

Letter of Findings: 04-20090555
Sales and Use Tax
For the Years 2005, 2006, 2007

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ISSUES

I. Sales and Use Tax – Manufacturing Exemptions.

Authority: IC § 6-2.5-3-2; IC § 6-2.5-5-3; IC § 6-2.5-5-4; IC § 6-2.5-5-5.1; IC § 6-8.1-5-1; [45 IAC 2.2-5-8](#); [45 IAC 2.2-5-10](#); Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Indiana Dep't of Revenue v. Cave Stone Inc., 457 N.E.2d 520 (Ind. 1983); General Motors Corp. v. Indiana Dep't of Revenue, 578 N.E.2d 399 (Ind. Tax Ct. 1991); Mechanics Laundry & Supply, Inc. v. Indiana Dep't of State Revenue, 650 N.E.2d 1223 (Ind. Tax Ct. 1995); Rotation Products Corp. v. Indiana Dep't of State Revenue, 690 N.E.2d 795 (Ind. Tax Ct. 1998); North Cent. Indus., Inc., Co. v. Indiana Dep't of State Revenue, 790 N.E.2d 198 (Ind. Tax Ct. 2003); Indiana Dep't of Revenue v. Interstate Warehousing, Inc., 783 N.E.2d 248 (Ind. 2003).

Taxpayer protests the assessment of use tax on several items it claims qualify for the manufacturing exemption.

II. Sales and Use Tax – "Wrapping Materials and Containers" Exemption.

Authority: IC § 6-2.5-5-9; [45 IAC 2.2-5-16](#).

Taxpayer protests the imposition of use tax on certain items it claims are subject to this exemption.

III. Sales and Use Tax – Credits for Overpayment of Sales Tax.

Authority: IC § 6-8.1-5-1.

Taxpayer presents invoices that were not available during the audit that show that Taxpayer paid sales tax and is therefore asking for a credit for those overpayments.

IV. Sales and Use Tax – Retail Transactions.

Authority: IC § 6-2.5-3-2; IC § 6-2.5-4-1; Sales Tax Information Bulletin 8 (May 2002), 25 Ind. Reg. 3934; Cowden & Sons v. Indiana Dep't of Revenue, 575 N.E.2d 718 (Ind. Tax Ct. 1991).

Taxpayer protests that certain transactions it engaged in were not retail transactions because the reports that were transmitted were incidental to the "true object" of the service, which was the provision of information.

V. 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, an Indiana company, processes scrap material including aluminum, copper, brass, wire, steel, insulation, and plastic. During the years at issue, Taxpayer purchased scrap, checked it for radiation and sorted the scrap. Some scrap material is sold "as is" and some scrap is processed by cutting, crushing, shredding, and granulating the scrap. The scrap is sold exempt to manufacturers.

Pursuant to a sales and use tax audit for the years 2005, 2006, and 2007, the Indiana Department of Revenue ("Department") assessed Taxpayer additional use tax, penalty and interest on items Taxpayer claimed were directly used in its direct manufacturing process and therefore should be exempt from sales and use tax. For the years at issue Taxpayer filed as an S corporation. In late 2007 Taxpayer's individual shareholders sold their stock to an unrelated Indiana corporation. Taxpayer owns numerous disregarded entities and joint ventures. The audit included 21 locations.

Taxpayer protested the Department's assessment of additional tax and penalty. In its protest letter dated August 5, 2010, Taxpayer sets out ten (10) protest issues which are, as Taxpayer enumerates:

- (1) Transportation Equipment and Supplies Used to Transport Work in Process
- (2) Transportation Equipment Used in Production
- (3) Equipment Used to Weigh, Inspect, Test Products During Production Process
- (4) Environmental Quality Control
- (5) Packaging
- (6) Safety Equipment
- (7) Miscellaneous Equipment or Supplies Used of Consumed During Production
- (8) Credits for Overpaid Tax and Duplications
- (9) Non Retail Transactions
- (10) Penalty

A hearing was held on Taxpayer's protest and this Letter of Findings ensues. Additional facts will be provided as necessary.

I. Sales and Use Tax – Manufacturing Exemptions.**DISCUSSION**

Taxpayer maintains that as a processor of scrap materials, the purchases of certain items it used in its processes were exempt under the "manufacturing exemptions." The items at issue in this section fall under the issues enumerated as (1), (2), (3), (4), (6), and (7) in the "Statement of Facts" section above.

Taxpayer is reminded that all tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(b), (c); Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007). Furthermore, the taxpayer claiming exemption has the burden of showing the terms of the exemption statute are met. General Motors Corp. v. Indiana Dept. of State Revenue, 578 N.E.2d 399, 404 (Ind. Tax Ct. 1991) aff'd 599 N.E.2d 588 (Ind. 1992) (Internal citations omitted). Additionally "[e]xemption statutes are strictly construed because an exemption releases property from the obligation of bearing its fair share of the cost of government." Id.

Indiana imposes "an excise tax, known as the use tax," on tangible personal property that is acquired in retail transactions and is stored, used, or consumed in Indiana. IC § 6-2.5-3-2(a).

In general, all purchases of tangible personal property by persons engaged in the direct production, manufacture, fabrication, assembly or finishing of tangible personal property are taxable. [45 IAC 2.2-5-8\(a\)](#). The exemption only applies to manufacturing machinery, tools, and equipment directly used by the purchaser in direct production. Id. Machinery, tools, and equipment are directly used in the production process if they have an immediate effect on the article being produced. [45 IAC 2.2-5-8\(c\)](#). A machine, tool, or equipment has an immediate effect on the product being produced if it is an essential and integral part of an integrated process that produces the product. [45 IAC 2.2-5-8\(c\)](#); Indiana Dep't of Revenue v. Cave Stone Inc., 457 N.E.2d 520 (Ind. 1983). An integrated process is one where the total production process is comprised of activities or steps that are functionally interrelated and where there is a flow of "work-in-process." [45 IAC 2.2-5-8\(c\)\(1\)](#).

IC § 6-2.5-5-4 extends the exemption to tools used to build exempt machinery and equipment.

Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for his direct use in the direct production of the machinery, tools, or equipment described in section 2 or 3 of this chapter.

To summarize, machinery, tools, and equipment purchased for direct use in the production of a manufactured good are subject to use tax unless the property used has an immediate effect on the good produced and is essential to the integrated process used to produce the marketable good.

[45 IAC 2.2-5-8\(d\)](#) states:

Pre-production and post-production activities. "Direct use 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 has altered the item to its completed form, including packaging, if required.

The Department's audit deemed certain of Taxpayer's processes as production processes and therefore exempt. For example, the Department's audit states that "torching, cutting, crushing, shredding, and granulating scrap is within the confines of processing scrap," and because these materials change the form of the raw materials and have an immediate effect on the scrap, they are exempt processes. However, the Department's audit is incorrect.

The Department's regulations emphasize that the tangible personal property that are the "raw materials" of a manufacturing/processing/refining process must be substantially changed in their "form, composition, or character" such that the resulting tangible personal property is a different product having a distinctive "name, character, and use." The resulting product must be substantially different from the component materials used.

[45 IAC 2.2-5-8\(k\)](#) states:

"Direct production, manufacture, fabrication, assembly, or finishing of tangible personal property" is performance as a business of an integrated series of operations which places tangible personal property in a form, composition, or character different from that in which it was acquired. The change in form, composition, or character must be a substantial change, and it must result in a transformation of property into a different product having a distinctive name, character, and use. Operations such as compounding, fabricating, or assembling are illustrative of the types of operations which may qualify under this definition.

[45 IAC 2.2-5-10\(k\)](#) states:

Definitions. Processing or refining is defined as the performance by a business of an integrated series of operations which places tangible personal property in a form, composition, or character different from that in which it was acquired. The change in form, composition, or character must be a substantial change. Operations such as distilling, brewing, pasteurizing, electroplating, galvanizing, anodizing, impregnating, cooking, heat treating, and slaughtering of animals for meal or meal products are illustrative of the types of operations which constitute processing or refining, although any operation which has such a result may be processing or refining. A processed or refined end product, however, must be substantially different from the component materials used.

Accordingly, the property must be directly used in the direct production, manufacture, fabrication, assembly, extraction, mining, processing, refining, or finishing of other tangible personal property in order to be exempt from

sales tax under either IC § 6-2.5-5-3 or IC § 6-2.5-5-1(b).

The Indiana Supreme Court has provided guidance on this issue in *Indiana Dep't of Revenue v. Interstate Warehousing, Inc.*, 783 N.E.2d 248 (Ind. 2003). The Indiana Supreme Court explained that the Indiana Tax Court had addressed the exemption in several prior cases. The court stated:

The common thread in all of these cases is that where the taxpayer did not transform property into a distinct marketable product for customer consumption, the Tax Court held that the taxpayer was not engaged in the "production of other tangible personal property." We agree with the Tax Court's analysis in those cases. *Id.* at 251.

As provided above by the court in *Interstate Warehousing*, any taxpayer claiming the exemption provided by IC § 6-2.5-5-1 must transform property into a "distinct marketable product for customer consumption" in order to qualify for the exemption. This requirement also applies to the exemption provided by IC § 6-2.5-5-3. The Indiana Tax Court has provided guidance when determining what constitutes manufacturing. In *Rotation Products Corp. v. Indiana Dep't of State Revenue*, 690 N.E.2d 795 (Ind. Tax Ct. 1998), that taxpayer claimed that it was remanufacturing ball bearings and was therefore eligible for the manufacturing exemption. The court explained:

Usually, a substantial amount of work will have to be performed to transform materials with only scrap value into serviceable and marketable products. In most cases, the substantial amount of work required will "result in an 'end product' that is 'substantially different from the component materials used.'" *Id.*, at 802.

In *Rotation Products*, the discussion focused on whether or not remanufacturing constituted manufacturing as used in the exemption statutes. While this protest concerns a recycling operation instead of a remanufacturing operation, a review of the court's reasoning is helpful. The court provided a four-part test to answer the question of how to determine if a taxpayer is in the business of manufacturing, as follows:

The case law reveals three factors germane to this fact-sensitive inquiry. The first is an adaptation of the requirement of a substantially different end product: the substantiality and complexity of the work done on the existing article and the physical changes to the existing article, including the addition of new parts. The other two factors derive from the observations of the courts dealing with this issue: a comparison of the article's value before and after the work, *MACROBUTTON HtmlResAnchor* and how favorably the performance of the remanufactured article compares with the performance of newly manufactured articles of its kind.

Additionally, this Court concludes that another factor is applicable to this inquiry: whether the work performed was contemplated as a normal part of the life cycle of the existing article. This additional factor will prevent work that merely perpetuates existing products from qualifying for an industrial exemption. *Id.*, at 802-3.

The first factor weighs the substantiality and complexity of the work done on the existing article, including the addition of new parts. In the instant case, Taxpayer does not add new parts to the articles; in most cases, Taxpayer merely separates and "repackages" the items. Taxpayer, at most, removes parts, separates items into groupings defined by their material composition, cleans items, and/or crushes items before bundling them into cubes-i.e., an all plastic cube or an all paper cube. The recyclable materials have no functionality as products, but only have value as the metals or other recyclable content. Taxpayer starts with scrap aluminum, copper, brass, steel, etc., and then ends with scrap aluminum, copper, brass, steel, etc. Taxpayer does not create a new product-i.e., such as a new alloyed metal. Thus, while Taxpayer's customers may prefer to purchase only in cubes or bundles and pay Taxpayer for the convenience of these services, Taxpayer has merely repackaged the existing recyclable material. The Tax Court addressed the issue of repacking in *North Cent. Indus., Inc., Co. v. Indiana Dep't of State Revenue*, 790 N.E.2d 198, 201 (Ind. Tax Ct. 2003) and explained that "merely packag[ing] existing [property]... is not the sort of substantial change or transformation that places property 'in a form, composition, or character different from that in which [they were] acquired.'" [45 IAC 2.2-5-8\(k\)](#)."

In the instant case, there is no new article produced. Taxpayer does not add new parts to the articles being disassembled, but instead removes parts and separates them into groupings defined by their material composition. The disassembled parts themselves have no value as parts. The only value is the metal or other recyclable content. The recyclable materials have no functionality and, after removal from the original article, have no value as parts. Since there is no new article produced, Taxpayer's activities do not pass the first factor of the *Rotation Products* test and review of the other factors is unnecessary. Therefore, under *Interstate Warehousing*, Taxpayer's activities do not qualify for the manufacturing exemption provided under IC § 6-2.5-5-3. Therefore, Taxpayer should have paid sales tax on the items at the time of purchase.

Since sales tax was not paid, use tax should have been imposed as a result of the Department's audit. The Department's audit incorrectly treated some of Taxpayer's processes as exempt. The Department's final determination does not reverse the audit on the items the audit treated as exempt. However, Taxpayer is forewarned that, going forward, its recycling processes are not exempt. Therefore, since Taxpayer's activities do not qualify for the manufacturing exemptions provided under IC § 6-2.5-5-3, the items protested under the issues 1, 2, 3, 4, 6, and 7 as enumerated in the "Statement of Facts" above also do not qualify for exemption from sales or use tax since they presume the existence of a manufacturing process.

As Letter of Findings 04-20090014.SLOF (December 17, 2010) states:

The Department does not disparage the rationale of Taxpayer's protest or seek to underestimate the value of Taxpayer's operations nor does it treat as insignificant the costs related to those operations. However, in asking the question of whether the Taxpayer's recycling process results in a "substantially different" product, the Department concludes that it does not; the various metals and other materials are essentially the same metals and materials at the beginning and at the end of the process. In answering the question of whether Taxpayer's recycling activity can be "strictly construed" as entitled to an exemption under IC § 6-2.5-5-3(b) the Department must likewise conclude that it does not. Taxpayer's protest de facto seeks by administrative review to broaden the statutory sales and use tax exemptions to include recycling equipment; the expansion of this exemption is a task more properly addressed by the General Assembly.

As *Mechanics Laundry & Supply, Inc. v. Indiana Dep't of State Revenue*, 650 N.E.2d 1223 (Ind. Tax Ct. 1995) states unequivocally in footnote 11 (reiterated a few years later in *Rotation Products*, 690 N.E.2d at 803 n. 15):

If the equipment exemption is to be broadened to include recycling, as perhaps it should be, such action must come from the Indiana General Assembly.
Mechanics Laundry at 1230.

FINDING

Taxpayer's protest under this section is respectfully denied.

II. Sales and Use Tax – "Wrapping Materials and Containers" Exemption.

DISCUSSION

Taxpayer argues that its purchase of certain seals and bolts that it used to seal rail cars are exempt from sales and use tax pursuant to the "packaging" exemption, IC § 6-2.5-5-9, because Taxpayer argues the rail cars are containers to which it adds the items it sells to its customers. Pursuant to the same exemption statute, Taxpayer also argues that its purchases of lumber to use in international shipping containers to keep the scrap from spilling out of the containers when inspected by customs officials are exempt. Lastly, Taxpayer argues that barrels it uses to fill with graded scrap to sell to customers are also exempt under IC § 6-2.5-5-9. Taxpayer states that it does not receive the barrels back from customers and therefore, Taxpayer argues, the barrels should be considered "nonreturnable containers."

IC § 6-2.5-5-9 states:

- (a) As used in this section, "returnable containers" means containers customarily returned by the buyer of the contents for reuse as containers.
- (b) Sales of returnable containers are exempt from the state gross retail tax if the transaction constitutes selling at retail as defined in [IC 6-2.5-4-1](#) and if the returnable containers contain contents.
- (c) Sales of returnable containers are exempt from the state gross retail tax if the containers are transferred empty for the purpose of refilling.
- (d) Sales of wrapping material and empty containers are exempt from the state gross retail tax if the person acquiring the material or containers acquires them for use as nonreturnable packages for selling the contents that he adds.

[45 IAC 2.2-5-16](#) elaborates the above statute:

- (a) The state gross retail tax shall not apply to sales of nonreturnable wrapping materials and empty containers to be used by the purchaser as enclosures or containers for selling contents to be added, and returnable containers containing contents sold in a sale constituting selling at retail and returnable containers sold empty for refilling.
- (b) In general the gross proceeds from the sale of tangible personal property in a transaction of a retail merchant constituting selling at retail are taxable. This regulation [[45 IAC 2.2](#)] provided an exemption for wrapping materials and containers.
- (c) General rule. The receipt from a sale by a retail merchant of the following types of tangible personal property are exempt from state gross retail tax:
 - (1) Nonreturnable containers and wrapping materials including steel strap and shipping pallets to be used by the purchaser as enclosures for selling tangible personal property.
 - (2) Deposits for returnable containers received as an incident to a transaction of a retail merchant constituting selling at retail.
 - (3) Returnable containers sold empty for refilling.
- (d) Application of general rule.
 - (1) Nonreturnable wrapping material and empty containers. To qualify for this exemption, nonreturnable wrapping materials and empty containers must be used by the purchaser in the following way:
 - (A) The purchaser must add contents to the containers purchased; and
 - (B) The purchaser must sell the contents added.
 - (2) Returnable containers sold at retail with contents. To qualify for this exemption, the returnable containers must be:
 - (A) Sold in a taxable transaction of a retail merchant constituting selling at retail; and
 - (B) Billed as a separate charge by the retail merchant to his customer. If there is a separate charge for

such containers, the sale of the container is exempt from tax under this regulation [45 IAC 2.2].

(3) Returnable containers sold empty. To qualify for this exemption the returnable container must be resold with the purpose of refilling. The sale of returnable containers to the original or first user thereof is taxable.

(e) Definitions.

(1) Returnable containers. As used in this regulation [45 IAC 2.2], the term returnable container means containers customarily returned by the buyer of the contents for reuse as containers.

(2) Nonreturnable containers. As used in this regulation [45 IAC 2.2], the term "nonreturnable containers" means all containers which are not returnable containers.

The Department's audit states that the seals and bolts are used to secure the container against theft and are actually returned to Taxpayer. The Taxpayer has not contested the fact that these items are returned to Taxpayer, therefore, under the statute and regulation above, the seals and bolts cannot be exempt.

The lumber used to prevent the materials placed in non-returnable containers from spilling out of the containers during international shipping customs inspections fall loosely within the "wrapping materials" category and are therefore exempt.

The non-returnable barrels are also exempt under the referenced statute and regulation.

Therefore, the lumber and barrels described in this section are exempt; but the seals and bolts are not.

FINDING

Taxpayer is sustained in part and denied in part - the lumber and barrels described in this section are exempt; but the seals and bolts are not.

III. Sales and Use Tax – Credits for Overpayment of Sales Tax.

DISCUSSION

Taxpayer protests certain items upon which the audit has assessed use tax. The invoices were not available during the audit, but Taxpayer presented them after the hearing. Exhibit II of Taxpayer's hearing documentation (titled [Taxpayer] Indiana Sales and Use Tax Audit Protest 2005 Through 2007) itemizes all Taxpayer's protest items and includes reference to the subject invoices. IC § 6-8.1-5-1(c).

A supplemental audit will review the invoices presented and assign credit to Taxpayer as appropriate.

FINDING

Taxpayer's protest is sustained pending the results of a supplemental audit.

IV. Sales and Use Tax – Retail Transactions.

DISCUSSION

Taxpayer protests that certain transactions it engaged in were not retail transactions and therefore not subject to sales or use tax. IC § 6-2.5-2-1. The Department's audit, relying on Sales Tax Information Bulletin 8 (May 2002), 25 Ind. Reg. 3934, assessed use tax on these transactions because they involved the transfer of tangible personal property in the form of reports. In other words, the distinction is made between the information per se and the format in which it is delivered.

IC § 6-2.5-2-1 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.

IC § 6-2.5-4-1 discusses what "selling at retail" means:

(a) A person is a retail merchant making a retail transaction when he engages in selling at retail.

(b) A person is engaged in selling at retail when, in the ordinary course of his regularly conducted trade or business, he:

(1) acquires tangible personal property for the purpose of resale; and

(2) transfers that property to another person for consideration.

(c) For purposes of determining what constitutes selling at retail, it does not matter whether:

(1) the property is transferred in the same form as when it was acquired;

(2) the property is transferred alone or in conjunction with other property or services; or

(3) the property is transferred conditionally or otherwise.

(d) Notwithstanding subsection (b), a person is not selling at retail if he is making a wholesale sale as described in section 2 of this chapter.

(e) The gross retail income received from selling at retail is only taxable under this article to the extent that the income represents:

(1) the price of the property transferred, without the rendition of any service; and

(2) except as provided in subsection (g), any bona fide charges which are made for preparation, fabrication, alteration, modification, finishing, completion, delivery, or other service performed in respect to the property transferred before its transfer and which are separately stated on the transferor's records.

For purposes of this subsection, a transfer is considered to have occurred after delivery of the property to the purchaser.

(f) Notwithstanding subsection (e):

(1) in the case of retail sales of gasoline (as defined in [IC 6-6-1.1-103](#)) and special fuel (as defined in [IC 6-6-2.5-22](#)), the gross retail income received from selling at retail is the total sales price of the gasoline or special fuel minus the part of that price attributable to tax imposed under [IC 6-6-1.1](#), [IC 6-6-2.5](#), or Section 4041(a) or Section 4081 of the Internal Revenue Code; and

(2) in the case of retail sales of cigarettes (as defined in [IC 6-7-1-2](#)), the gross retail income received from selling at retail is the total sales price of the cigarettes including the tax imposed under [IC 6-7-1](#).

(g) Gross retail income does not include income that represents charges for serving or delivering food and food ingredients furnished, prepared, or served for consumption at a location, or on equipment, provided by the retail merchant. However, the exclusion under this subsection only applies if the charges for the serving or delivery are stated separately from the price of the food and food ingredients when the purchaser pays the charges.

Specifically, Taxpayer argues that certain charges from Metalprices.com were for services and therefore the transactions do not qualify as retail transactions. Taxpayer asserts that the transactions with Metalprices.com are not subject to use tax because the "true object" of the transaction is the provision of service to which the transfer of tangible personal property is only incidental.

Sales Tax Information Bulletin 8 (May 2002) states in relevant part:

F. Sale of Miscellaneous Data:

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 makes several points in support of its protest. Taxpayer argues that the Department's reliance on the referenced information bulletin is misplaced because information bulletins are not given the force and effect of law, nor are they considered precedential. Taxpayer points out that the Department's own disclaimer on each bulletin makes it clear that the information is advisory in nature and may not reflect current law. Taxpayer is correct, however, unless and until Taxpayer succeeds in demonstrating that the Information Bulletin contradicts established law on this issue, its advisory nature is not challenged.

Furthermore, Taxpayer points out that the Information Bulletin language, referenced above, is the same language as the prior 1983 version which could not have contemplated transactions such as the one subject to protest here. However, the very language quoted above, "information produced or compiled by a computer and sold or reproduced for sale in substantially the same form as it is so produced," is exactly the case here.

Taxpayer insists that the issue is whether the transfer of information constitutes a retail transaction, and that the Department's position is not supported by any law in Indiana. Taxpayer points to *Cowden & Sons v. Indiana Dep't of Revenue*, 575 N.E.2d 718 (Ind. Tax Ct. 1991) in which the Tax Court held that the determination of whether a sale was a retail transaction turned on whether the "true object" of the transaction was service or property, and in *Cowden* the taxpayer was a hauler who only on occasion sold stone at cost to his customers as a convenience, therefore the Court concluded that the "true object" of the transaction was the provision of service and not the sale of stone. Taxpayer analogizes itself to *Cowden* by arguing that the "true object" of its transactions is the provision of information and not reports.

In *Cowden* a trucking company, having engaged in certain transactions in which it transported stone, was assessed sales tax on the value of the transportation services. Ninety-five percent of the taxpayer's customers were contractors that engaged *Cowden* exclusively for its hauling services and where the customers paid the quarries directly for the stone *Cowden* hauled. *Id.* at 719. The remaining 5 percent of *Cowden's* customers were non-contractors who did not have existing accounts with the quarries, as a result *Cowden* paid for the stone at the quarry, including sales tax, and the non-contractor customer reimbursed *Cowden*. *Id.* The Department argued that the service costs were taxable because *Cowden* had entered into a unitary transaction which included hauling services and the sale of stone. The court disagreed, finding that the sale of the stone was not inextricable and indivisible from the transportation services. The court stated that the issue should be resolved by discerning *Cowden's* intent and that evidence supported *Cowden's* "assertion that the acquisition of stone was for the convenience and accommodation of its customers, incidental to its hauling services and not for the purposes of resale." *Id.* at 721. The court found that the sale of the stone was one transaction and the provision of the services was a second, severable transaction and that the second transaction was not subject to the sales tax. *Id.* at 722. The court found relevant the fact *Cowden* did not maintain an inventory of stone to sell to its customers, did not advertise the sale of stone, and did not hold itself out as a stone merchant. *Id.* at 721. In addition, *Cowden* – because it merely charged its customers for the cost of the stone – had no profit motive in selling stone to its customers and that transfer of stone was entirely incidental to *Cowden's* provision of transportation services. *Id.* at 721-722.

Taxpayer relies on *Cowden* to support the proposition that services may be provided to a customer in which the transfer of tangible personal property is entirely incidental to the provision of the services. Taxpayer is correct. The court found that *Cowden* was in the business of providing transportation services. *Cowden* owned equipment for the provision of those services and did not maintain an inventory of stone. *Cowden* did not advertise for the

sale of stone and did not hold itself out as a stone merchant. Ninety-five percent of Cowden's customers sought out Cowden for its hauling services. On occasion, Cowden purchased stone on behalf of its customers "merely for the convenience of its... customers." *Id.* at 721.

However, the facts of this protested item are different. The provision of information in report format is a substantial component of MetalPrices.com business - unlike Cowden who only in very few cases actually transferred stone at cost. MetalPrices.com maintains an "inventory" of information - unlike Cowden which did not maintain an inventory of stone. MetalPrices.com's own website describes its mission as follows:

MetalPrices.com is a metal pricing utility. The service is specifically targeted to anyone responsible for tracking the raw material value of any metal product. Industries we serve are mills, foundries, service centers, fabricators, forge shops, machine shops, mining producers, scrap processors, traders, researchers, and the financial industry. Our primary function is to publish prompt, accurate metal prices in a useful format. (Emphasis added).

The information that MetalPrices.com provides and the format in which it provides it; i.e., the reports, are "inextricable and indivisible." The "true object" of MetalPrices.com's business is the provision of information to its customers in usable formats. The amount of information available even in Taxpayer's specialized business is mind-boggling, what makes the information usable to Taxpayer is the format – the reports - in which it is delivered.

FINDING

Taxpayer's protest is respectfully denied.

V. Tax Administration – Negligence Penalty.

DISCUSSION

The Department issued ten percent negligence penalties for the tax years in question. Taxpayer protests the imposition of the penalties. The Department refers to IC § 6-8.1-10-2.1(a)(3), which provides "if a person... 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.

The Department may waive a negligence penalty as provided in [45 IAC 15-11-2](#)(c), as follows:

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.

Taxpayer has met its burden of proof to show that the deficiencies they incurred are due to reasonable cause and are therefore not subject to a penalty under IC § 6-8.1-10-2.1(a).

FINDING

Taxpayer's protest is sustained.

SUMMARY

Taxpayer does not qualify for any of the manufacturing exemptions. (Issue I).

The lumber and barrels used as "wrapping materials" and "non-returnable containers" are exempt; but the seals and bolts are not. (Issue II).

A supplemental audit will review the invoices presented by Taxpayer at hearing to determine sufficiency for exemption. (Issue III).

Taxpayer's transactions with MetalPrices.com are subject to use tax. (Issue IV).

The ten-percent negligence penalty assessed against Taxpayer is waived. (Issue V).

Posted: 03/23/2011 by Legislative Services Agency
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