DEPARTMENT OF STATE REVENUE

04-20140646.LOF

Letter of Findings Number: 04-20140646
Sales Tax
For Tax Periods 01/01/2005 through 09/30/2013

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Retail merchant was required to collect sales tax on retail unitary transactions. Retail merchant was also liable for fraud penalty.

ISSUES

I. Sales Tax - Imposition.

Authority: IC § 6-2.5-1-1; IC § 6-2.5-1-2; IC § 6-2.5-2-1; IC § 6-2.5-4-1; IC § 6-8.1-5-1; IC § 6-8.1-5-4; IC § 6-2.5-9-3; Indiana Dep't. of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Scopelite v. Indiana Dep't of Local Gov't Fin., 939 N.E.2d 1138 (Ind. Tax Ct. 2010); Wendt LLP v. Indiana Dep't of State Revenue, 977 N.E.2d 480 (Ind. Tax Ct. 2012); 45 IAC 2.2-4-2.

Taxpayer protests the Department's proposed assessments on certain retail sales, claiming that it was not liable for collecting and remitting sales tax on the materials it used in performing maintenance/repair heating and air conditioning system.

II. Tax Administration - Fraud Penalty.

Authority: IC § 6-8.1-5-1; IC § 6-8.1-10-4; Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Scopelite v. Indiana Dep't of Local Gov't Fin., 939 N.E.2d 1138 (Ind. Tax Ct. 2010); Wendt LLP v. Indiana Dep't of State Revenue, 977 N.E.2d 480 (Ind. Tax Ct. 2012); 45 IAC 15-5-7; 45 IAC 15-11-4.

Taxpayer challenges the imposition of a 100 percent fraud penalty.

STATEMENT OF FACTS

Taxpayer, an Indiana S corporation, was in the business of installing, maintaining, and repairing heating and air conditioning system ("HVAC"). In early 2005, Taxpayer was audited for 2003 and 2004 tax years ("2005 Audit"). In the 2005 Audit, the Indiana Department of Revenue ("Department") determined that Taxpayer performed HVAC maintenance/repair services and charged its customers on one price for both materials and service(s). The charge included the materials with mark-ups. The 2005 Audit concluded that Taxpayer is a retail merchant and should have collected sales tax on the retail transactions involving the materials sold. The 2005 Audit notified Taxpayer that it was required to file the sales tax returns, ST-103 forms, and remit the sales tax. The 2005 Audit also allowed a credit of sales tax which Taxpayer had paid when it purchased the materials. Taxpayer filed one sales tax return, reporting zero sales tax initially after the 2005 Audit; it stopped filing its sales tax returns afterwards. September 30, 2013, Taxpayer ceased doing business.

In 2014, the Department conducted a sales/use tax audit for 2005 through 2013 tax years ("2014 Audit"). Similar to the 2005 Audit findings, the 2014 Audit found that Taxpayer charged its customer(s) one price when it performed both HVAC maintenance/repair services, but it did not collect sales tax on those transaction(s). The 2014 Audit also found that Taxpayer failed to maintain adequate records and failed to properly and timely file the required ST-103 returns for tax years 2005 through September 30, 2013. Based on the best information available at the time of the audit, the Department imposed additional sales tax for the tax years at issue using the same methodology employed in the 2005 Audit. The 2014 Audit further imposed a 100 percent penalty because

Taxpayer knowingly chose not to comply with the Indiana law.

Taxpayer protested the assessment, claiming that it was not liable for the assessment of sales tax and 100 percent penalty. An administrative hearing was held. Taxpayer requested additional time to submit supporting documents, which were scanned copies of sales invoices. This Letter of Findings ensues. Additional facts will be provided as necessary.

I. Sales Tax - Imposition.

DISCUSSION

The 2014 Audit determined that Taxpayer failed to collect and remit sales tax in connection with the HVAC maintenance/repair services, which Taxpayer charged one price for both and therefore were taxable retail unitary transactions. Taxpayer argues that it was not responsible for collecting sales tax because it paid sales tax at the time when it acquired the materials from its suppliers. Taxpayer, referencing its "Item Price List," claimed that it charged "$55" for "Replac[ing] standard oil filter" for example. Taxpayer argued that it was not responsible for collecting the sales tax on the $55 because it had paid sales tax on the "oil filter" at the time of its purchase of that oil filter.

As a threshold issue, all tax assessments are prima facie evidence that the Department's claim for the unpaid tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007); Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012). Thus, the taxpayer is required to provide documentation explaining and supporting its challenge that the Department's assessment 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).

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 "purchaser") is liable for the sales tax on the transaction. IC § 6-2.5-2-1(b). The purchaser in general "shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction." Id. "The retail merchant shall collect the tax as agent for the state." Id. If the retail merchant fails to do so, the retail merchant "is personally liable for the payment of those taxes, plus any penalties and interest attributable to those taxes, to the state." IC § 6-2.5-9-3.

"Retail transaction" is "a transaction of a retail merchant that constitutes selling at retail as described in IC 6-2.5-4-1 . . . or . . . in any other section of IC 6-2.5-4." IC § 6-2.5-1-2(a).

IC § 6-2.5-4-1 (as in effect for tax years at issue), in relevant part, provides:

> (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.
> . . .
> (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) . . . 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.

"Retail unitary transaction" is "a unitary transaction that is also a retail transaction." IC § 6-2.5-1-2(b). " '[U]nitary transaction' includes all items of personal property and services which are furnished under a single order or

agreement and for which a total combined charge or price is calculated." IC § 6-2.5-1-1(a). 45 IAC 2.2-4-2(a) explains that services generally are not subject to sales/use tax. However, "in conjunction with rendering . . . services, the serviceman also transfers tangible personal property for a consideration, this will constitute a transaction of a retail merchant constituting selling at retail" Id. 45 IAC 2.2-4-2(a) affords an exception which all of the following conditions must be met:

> (1) The serviceman is in an occupation which primarily furnishes and sells services, as distinguished from tangible personal property;
> (2) The tangible personal property purchased is used or consumed as a necessary incident to the service;
> (3) The price charged for tangible personal property is inconsequential (not to exceed 10[percent]) compared with the service charge; and
> (4) The serviceman pays gross retail tax or use tax upon the tangible personal property at the time of acquisition.

Therefore, a taxpayer who is occupationally engaged in providing services is presumed to be a retail merchant selling at retail with respect to any tangible personal property sold in the course of rendering such services, unless the taxpayer can demonstrate that the transaction satisfies the above four (4) requirements. 45 IAC 2.2-4-2(d); see also IC § 6-2.5-4-1(c). In the event that the taxpayer enters a retail unitary transaction–i.e., one price for both material(s) and service(s)– the taxpayer is required to collect and remit the sales tax on the total combined or price. If the taxpayer fails to do so, the taxpayer is liable for the tax, plus penalty and interest.

During the protest process, Taxpayer argued that it was not responsible for collecting sales tax because it paid sales tax at the time when it acquired the materials from its suppliers. Taxpayer offered scanned copies of its invoices to support its protest.

Upon review the documentation submitted, however, Taxpayer's reliance on its invoices is mistaken. First, Taxpayer provided some but not all copies of invoices. Upon responding to customer's service calls, Taxpayer sent its technicians to conduct an in-person examination of the HVAC in question and to diagnose problems, if any. Thereafter, Taxpayer's technicians then manually completed the pre-printed and pre-numbered invoices supplying information needed regarding the materials needed and/or services rendered. However, some invoices were missing and the scanned invoices were not sequential. In the absence of the complete source documents, Taxpayer failed to meet its burden.

Second, Taxpayer's invoices demonstrated that it charged one price for both material(s) used and maintenance/repair service(s) rendered; the charge thus is a retail unitary transaction subject to Indiana sales tax. In the example that Taxpayer charged "$55" for "[r]eplac[ing] standard oil filter," it must collect and remit the sales tax on the $55. Taxpayer failed to do so. Thus, Taxpayer is liable for the sales tax on the $55. Specifically, the 2014 Audit noted that since Taxpayer has "paid sales tax on the cost of repair parts and materials at the point of purchase, additional sales tax is being assessed on the difference between the cost of the parts and materials, and the retail charges to the customers." The 2014 Audit found that Taxpayer failed to maintain adequate records and source documents mandated by IC § 6-8.1-5-4(a). The 2014 Audit thus employed the methodology used in the 2005 Audit pursuant to IC § 6-8.1-5-1(b), and adopted the agreed average mark-up of ninety percent on the parts and materials used. Taxpayer did not provide source documentation to address his protest of the audit methodology.

Thus, given the totality of the circumstances, in the absence of other supporting documentation, the Department is not able to agree that Taxpayer met its burden of proof to demonstrate the proposed assessment is wrong.

FINDING

Taxpayer's protest is respectfully denied.

II. Tax Administration - Fraud Penalty.

DISCUSSION

Taxpayer maintains that the Department erroneously imposed the fraud penalty.

Again, as a threshold issue, all tax assessments are prima facie evidence that the Department's claim for the unpaid tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007);

Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012). Thus, the taxpayer is required to provide documentation explaining and supporting its challenge that the Department's assessment 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).

The fraud penalty is found at 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, IC [§] 6-6-5.1, 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.

45 IAC 15-11-4 further illustrates:

> 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 15-5-7(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.

Additionally, 45 IAC 15-5-7(f)(3) 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**).

In this instance, Taxpayer simply claimed that it paid sales tax at the time when it purchased the materials and parts. It did not provide documents to support its protest of the penalty.

The 2014 Audit imposed the fraud penalty because Taxpayer was audited previously on the exactly same issue(s). The 2014 Audit found that Taxpayer failed to comply with the Indiana law even after Taxpayer's 2005 Audit and Taxpayer was on notice of its violation. Specifically, the 2014 Audit found that Taxpayer failed to maintain adequate records and source documents as statutorily required and did not properly and timely file sales tax returns after the 2005 Audit. Given the totality of the circumstances, in the absence of other supporting documentation, the Department is not able to agree that the fraud penalty should be abated.

FINDING

Taxpayer's protest of the fraud penalty is denied.

SUMMARY

Taxpayer's protest of the imposition of additional sales tax is respectfully denied. Taxpayer's protest of the imposition of the fraud penalty is also respectfully denied.

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