DEPARTMENT OF STATE REVENUE

04-20150073.LOF

Letter of Findings Number: 04-20150073
Use Tax
For Tax Years 2011-12

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 This document is effective as of its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

Manufacturer was able to produce documentation and explanation showing that some purchases under protest were not subject to use tax. Therefore, those purchases will be removed from the Department's calculations of use tax due. Other items under protest were not proven to be incorrect. Therefore, those purchases will remain in the Department's calculations of use tax due.

ISSUE

I. Use Tax–Imposition.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-8.1-5-1; Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579 (Ind. 2014); Indiana Dept. of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dept. of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Wendt LLP v. Indiana Dept. of State Revenue, 977 N.E.2d 480 (Ind. Tax Ct. 2012); 45 IAC 2.2-3-4; 45 IAC 2.2-4-27.

Taxpayer protests the imposition of use tax on certain transactions.

STATEMENT OF FACTS

Taxpayer is a manufacturer with operations in Indiana. As the result of an audit, the Indiana Department of Revenue ("Department") determined that Taxpayer had not paid sales tax or remitted use tax on all transactions it made as a consumer during the tax years 2011 and 2012. The Department therefore issued proposed assessments for use tax, penalty, and interest for those years. Due to the large number of Taxpayer's purchases as a consumer, the Department used a sample and projection method to determine Taxpayer's compliance rate regarding its use tax remittance duties. The Department applied the use tax compliance rate against the amount of use tax remitted and imposed use tax on the difference. Taxpayer protested the imposition of use tax on some transactions. Taxpayer also protested the imposition of penalty. An administrative hearing was conducted and this Letter of Findings results. Further facts will be supplied as required.

I. Use Tax–Imposition.

DISCUSSION

Taxpayer protests the results of an audit performed by the Department for the tax years 2011 and 2012. Due to the large amount of purchases during the tax years, the Department used a sample and projection method to review Taxpayer's purchases for sales tax and use tax compliance. For each transaction considered to be subject to use tax, that amount was added to the numerator of the Department's calculations, while all purchases were added to the denominator of the Department's calculations. The resulting percentage was considered to be the percent of transactions subject to use tax. The Department divided Taxpayer's purchases into six "strata" in order to more accurately sample and project Taxpayer's tax compliance. Each stratum was sampled and reviewed on its own merits and the results for each stratum were then totaled to reach the overall compliance rate. Taxpayer protests the inclusion of some items as taxable purchases in the Department's projection calculations for use tax due. Also, Taxpayer protests that some items were entered incorrectly and that they should be entered at the correct amounts. Taxpayer provided documentation and analysis in support of its position.

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 Dept. of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dept. 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, all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, shall be entitled to deference.

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.

Use tax is imposed by IC § 6-2.5-3-2(a), which states:

> 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.

45 IAC 2.2-3-4 further explains:

> 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 ("TPP") is used, stored, or consumed in Indiana, use tax is due unless sales tax was paid at the time of the transaction, unless there is an applicable exemption available for that transaction.

Taxpayer's first point of protest is in regard to the amount of the price of the TPP which it purchased during the tax years. Specifically, Taxpayer protests that the taxable amount of stratum One-Sort 15 was overstated and thus resulted in an overstatement of tax due for that stratum. The amount listed as taxable in the Department's workpapers is $324.93, while Taxpayer states that the taxable amount is actually $.03. A review of the invoice supplied by Taxpayer during the hearing process does not support Taxpayer's position. The TPP in question was forty 50-pound bags of Oil Dri Clay used to clean up oil spills. Taxpayer stored, used, or consumed the TPP in Indiana, which makes the TPP subject to use tax under IC § 6-2.5-3-2(a). Taxpayer has not established that such TPP is exempt in any manner while the invoice does establish that the TPP was purchased for $324.93. Therefore, Taxpayer has not met the burden imposed under IC § 6-8.1-5-1(c) of proving this portion of the proposed assessment wrong.

Taxpayer's second point of protest is in regard to the amount of use tax due on its purchase of price books. The specific transaction is in stratum 2-sort 239. Taxpayer states that it remitted use tax on the books which were shipped to Indiana and that it did not remit use tax on the books which were shipped out-of-state. The Department considered the books to be wholly subject to sales or use tax and imposed use tax on the $10,348.86 purchase price. Taxpayer protests that 1,485 of the 1,510 books ordered were shipped directly from the printer to out-of-state locations. Taxpayer states that it did remit use tax on the twenty-five books that were shipped to its location in Indiana. After review of the invoice from the printer, the Department agrees that only the twenty-five books shipped to Indiana were used, stored, or consumed in Indiana and only those twenty-five books were subject to Indiana sales or use taxes. Further, while Taxpayer ordered 1,500 books, the printer delivered 1,510. Therefore, Taxpayer argues that use tax is only due on the additional ten books delivered to Indiana. Since IC § 6-2.5-3-2(a) imposes Indiana use tax on TPP stored, used, or consumed in Indiana, and since Taxpayer has already remitted use tax on fifteen of the twenty-five books the Department agrees with this argument. Under IC § 6-8.1-5-1(c), Taxpayer has the burden of proving this portion of the proposed assessment wrong and has done so. Use tax will only be imposed on the remaining ten books which were delivered into Indiana.

Taxpayer's third point of protest is in regard to the amount of a transaction subject to use tax. Specifically, stratum 2-sort 249, was determined by the Department to be in the amount of $4,750.00, and wholly subject to use tax.

Taxpayer argues that only the $395.87 amount it originally reported is subject to use tax. The transaction in question was an annual maintenance agreement, which Taxpayer agrees was subject to sales tax or use tax since the agreement called for the transfer of TPP. However, Taxpayer states that the amount listed on the invoice was the total of the purchase price, but that $4,354.13 had been prepaid, leaving only $395.87 due to the vendor and upon which use tax would be imposed. While the Department understands Taxpayer's position, the available documentation does not establish that any prepayment was made. Neither does the available documentation establish, even assuming arguendo that such a payment was made, that use tax was remitted on such a prepayment. Therefore, Taxpayer has not met the burden imposed under IC § 6-8.1-5-1(c) of proving this portion of the proposed assessment wrong.

Taxpayer's fourth point of protest is in regard to the amount of a transaction subject to use tax. Specifically, stratum 3-sort 193, was determined by the Department to be in the amount of $2,501.65. Taxpayer argues that only the $1,139.15 originally reported was actually subject to use tax. After review of the invoice supplied in the protest process, the Department is unable to agree with Taxpayer's position. The invoice shows that Taxpayer ordered TPP in the amount of $2,501.65. Taxpayer has supplied no documentation or analysis supporting its position that only $1,139.15 is subject to use tax. Therefore, Taxpayer has not met the burden imposed under IC § 6-8.1-5-1(c) of proving this portion of the proposed assessment wrong.

Taxpayer's fifth point of protest is in regard to several amounts charged to Taxpayer by a third party which provided temporary warehousing services. Taxpayer's production plant requires periodic deep-cleaning and Taxpayer's product overstock was stored off-site in a third-party warehouse. Taxpayer explained that the warehouse service provider performed all activities within the warehouse except for periodic climate control inspections to ensure its product's proper storage. Specifically, the Department determined that Taxpayer stored, used, or consumed TPP listed under entries for stratum 4-sort 204, sort 268, and sort 270, and therefore owed use tax on those purchases. Taxpayer states that these invoices were for TPP which was used by the warehousing service provider and that the service provider is responsible for taxes on the TPP. Taxpayer refers to 45 IAC 2.2-4-27, which states:

> (a) In general, the gross receipts from renting or leasing tangible personal property are taxable. This regulation [45 IAC 2.2] only exempts from tax those transactions which would have been exempt in an equivalent sales transaction.
> (b) Every person engaged in the business of the rental or leasing of tangible personal property, other than a public utility, shall be deemed to be a retail merchant in respect thereto and such rental or leasing transaction shall constitute a retail transaction subject to the state gross retail tax on the amount of the actual receipts from such rental or leasing.
> (c) In general, the gross receipts from renting or leasing tangible personal property are subject to tax. The rental or leasing of tangible personal property constitutes a retail transaction, and every lessor is a retail merchant with respect to such transactions. The lessor must collect and remit the gross retail tax or use tax on the amount of actual receipts as agent for the state of Indiana. The tax is borne by the lessee, except when the lessee is otherwise exempt from taxation.
> (d) The rental or leasing of tangible personal property, by whatever means effected and irrespective of the terms employed by the parties to describe such transaction, is taxable.
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> (1) Amount of actual receipts. The amount of actual receipts means the gross receipts from the rental or leasing of tangible personal property without any deduction whatever for expenses or costs incidental to the conduct of the business. The gross receipts include any consideration received from the exercise of an option contained in the rental of lease agreement; royalties paid, or agreed to be paid, either on a lump sum or other production basis, for use of tangible personal property; and any receipts held by the lessor which may at the time of their receipt or some future time be applied by the lessor as rentals.
> (2) Rental or lease period. For purposes of the imposition of the gross retail tax or use tax on rental or leasing transactions, each period for which a rental is payable shall be considered a complete transaction. In the case of a weekly rate, each week shall be considered a complete transaction. In the case of a continuing lease or contract, with or without a definite expiration date, where rental payments are to be made monthly or on some other periodic basis, each payment period shall be considered a completed transaction.
> (3) Renting or leasing property with an operator:
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> (A) The renting or leasing of tangible personal property, together with the services of an operator shall be subject to the tax when control of the property is exercised by the lessee. Control is exercised when the lessee has exclusive use of the property, and the lessee has the right to direct the manner of the use of the property. If these conditions are present, control is deemed to be exercised even though it is not actually exercised.
> (B) The rental of tangible personal property together with an operator as part of a contract to perform a

specific job in a manner to be determined by the owner of the property or the operator shall be considered the performance of a service rather than a rental or lease provided the lessee cannot exercise control over such property and operator.

(C) When tangible personal property is rented or leased together with the service of an operator, the gross retail tax or use tax is imposed on the property rentals. The tax is not imposed upon the charges for the operator's services, provided such charges are separately stated on the invoice rendered by the lessor to the lessee.

(D) Notwithstanding any other provision of this regulation [45 IAC 2.2] any lessee leasing or renting a vehicle(s) from any lessor, including an individual lessor, with or without operators, driver(s), or even if the operator (driver) himself is the lessor, regardless of control exercised, shall not be subject to the gross retail tax or use tax, if the leased or rented vehicle(s) are directly used in the rendering of public transportation.

(4) Supplies furnished with leased property. A person engaged in the business of renting or leasing tangible personal property is considered the consumer of supplies, fuels, and other consumables which are furnished with the property which is rented or leased.

In the course of the protest process, Taxpayer was able to establish that the amounts charged by the warehouse service provider were charges for consumables used by the warehouse service provider while providing the warehousing services. Therefore, the burden of paying the sales or use tax on the purchase of the consumables rests with the service provider, as provided by 45 IAC 2.2-4-27(d)(4). Taxpayer has met the burden of proving the proposed assessments wrong with regard to these transactions, as required by IC § 6-8.1-5-1(c).

Taxpayer's sixth point of protest is in regard to charges by the same warehouse service provider discussed in Taxpayer's fifth point of protest above. Specifically, the Department determined that Taxpayer stored, used, or consumed TPP listed under entries for stratum 4-sort 166, sort 261, sort 270, and sort 275, as well as stratum 5-sort 135 and stratum 6-sort 167. For each of these transactions, the Department determined that the warehouse service provider had charged Taxpayer for the storage, use or consumption of TPP as a portion of the total amount charged on the invoice. For instance, the invoice for Sort 166 lists charges of $2,086.50 for two fork lift leases, $88.14 for disposal services, and $2,996.90 for utilities. The Department considered the $2,086.50 charge for fork lifts leases to be subject to use tax, but did not add the other amounts to the numerator of its use tax calculations.

Taxpayer protests that the fork lifts were not under its control, but rather were under the control of the warehouse service provider at all times. Taxpayer believes that 45 IAC 2.2-4-27(d)(3)(A) and 45 IAC 2.2-4-27(d)(3)(B) clearly provides that the rental of the forklifts with an operator is not subject to use tax since Taxpayer never had control over the forklifts. As discussed above, the warehouse service provider performed all substantive activities within the warehouse and therefore Taxpayer could not have had control over the forklifts or their operators. Therefore, Taxpayer did not have exclusive control over the forklifts as required by 45 IAC 2.2-4-27(d)(3)(A). Also, 45 IAC 2.2-4-27(d)(3)(B) plainly states that the rental of TPP with an operator when the renter cannot exercise control over the TPP or the operator shall be considered the performance of a service. Since that is the case here, Taxpayer is correct that the amounts listed for the rental of forklifts is not subject to use tax. Also, the charges for consumables in any of these invoices is not subject to use tax as described under protest point five above. Taxpayer has met the burden of proving the proposed assessments wrong with regard to these transactions, as required by IC § 6-8.1-5-1(c).

Taxpayer's seventh and final point of protest is in regard to the purchase of a truck body. Specifically, stratum 6-sort 102, was determined by the Department to be taxable in the amount of $1,800.00 which was charged for delivery of the truck body. Taxpayer believes that the Department did not take into account that Taxpayer already self-remitted use tax on the total amount of the base cost plus delivery charges for the truck body. Taxpayer provided documentation which establishes that the total amount charged for the base cost plus delivery charges was $75,000.00 and that Taxpayer remitted $5,250.00 use tax on that amount. Therefore, Taxpayer has already paid the use tax on the $1,800.00 of delivery charge and does not need to pay it again. Taxpayer has met the burden of proving the proposed assessments wrong with regard to this transaction, as required by IC § 6-8.1-5-1(c).

In conclusion, Taxpayer has met the burden of proving the proposed assessments with regard to most of those amounts under protest and listed as subject to use tax in the Department's use tax compliance projection calculations. The only amounts under protest upon which Taxpayer has not been sustained are stratum One-sort 15, stratum 2-sort 249, and stratum 3-sort 193. The Department notes that Taxpayer supplied several other invoices in the protest process but did not include those amounts in its protest letter. As explained during the hearing and in the Department's letter setting the hearing, the protest process is a taxpayer's opportunity to

clearly explain their protest and to provide relevant and cogent supporting documentation. Taxpayer has not presented a sufficiently developed argument for the Department to address with regard to these other invoices. See Wendt LLP v. Indiana Dept. of State Revenue, 977 N.E.2d 480, 485 n.9, (Ind. Tax Ct. 2012) (stating in a footnote parenthetical "that poorly developed and non-cogent arguments are subject to waiver" by the Indiana Tax Court) (citing Scopelite v. Indiana Dep't of Local Gov't Fin., 939 N.E.2d 1138, 1145 (Ind. Tax. Ct. 2010)). Taxpayer has not met the burden of proving these portions of the proposed assessments wrong, as required by IC § 6-8.1-5-1(c).

FINDING

Taxpayer's protest is sustained in part and denied in part, as explained above.

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