by written documentation of payment from the warranty provider." Since the dealer did not warrant service or repairs would be done, and it was stated that the manufacturer was the warranty provider in the Conditional Purchase Order, the written documentation would have to come from the manufacturer. Since the written documentation from the manufacturer is ambiguous in this respect, the exemption from sales and use tax is not sufficiently supported.

Taxpayer's president stated that it was discretionary for the managers to determine that the Taxpayer should

provide a rental vehicle to a customer. Loaner vehicles were also apparently provided under circumstances when warranty work was not being done in order to satisfy or to not inconvenience a customer. Therefore, even if Taxpayer was providing loaner vehicles pursuant to a warranty, Taxpayer has not sufficiently shown on which occasions a loaner vehicle was provided pursuant to that warranty and when a loaner vehicle was provided in order to satisfy a customer even though the work being performed was not warranty work. However, it is apparent that Taxpayer was not providing loaner vehicles pursuant to an explicit warranty.

Furthermore, the documentation provided by Taxpayer indicates that the vehicle rentals were only provided under the Loaner Car Program, and not under, or in conjunction with, the manufacturer's customer service program. In other words, Taxpayer provided rented vehicles pursuant to their Loaner Car Program, and not because the manufacturer's warranty required them to provide the vehicles. This is further evidenced by the fact that the Loaner Car Program existed, and rental vehicles were provided to customers, in years where the customer support program did not exist.

Finally, Taxpayer also points to what are referred to as a "We Owe," which Taxpayer's sales representatives fill out in order to show what Taxpayer owes to the purchaser that is included within the sales price. However, although the loaner program is claimed to be factored into the sales price, there is nothing provided to the Department that specifically delineates that the vehicle rentals are a part of the transaction.

FINDING

In summary, Taxpayer's protests of Subsection A & B are respectfully denied.

II. Tax Administration – Ten Percent Negligence Penalty.

DISCUSSION

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.
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> The standard for waiving the negligence penalty is given at 45 IAC 15-11-2(c) as follows:
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> 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:
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> (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.

Taxpayer established that its failure to pay the assessed tax was due to reasonable cause rather than negligence.

FINDING

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

III. Tax Administration – Interest.

DISCUSSION

Taxpayer protests the interest assessed and argues that it is an unfair burden, given that he was not informed of the relevant law.

Taxpayers who fail to file a return, to pay taxes, or who "incurs a deficiency upon a determination by the department," are subject to interest on the nonpayment. IC § 6-8.1-10-1(a). Interest continues to accrue until final payment is made. IC § 6-8.1-10-1(e) does not allow the waiver of interest by statute.

Taxpayer has not provided documentation in support of its protest of the imposition of interest, but more importantly, the Department is not authorized to waive interest under IC § 6-8.1-10-1(e). As such, the Department finds the assessment of interest proper and denies the interest protest.

FINDING

Taxpayer's protest is denied.

CONCLUSION

In summary, Taxpayer's protests of Issue I(A), Issue I(B), and Issue III are denied; however, Taxpayer's protest of Issue II is sustained.

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