

**Letter of Findings: 09-0684
Indiana Sales and Use Tax
For 2006 and 2007**

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ISSUES

I. Exempt Propane – 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); [45 IAC 2.2-5-8\(f\)](#); [45 IAC 2.2-5-12](#).

Taxpayer argues that the Department of Revenue erroneously concluded that 41.12 percent of the propane it uses to fuel its forklifts is subject to sales tax; Taxpayer maintains that only 36.71 percent of the propane is subject to sales tax.

II. Forklift Expenses – Gross Retail Tax.

Authority: IC § 6-8.1-5-1(c); [45 IAC 2.2-5-12\(d\)\(1\)](#).

Taxpayer maintains that 55.35 percent of the repairs and maintenance costs associated with its forklifts are exempt and not the 51.74 percent as determined by the Department.

III. Exempt Lift Equipment – Gross Retail Tax.

Authority: IC § 6-8.1-5-1(c); [45 IAC 2.2-5-8\(f\)\(3\)](#).

Taxpayer states that a lift device called a "Hyster" is exempt because the device is used in the direct production of its wood veneer products.

IV. Administrative Error.

Authority: IC § 6-8.1-5-1(c).

Taxpayer argues that the Department erred in concluding that a particular item of equipment designated as "Timbersoft Husky-Logbuyers" was acquired in 2007.

STATEMENT OF FACTS

Taxpayer is an Indiana company in the business of producing wood veneer products. Taxpayer also sells logs, bark, and provides veneer cutting services for its customers. The Department of Revenue conducted an audit review of Taxpayer's business records and found that Taxpayer owed additional sales and use tax. Taxpayer disagreed with the assessment and – following a review of Taxpayer's contentions by the audit division – submitted a protest on the remaining disputed issues. An administrative hearing was conducted during which Taxpayer's representatives explained the basis for the protest. This Letter of Findings results.

I. Exempt Propane – Gross Retail Tax.

DISCUSSION

Taxpayer purchases propane which is used to fuel its forklifts. Taxpayer purchased the propane without paying sales tax. The audit assessed use tax on these purchases. After Taxpayer initially objected, the audit conducted a supplementary review concluding that the propane was used in a non-exempt manner 41.12 percent of the time. Taxpayer disagrees arguing that the propane *[sic]* is used in a non-exempt manner 36.71 percent of the time.

Taxpayer's calculation is based on the contention that it is entitled to an exemption for fuel used to move its product to the "grading" stage of its operation. The audit report describes the "grading" stage as follows:

The majority of [Taxpayer's] production is for the export market. Export market veneer is next moved in pallets to the clipping line where it is trimmed for suitability to that market. The exempt manufacturing of export veneer ends at the end of the clipping line. The trimmed veneer is again loaded [unto] pallets and moved to the grading line where the product is graded and sorted according to grade. The export veneer is next moved to the export warehouse/display building where it may be placed in storage or moved directly to the sales area for display to possible customers. (Emphasis added).

Later on in the report, the audit described the equipment within the "grading" line as used to "permit the examination of [Taxpayer's] export product by plant personnel so that the product can be graded as to quality and for pricing [and that the] product is not changed by this procedure and production is complete before this step...."

The italicized language cited above is at the heart of Taxpayer's protest. Taxpayer contends that movement of the veneer to and within the "grading" area is exempt because "grading" is simply a continuation of the manufacturing process.

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.

[45 IAC 2.2-5-8](#)(f) provides guidance in resolving the issue.

- (1) Tangible personal property used for moving raw materials to the plant prior to their entrance into the production process is taxable.
- (2) Tangible personal property used for moving finished goods from the plant after manufacture is subject to tax.
- (3) Transportation equipment used to transport work-in-process or semi-finished materials to or from storage is not subject to tax if the transportation is within the production process.
- (4) Transportation equipment used to transport work-in-process, semi-finished, or finished goods between plants is taxable, if the plants are not part of the same integrated production process. **EXAMPLES:**
 - (1) A manufacturer of clay pipe uses forklift tractors to transport the pipe from the machine in which it is formed to the kiln. The forklift tractors are exempt.
 - (2) A metal and alloy manufacturer pulverizes raw materials for use in an exempt furnace. Weigh bins are utilized for the temporary storage of the exempt materials after pulverization and prior to use in an exempt furnace. Transportation equipment used to transport the pulverized raw material to and from the weigh bins is exempt.
 - (3) A forklift is used exclusively to move work-in-process from a temporary storage area in a plant and to transport it to a production machine for processing. Because the forklift functions as an integral part of the integrated system comprising the production operations, it is exempt.
 - (4) A forklift is used exclusively to move finished goods from a storage warehouse and to load them on trucks for shipment to customers. The forklift is taxable because it is used outside the integrated production process.
 - (5) A forklift is regularly used 40 [percent] of the time for the purpose described in Example (3) and 60 [percent] of the time for the purpose described in Example (4). The taxpayer is entitled to an exemption equal to 40 [percent] of the gross retail income attributable to the transaction in which the fork lift was purchased. (Emphasis added).

[45 IAC 2.2-5-12](#) provides:

- (a) The state gross retail tax shall not apply to sales of any tangible personal property consumed in direct production by the purchaser in the business of producing tangible personal property by manufacturing, processing, refining, or mining.
- (b) The exemption provided by this regulation [\[45 IAC 2.2\]](#) applies only to tangible personal property to be directly consumed in direct production by manufacturing, processing, refining, or mining. It does not apply to machinery, tools, and equipment used in direct production or to materials incorporated into the tangible personal property produced.
- (c) The state gross retail tax does not apply to purchases of materials to be directly consumed in the production process or in mining, provided that such materials are directly used in the production process; i.e., they have an immediate effect on the article being produced. The 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.
- (d) Pre-production and post-production activities.

- (1) Direct consumption in the production process begins at the point of the first operation or activity constituting part of the integrated production process and ends at the point that the production process has altered the item to its completed form, including packaging, if required.

Taxpayer uses its forklifts both within the veneer production process and outside the veneer production process. Under [45 IAC 2.2-5-12](#), the propane fuel used by forklifts within the production process is exempt because it is "consumed" within the production process.

The audit found that the "grading process" was outside the "integrated production process" and the Department is reluctant to disturb that decision absent compelling evidence to the contrary. Based on the information provided, the "grading" of the Taxpayer's veneer takes place after the veneer has been produced. Absent that compelling evidence, the Department is unable to conclude that the propane is used in a non-exempt manner 36.71 percent of the time.

FINDING

Taxpayer's protest is respectfully denied.

II. Forklift Expenses – Gross Retail Tax.

DISCUSSION

Taxpayer purchased supplies and equipment to service and maintain its forklifts. Taxpayer calculated that 51.74 percent of the supplies and equipment were used to service forklifts operating outside Taxpayer's production process. The audit found 55.35 percent of the supplies and equipment was taxable because the

supplies and equipment were used to service forklifts used outside Taxpayer's production process.

As noted in Part I of this Letter of Findings, the difference between the audit's calculation and the Department's calculation stems from the question of whether or not Taxpayer's "grading" process is included within Taxpayer's veneer production process.

Under IC § 6-8.1-5-1(c), Taxpayer is required to prove that the proposed assessment is wrong. Again, the Department is not prepared – on the basis of a brief phone hearing – to second-guess an auditor who spent two months preparing the audit report, toured Taxpayer's facility, and engaged in extensive direct communication with Taxpayer's representatives.

The determination that Taxpayer's "grading" process takes place following the "integrated production process" is neither unreasonable nor unsupported by the available information. [45 IAC 2.2-5-12\(d\)\(1\)](#).

FINDING

Taxpayer's protest is respectfully denied.

III. Exempt Lift Equipment – Gross Retail Tax.

DISCUSSION

Taxpayer purchased a "Hyster" which appears to be a device similar to a forklift. Taxpayer maintains that the "Hyster" is exempt because it is directly used in the veneer production process as explained in [45 IAC 2.2-5-8\(f\)\(3\)](#) which states that, "Transportation equipment used to transport work-in-process or semi-finished materials to or from storage is not subject to tax if the transportation is within the production process."

The audit found that the "Hyster" is used to move the veneer from the "drying department" and that "not all movement of product from the drying department is still within production." However, Taxpayer's representative states that the "Hyster" is used within the drying department.

There appears to be little dispute that drying Taxpayer's veneer is part and parcel of the production process and that equipment used within the drying department is exempt. What is disputed is whether the "Hyster" is used within the drying department or to move veneer after the drying has occurred.

Taxpayer has not provided sufficient evidence to refute the audit's conclusion that the "Hyster" is not exempt. Under IC § 6-8.1-5-1(c), Taxpayer has failed to prove the Department's determination was wrong.

FINDING

Taxpayer's protest is respectfully denied.

IV. Administrative Error.

DISCUSSION

Taxpayer complains that the audit stated that the purchase of "Timbersoft Husky-Logbuyers" occurred in 2007 but that it was actually purchased in 2006. As noted above, IC § 6-8.1-5-1(c), requires that Taxpayer bear the burden of demonstrating that the proposed assessment is wrong. Presumably Taxpayer's objection ultimately relates to that proposed assessment. However, in this case Taxpayer is simply off the mark. The audit report does not classify the "Timbersoft Husky-Logbuyers" as having been acquired in 2007 but does – as Taxpayer insists it should – designate this item as having been acquired in 2006.

In this particular instance, there is nothing to which the Taxpayer can object. Therefore, the issue is moot.

FINDING

Taxpayer's protest is denied.

SUMMARY

Taxpayer's protest is denied in its entirety.

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