

Supplemental Letter of Findings: 04-20140502
Gross Retail Tax
For the Years 2010, 2011, and 2012

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

HOLDING

Service Provider established that its related Transportation Company was entitled to the public transportation sales tax exemption because the two parties had a commercially reasonable, arms-length business relationship.

ISSUES

I. Gross Retail Tax - Public Transportation Exemption.

Authority: IC § 6-2.5-5-27; IC § 6-8.1-5-1(c); Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579, 583 (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); Indiana Dep't. of State Revenue, Sales Tax Division v. RCA Corp., 310 N.E.2d 96 (Ind. Ct. App. 1974); [45 IAC 2.2-5-61](#); Sales Tax Information Bulletin 12 (December 2014); Sales Tax Information Bulletin 12 (July 1, 2010); Letter of Findings 04-20140502 (April 8, 2015).

Taxpayer argues that its Transportation Company is entitled to claim the public transportation exemption and that the Department's audit and administrative decisions to the contrary were erroneous.

II. Imposition - Exemption Certificates.

Authority: IC § 6-2.5-8-8(a); IC § 6-8.1-3-12(b).

Taxpayer asks that the Department review additional exemption certificates and adjust the assessment of sales tax.

STATEMENT OF FACTS

Taxpayer is an out-of-state service provider with multiple business locations across the country including locations in Indiana. The Indiana Department of Revenue ("Department") conducted a sales and use tax audit of Taxpayer's business records.

The audit resulted in an assessment of additional sales and use tax on the ground that Taxpayer and its separate, disregarded entity ("Transportation Company") were not entitled to claim the public transportation exemption on behalf of Transportation Company.

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. A Letter of Findings was issued April 2015. The Letter of Findings concluded that Taxpayer's Transportation Company was not entitled to claim the exemption. Taxpayer continued to disagree and requested a rehearing. A second administrative hearing was conducted, and this Supplemental Letter of Findings results.

I. Gross Retail Tax - Public Transportation Exemption.

DISCUSSION

The issue is whether Taxpayer has met its burden of establishing that its related Transportation Company is a separate, distinct entity entitled to claim the public transportation exemption on the purchase of equipment and

supplies used by Transportation Company.

The Department's audit assessed Taxpayer sales and use tax on the purchases of the equipment and supplies. Taxpayer maintains that the purchases were made by its Transportation Company which was purportedly exempt from those taxes.

This Supplemental Letter of Findings addresses Taxpayer's protest and incorporates by reference the statements of facts, law, and conclusions set out in the April 2015 Letter of Findings.

As a threshold issue, it is the Taxpayer's responsibility to establish that the pending 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 an 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, all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

Taxpayer relies on the statutory exemption set out at IC § 6-2.5-5-27 as follows:

Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property.

[45 IAC 2.2-5-61](#), in relevant part, provides:

(a) The state gross retail tax shall not apply to the sale and storage or use in this state of tangible personal property which is directly used in the rendering of public transportation of persons or property.

(b) Definition: Public Transportation. Public transportation shall mean and include the movement, transportation, or carrying of persons and/or property for consideration by a common carrier, contract carrier, household goods carrier, carriers of exempt commodities, and other specialized carriers performing public transportation service for compensation by highway, rail, air, or water, which carriers operate under authority issued by, or are specifically exempt by statute or regulation from economic regulation of, the public service commission of Indiana, the Interstate Commerce Commission, the aeronautics commission of Indiana, the U.S. Civil Aeronautics Board, the U.S. Department of Transportation, or the Federal Maritime Commissioner; however, the fact that a company possesses a permit or authority issued by the P.S.C.I., I.C.C., etc., does not of itself mean that such a company is engaged in public transportation unless it is in fact engaged in the transportation of persons or property for consideration as defined above.

(c) In order to qualify for exemption, the tangible personal property must be reasonably necessary to the rendering of public transportation. The tangible personal property must be indispensable and essential in directly transporting persons or property.

Taxpayer is - of course - in the business of providing delivery and other services to its customers. It is not in the business of providing public transportation. Taxpayer necessarily relies on the proposition that its related Transportation Company is a distinct entity which independently qualifies for the exemption.

The Department's explanation and application of the exemption is set out in Sales Tax Information Bulletin 12 (December 2014) (20150128 Ind. Reg. 045150028NRA). The Bulletin sets out certain benchmarks necessary for a transportation business to qualify for the exemption. See also Sales Tax Information Bulletin 12 (July 1, 2010) (20100623 Ind. Reg. 045100390NRA).

The Bulletin provides: "The following requirements are factors the department weighs in determining whether a transportation company is engaged in public transportation." The requirements below are classified as "critical factors" necessary to qualify for the exemption. As stated in the Bulletin, "A transportation company fails to qualify for the exemption if it does not, at a minimum, adhere to all the critical requirements." (Emphasis added).

- The transportation company must transport the persons or property of another.

- The transportation company must maintain all shipping/transporting documents for all transactions (e.g., trip reports, truck logs, and invoices).
- The transportation company must receive compensation for the services it provides.
- The transportation company must hold and pay for appropriate public transportation insurance.
- The transportation company must be fully and independently authorized by federal and/or state authorities to provide public transportation services.
- If an employee of the parent company performs duties for the parent company and also performs "leased" duties for the transportation company, the parent company must maintain detailed records of when and which duties that employee is performing for the parent company and when and which duties that employee is performing under the lease.
- If the parent company makes a capital contribution of the vehicles to the transportation company, titles to the vehicles must be transferred to the transportation company.
- The transportation company and the parent company must maintain separate books and records, including separate charts of accounts for each company.
- Transactions between the parent company and the transportation company must evidence a commercially reasonable, arms-length relationship between the parties.
- Transactions between the parent company and the transportation company must be evidenced by actual invoicing and payments for all transactions.
- The parent company and the transportation company must segregate and account for each entity's purchases and expenses.
- The parent company and the transportation company must maintain separate bank accounts.

The April 2015 Letter of Findings addressed whether: (1) "Transportation Company receives compensation for providing transportation services;" (2) whether Transportation Company had "separate employees;" (3) whether the parties' vehicles were titled in the name of Transportation Company; (4) whether Taxpayer and Transportation Company "segregate[d] and account[ed] for each entity's purchases and expenses;" (5) whether "[T]ransportation [C]ompany [had] a distinct, arms-length business relationship;" and (6) whether "[Taxpayer] maintain[ed] separate depreciation schedules for the [Transportation Company]."

In addition to the statutory burden of establishing the audit's assessment was "wrong," the April 2015 Letter of Finding notes Indiana law under which tax exemptions are "strictly construed" against the taxpayer and that parties "claiming an exemption must establish their case which by sufficient evidence, which is clearly within the exact letter of the law." Indiana Dep't. of State Revenue, Sales Tax Division v. RCA Corp., 310 N.E.2d 96, 97 (Ind. Ct. App. 1974).

The April 2015 Letter of Findings concluded:

[T]he Department is unable to agree that Taxpayer has met its burden under IC § 6-8.1-5-1(c) of establishing that it and its Transportation Company established and maintained a distinct arm's-length business relationship and that the Transportation Company qualifies for the public transportation exemption.

During the course of the rehearing, Taxpayer supplied additional documentation.

In asking that the Department's decisions be reviewed, Taxpayer addressed the question of whether Transportation Company is paid by Taxpayer for providing the transportation services. Taxpayer explains that it has a "cost-plus" agreement with Transportation Company. Transportation Company calculates each month the expenses incurred in providing the services, applies an agreed upon mark-up, and invoices Taxpayer the total amount. Taxpayer has provided a sample monthly invoice issued by Transportation Company. Taxpayer explains that the invoice does not detail the cost-plus calculation but that the detailed information is "freely available to the relevant corporate personnel."

Similarly, Taxpayer explains that it has an "employee leasing agreement" between itself and Transportation Company. Under that agreement, Transportation Company's "employees will be provided on a cost-plus basis." Taxpayer "produces a detailed schedule of the employee costs associated with the contract." The Transportation Company is provided a monthly invoice of those costs which includes the employee expenses along with a monthly "management fee." Transportation Company provided a sample "income statement" which details the management fee, fuel expense, labor costs, vehicle expenses, licensing, and other detailed, monthly expenses.

Taxpayer explains its financial arrangement with Transportation Company. According to Taxpayer, it has a distinct identity from Transportation Company but that both and Transportation Company's finances are managed by yet a third entity here designated as "Services."

Taxpayer states that Transportation Company maintains a separate bank account.

[Transportation Company] deposits from [Taxpayer] for transportation services in this account. However, that cash is immediately swept into a corporate account owned by [Services]. The sweeping of cash to a centralized corporate account is a common cash management tool used by many companies. The sweep is not a dividend or distribution of any type. The cash is still on [Transportation Company's] books in the form of an intercompany receivable. This is the procedure for all [Taxpayer's] subsidiaries.

Taxpayer further explains that Transportation Company's expenses are not paid by Taxpayer. These expenses are paid for by Services and that "there is no direct circular flow to the payments made to [Transportation Company] or the payment of expenses for [Transportation Company]."

Taxpayer addressed issues related to the acquisition, ownership, and titling of the vehicles used to provide transportation.

All of the vehicles used in public transportation were contributed by [Taxpayer] to [Transportation Company]. These vehicles were retitled to [Transportation Company] when their registrations were due.

Taxpayer provided copies of the registration and titling of a cross-section of the vehicles at issue.

Taxpayer admits that certain of the vendor invoices issued for transportation expenses were not issued in Transportation Company's name. Nonetheless, Taxpayer explains that "[t]his does not change the fact that the equipment was paid for by [Transportation Company] and used in public transportation by [Transportation Company]."

The Department agrees that Taxpayer has met its statutory burden under IC § 6-8.1-5-1(c) of establishing that the proposed assessment - insofar as it addresses the "public transportation" issue - is wrong. The Department agrees that Taxpayer has met each of the substantive requirements set out in Sales Tax Information Bulletin 12, that Taxpayer and Transportation Company have a commercially reasonable arms-length relationship, and that Transportation Company is entitled to the sales tax exemption set out at IC § 6-2.5-5-27.

FINDING

Taxpayer's protest is sustained.

II. Imposition - Exemption Certificates.

DISCUSSION

The Department's audit employed a "statistical sample and projection of adjustments" to calculate any amounts of additional use tax due. Taxpayer indicates that it now has additional exemption certificates which were not available at the time the use tax assessment was calculated.

IC § 6-8.1-3-12(b) allows, as follows, the Department to employ a sampling methodology in determining a taxpayer's liability:

The department may audit any returns with respect to the listed taxes using statistical sampling. If the taxpayer and the department agree to a sampling method to be used, the sampling method is binding on the taxpayer and the department in determining the total amount of additional tax due or amounts to be refunded.

Taxpayer asks that the Department belatedly accept two additional "exemption certificates" in order to establish that it was not required to collect sales tax from those entities. IC § 6-2.5-8-8(a) states:

A person, authorized under subsection (b), who makes a purchase in a transaction which is exempt from the state gross retail and use taxes, may issue an exemption certificate to the seller instead of paying the tax. The person shall issue the certificate on forms and in the manner prescribed by the department. A seller accepting a proper exemption certificate under this section has no duty to collect or remit the state gross retail or use tax on that purchase.

The Audit Division is requested to review the exemption certificates and - assuming that the certificates have

been submitted "in the manner prescribed by the department" - adjust the "error percentage" and the assessment amount as warranted.

FINDING

The Department's Audit Division is asked to review the exemption certificates and to revise the original assessment as warranted.

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