

**Letter of Findings: 04-20160563
Gross Retail and Use Tax
For the Years 2013 and 2014**

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 requires 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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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 Letter of Findings.

HOLDING

Restaurant Business - which operated locations inside and outside of Indiana - presented sufficient documentation justifying a supplemental review by the Department's Audit Division to assure that any sales or use tax liability was properly allocated between Restaurant Business's in-state and out-of-state locations.

I. Gross Retail and Use Tax - Allocation of In-State and Out-of-State Sales/Use Tax Liabilities.

Authority: IC § 6-2.5-1-2; IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-4-1; IC § 6-2.5-5 et seq.; IC § 6-8.1-5-1(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); 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)

Taxpayer argues that the Department's assessment of additional tax did not properly allocate the liability between Taxpayer's in-state and out-of-state restaurant locations.

STATEMENT OF FACTS

Taxpayer is a multi-state company which operates various restaurant businesses both inside Indiana and outside Indiana.

The Department of Revenue ("Department") conducted an audit review of Taxpayer's business records and tax returns. The Department made no adjustments to Taxpayer's sales tax liabilities. The audit found that although Taxpayer had a use tax accrual system in place, the audit "revealed that there were several asset and expense purchases that were missed in [Taxpayer's] use tax accrual account and [were] subject to use tax during the audit period."

The audit and Taxpayer agreed to the following methodology to extrapolate the amount of additional use tax owed.

The [T]axpayer had [] restaurants located in Indiana during the audit period. Based on the volume of expense purchases for the [] locations, the [T]axpayer and the auditor agreed to project expense purchases . . . based on a four month sample of selected expense accounts. Capital expenses have been excluded from the sample.

. . . .

Purchases where no sales tax was paid at the time of purchase and no use tax was self-assessed and remitted to the Department were identified and listed as subject to use tax (the numerator for the projection calculation). The total monthly expense for the selected expense accounts and selected months was used as the denominator for the projection calculation.

The audit found that Taxpayer had made purchases of equipment - originally delivered to one of Taxpayer's out-of-state locations - for which it had not paid use tax and which were - according to the audit report - subject to tax.

- Cotton hats, aprons, chef pants worn by Taxpayer's "employees and not directly used in the processing of

food for human consumption" were subject to tax.

- Purchases of music played over the restaurants sound system were subject to tax as "specified digital products."
- Rental of audio equipment used with Taxpayer's restaurants and used to play background music were subject to tax.
- Maintenance and repair parts such as ice melt and salt for the restaurants' parking lots, "Roundup" weed control for restaurant lawn maintenance, and miscellaneous parts such as cable links, valve spray, LED lights, light ballasts, electrical parts, and batteries were subject to tax.
- Maintenance agreements for the restaurants' point-of-sales computer registers. The maintenance agreements included software updates and replacement parts were subject to tax.
- Administrative supplies such as newsletters, planners, paper forms, and name badges were subject to tax.

However, the audit gave credit for taxes paid on the purchase of kitchen equipment such as fry pans, strainers, fry cutters, and various cooking utensils directly used in preparing food for human consumption. The audit found that since these items were "directly used" in the production of the Taxpayer's food products, the items were not subject to sales tax; the audit provided credit for any sales tax paid at the time the Taxpayer purchased this equipment.

The audit found that Taxpayer had made various capital purchases without paying sales tax.

- Taxpayer purchased a cash register system from "Squirrel Hardware." Publicly available information indicates that "Squirrel Hardware" supplies point-of-sale equipment and software.
- Taxpayer purchased various art prints, shades, blinds, doors, cabinets, bar stools, side chairs, and bar rails all of which - according to the audit report - were subject to use tax.
- Taxpayer engaged in "Job Cost Clearing" which allocated bulk purchases of hardware, software, and furniture. The audit noted that Taxpayer provided "no invoices . . . to verify that if sales tax was paid at the time of purchase" and concluded that "these purchases were subject to use tax in accordance with Indiana law."
- Taxpayer purchased "canned" software for use at its "point of sales" cash registers. Because the software was "canned" and not custom written to Taxpayer's specifications, the software was subject to sales/use tax.

The audit also found that Taxpayer had purchased heating and cooling equipment and paid six percent sales tax on the purchases. Since Indiana's sales tax rate was seven percent during the years under review, the audit assessed Taxpayer an additional one percent sales/use tax on the purchase of this equipment.

Taxpayer's representatives disagreed with the assessment of additional tax 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 and Use Tax - Allocation of In-State and Out-of-State Sales/Use Tax Liabilities.

DISCUSSION

The issue is whether the Department properly allocated the tax liability between Taxpayer's in-state restaurants and Taxpayer's out-of-state restaurants.

Taxpayer does not challenge any of the audit decisions which found that the purchase of certain items - computer software, point-of-sale registers, "specified digital goods - were subject to sales or use tax. Taxpayer simply argues that the audit failed to properly allocate those purchase expenses between its Indiana restaurants and its out-of-state restaurants. According to Taxpayer, the audit failure to properly allocate the expenses resulted in an overstatement of its Indiana sales and use tax liability.

Pursuant to IC § 6-2.5-2-1, a sales tax, known as state gross retail tax, is imposed on retail transactions made in

Indiana unless a valid exemption is applicable. IC § 6-2.5-5 et seq. Retail transactions involve the transfer of tangible personal property. IC § 6-2.5-1-2; IC § 6-2.5-4-1. A complementary 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. IC § 6-2.5-3-2.

The proposed assessment constitutes evidence that the Department's claim for the unpaid tax is valid, and each taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); *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). In reviewing a taxpayer's argument, the Indiana Supreme Court has held, that when it examines a statute that an agency is "charged with enforcing . . . we 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).

Taxpayer explains its argument; "In summary, we are contesting that the auditor erroneously assessed tax on asset allocations to [Taxpayer's] locations in Indiana where sales tax was paid to various vendors for [point-of-sale] terminals." Taxpayer admits that "[f]or portions relating to [point-of-sale] Terminals, Printers, Cash Drawers, and Licenses, tax was not properly paid so the assessments on these allocations by store are still due." (Emphasis deleted). Taxpayer states that it has now provided a "protest schedule" which "delineates the allocations from the audit work papers for each of the [] locations where an assessment occurred and breaks out each of the [] allocation categories within these [] store allocations for this project."

Taxpayer has provided various documents which - according to Taxpayer - had they been considered at the time of the original audit would have more properly allocated its tax liabilities amongst its various locations reducing the amount of the original assessment.

Taxpayer has not met its burden under IC § 6-8.1-5-1(c) of establishing that the assessment was "wrong." In other words, Taxpayer has not established that audit assessment should be decreased by \$1 or by \$1,000. Instead, Taxpayer has provided documentation which justifies review by the Department's Audit Division to determine whether the equipment it purchased - and arranged to have delivered to one of Taxpayer's out-of-state locations - was used in Indiana or whether the equipment was eventually used at one of Taxpayer's out-of-state restaurants. The Audit Division is requested to review that documentation and to adjust Taxpayer's liability to the extent warranted.

FINDING

To the extent that Taxpayer has documented that it purchased tangible personal property for storage, use or consumption in a location other than Indiana (rendering it exempt from Indiana's "use" tax) and subject to review by the Department's Audit Division, Taxpayer's protest is sustained.

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