DEPARTMENT OF STATE REVENUE

04-20140523.LOF

Letter of Findings: 04-20140523
Gross Retail Tax
For the Years 2011, 2012, and 2013

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.

ISSUE

I. Gross Retail Tax - Out-of-State Vehicle Sales.

Authority: IC § 6-2.5-2-1(a); IC § 6-2.5-2-1(b); IC § 6-2.5-5-15 (Repealed July 1, 2004); IC § 6-8.1-5-1(c); IC § 6-2.5-9-3; IC § 34-37-1-7; Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Jordan v. Deery, 609 N.E.2d 1104 (Ind. 1993); Wendt LLP v. Indiana Dep't of State Revenue, 977 N.E.2d 480 (Ind. Tax Ct. 2012); Scopelite v. Indiana Dep't of Local Gov't Fin., 939 N.E.2d 1138 (Ind. Tax Ct. 2010); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); 45 IAC 2.2-6-8; Commissioner's Directive 25 (July 2004); Sales Tax Information Bulletin 28S (April 2012); Sales Tax Information Bulletin 28S (October 2011); Sales Tax Information Bulletin 28S (December 2009); Sales Tax Information Bulletin 28 (July 2004).

Taxpayer maintains it was not required to collect sales tax on sales of motor vehicles which it sold to out-of-state customers because the audit's "error rate" analysis was flawed.

STATEMENT OF FACTS

Taxpayer is an Indiana company in the business of selling new and used, premium-priced vehicles. Taxpayer also operates a service and parts department.

The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayer's business records and tax returns. The audit resulted in an assessment of additional sales/use tax.

Taxpayer disagreed with the assessment and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representative explained the basis for the protest. This Letter of Findings results.

I. Gross Retail Tax - Out-of-State Vehicle Sales.

DISCUSSION

The issue is whether the Department was correct in relying on a statistical sample to assess additional sales tax on Taxpayer's sales of vehicles to its out-of-state customers.

The Department's audit reviewed "dealer jackets" for vehicle sales which occurred during 2011, 2012, and 2013. The sales records indicated that Taxpayer "had over a hundred nonresident customers who purchased vehicles exempt in Indiana."

The audit explained that each dealer jacket "contained an affidavit signed by the customer which stated the vehicle was delivered at an out of state location."

In order to verify the validity of the signed affidavits, the Department sent 170 letters to out-of-state customers requesting confirmation of the delivery location. The Department received 86 customer responses with 34 of the customers - under penalty of perjury - stating that "they picked the vehicle up at the dealership in Indiana."

The audit calculated an "error rate" as follows:

> An error rate concerning the claimed out-of-state delivery was calculated for each year with the numerator being the taxable amount of sales (sales less trade) where the customer responded that delivery of the

vehicle took place at the car dealership in Indiana; and the denominator being the total taxable amount of sales on all customer responses to the letters.

The error rate "was then applied to the total taxable sales amount for the remaining taxable sales to nonresident customer sales on which letters were sent and no response was received."

As authority for its decision assessing additional tax, the audit cited to 45 IAC 2.2-6-8 which provides as follows:

> (a) In determining the retail merchants' tax liability for a particular reporting period, the retail merchant shall multiply the retail merchant's total gross retail income from taxable transactions made during the reporting period except as otherwise provided in IC 6-2.5-5-7 or in this chapter of Regulations [45 IAC 2.2-6], by the sales tax rate.
> (b) The amount determined under this Regulation [45 IAC 2.2] is the retail merchant's state gross retail and use tax liability regardless of the amount of tax he actually collects.

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 retail merchant - such as Taxpayer - is required to "collect the tax as agent for the state." IC § 6-2.5-2-1(b). The retail merchant "holds those taxes in trust for the state and is personally liable for the payment of those taxes . . . ." IC § 6-2.5-9-3.

IC § 6-2.5-5-15 (Repealed July 1, 2004) originally exempted sales of vehicles to out-of-state customers. The Department issued Commissioner's Directive 25 (July 2004), 27 Ind. Reg. 3381, and Sales Tax Information Bulletin 28 (July 2004), 27 Ind. Reg. 3387, to address the change in law. Commissioner's Directive 25 stated that the repeal of IC § 6-2.5-5-15 "only affect[ed] situations where the purchaser [took] possession of the vehicle prior to taking the vehicle out of state." The Directive stated that:

> [The] repeal does not affect out of state sales by Indiana dealers. For a sale of a vehicle to be considered out of state, the purchaser must take possession via delivery outside of Indiana. No exemption certificate is required when making an out of state sale. However, the sales contract must specify that the vehicle is to be delivered out of state and the dealer must maintain shipping documentation to verify that the vehicle was delivered to the purchaser at a specific out of state location.

Sales Tax Information Bulletin 28S (April 2012), 20120530 Ind. Reg. 045120259NRA, provides as follows:

> A vehicle or trailer sold in **interstate commerce** is not subject to the Indiana sales tax. To qualify as being "sold in interstate commerce," the vehicle or trailer **must be physically delivered, by the selling dealer to a delivery point outside Indiana.** The delivery may be made by the dealer, or the dealer may hire a third-party carrier. Terms and the method of delivery must be indicated on the sales invoice. The dealer must document terms of delivery and must keep a copy of such terms of delivery to substantiate the interstate sale. The exemption does not apply to sales to out-of-state buyers in which the buyer takes physical possession of a vehicle or trailer in Indiana, nor is the exemption valid if the buyer, and not the seller, hires a third-party carrier to transport the vehicle or trailer outside Indiana. If the buyer hires the carrier, the carrier is acting as an agent for the buyer; thus, the buyer takes physical possession within Indiana. Possession taken within the state does not qualify as an interstate sale. (**Emphasis in original.**) See also Sales Tax Information Bulletin 28S (October 2011), 20110928 Ind. Reg. 045110549NRA; Sales Tax Information Bulletin 28S (December 2009), 20100127 Ind. Reg. 045100029NRA.

Taxpayer objects to the Department's methodology challenging the calculation and application of the error rate. To that end, Taxpayer sought the services of an out-of-state business which prepared a three-page "Analysis of Indiana Department of Revenue Statistical Methodology" ("Analysis"). The Analysis purports to support Taxpayer's argument that the audit's statistical analysis was faulty. As explained in the Taxpayer's Analysis:

> The [audit] sample is aggregated incorrectly.
> Implicit assumptions about non-respondents are incorrect.
> Inferences made across time periods are improper.

The Analysis explains that there was a large "variation in calculated error rates between years and makes." Taxpayer objects; "By projecting an error rate from 2012 onto other years, the Department incorrectly assumed that both consumer and dealership habits remained constant from year to year." In addition, the Analysis states that there was a "wide variation in response rates" from 2012 to 2013. (The Analysis makes no mention of the 2011 response rates).

In addition, the Analysis criticized the audit's finding based upon a "sensitivity analysis."

> The large variation seen in the sensitivity analysis exhibits the problems that arise by the Department making assumptions about the error rate of non-respondents, and how drastically they can affect the calculated amount of tax due by [Taxpayer] . . . . [T]he relatively high rate of non-response could easily sway the Department's analysis because of the sample size.

As a result, the analysis concludes that "the Department's estimates of tax due are clearly wrong."

In addition to objecting to the audit's projection, Taxpayer states that the 170 letters sent to Taxpayer's out-of-state customers prejudiced the results because the letters were intimidating and caused the 86 respondents to provide incorrect responses. However, Taxpayer's argument that the out-of-state customers were confused or unsettled by the audit letter is speculative. A review of the letter reveals nothing prejudicial or intimidating in either the contents or tone of the letter. Taxpayer also argues that the person who signed and returned the letter may not have been aware of nor had actual knowledge of the circumstances surrounding the original vehicle transaction. Again, Taxpayer speculates but it is reasonable to assume that the purchase of a car represents a major investment and commitment by the purchaser. Parties making such a purchase are unlikely to be only dimly aware of the circumstances surrounding that purchase. "Did I take delivery of my new car at the dealer or did the dealer deliver that car across state lines to my front door?" is a question a customer might reasonably be expected to answer with a substantial degree of certainty and reliability.

In considering Taxpayer's objection to the audit's "error rate" analysis, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect and that the results of the audit should be discarded. 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." Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007). Thus, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Poorly developed and non-cogent arguments are subject to waiver. Scopelite v. Indiana Dep't of Local Gov't Fin., 939 N.E.2d 1138, 1145 (Ind. Tax Ct. 2010); Wendt LLP v. Indiana Dep't of State Revenue, 977 N.E.2d 480, 486 n.9 (Ind. Tax Ct. 2012).

Taxpayer impliedly relies on the reliability of the customer affidavits contained within its dealer jackets. Indiana law sets out the requirements necessary to determine that reliability. An affidavit is defined as a "written state of fact which is sworn to as the truth before an authorized officer." Jordan v. Deery, 609 N.E.2d 1104, 1110 (Ind. 1993).

IC § 34-37-1-7 sets out the requirements when an affidavit is prepared in an out-of-state location.

> When an affidavit taken in another state is:
> (1) certified by the officer or justice of the peace taking the affidavit, under the:
> (A) hand of the officer or justice of the peace; and
> (B) seal of office, if the officer or justice of the peace has a seal; and
> (2) attested by the clerk of the:
> (A) circuit or district court; or
> (B) court of common pleas;
> of the county where the officer exercises the duties of office, under the hand of the clerk and seal of the court; and the clerk certifies that the officer or justice of the peace is, by the laws of the other state, duly empowered to administer oaths and affirmations and to take affidavits, the affidavit is sufficiently authenticated and may be received and used in any Indiana court.

Taxpayer asks the Department to reject the results of the audit, revoke the proposed assessment, and direct a second audit of Taxpayer's business records and tax returns. Taxpayer does not explain what the results of this second audit would or should be.

The Department does not agree that Taxpayer has established that the 170 audit letters were inherently flawed or prejudicial. The letter is straightforward and matter-of-fact. There is nothing to suggest that the customer responses - signed under penalty of perjury - were affected by either the tone or substance of the audit letter.

Taxpayer suggests that the error rate is flawed because the underlying analysis does not take into consideration variations in customer or dealership habits from year-to-year or month-to-month. Taxpayer's customers may indeed have purchased more expensive cars one year and less expensive cars the next. Similarly, Taxpayer may have sold more cars in June than in February, but whether or not those variances would or should have affected the assessment is not made clear in Taxpayer's "Analysis." Taxpayer's objections are no more than speculation. Given the potential variance in sales from year-to-year and from vehicle-to-vehicle, the audit's error rate could just as well have been too low rather than - as Taxpayer suggests - too high and is simply no basis upon which to conclude that the audit's results should be discarded.

The Department is unable to agree that Taxpayer has met its burden under IC § 6-8.1-5-1(c) of establishing that the audit's error rate calculation is "wrong" or that any purported flaws in the audit's methodology are sufficient to justify a second audit review.

FINDING

Taxpayer's protest is respectfully denied.

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