

Letter of Findings: 04-20100458
Gross Retail Tax
For 2006 and 2007

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ISSUES

I. Taxes Paid – Gross Retail Tax.

Authority: IC § 6-2.5-1-2; IC § 6-2.5-2-1(a); IC § 6-2.5-2-1(b); IC § 6-2.5-3-1(a); IC § 6-2.5-3-2(a); IC § 6-2.5-4-1(b)(c); IC § 6-8.1-5-1(c); USAir, Inc. v. Ind. Dep't of State Revenue, 623 N.E.2d 466 (Ind. Tax. Ct. 1993); Rhoades v. Ind. Dep't of State Revenue, 774 N.E.2d 1044 (Ind. Tax Ct. 2002).

Taxpayer argues that it was incorrectly assessed sales/use tax on items for which tax had previously been paid.

II. Fixed Asset Transfers – Gross Retail Tax.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-2(a); IC § 6-8.1-5-1(c).

Taxpayer states that the Department incorrectly assessed sales/use tax on "fixed asset transfers" when the documentation establishes that the item was simply moved from one location to another.

III. Exempt Transactions – Gross Retail Tax.

Authority: IC § 6-2.5-2-1(b); IC § 6-2.5-3-2(a); Sales Tax Information Bulletin 4 (May 2010).

Taxpayer claims that the Department incorrectly assessed sales/use tax on transactions it entered into with an exempt organization.

IV. Computer Services – Gross Retail Tax.

Authority: IC § 6-2.5-1-2; IC § 6-2.5-2-1(a); IC § 6-2.5-3-1(a); IC § 6-2.5-4-1(a); IC § 6-2.5-4-1(b); IC § 6-8.1-5-1(c).

Taxpayer argues that the Department incorrectly assessed sales/use tax on transactions which represented the cost of exempt services.

V. Ten-Percent Negligence 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)(2); IC § 6-8.1-10-2.1(d); [45 IAC 15-11-2\(b\)](#); [45 IAC 15-11-2\(c\)](#).

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

STATEMENT OF FACTS

Taxpayer is in the business of providing a range of computer services. Taxpayer is located outside Indiana but has business locations in Indiana. The Department of Revenue (Department) conducted an audit review of Taxpayer's business records and determined that Taxpayer owed additional sales/use tax. Taxpayer disagreed 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. Taxes Paid – Gross Retail Tax.

DISCUSSION

Taxpayer maintains that the Department's audit assessed tax on items for which tax had previously been paid.

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). A person who acquires property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. IC § 6-2.5-2-1(b).

Indiana also imposes a complementary excise tax called "the use tax" 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." IC § 6-2.5-3-2(a). Use means the "exercise of any right or power of ownership over tangible personal property." IC § 6-2.5-3-1(a). The use tax is functionally equivalent to the sales tax. See Rhoades v. Ind. Dep't of State Revenue, 774 N.E.2d 1044, 1047 (Ind. Tax Ct. 2002).

By complementing the sales tax, the use tax ensures that non-exempt retail transactions (particularly out-of-state retail transactions) that escape sales tax liability are nevertheless taxed. Rhoades, 774 N.E.2d at 1047; USAir, Inc. v. Ind. Dep't of State Revenue, 623 N.E.2d 466, 468–69 (Ind. Tax. Ct. 1993). The use tax ensures that, after such goods arrive in Indiana, the retail purchasers of the goods bear their fair share of the tax burden. To trigger imposition of Indiana's use tax, tangible personal property must (as a threshold matter) be acquired in a retail transaction. Id. A taxable retail transaction occurs when: a party acquires tangible personal property as part of its ordinary business for the purpose of reselling the property; that property is then exchanged between parties for consideration; and the property is used in Indiana. See IC § 6-2.5-1-2; IC § 6-2.5-4-1(b)(c); IC § 6-2.5-3-2(a).

Taxpayer provides computer service to its nation-wide roster of clients. During the course of providing those services, Taxpayer purchases items in the ordinary course of that business and either sells those items to its clients or uses the items itself.

However, Taxpayer states that the audit included as "taxable" certain items for which either sales tax was paid at the time the transaction originally occurred or that Taxpayer had self-assessed use tax.

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."

In this case, the Department is prepared to agree that Taxpayer has presented documentation that warrants review in order to assure that the original assessment is warranted for a particular item of equipment or for a particular transaction.

FINDING

Taxpayer's protest is sustained subject to audit verification.

II. Fixed Asset Transfers – Gross Retail Tax.

DISCUSSION

Taxpayer maintains that the audit assessed sales/use tax on "fixed asset transfers." According to Taxpayer, it records instances in which a particular asset is transferred from one particular location to another. On occasion, the move is one state to the next; on occasion, the move is from one Indiana location to another Indiana location.

IC § 6-2.5-2-1 imposes sales tax "on retail transactions made in Indiana" while use tax is imposed on "the storage, use, or consumption of tangible personal property in Indiana...." IC § 6-2.5-3-2(a). However, the Department is unable to agree that the transfer of a "fixed asset" from one location to another necessarily triggers either a sales or use tax liability when the consumer can establish that sales tax was paid at the time of the original transaction.

Taxpayer has met its burden under IC § 6-8.1-5-1(c) establishing that the particular account at issue should be reviewed and the original assessment adjusted as warranted.

FINDING

Taxpayer's protest is sustained subject to audit verification.

III. Exempt Transactions – Gross Retail Tax.

FINDING

Taxpayer argues that certain items it purchased are exempt because the items are attributable to a contract it has with an agency of the federal government.

The Department's position on the issue is set out in Sales Tax Information Bulletin 4 (May 2010), 20100526 Ind. Reg. 045100330NRA which states in part:

The United States Constitution prohibits any state from imposing any tax directly on the U.S. government or any of its agencies, unless the Congress consents to being taxed. Thus, much federal purchasing, leasing, and renting of tangible personal property; the use of utilities; meals consumed in restaurants; and other normally taxable goods or services (including accommodations for fewer than 30 days) are exempt from Indiana sales and other transaction-based taxes... A vendor is not required to collect sales tax on sales made directly to the U.S government if the exemption can be verified by documenting the facts and circumstances of the transaction. (Emphasis added).

Taxpayer is correct that when it enters into a leasing contract with the federal government or one of the federal government's agencies, it is not required to collect sales tax or self-assess use tax on items sold or leased to the government. However, the information provided by Taxpayer does not support Taxpayer's proposition that the items purchased were leased or sold to an agency of the federal government. Rather it appears simply that the items were purchased by Taxpayer and are related to the provision of services to the federal government. It appears that Taxpayer entered into a contact with an agency of the federal government for the provision of computer services and that Taxpayer purchased or leased items which it used to provide those services. If Taxpayer purchased computer cables which it then leased to the federal government, those cables are exempt. If Taxpayer purchased computer cables necessary for it to provide services to the government, those cables are subject to sales/use tax pursuant to IC § 6-2.5-2-1(b) or IC § 6-2.5-3-2(a).

FINDING

Taxpayer's protest is respectfully denied.

IV. Computer Services – Gross Retail Tax.

DISCUSSION

Taxpayer argues that the Department erred in assessing sales/use tax on transactions it entered into with its customers on the ground that the transactions involved computer services.

IC § 6-2.5-2-1(a) imposes sales tax on retail transactions made in Indiana. IC § 6-2.5-1-2 defines a retail transaction as "a transaction of a retail merchant that constitutes selling at retail as described in IC § 6-2.5-4-1... or that is described in any other section of IC § 6-2.5-4." IC § 6-2.5-4-1(a) provides that "[a] person is a retail merchant making a retail transaction when he engages in selling at retail." IC § 6-2.5-4-1(b) further explains that a

person sells at retail when he "(1) acquires tangible personal property for the purpose of resale; and (2) transfers that property to another person for consideration." (Emphasis added). Indiana's use tax provision mirror the sales tax provisions stating in IC § 6-2.5-3-1(a) that use means the "exercise of any right or power of ownership over tangible personal property."

A transaction subject to the state's sales tax necessarily involves the transfer of "tangible personal property." The state's use tax is triggered when a person exercises ownership over "tangible personal property."

Taxpayer has met its burden under IC § 6-8.1-5-1(c) of establishing that the certain of the subject transactions at issue may well have been for the provision of services and that the contract underlying those transactions gives evidence of that. The audit division is requested to review transactions and to make any adjustments it deems appropriate.

FINDING

Taxpayer's protest is sustained subject to audit verification.

V. Ten-Percent Negligence Penalty.

DISCUSSION

Taxpayer believes that it is entitled to abatement of the ten-percent negligence penalty. According to the "Audit Progress Report," the penalty was imposed because Taxpayer "did not provide a substantial amount of information that was requested to assure [t]he auditor that use tax was accrued or tax paid to the vendor." In addition, there were "a substantial number of recorded transactions in which no back up document or documentation or proof was made available to the auditor."

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)(2) 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.

The Department believes that taxpayer erred in determining its sales and use tax liability on a number of significant items. However, there is insufficient information to establish that Taxpayer's position was so egregious as to constitute "willful neglect." Based on a "case-by-case" analysis and after reviewing "the facts and circumstances of each taxpayer" the Department agrees that the ten-percent negligence penalty should be abated.

FINDING

Taxpayer's protest is sustained.

SUMMARY

Subject to audit verification, Taxpayer's protest challenging the assessment of sales/use tax on items for which tax had previously been paid is sustained; Taxpayer's protest challenging the assessment of sales/use tax on the transfer of fixed assets is sustained; Taxpayer's protest challenging the assessment of sales/use tax on transactions related to the provision of computer services is sustained; taxpayer's protest challenging the assessment of the ten-percent negligence penalty is sustained. In all other respects, Taxpayer's protest is denied.

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