

Letter of Findings: 04-20110326
Use Tax
For the Year 2008

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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 (2nd Cir. 1949); Horn v. Comm'r, 968 F.2d 1229 (D.C. Cir. 1992); Lee v. Comm'r, 155 F.3d 584 (2nd 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 - Penalty.

Authority: IC § 6-8.1-10-4; [45 IAC 15-11-4](#); [45 IAC 15-5-7](#).

Taxpayer protests the imposition of penalty.

STATEMENT OF FACTS

Taxpayer is a resident of Indiana. The Indiana Department of Revenue ("Department") determined that on February 13, 2008, Taxpayer purchased a recreational vehicle ("RV") in Florida 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, one hundred (100) percent fraud penalty, and interest. Taxpayer protests that the RV was titled by a Montana LLC, that the RV mostly remained outside of Indiana, and that no Indiana use tax is due. An administrative hearing was conducted and this Letter of Findings results. Further facts will be provided as required.

I. Use Tax—Recreational Vehicle.

DISCUSSION

Taxpayer protests the imposition of use tax on the use and storage of the 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 all legal documents establishing the existence of the LLC were properly filed in Montana. 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 purchased the RV in Florida in a retail transaction on February 13, 2008, and as a resident of Indiana, stored or used the RV in Indiana but did not pay sales tax anywhere. The Department therefore issued proposed assessments for use tax.

Taxpayer states that the Montana LLC's legal documents were properly filed by a Montana attorney. Furthermore, Taxpayer argues that the RV is neither permanently located, nor stored in Indiana. Taxpayer states that the RV remained in Indiana only for a month. Taxpayer also states that the RV is used by members and customers of his LLC for business and recreation purposes.

As provided by Article III of the LLC's Articles of Organization (dated February 8, 2008):

This LLC is formed to acquire, by purchase, lease or otherwise, any real and/or personal property, to maintain such ownership and to manage such real and/or personal property and to dispose of it, in any manner.

Also, the RV sales invoice and its insurance document establish that the address Taxpayer uses is the same as Taxpayer's Indiana residential address. Furthermore, Taxpayer created the LLC on February 8, 2008, at approximately the same time he purchased the RV on February 13, 2008.

There are no LLC documents establishing any business activity in Indiana, Montana, or any other state. Although Taxpayer provided a RV lease agreement of its Montana LLC, the agreement lacks any signatures. Taxpayer also failed to provide any evidence of his alleged lease activity and lease payment, other than the declaration page that showed a payment to the RV's lien holder, signed by himself as a lessee and his wife as a lessor. Plainly, the LLC was not pursuing a business purpose. The sole activity of the Montana LLC was to hold title to the RV.

While the Montana LLC made no attempt to undertake any business activity, the titling of the RV by the LLC did have a significant impact on Taxpayer's sales taxes. 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 (2nd 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 (2nd Cir. 1998).

In this case, the facts are that the officially stated purpose of the LLC's formation was to purchase and own the RV, the Montana LLC neither had business functions, nor attempted to conduct any business 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."

Since Taxpayer is an Indiana resident and purchased the RV, Taxpayer should have paid sales tax or use tax. The RV's travel logs Taxpayer provided clearly shows that the RV has been used in Indiana. Taxpayer also failed to provide any invoices or receipts that show the RV's camp ground use in other states.

In conclusion, the formation of the LLC and the titling of the RV by the LLC was a sham transaction. Taxpayer acquired tangible personal property in a retail transaction, used and stored it in Indiana, 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](#).

FINDING

Taxpayer's protest is respectfully denied.

II. Tax Administration - Penalty.

DISCUSSION

Taxpayer also protested the imposition of the fraud penalty.

The fraud penalty is imposed under IC § 6-8.1-10-4, which states:

- (a) If a person fails to file a return or to make a full tax payment with that return with the fraudulent intent of evading the tax, the person is subject to a penalty.
- (b) The amount of the penalty imposed for a fraudulent failure described in subsection (a) is one hundred percent (100[percent]) multiplied by:
 - (1) the full amount of the tax, if the person failed to file a return; or
 - (2) the amount of the tax that is not paid, if the person failed to pay the full amount of the tax.
- (c) In addition to the civil penalty imposed under this section, a person who knowingly fails to file a return with the department or fails to pay the tax due under [IC 6-6-5](#) or [IC 6-6-5.5](#) commits a Class A misdemeanor.
- (d) The penalty imposed under this section is imposed in place of and not in addition to the penalty imposed under section 2.1 of this chapter.

(Emphasis added).

Pursuant to [45 IAC 15-11-4](#):

The penalty for failure to file a return or to make full payment with that return with the fraudulent intent of evading the tax is one hundred percent (100 [percent]) of the tax owing. Fraudulent intent encompasses the making of a misrepresentation of a material fact (See [45 IAC 15-5-7\(f\)\(3\)](#)) which is known (See [45 IAC 15-5-](#)

(f)(3)(B)) to be false, or believed not to be true, in order to evade taxes. Negligence, whether slight or great, is not equivalent to the intent required. An act is fraudulent if it is an actual, intentional wrongdoing, and the intent required is the specific purpose of evading tax believed to be owing.

(Emphasis added).

The fraud penalty is further explained by [45 IAC 15-5-7\(f\)\(3\)](#), which states:

A person who files a return which makes a false representation(s) with knowledge or reckless ignorance of the falsity will be deemed to have filed a fraudulent return. There are five elements to fraud.

(A) Misrepresentation of a material fact: A person must truthfully and correctly report all information required by the Indiana Code and the department's regulations. Any failure to correctly report such information is a misrepresentation of a material fact. Failure to file a return may be a misrepresentation.

(B) Scienter: This is a legal term meaning guilty knowledge or previous knowledge of a state of facts, such as evasion of tax, which it was a person's duty to guard against. A person must have actual knowledge of the responsibility of reporting the information under contention. However, the reckless making of statements without regard to their truth or falsity may serve as an imputation of scienter for purpose of proving fraud.

(C) Deception: Deception operates on the mind of the victim of the fraud. If a person's actions or failure to act causes the department to believe a given set of facts which are not true, the person has deceived the department.

(D) Reliance: Reliance also concerns the state of mind of the victim and is generally considered along with deception. If the person's actions, failure to act, or misrepresentations cause the department to rely on these acts to the detriment or injury of the department, the reliance requirement of fraud will be met.

(E) Injury: The fraud instituted upon the department must cause an injury. This can be satisfied simply by the fact that the misrepresentation(s) caused the department not to have collected the money which properly belongs to the state of Indiana.

In order to demonstrate fraud, the department is required to prove all of the above elements are present.

This must be shown by clear and convincing evidence.

(Emphasis added.)

A review of the information in the protest file establishes that Taxpayer has not met those statutory requirements of fraud. Accordingly, the fraud penalty imposed under IC § 6-8.1-10-4 is unwarranted.

FINDING

Taxpayer's protest is sustained.

CONCLUSION

While Taxpayer's protest of the use tax assessment is denied, Taxpayer's protest of the penalty is sustained.

Posted: 01/25/2012 by Legislative Services Agency

An [html](#) version of this document.