DEPARTMENT OF STATE REVENUE

Final Order Denying Refund; 04-20181408R; 04-20181413R; 04-20181414R; 04-20181415R; 04-20181416R; 04-20181417R; 04-20181418R; 04-20181419R; 04-20181420R; 04-20181421R; 04-20181422R; 04-20181423R; 04-20181424R; 04-20181425R; 04-20181426R; 04-20181427R; 04-20181428R; 04-20181429R; 04-20181430R; 04-20181431R; 04-20181432R; 04-20181433R; 04-20181434R; 04-20181435R; 04-20181436R; 04-20181437R; 04-20181438R; 04-20181439R; 04-20181440R; 04-20181441R; 04-20181442R; 04-20181443R; 04-20181444R; 04-20181445R; 04-20181446R; 04-20181447R; 04-20181448R
Gross Retail Tax
For the Year 2014

NOTICE: IC § 4-22-7-7 permits the publication of this document in the Indiana Register. The publication of this document provides the general public with information about the Indiana Department of Revenue's official position concerning a specific set of facts and issues. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Final Order Denying Refund.

HOLDING

Restaurant Company failed to produce documentation and explanation establishing a higher exemption rate for utility usage than originally determined by the Department; the Department disagreed that Restaurant Company's refrigerators, ovens, and other electrical devices consumed electricity at 100 percent capacity every hour of every day the Restaurant Company's business locations were in operation.

ISSUE

I. Gross Retail Tax - Predominant Use Utility Exemption.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-5-5.1; *Dept. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Aztec Partners, LLC v. Indiana Dep't of State Revenue*, 35 N.E.3d 320 (Ind. Tax Ct. 2015); *Mynsberge v. Dep't of State Revenue*, 716 N.E.2d 629 (Ind. Tax Ct. 1999); *Tri-States Double Cola Bottling Co. v. Dep't of State Revenue*, 706 N.E.2d 282 (Ind. Tax Ct. 1999*); General Motors Corp. v. Indiana Dept. of State Revenue*, 578 N.E.2d 399 (Ind. Tax Ct. 1991); 45 IAC 2.2-4-13; *Indiana Department of Revenue Utility Study Workpaper - Electric*, https://www.in.gov/dor/5317.htm.

Taxpayer argues that the Department erred in determining the extent to which its restaurants were entitled to a sales tax exemption on the purchase of utilities directly used in the preparation of its food offerings.

STATEMENT OF FACTS

Taxpayer is an out-of-state company which operates Indiana restaurants. Taxpayer submitted multiple requests for refunds of sales tax paid on the purchase of electricity consumed by its restaurants. The Indiana Department of Revenue ("Department") reviewed the information submitted by Taxpayer. The Department's representative conducted an on-site visit to one of the restaurants claiming the refund. The Department concluded that Taxpayer's assertion - that approximately 53 percent of its electricity was consumed in an exempt fashion - was incorrect and that approximately 24 percent of its electricity was entitled to the sales tax exemption.

The Department's decision resulted in a partial refund of the amount of sales tax originally requested. Taxpayer disagreed with the Department's decision arguing that all of its restaurants were entitled to the 100 percent exemption and a refund of the entire amount of tax originally sought. Taxpayer submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representative explained the basis for the protest and submitted additional documentation intended to support its argument. This Final Order Denying Refund results.

I. Gross Retail Tax - Predominant Use Utility Exemption.

DISCUSSION

The issue is whether the Department erred in calculating its exempt electricity consumption by employing a "load factor" and that Taxpayer was entitled to calculate that consumption by using a 100 percent "power factor." If

Taxpayer is correct, then its exempt electricity consumption exceeds "predominate usage" threshold.

Indiana sales tax is imposed pursuant to 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.
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> (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.

An exemption from sales and use tax is provided for tangible personal property purchased for use in direct production of other tangible personal property. This exemption is found in IC § 6-2.5-5-5.1, which states:

> (a) As used in this section, **"tangible personal property" includes electrical energy,** natural or artificial gas, water, steam, and steam heat.
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> (b) Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for direct consumption as a material to be consumed in the direct production of other tangible personal property in the person's business of manufacturing, processing, refining, repairing, mining, agriculture, horticulture, floriculture, or arboriculture. This exemption includes transactions involving acquisitions of tangible personal property used in commercial printing.

(**Emphasis added**).

In the case of electrical usage, 45 IAC 2.2-4-13 explains:

> (a) In general, the furnishing of electricity, gas, water, steam, or steam heating services by public utilities to consumers is subject to tax.
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> (b) The gross receipt of every person engaged as a power subsidiary or a public utility derived from selling electrical energy, gas, water, or steam to consumers for direct use in direct manufacturing, mining, production, refining, oil or mineral extraction, irrigation, agriculture, horticulture, or another public utility or power subsidiary described in IC 6-2.5-4-5 shall not constitute gross retail income of a retail merchant received from a retail transaction. Electrical energy, gas, water, or steam will only be considered directly used in direct production, manufacturing, mining, refining, oil or mineral extraction, irrigation, agriculture, or horticulture if the utilities would be exempt under IC 6-2.5-5-5.1.
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> (c) Sales of public utility services or commodities to consumers engaged in manufacturing, mining, production, refining, oil or mineral extraction, irrigation, agriculture, horticulture, or another public utility or power subsidiary described in IC 6-2.5-4-5, based on a single meter charge, flat rate charge, or other charge, are excepted if such services are separately metered or billed and will be used predominantly for the excepted purposes.
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> (d) Sales of public utility services and commodities to consumers engaged in manufacturing, mining, production, refining, oil or mineral extraction, irrigation, agriculture, or horticulture, based on a single meter charge, flat rate charge, or other charge, which will be used for both excepted and nonexcepted purposes are taxable unless such services and commodities are used predominantly for excepted purposes.
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> (e) **Where public utility services are sold from a single meter and the services or commodities are utilized for both exempt and nonexempt uses, the entire gross receipts will be subject to tax unless the services or commodities are used predominantly for excepted purposes. Predominant use shall mean that more than fifty percent (50[percent]) of the utility services and commodities are consumed for excepted uses.**

(**Emphasis added**).

Therefore, if fifty percent or more of electricity sold from a single meter is used in an exempt manner, the purchaser/taxpayer is considered to have predominantly used the electricity for exempt purposes, and the electricity sold through that meter is wholly exempt from sales tax and use tax. In order to qualify for the exemption, a taxpayer must show that "1) it is engaged in production, 2) it has an integrated production process, and 3) the electricity is essential and integral to its integrated production process." *Aztec Partners, LLC v. Indiana*

Dep't of State Revenue, 35 N.E.3d 320, 324 (Ind. Tax Ct. 2015).

IC § 6-2.5-5-5.1, like all tax exemption provisions, is strictly construed against exemption from the tax. *Tri-States Double Cola Bottling Co. v. Dep't of State Revenue*, 706 N.E.2d 282, 283 (Ind. Tax Ct. 1999*); Mynsberge v. Dep't of State Revenue*, 716 N.E.2d 629, 636 (Ind. Tax Ct. 1999). 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 decision denying a portion of the requested refund, are entitled to deference.

Nevertheless, the Department is well aware of the countervailing rule that a "statute must not be construed so narrowly that it does not give effect to legislative intent because the intent of the legislature embodied in a statute constitutes the law." *General Motors Corp. v. Indiana Dept. of State Revenue*, 578 N.E.2d 399, 404 (Ind. Tax Ct. 1991).

Taxpayer and the Department agree that Taxpayer's restaurants use electricity in an exempt fashion because the restaurants produce "tangible personal property." Taxpayer and the Department agree that Taxpayer operates refrigerators, ovens, and "prep tables" which use electricity in an exempt fashion. Taxpayer and the Department agree on the voltage and amperage of each of these devices. However, Taxpayer disagrees on the Department's employment of a "load factor" in calculating each device's exempt power consumption.

For example, Taxpayer operates ovens rated at 230 volts and 20 amps. The Department found that the ovens were used 14 hours each day and were entitled to a "load factor of 40 percent." "Load factor" is the key variable in determining the energy consumption of each electrical device based on the assumption that each device is not operating at full capacity each hour of each day.

Taxpayer disagrees and states that instead of using a "load factor," the Department's own instructions mandate the use of a 100 percent "power factor." Taxpayer quotes the Department's instructions:

> Power Factor: The percentage of time that equipment is on and running at maximum power draw. If an accurate time measurement can be given for a piece of equipment, the power factor will be closer to 100[percent]. For example, if a drill press is turned on and used 60 times in a day for 3 minutes at a time (180 minutes) the drill press would have close to 100[percent] power use for three hours per day. But if the hours of use for same press are given as 8 hours, a power factor would be assigned to 37.5 percent. *Indiana Department of Revenue Utility Study Workpaper - Electric*, https://www.in.gov/dor/5317.htm (last visited June 8, 2018).

Taxpayer concludes that "the power rating of equipment is the highest input allowed to flow through particular equipment." In other words, once the volts and amperage of each device is known, that device should be allotted a 100 percent power factor unless it is known with certainty that the device only operates a portion of each day. Taxpayer concludes that its refrigerators, ovens, prep tables, oven hoods and similar devices are operating at full-tilt, 100 percent capacity every hour of every day every restaurant is open for business.

The Department must respectfully disagree with Taxpayer's analysis and conclusion. Although the administrative hearing is not an appropriate venue for concluding whether the load or "power" factor of any particular device is or is not 40 percent (or 41 or 39 percent), the Department finds Taxpayer's analysis counter-intuitive. Although agreeing that the refrigerators and ovens are in operation each hour the restaurant is open, the Department's audit concluded that Taxpayer's refrigerators and ovens cycle on and off periodically during the day and that the refrigerators and ovens were not constantly "pulling" electricity at their full capacity.

The Department must respectfully decline Taxpayer's invitation to grant a wholesale 100 percent exemption based on Taxpayer's assertions. As noted above Taxpayer exemptions are "strictly construed against exemption from [] tax." *Tri-States Double Cola Bottling Co.*, 706 N.E.2d at 283. Simply stated, in determining the extent to which Taxpayer's restaurants are entitled to the exemption, "the numbers are what the numbers are" unless the Taxpayer can provide specific documentation to the contrary. The decision driving any decision to grant a refund or determining the extent to which a taxpayer is entitled to an exemption is driven strictly by the reliable, substantive, quantifiable information provided by that taxpayer. In this case, Taxpayer's argument is based on a speculative interpretation of the Department's explanation of whether to use the "load factor" determined after the Department's on-site inspection of Taxpayer's restaurant operation or to automatically revert to a 100 percent

"power percent factor" for its own refrigerators, ovens, and other electrical devices. The Department does not agree that Taxpayer has clearly established its analysis is correct.

FINDING

Taxpayer's protest is respectfully denied.

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