

Letter of Findings: 04-20190521
Sales and Use Tax
For Tax Years 2015-17

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

HOLDING

Business provided sufficient evidence to show that its raw materials qualified as scrap metal and that it engaged in processing of recycling materials. Business therefore qualifies for the recycling exemption.

ISSUE

I. Use Tax–Exemption.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-5-45.8; 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); *Brandenburg Indus. Serv. Co. v. Indiana Dep't of State Revenue*, 60 N.E.3d 300 (Ind. Tax Ct. 2016); *Lafayette Square Amoco, Inc. v. Indiana Dept. of State Revenue*, 867 N.E.2d 289 (Ind. Tax Ct. 2007); [45 IAC 2.2-3-4](#).

Taxpayer protests assessment of use tax.

STATEMENT OF FACTS

Taxpayer operates a steel mill in Indiana. As the result of an audit, the Indiana Department of Revenue ("Department") determined that Taxpayer had not paid proper amounts of Indiana sales tax for the 2015-2017 tax years. This underpayment resulted in a proposed assessment of Indiana use tax. Taxpayer is protesting the imposition of use tax resulting from the proposed assessment findings. An administrative hearing was held and this Letter of Findings results. Further facts will be supplied as required.

I. Use Tax–Exemption.

DISCUSSION

Taxpayer protests proposed assessments of use tax for the 2015-2017 tax years. Taxpayer claims certain items used in the business are exempt under the recycling exemption found in the Indiana code. In an audit, the Department concluded that Taxpayer did not use scrap as raw materials and did not engage in the processing of recycled materials.

As a threshold issue, it is 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.

Use tax is imposed under 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 is used, stored, or consumed in Indiana, use tax is due unless sales tax was paid at the time of the transaction, or if there is an applicable exemption to sales and use taxes.

Taxpayer claims that it qualifies for the recycling exemption found at IC § 6-2.5-5-45.8 which states:

- (a) For purposes of this section, [IC 6-2.5-4-5](#), and section 30 of this chapter, the following definitions apply:
 - (1) "Recycling" means the processing of recycling materials and other tangible personal property into a product for sale if the product is predominantly composed of recycling materials. The term does not include the following:
 - (A) The demolition of improvements to real estate.
 - (B) The processing of tangible personal property primarily for disposal in a licensed solid waste disposal facility rather than for sale.
 - (C) The collection of recycling materials.
 - (2) "Recycling materials" means tangible personal property, including metal, paper, glass, plastic, textile, or rubber, that:
 - (A) is considered "scrap" by industry standards or has no more than scrap value;
 - (B) is a byproduct of another person's manufacturing or production process;
 - (C) was previously manufactured or incorporated into a product;
 - (D) would otherwise reasonably be expected to be destined for disposal in a licensed solid waste disposal facility; or
 - (E) has been removed or diverted from the solid waste stream for sale, use, or reuse as raw materials, regardless of whether or not the materials require subsequent processing or separation from each other.
 - (3) "Processing of recycling materials" means:
 - (A) receiving recycling materials and other tangible personal property; and
 - (B) creating a product for sale by changing the original form, use, or composition of the property (whether manually, mechanically, chemically, or otherwise) through weighing, sorting, grading, separating, shredding, crushing, compacting, breaking, cutting, baling, shearing, torching, wire-stripping, or other means.
 - (4) "Occupationally engaged in the business of recycling" means to engage in recycling with the intention of doing so at a profit.
 - (5) "Recycling cart" means a manually propelled container with a capacity of not more than one hundred (100) gallons of recycling materials.
- (b) Transactions involving recycling materials and other tangible personal property are exempt from the state gross retail tax if:
 - (1) the person acquiring that property acquires it for the person's direct use in the processing of recycling materials; and
 - (2) the person acquiring that property is occupationally engaged in the business of recycling.
- (c) Notwithstanding subsection (a)(1)(C), transactions involving a recycling cart are exempt from the state gross retail tax if the person acquiring the recycling cart is occupationally engaged in the business of recycling.

The audit completed by the Department found that Taxpayer did not qualify for this exemption for two reasons. First, the audit states that Taxpayer's raw materials are not "recycling materials" because they are not scrap. Notably, the Taxpayer's scrap specifications manual includes descriptions of the chemical composition allowed in

the metals Taxpayer buys, as well as the size, density, and source restrictions.

The Indiana Tax Court discussed the requirements of scrap metal in *Brandenburg Indus. Serv. Co. v. Indiana Dep't of State Revenue*, 60 N.E.3d 300 (Ind. Tax Ct. 2016). Brandenburg removed metal from buildings being demolished and produced scrap metal. The Tax Court found that "Brandenburg's process substantially transforms the metal from obsolete, valueless, and unmarketable debris into newly marketable scrap steel." *Id.* at 307. In that case, the standards for scrap steel were dictated by the Scrap Specifications Circular, published by the Institute of Scrap Recycling Industries. *Id.* at 307. 306 n.7. This same guide is specifically referenced in Taxpayer's guide for scrap, and the two guides share terminology and requirements for quality and composition. Although Taxpayer requires specific composition and quality for metal it purchases, this does not mean that the metal is not scrap metal. The ISRI establishes industry standards for scrap metal, and the Taxpayer's standards correlate with these standards. Therefore, based on industry standards, Taxpayer purchases scrap metal based.

Second, the audit states that the Taxpayer was not engaged in the "processing of recycled materials" because it was not changing the original form, use, or composition of the metal it was purchasing. The audit notes instead that Taxpayer's raw material suppliers were changing the form of the metals sold to Taxpayer. But this does not preclude the Taxpayer from also changing the form of the metal it was purchasing.

IC § 6-2.5-5-45.8(a)(3)(B) explains that "the processing of recycled materials" requires "creating a product for sale by changing its original form." This can be done through sorting, grading, shredding, or one of several other listed methods. The statute also allows for "other means" of changing the form of the scrap metal. In this case, Taxpayer melts the scrap metal and casts or rolls it into steel products. This qualifies as a change in form accomplished by "other means" under IC § 6-2.5-5-45.8(a)(3)(B).

In conclusion, Taxpayer buys scrap metal, as defined by industry standards, which it uses directly in its process to manufacture salable steel products. Taxpayer is occupationally engaged in the business of recycling and thus qualifies for an exemption under IC § 6-2.5-5-45.8(b).

FINDING

Taxpayer's protest is sustained.

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