

Letter of Findings: 09-0133; 09-0134
Gross Retail Tax
For 2005, 2006, and 2007

NOTICE: Under IC § 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of the document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Information Technologies – Gross Retail Tax.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-3-2(a); IC § 6-8.1-5-1(c); Sales Tax Information Bulletin 8 (May 2002); [45 IAC 2.2-4-2\(a\)\(2\)](#).

Taxpayer argues that its purchases of certain information related technologies were not subject to the gross retail tax.

II. Prospective Treatment

Authority: City Securities Corp. v. Dept. of State Revenue, 704 N.E.2d 1122 (Ind. Tax Ct. 1998); IC § 6-8.1-3-3; IC § 6-8.1-3-3(b).

As an alternative argument, Taxpayer maintains that if the Department concludes that the purchase of information related technologies is subject to gross retail tax, that determination should be applied on a prospective basis.

III. Ten-Percent Penalty

Authority: IC § 6-8.1-5-1(c); IC § 6-8.1-10-2.1(a)(3); IC § 6-8.1-10-2.1(a)(4); IC § 6-8.1-10-2.1(d); [45 IAC 15-11-2\(b\)](#); [45 IAC 15-11-2\(c\)](#).

Taxpayer requests that the Department exercise its discretion to abate the ten-percent negligence penalty.

STATEMENT OF FACTS

For purposes of this Letter of Findings, "Taxpayer" consists of two related entities. One entity is in the banking business; this first entity provides checking account services, commercial and residential mortgage loans, installment loans, along with a typical spectrum of banking services. "Taxpayer" also consists of a related holding and parent company. Both entities are located in Indiana.

The Indiana Department of Revenue (Department) conducted an audit review of Taxpayer's sales tax returns, supporting schedules, and related business records for the years 2005, 2006, and 2007. The audit resulted in the assessment of additional sales/use tax. Taxpayer disagreed with a portion of the additional assessment and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representatives explained the basis for the protest. This Letter of Findings results.

I. Information Technologies – Gross Retail Tax.

DISCUSSION

The audit report found that Taxpayer purchased "computer software and updates including licensing fees [and] maintenance contracts" and that certain of these purchases were subject to sales tax. In addition, the audit concluded that Taxpayer's purchase of "online subscriptions to publications, periodicals, magazines and bulletins were exempt from sales tax" and that certain of these purchases were not exempt.

As a threshold issue, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "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."

Pursuant to IC § 6-2.5-2-1, a sales tax, known as state gross retail tax, is imposed on retail transactions made in Indiana unless a valid exemption is applicable. Retail transactions involve the transfer of tangible personal property. IC § 6-2.5-3-2(a). A complementary excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction. IC § 6-2.5-3-2.

Specifically, IC § 6-2.5-2-1 provides as follows:

(a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana.

(b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state.

IC § 6-2.5-3-2(a) provides for the complementary use tax:

An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

A. Midwest Backgrounds:

Taxpayer purchased what it designates as "screening services" from a company called Midwest Backgrounds. According to Taxpayer, Midwest Backgrounds provides criminal record searches by means of linked public databases which allow customers to screen prospective customers and employees. The audit concluded that purchases from Midwest Background were subject to sales tax.

Taxpayer provided a sample invoice indicating that Taxpayer was billed a certain set amount for each search. The price of each search varied depending on the information sought for that particular search. The contract between Midwest Backgrounds and Taxpayer provides that Midwest Backgrounds agrees "To furnish consumer reports as requested by Subscriber."

Essentially, Taxpayer conducts individual background searches and is billed for each search depending on the nature and extent of the search requested. The issue is whether the costs are subject to sales tax.

The issue of whether that "information" is subject to sales tax is also addressed in the Sales Tax Information Bulletin 8 (May 2002) which states as follows:

The sale of statistical reports, graphs, diagrams or any other information produced or compiled by a computer and sold or reproduced for sale in substantially the same form as it is so produced is considered to be the sale of tangible personal property unless the information from which such reports was compiled was furnished by the same person to whom the finished report is sold.

Taxpayer purchases criminal background reports from Midwest Backgrounds. The reports consist of information "compiled by a computer [and] sold or reproduced for sale in substantially the same form as it is so produced...." Therefore, the reports – by whatever means transmitted – constitute "tangible personal property" obtained in a retail transaction, and the cost of the reports is subject to sales tax.

B. World-Check:

Taxpayer subscribes to a "screening service" which Taxpayer describes as follows: "World-Check offers access to a repository containing detailed profiles of terrorists, money launderers, fraudsters, and other high-risk individuals and entities."

Taxpayer cites to [45 IAC 2.2-4-2\(a\)\(2\)](#) in support of its argument that the payments made to World-Check are not subject to sales tax. That portion of the regulation states in part as follows:

Professional services, personal services, and services in respect to property not owned by the person rendering such services are not "transactions of a retail merchant constituting selling at retail", and are not subject to gross retail tax. Where, in conjunction with rendering professional services, personal services, or other services, the serviceman also transfers tangible personal property for a consideration, this will constitute a transaction of a retail merchant constituting selling at retail unless: (1) The serviceman is in an occupation which primarily furnishes and sells services, as distinguished from tangible personal property; (2) The tangible personal property purchased is used or consumed as a necessary incident to the service; (3) The price charged for tangible personal property is inconsequential (not to exceed 10 [percent]) compared with the service charge; and (4) The serviceman pays gross retail tax or use tax upon the tangible personal property at the time of acquisition.

Taxpayer supplied a copy of an invoice paid to "World-Check" and a copy of the agreement between itself and the vendor. In this case, Taxpayer pays an annual cost of \$5,000 as a "license fee." The agreement provides Taxpayer with access to the "World-Check reference database." The license fee includes the access by means of World-Check's web address and includes "print-outs, copies or other derivatives...."

In this case, Taxpayer is not paying for "statistical reports, graphs, diagrams or any other information produced or compiled by a computer...." Instead, Taxpayer is paying a specific amount for access to the information compiled by the vendor. In effect, Taxpayer is paying a fixed price for the ability to roam freely through World-Check's information; metaphorically speaking, Taxpayer paid \$5,000 for a key to the front door of World-Check's information library. As such, the fee is not subject to sales tax.

C. CSC Credit Services:

Taxpayer provided a copy of its "Service Agreement" with CSC Credit Services. That agreement is the means by which CSC agrees to provide various forms of credit information to Taxpayer. In the agreement, that information is designated as being transferred in the form of "reports." For example, the agreement states that, "[Taxpayer] will not resell reports to anyone, including the consumer who is the subject of the report." In addition to the basic, "Service Agreement," Taxpayer also furnished a copy of the "Pricing Addendum to Service Agreement." That addendum essentially outlines a plan by which Taxpayer becomes obligated to pay a flat fee for each of the various forms of credit report. Certain types of reports cost one price while other reports cost another price.

Based upon the information provided, Taxpayer appears to have entered an agreement with CSC under which CSC furnishes the electronic equivalent of "tangible personal property" and Taxpayer becomes obligated to pay a unit price for each of the reports which Taxpayer receives. Accordingly, Taxpayer should pay sales tax on the cost of the reports.

D. CBC Innovis:

Taxpayer states that it pays for "services of several credit scoring and reporting agencies." CBC Innovis is

one of those vendors. According to Taxpayer, CBC Innovis "analyze[s] an individual's potential credit risk." Taxpayer states that the money it pays this vendor is not subject to sales tax because CBC Innovis is providing an exempt service. Taxpayer asserts that if the information was supplied by telephone, the information would not be subject to tax because there would have been no transfer of tangible personal property. Essentially, Taxpayer concludes that the "true object" of the transactions between itself and CBC Innovis is an intangible service.

In the supplementary information provided by Taxpayer, it becomes apparent that Taxpayer is paying CBC Innovis for each credit report requested by Taxpayer. In this case, the transactions are similar to those described in "Midwest Backgrounds" above. Taxpayer purchases credit reports from CBC Innovis. The reports consist of information "compiled by a computer [and is] sold or reproduced for sale in substantially the same form as it is so produced...." Sales Tax Information Bulletin 8 (May 2002). Therefore, the reports constitute "tangible personal property" obtained in a retail transaction, and the cost of the reports is subject to sales tax.

E. Experian:

Taxpayer states that the invoices received from Experian are not subject to sales tax. To that end, Taxpayer furnished documentation outlining its agreement with Experian including a document entitled "Experian Standard Terms and Conditions." That agreement establishes that Experian provides "products and services" to Taxpayer. The agreement specifically cautions that "Experian has expended substantial time, effort and funds to create and deliver the Services and compile its various databases." However, the supervening "Practicing Agreement" establishes that Experian is furnishing reports for which Experian charges a "Per Unit Price." Therefore, Taxpayer pays for and is provided the electronic equivalent of "tangible personal property," and Taxpayer should pay sales tax on the price it pays for that property.

F. LexisNexis:

Taxpayer maintains that the "Debtor Discovery" service it purchases from LexisNexis is not subject to sales tax. Taxpayer states that this service "allows [Taxpayer] to access a delinquent debtor's background information." The background information consists of "current contact information, uncovering assets, identifying relatives and/or business affiliations." Taxpayer concludes that the "true object" of the purchases from LexisNexis "is the receipt of information and not the tangible means in which it was provided."

In this instance, Taxpayer has failed to provide information sufficient to sustain its protest as required to IC § 6-8.1-5-1(c).

FINDING

Taxpayer's protest is denied in part and sustained in part. The payments to World-Check are not subject to sales tax. Insofar as the remainder of the issues related to "Information Technologies," Taxpayer's protest is respectfully denied.

II. Prospective Treatment

DISCUSSION

Taxpayer sets out a general equitable argument – unsupported by citations to statutory or regulatory authority – that the Department, having found that the cost of certain information technologies is subject to the sales tax, should impose that tax liability on a prospective basis only.

Under IC § 6-8.1-3-3, the Department is without authority to reinterpret a taxpayer's tax liability without promulgating and publishing a regulation giving Taxpayer notice of that reinterpretation. IC § 6-8.1-3-3(b) states that "[n]o change in the department's interpretation of a listed tax may take effect before the date the change is: (1) adopted in a rule under this section; or (2) published in the Indiana Register...."

In *City Securities Corp. v. Dept. of State Revenue*, 704 N.E.2d 1122 (Ind. Tax Ct. 1998), plaintiff taxpayer argued that the Department could not impose gross income tax on the gain realized from the sale of tax exempt bonds, because that gain had been treated as exempt for 42 years. *Id.* at 1128. Plaintiff taxpayer argued that, in the absence of a new rule or regulation, the Department's assessment of gross income taxes against the gain realized from the sale of bonds was invalid. *Id.* at 1129. The Tax Court found that, despite the intervening adoption of regulations to the contrary, the Department could not impose the additional taxes when the Department had permitted plaintiff taxpayer to claim an exemption from the taxes subsequent to the adoption of the intervening regulations. *Id.*

Unlike the plaintiff taxpayer in *City Securities*, Taxpayer is unable to point to a prior court case, Letter of Findings, or Department advisory letter indicating that the purchase of the information technologies was exempt from sales tax. *City Securities*, 704 N.E.2d at 1129. Rather, the statutory and regulatory authority supporting imposition of the gross retail tax on the cost of the information technologies was fully in place at the time of Taxpayer's audit and is set out in Sales Tax Information Bulletin 8 (May 2002). Absent any indication that the Department has changed its interpretation of the gross retail tax since Taxpayer's previous audit, IC § 6-8.1-3-3 does not require the Department to give effect to Taxpayer's sales tax liabilities on a prospective basis. Absent any requirement to do otherwise, the Department has no independent authority whatsoever to grant Taxpayer's equitable request for prospective treatment of its sales tax liabilities.

FINDING

Taxpayer's protest is respectfully denied.

III. Ten-Percent Penalty

DISCUSSION

Taxpayer believes that it is entitled to abatement of the ten-percent negligence penalty because it exercised reasonable business judgment.

IC § 6-8.1-10-2.1(a)(3) requires that a ten-percent penalty be imposed if the tax deficiency results from the taxpayer's negligence. IC § 6-8.1-10-2.1(a)(4) requires a ten-percent penalty if the taxpayer "fails to pay the full amount of tax shown on the person's return on or before the due date for the return or payment."

IC § 6-8.1-10-2.1(d) states that, "If a person subject to the penalty imposed under this section can show that the failure to... pay the full amount of tax shown on the person's return... or pay the deficiency determined by the department was due to reasonable cause and not due to willful neglect, the department shall wave the penalty."

Departmental regulation [45 IAC 15-11-2](#)(b) defines negligence as "the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." Negligence is to "be determined on a case-by-case basis according to the facts and circumstances of each taxpayer." Id.

IC § 6-8.1-10-2.1(d) allows the Department to waive the penalty upon a showing that the failure to pay the deficiency was based on "reasonable cause and not due to willful neglect." Departmental regulation [45 IAC 15-11-2](#)(c) requires that 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 IC § 6-8.1-5-1(c), "The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." An assessment – including the negligence penalty – is presumptively valid.

Given the number of items for which Taxpayer failed to self-assess use tax, the fact that the Taxpayer has been previously audited, and that Taxpayer underreported its use tax liability by approximately 45 percent, the Department is unable to agree that the Taxpayer exercised ordinary business care in determining its sales/use tax liabilities.

FINDING

Taxpayer's protest respectfully denied.

SUMMARY

Taxpayer is subject to sales tax on purchases made from Midwest Backgrounds, CSC Credit Services, CBC Innovis, Experian, and LexisNexis; taxpayer is not subject to sales tax on purchases made from World-Check. Taxpayer is not entitled to prospective treatment on the Department's determination that sales tax is due on the purchase of certain information technologies. Taxpayer is not entitled to abatement of the ten-percent negligence penalty.

Posted: 10/28/2009 by Legislative Services Agency
An [html](#) version of this document.