DEPARTMENT OF STATE REVENUE

04-20170124.LOF

Letter of Findings: 04-20170124
Use Tax
For the Years 2014 and 2015

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

The Department disagreed with Indiana Company that it was not required to self-assess use tax on the purchase of trucks subsequently resold to its customer; the Department did not agree that the trucks were "incorporated" into other tangible personal property or that the sales were exempt under the "temporary storage" use tax exemption. The Department found no evidence that, in a previous audit, it had previously determined that purchase of trucks was exempt from tax.

ISSUES

I. Use Tax - Incorporation Exemption.

Authority: IC § 6-2.5-2-1(a); IC § 6-2.5-2-1(b); IC § 6-2.5-3-2(a); IC § 6-2.5-5-6; 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); Conklin v. Town of Cambridge City, 58 Ind. 130 (1877); 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); Rhoade v. Indiana Dep't of State Revenue, 774 N.E.2d 1044 (Ind. Tax Ct. 2002); Indiana Dept. of State Rev. v. Kimball Int'l Inc., 520 N.E.2d 454, 456 (Ind. Ct. App. 1988); Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp., 310 N.E.2d 96 (Ind. Ct. App. 1974); 45 IAC 2.2-5-14.

Taxpayer argues it was not required to self-assess use tax on the purchase of trucks on the ground that the trucks were incorporated into tangible personal property intended for resale.

II. Use Tax - Temporary Storage Exemption.

Authority: IC § 6-2.5-3-2(e).

Taxpayer states it was not required to pay sales tax or use tax on the purchase and then sale of trucks on the ground that the trucks were intended for use solely outside Indiana.

III. Use Tax - Prospective Treatment.

Authority: IC § 6-8.1-5-1(c); 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 maintains that it is not required to self-assess use tax on the purchase of trucks because it is entitled to prospective treatment of the Department's most recent audit conclusion.

STATEMENT OF FACTS

Taxpayer is an out-of-state company that owns and operates an Indiana manufacturing and repair facility. Taxpayer fabricates transportation vehicles furnished with pressure tanks. Taxpayer manufactures the pressurized tanks itself at its out-of-state location. Some of these tanks are shipped to the Indiana facility. Taxpayer attaches axles, wheels, brakes, lights and other parts to the tanks producing a self-contained vehicle called a "bobtail."

Taxpayer also repairs and updates pressure tanks on behalf of its customers because the tanks have a longer life

than the vehicle and/or its various parts. After remanufacturing the customer-owned tanks, Taxpayer attaches axles, wheels, brakes, lights and other parts to the refurbished tanks. On occasion, Taxpayer will attach the tank and parts to a completed truck chassis.

On occasion, Taxpayer will attach a pressure tank to a vehicle owned by one of its customers.

The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayer's tax returns and business records. The audit resulted in an assessment of additional sales/use tax. Taxpayer disagreed with a portion of the assessment and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representatives explained the basis for the protest. This Letter of Findings results.

I. Use Tax - Incorporation Exemption.

DISCUSSION

The issue is whether Taxpayer was required to self-assess use tax on the purchase and then subsequent sale of five 2015 International trucks (cab and chassis). After Taxpayer acquired the trucks, Taxpayer attached customer-owned pressure tanks to each vehicle. Taxpayer sold the vehicles to the customer which had provided the pressure tanks. Taxpayer billed the customer in an invoice which separately stated charges for "parts and materials," "labor," and the "2015 International Chassis."

The Department's audit concluded that Taxpayer should have self-assessed use tax on the purchase of the five trucks because Taxpayer did not qualify for the "resale exemption" and did not qualify for the "incorporation exemption."

Taxpayer disagrees, arguing that the trucks were incorporated into a distinctly new product of which the trucks were simply a component. Taxpayer points out that the "new products" delivered to its customer were superior to the customer's original delivery vehicles, that the reconditioned tanks were worth substantially more than the original tanks, and that the newly delivered vehicles "ha[d] vastly superior performance over the delivery truck of which the now refurbished tank was a component."

As authority for its position, Taxpayer cites to 45 IAC 2.2-5-14 which provides as follows:

> (a) The state gross retail tax shall not apply to sales of any tangible personal property which is to be incorporated by the purchaser as a material or an integral part into tangible personal property produced for sale by such purchaser in the business of manufacturing, assembling, refining or processing.
>
> (b) The exemption provided by this regulation [45 IAC 2.2] applies only to tangible personal property to be incorporated as a material or an integral part into tangible personal property produced for sale by a purchaser engaged in the business of manufacturing, assembling, refining or processing. This regulation [45 IAC 2.2] does not apply to persons engaged in producing tangible personal property for their own use.
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> (c) This regulation [45 IAC 2.2] does not exempt from tax tangible personal property to be used in production, such as supplies, parts, fuel, machinery, etc., refer to Regs. 6-2.5-5-5(010) and 6-2.5-5-5(020) (dealing with material consumed in direct production) for the application of those regulations to taxpayers engaged in the production of tangible personal property.
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> (d) The purchase of tangible personal property which is to be incorporated by the purchaser as a material or an integral part is exempt from tax. "Incorporated as a material or an integral part into tangible personal property for sale by such purchaser" means:
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> (1) That the material must be physically incorporated into and become a component of the finished product;
> (2) The material must constitute a material or an integral part of the finished product; and
> (3) The tangible personal property must be produced for sale by the purchaser.
>
> (e) Application of general rule.
>
> (1) Incorporation into the finished product. The material must be physically incorporated into and become a component part of the finished product.
> (2) Integral or material part. The material must constitute a material or integral part of the finished product.

(3) The finished product must be produced for sale by the purchaser.

As a threshold issue, it is the Taxpayer's responsibility to establish that the assessment of sales and/or use tax 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). 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, fn. 9 (Ind. Tax Ct. 2012). 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 investigation, are entitled to deference.

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 "retail purchaser") is liable for the sales tax on the transaction. IC § 6-2.5-2-1(b).

Indiana also imposes a complementary excise tax called "the use tax" 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." IC § 6-2.5-3-2(a). A taxable "use" means the "exercise of any right or power of ownership over tangible personal property." IC § 6-2.5-3-1(a). The "use tax is functionally equivalent to [the] sales tax . . . ." Rhoade v. Indiana Dep't of State Revenue, 774 N.E.2d 1044, 1047 (Ind. Tax Ct. 2002).

As authority for its conclusion that the five International trucks at issue were exempt, Taxpayer cites to the Indiana statute, IC § 6-2.5-5-6, which provides an exception to this "general rule." The statute provides as follows:

> Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for incorporation as a material part of other tangible personal property which the purchaser manufactures, assembles, refines, or processes for sale in his business. This exemption includes transactions involving acquisitions of tangible personal property used in commercial printing.

In applying any tax exemption such as IC § 6-2.5-5-6 (or 45 IAC 2.2-5-14), the general rule is that "tax exemptions are strictly construed in favor of taxation and against the exemption." Indiana Dept. of State Rev. v. Kimball Int'l Inc., 520 N.E.2d 454, 456 (Ind. Ct. App. 1988). A statute which provides a tax exemption, however, is strictly construed against the taxpayer. Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp., 310 N.E.2d 96, 97 (Ind. Ct. App. 1974). "[W]here such an exemption is claimed, the party claiming the same must show a case, by sufficient evidence, which is clearly within the exact letter of the law." Id. at 101 (citing Conklin v. Town of Cambridge City, 58 Ind. 130, 133 (1877)).

In this case, the Department is unable to agree that the five trucks were incorporated into and became a simple component of another item of tangible personal property pursuant to IC § 6-2.5-5-6 because, as explained in the audit report, "the tanks that were incorporated with the new trucks were owned by the customer, not the [T]axpayer." Taxpayer simply acquired the trucks to which it attached the customer-owned tanks. The subsequent invoice sent to its customer buttresses this conclusion because the customer was billed for - among other things - each "2015 International Chassis."

As noted above, Taxpayer bears the statutory burden of establishing both that the assessment was "wrong" and that it is entitled to claim - by "sufficient evidence" - an exemption under circumstances which are "clearly within the exact letter of the law." In this case, Taxpayer purchased trucks, did not self-assess use tax on the purchases, and the cited exemption is not "clearly within the exact letter of the law."

FINDING

Taxpayer's protest is respectfully denied.

II. Use Tax - Temporary Storage Exemption.

DISCUSSION

As an alternative to the "incorporation exemption" discussed in Part I above, Taxpayer argues it was not required self-assess use tax on the purchase of the trucks because the completed and finished products (trucks, tanks, parts) were only temporarily stored in Indiana.

Taxpayer relies on IC § 6-2.5-3-2(e) which states:

> (e) Notwithstanding any other provision of this section, the use tax is not imposed on the keeping, retaining, or exercising of any right or power over tangible personal property, if:
> (1) the property is delivered into Indiana by or for the purchaser of the property;
> (2) the property is delivered in Indiana for the sole purpose of being processed, printed, fabricated, or manufactured into, attached to, or incorporated into other tangible personal property; and
> (3) the property is subsequently transported out of state for use solely outside Indiana.

Taxpayer is correct in part. IC § 6-2.5-3-2(e) provides a "temporary storage" exclusion from use tax when the tangible personal property is purchased from an out-of-state vendor, shipped or delivered to an Indiana location, but then subsequently "transported out of state for use solely outside Indiana." However, the Department does not agree that Taxpayer has established that the five trucks were purchased from an out-of-state location or that the completed vehicles were destined "for use solely outside Indiana."

FINDING

Taxpayer's protest is respectfully denied.

III. Use Tax - Prospective Treatment.

DISCUSSION

As an alternative to Taxpayer's "incorporation" and "temporary storage" arguments, Taxpayer argues that it should not be required to self-assess use tax on the purchase of the five trucks because the Department had previously found that acquisition of and then sale of trucks was exempt. Specifically, Taxpayer points to an audit conducted by the Department for the years 2009 through 2011 and issued in August 2012.

As with the Parts I and II above, it is the Taxpayer's responsibility to establish that the assessment of sales tax was 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).

In Taxpayer's case, it cites to a previous audit conducted by the Department which reviewed Taxpayer's 2009, 2010, and 2011 transactions. Although the audit resulted in an assessment of additional sales/use tax, Taxpayer states that there is nothing in the report which indicated that Taxpayer was required to self-assess use tax on the purchase of trucks.

The audit did find "[t]he majority of [Taxpayer's] customers are public transportation companies and are exempt from sales tax." The audit further noted that "[a] exemption certificates for exempted sales were present."

A review of the transactions included in the sales/use tax "projection" sample includes various parts, supplies, and equipment but includes nothing similar to Taxpayer's more recent purchase and then sale of International trucks to its customer. Taxpayer very well may have acquired and then sold trucks to customers during 2009, 2010, and 2011; however, a review of the audit report contains nothing which could be interpreted as the Department's agreement or ruling that the purchase of trucks was exempt from use tax.

FINDING

Taxpayer's protest is respectfully denied.

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