

Letter of Findings Number: 10-0204
Use Tax
For Tax Year 2006

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ISSUES

I. Use Tax—Recreational Vehicle.

Authority: Gregory v. Helvering, 293 U.S. 465 (1935); Comm'r v. Transp. Trading & Terminal Corp., 176 F.2d 570 (2d Cir. 1949); Horn v. Comm'r, 968 F.2d 1229 (D.C. Cir. 1992); Lee v. Comm'r, 155 F.3d 584 (2d Cir. 1998); IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-8.1-5-1; [45 IAC 2.2-3-4](#).

Taxpayer protests the imposition of use tax on the use of a recreational vehicle.

II. Tax Administration—Negligence Penalty.

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

Taxpayer protests the imposition of a ten percent negligence penalty.

STATEMENT OF FACTS

Taxpayer is an individual and is a resident of Indiana. The Indiana Department of Revenue ("Department") determined that on March 28, 2006, Taxpayer purchased a recreational vehicle ("RV") in Kentucky and had been using the RV in Indiana and other states without paying sales tax in any jurisdiction. As a result, the Department issued proposed assessments for use tax, ten percent negligence penalty, and interest. Taxpayer protests that the RV was titled by a Montana LLC, that the RV was transported directly from Kentucky to Florida, where it remained, and that no Indiana use tax or negligence penalty is due. An administrative hearing was conducted and this Letter of Findings results. Further facts will be supplied as required.

I. Use Tax—Recreational Vehicle.

DISCUSSION

Taxpayer protests the imposition of use tax on the use and storage of an RV in Indiana. The Department imposed use tax after determining that Taxpayer had been using and storing the RV in Indiana and that no sales tax had been paid on the purchase of the RV. Taxpayer protests that the RV was titled by a Montana LLC and that the RV was transported directly from the purchase point in Kentucky to its permanent storage/use point in Florida. The Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

The sales tax is imposed by IC § 6-2.5-2-1, which states:

(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.

The use tax is imposed under IC § 6-2.5-3-2(a), which states:

(a) 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.

Also, [45 IAC 2.2-3-4](#) provides:

Tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used, or otherwise consumed in Indiana is subject to Indiana use tax for such property, unless the Indiana state gross retail tax has been collected at the point of purchase.

Therefore, when tangible personal property is acquired in a retail transaction and is stored, used, or consumed in Indiana, Indiana use tax is due if sales tax has not been paid at the point of purchase. The Department determined that Taxpayer, an Indiana resident, purchased the RV in Kentucky in a retail transaction on March 28, 2006. The Department therefore issued proposed assessments for use tax.

Taxpayer protests that the RV was never stored, used, or otherwise consumed in Indiana and that Indiana use tax is therefore inapplicable. Taxpayer states that the RV was transported directly from Kentucky to Florida, where it was parked and used on a relative's property. Despite being given ample time, Taxpayer was unable to provide any documentation in support of this position.

In the alternative, Taxpayer states that the RV was titled by a Montana LLC. Taxpayer provided copies of invoices from several years, including 2006, which state that the LLC did pay Montana registration fees and that it paid for the establishment and formation of the LLC. Taxpayer has not provided any documentation establishing an underlying purpose for the LLC to title the RV. Neither has Taxpayer provided any documentation establishing any activity of any kind by the LLC. This leads to consideration of the "sham transaction" doctrine, which is long

established both in state and federal tax jurisprudence dating back to *Gregory v. Helvering*, 293 U.S. 465 (1935). In that case, the Court held that in order to qualify for favorable tax treatment, a corporate reorganization must be motivated by the furtherance of a legitimate corporate business purpose. *Id.* at 469. A corporate business activity undertaken merely for the purpose of avoiding taxes was without substance and "[T]o hold otherwise would be to exalt artifice above reality and to deprive the statutory provision in question of all serious purpose." *Id.* at 470.

The courts have subsequently held that "in construing words of a tax statute which describe [any] commercial transactions [the court is] to understand them to refer to transactions entered upon for commercial or industrial purposes and not to include transactions entered upon for no other motive but to escape taxation." *Comm'r v. Transp. Trading & Terminal Corp.*, 176 F.2d 570, 572 (2d Cir. 1949), cert. denied, 338 U.S. 955 (1950). "[T]ransactions that are invalidated by the [sham transaction] doctrine are those motivated by nothing other than the taxpayer's desire to secure the attached tax benefit" but are devoid of any economic substance. *Horn v. Comm'r*, 968 F.2d 1229, 1236-7 (D.C. Cir. 1992). In determining whether a business transaction was an economic sham, two factors can be considered; "(1) did the transaction have a reasonable prospect, ex ante, for economic gain (profit), and (2) was the transaction undertaken for a business purpose other than the tax benefits?" *Id.* at 1237. The question of whether or not a transaction is a sham, for purposes of the doctrine, is primarily a factual one. *Lee v. Comm'r*, 155 F.3d 584, 586 (2d Cir. 1998).

In this case, the facts are that the Montana LLC had no business or non-business functions and never attempted to conduct any functions of any kind. The titling of the RV in Montana, a state without a sales tax, was merely an attempt to reduce or eliminate Taxpayer's sales and use tax liabilities. The formation of the LLC and the titling of the RV in the name of the LLC was therefore a "sham transaction."

Additionally, the RV was invoiced in Kentucky on March 28, 2006, while the invoice regarding the formation/establishment of the LLC is dated March 30, 2006. This means that Taxpayer purchased the RV and then contributed it to the LLC. Since Taxpayer is an Indiana resident and since there is no documentation establishing that the RV was not brought into and used in Indiana, Indiana use tax is properly due.

In conclusion, the formation of the LLC and the titling of the RV by the LLC was a sham transaction. Also, the timing of the purchase of the RV by Taxpayer and contribution of the RV to the LLC would still require sales or use tax be paid by Taxpayer. Either of these reasons alone would establish that Taxpayer, an Indiana resident, acquired tangible personal property in a retail transaction, but did not pay sales tax at the point of purchase or anywhere else. In such circumstances, Indiana use tax is due, as explained by [45 IAC 2.2-3-4](#). Taxpayer has not met the burden of proving the proposed assessments wrong, as provided by IC § 6-8.1-5-1(c).

FINDING

Taxpayer's protest is denied.

II. Tax Administration—Negligence Penalty.

DISCUSSION

The Department issued proposed assessments and the ten percent negligence penalty for the tax years in question. Taxpayer protests the imposition of penalty. The Department refers to IC § 6-8.1-10-2.1(a), which states in relevant part:

If a person:

...
(3) incurs, upon examination by the department, a deficiency that is due to negligence;

...
the person is subject to a penalty.

The Department refers to [45 IAC 15-11-2\(b\)](#), which states:

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.

[45 IAC 15-11-2\(c\)](#) provides in pertinent part:

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.

In this case, Taxpayer incurred a deficiency which the Department determined was due to negligence under [45 IAC 15-11-2\(b\)](#), and so was subject to a penalty under IC § 6-8.1-10-2.1(a). No documentation was provided in support of Taxpayer's protest that the RV was driven directly from Kentucky to Florida. Taxpayer has not established that the failure to pay the deficiency was due to reasonable cause and not due to negligence, as required by [45 IAC 15-11-2\(c\)](#).

FINDING

Taxpayer's protest is denied.

CONCLUSION

Taxpayer's protest is denied on Issue I regarding the imposition of use tax. Taxpayer's protest is denied on Issue II regarding imposition of negligence penalty.

Posted: 09/29/2010 by Legislative Services Agency
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