

**Letter of Findings: 04-20150054**  
**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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. 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

Indiana Jewelry Retailer failed to meet its burden of establishing that it sold jewelry items at its Indiana retail location, that it shipped the jewelry to its customers' out-of-state locations, and that it was not individually responsible for paying the uncollected tax.

### ISSUE

#### **I. Gross Retail Tax - Out-of-State Jewelry Sales.**

**Authority:** IC § 6-2.5-2-1(a); IC § 6-2.5-2-1(b); IC § 6-2.5-9-3; IC § 6-8.1-5-1(c); IC § 6-8.1-5-4(a); IC § 6-8.1-5-4(c); Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579 (Ind. 2014); 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).

Taxpayer argues that it sold jewelry to customers, that the jewelry was delivered to the customers' out-of-state locations, and that it was not required to collect Indiana sales tax on those transactions.

### STATEMENT OF FACTS

Taxpayer is an Indiana retailer in the business of selling and repairing jewelry. Taxpayer sells jewelry that was purchased by Taxpayer for resale as well as custom-made jewelry items which were designed and manufactured by Taxpayer. Taxpayer conducts its business from its Indiana retail location and also sells jewelry through the Internet.

The Indiana Department of Revenue ("Department") conducted a sales and use tax audit of Taxpayer's business records. The audit concluded that Taxpayer failed to collect sales tax on certain transactions with its customers and assessed Taxpayer additional tax.

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

#### **I. Gross Retail Tax - Out-of-State Jewelry Sales.**

### DISCUSSION

The issue is whether Taxpayer has provided sufficient documentary evidence to establish that it sold jewelry to out-of-state customers, that the jewelry was delivered to the customers' out-of-state locations, that Taxpayer was not required to collect sales tax from these customers, and that the audit erred in assessing Taxpayer the additional 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." 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). Consequently, a taxpayer is required to provide documentation explaining

and supporting his or her challenge that the Department's position is wrong. Further, "[W]hen [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] defer to the agency's reasonable interpretation of [the] statute even over an equally reasonable interpretation by another party.'" Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579, 583 (Ind. 2014). Thus, interpretations of Indiana tax law contained within this decision, as well as the preceding audit, are entitled to deference.

#### **A. Audit Results.**

The audit found that Taxpayer's annual sales during the three-year audit period were approximately \$2.1 million, that income from providing repair services constituted approximately six percent of its sales and that income from designing and manufacturing custom jewelry constituted approximately fourteen percent of its sales. The bulk of Taxpayer's retail sales were conducted at its Indiana retail location.

The audit reviewed Taxpayer's sales invoices particularly invoices which contained an out-of-state customer address. As explained in the audit report, "The sales invoices do not include both a bill to and ship to address, but rather include only one address." The audit found that approximately sixty-five percent of Taxpayer's total revenue was derived from sales invoices that contained an out-of-state address. The audit report states:

Examination of various sales records for [out-of-state] invoices found that a significant portion of these sales were made and paid for in full or in part at Taxpayer's retail location; however, the items are reported to be shipped out of state as evidenced by the address on the sales invoice. No documents have been provided to explain the reasoning for shipping items out of state when a customer was in the store to purchase the item.

The audit questioned whether the purchased jewelry was shipped to customers' out-of-state locations. The audit report explained that "Taxpayer stated customers routinely request their purchases be shipped to locations outside of Indiana, which in many cases were reported to be other residences of the customers. Taxpayer made its determination as to whether a product would be taxed based solely on where the property was shipped."

The audit based its conclusion that Taxpayer should have collected sales tax on the purported out-of-state sales for the following reasons:

- Numerous sales were to customers who had either an Indiana residence or who operated a local business;
- Sales were made to customers who listed a phone number with a local area code;
- Sales were made to customers which public records established had a Indiana address;
- Taxpayer's shipping documents "were incomplete in that they did not provide documentation indicating receipt, or even actual shipment of the property;"
- Taxpayer purportedly shipped jewelry valued at "tens of thousands, even hundreds of thousands of dollars" for which no recipient signature was required;
- Taxpayer's shipping methods "did not comply with specified terms of Taxpayer's insurance policy" protecting Taxpayer from risk-of-loss during shipping;
- "[M]any of the shipping labels provided included Taxpayer's phone number as both the phone number for both the sender and recipient;"
- In reviewing Taxpayer's USPS shipping labels, the audit found that "virtually none of the tracking numbers could be tracked or identified as the USPS.com website;"
- In reviewing Taxpayer's FedEx shipping labels, the audit found that approximately one half of the labels were generated and cancelled by Taxpayer during 2014 and not during the years under audit;
- In reviewing Taxpayer's FedEx shipping labels, the audit found that approximately one half of the labels could not be verified at the FedEx.com website;
- In reviewing Taxpayer's FedEx shipping labels, the audit found that the labels provided could not be "matched to any of the FedEx bills provided by Taxpayer."

- Taxpayer failed to provide any shipping documentation for certain of the purported out-of-state transactions;
- In reviewing transactions purportedly directly delivered by Taxpayer's own personnel to locations in an adjoining state, Taxpayer was unable to provide any documentation documenting the deliveries and was unable to establish why it failed to register for and collect sales tax on behalf of that adjoining state.

The audit report summarized its finds:

Taxpayer was required to charge tax on a significant portion of these sales because Taxpayer was aware that the property would be used in Indiana. Although customers may have instructed Taxpayer to ship items out of state to the customers' other properties, the transaction was subject to tax. Many sales were reported to be shipped out of state even though the customer was present in the store and payment was made in full.

. . . .

[Taxpayer] . . . did not ship items in a manner consistent with its insurance policy nor that of a reasonable person. A signature was not required for a large number of shipments. [M]any shipments included jewelry valued in the ten and hundreds of thousands of dollars but Taxpayer did not request a signature to confirm receipt of the merchandise. In such case, a delivery driver would leave such box at the doorstep of the recipient. This practice does not comply with Taxpayer's insurance policy, and as such the items shipped in this manner were not covered by insurance. Taxpayer also shipped most items in small boxes, which is contrary to Taxpayer's insurance company's recommendations for shipment packaging.

#### **B. Taxpayer's Response.**

Taxpayer does not agree that it owes additional tax but criticizes the audit as deficient, the auditor as judgmental, and that the audit results were dictated not by the on-scene auditor but by Department personnel in "Indianapolis." Taxpayer explains:

From the onset of the Audit, it was clear that the Auditor wanted to re-class all out-of-state sales as taxable in-state sales. The Taxpayer provided documents to show the items were shipped out of state. The Auditor did not accept these documents and could not indicate what documentation would be accepted.

Taxpayer states that it was unaware that its insurance policy requires that shipments of jewelry to out-of-state locations be shipped in a certain manner and that the recipient is required to sign upon receipt. Taxpayer explains that it shipped the jewelry by "[p]riority mail to save the company money and increase profits; hereby leading to a higher employee bonus." Taxpayer further claims "[n]ot being in compliance with the insurance policy requirements does not make out-of-state sales in-state sales."

Taxpayer further criticizes both the Department and the audit for its purported failure to fully explain why the documentation it presented was deficient.

Taxpayer explains its failure to supply the audit with documentation requested during the audit:

The Auditor was informed that Taxpayer already put the records back into storage as she previously said [the audit] was done. It also appeared that this [document request] to be a waste of time as [the auditor] was still waiting on Indianapolis to decide . . . .

[I]t made no sense to gather documents on 120 sales. The documents would be same type for 2013 as they were for 2011 and 2012.

According to Taxpayer, the on-site auditor was informed that Taxpayer would want to administratively appeal the audit findings.

Taxpayer criticizes the audit's reliance on third-party documentation and information (phone records and/or real estate records) in determining that transactions with purported out-of-state customers were in fact transactions with customers located within Indiana. As explained by Taxpayer:

The Auditor performed various property searches and [I]nternet searches on the Taxpayer's customers to determine where they live. Neither the Taxpayer nor any other retailer in Indiana is required to perform these procedures on their customers.

Taxpayer claimed that the audit's assessment of use tax on purchases of "capital assets" was a "total fabrication on the part of the Auditor." However, during the administrative hearing, Taxpayer retreated from this initial position and admitted that it made purchases of tangible personal property which it used at its business location and which were properly subject to Indiana's use tax.

In addition, Taxpayer maintains that the audit results were never explained to Taxpayer's representative and that the audit did not include a "closing conference."

### **C. Hearing Analysis.**

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.

Taxpayer is obligated to maintain and preserve documentation on its jewelry sales. "Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for tax by reviewing those books and records." IC § 6-8.1-5-4(a). In addition, IC § 6-8.1-5-4(c) provides that, "A person must allow inspection of the books and records and returns by the department or its authorized agents at all reasonable times." IC § 6-8.1-5-4(c).

The Department notes that Taxpayer was not in accord with IC § 6-8.1-5-4(c) when it repeatedly denied the audit's request for documentation of its Indiana retail sales.

In its review of the audit report and the scanty records provided subsequent to the audit, the Department agrees with the audit report's conclusion:

Taxpayer did not maintain good documentation of shipping as evidenced by both the lack of shipping records as well as the fact that for many of the records that were provided, Taxpayer had to secure such records through various methods after the fact.

The Department is led to the conclusion that Taxpayer has not met its statutory burden under IC § 6-8.1-5-1(c) of establishing that the audit assessment was wrong. Taxpayer's protest consists almost entirely of a litany of generalized and unsubstantiated complaints levied against the auditor, the audit process, and the audit's conclusions.

There is an entirely reasonable expectation that a company in the business of selling high-priced items and claiming that it was not required to collect Indiana sales tax on those sales will maintain reasonably detailed records of those transactions. In the absence of those documents, Taxpayer asks the Department to blithely accept Taxpayer's "say-so" that it regularly sold and received payment for thousand dollar items to customers at its retail location, and that it then shipped the items to an out-of-state location in such a haphazard manner as that outlined in the audit report and admitted to by Taxpayer.

Taxpayer failed to document its purported out-of-state sales, failed to adequately explain why it should not have collected Indiana sales tax from customers at its Indiana business location, and is now "personally liable for the payment of those taxes, plus any penalties and interest attributable to those taxes . . . ." IC § 6-2.5-9-3.

### **FINDING**

Taxpayer's protest is denied.

*Posted: 11/25/2015 by Legislative Services Agency*  
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