

Letter of Findings: 08-0728R
Indiana Sales and Use Tax
For the Tax Periods 2005, 2006, 2007, 2008

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ISSUE

I. Processing Exemption – Sales/Use Tax.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-5-1; [45 IAC 2.2-5-12](#); [45 IAC 2.2-5-14](#).

Taxpayer maintains that testing supplies consumed during biological sampling qualify for the processing exemption.

STATEMENT OF FACTS

Taxpayer facilitates the use of biological samples by, and obtained from, its customers, which are predominately government agencies. A government agency typically provides taxpayer with a biological sample in order to obtain a DNA profile of the individual from whom the sample was acquired. Taxpayer combines that sample with chemical reagents to produce a suspension that contains the biological sample. Taxpayer performs various analyses of that suspension in order to produce a report showing the DNA profile of the individual. Taxpayer also stores both the suspension and the remains of the biological sample for its customers until customers request either the return or the destruction of the suspension and sample. Taxpayer bills the customer a fixed price per sample.

Taxpayer paid Indiana sales tax on the various chemicals and materials it asserts go into the creation of the suspension, the testing of the sample, and storage of the suspension and samples. Taxpayer filed refund claims pertaining to its payment of sales tax on the chemicals. After the Department rejected taxpayer's refund claims, taxpayer filed a protest. An administrative hearing was held, in which taxpayer again protested the Department's denial of refund of sales tax paid on chemicals and materials.

I. Processing Exemption – Sales/Use Tax.

DISCUSSION

Indiana imposes a sales tax on retail transactions. IC § 6-2.5-2-1. The state also imposes a complementary use tax on tangible personal property that is stored, used, or consumed within the state. IC § 6-2.5-3-2. Taxpayer maintains that the ingredients used to make the suspension are property consumed in the direct production of manufacturing tangible personal property and are exempt from sales or use tax under the "direct consumption manufacturing exemption" as defined in IC § 6-2.5-5-1.

The "direct consumption manufacturing exemption" to the use tax is provided, in relevant part, in IC § 6-2.5-5-1(b):

(b) Transactions involving personal property are exempt from the state [use] 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, [or] repairing....

[45 IAC 2.2-5-12\(c\)](#) further defines property obtained for "direct consumption as a material to be consumed in direct production" as "materials [that] are directly used in the production process" and that have "an immediate effect on the article being produced." Property has "an immediate effect" when it becomes "an essential and integral part of the integrated process which produces tangible personal property." [45 IAC 2.2-5-12\(c\)](#).

Accordingly, property purchased for use or consumption in the direct production of a manufactured good is subject to use tax unless the property used has an immediate effect on and is essential to the production of the marketable good.

The Department's regulation found at [45 IAC 2.2-5-14\(d\)](#) qualifies the definition of tangible personal property that has been "incorporated as a material or integral part" of property "produced for sale" to mean:

- (1) That the material must be physically incorporated into and become a component of the finished product;
- (2) The material must constitute a material or an integral part of the finished product; and
- (3) The tangible personal property must be produced for sale by the purchaser.

Taxpayer asserted that the price of the chemicals and materials consumed amounts to approximately fifty-two percent of the price charged per sample. But taxpayer did not provide any documents supporting the fifty-two percent allocation. Taxpayer did not provide any documents displaying a separation of the costs of the chemicals from the other costs incurred in producing, analyzing, and storing the suspensions. Further, taxpayer-supplied invoices showing purchases of the chemicals in bulk, and a customer invoice showing the flat fee charged per sample, do not demonstrate that the aforementioned chemicals and materials represent the object of the transaction.

Taxpayer argued that transactions with its customers represented the sale of tangible personal property.

However, the customer invoice submitted by taxpayer fails to show sales tax paid on the flat fee. Other documents submitted by taxpayer do not indicate that the suspension represents the object of the transaction, but rather that taxpayer's analysis of the biological sample, facilitated by taxpayer's creation of the suspension, and documented in a written report pursuant to customers' requirements, serves as the object of the transaction. Taxpayer's explanations and submissions do not support the sale of tangible personal property.

Taxpayer has failed to overcome the Department's determination that taxpayer provides a service to its customers. Taxpayer creates a report based upon testing, analyses, and procedures it conducts on specimens submitted by its customers.

FINDING

Taxpayer's protest is respectfully denied.

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