

Letter of Findings: 04-20191146
Gross Retail and Use Tax
For the Years 2015 and 2016

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

Out-of-State Medical Services Provider established that it was not required to pay use tax on payments for exempt services but did not establish that separately stated purchases of construction materials - supplied pursuant to time and material contracts - were also exempt. The Department agreed with Medical Services Provider it was not required to collect sales tax on transactions with two exempt public health agencies.

ISSUES

I. Gross Retail and Use Tax - Exempt Transactions.

Authority: IC § 6-2.5-2-1(a); IC § 6-2.5-3-1(a); IC § 6-2.5-3-2(a); IC § 6-2.5-3-2(e); IC § 6-2.5-4-9; IC § 6-2.5-8-8(a); IC § 6-2.5-13-1(d)(1); IC § 6-2.5-13-1(d)(2); IC § 6-8.1-5-1(c); *Indiana Dep't of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *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); *Rhoads v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044 (Ind. Tax Ct. 2002); [45 IAC 2.2-4-2](#) (November 2017, Retroactive eff. Jan 1, 2010).

Taxpayer states it was not required to pay sales tax or remit use tax on exempt transactions.

II. Gross Retail and Use Tax - Negligence Penalty.

Authority: IC § 6-8.1-5-1(c); IC § 6-8.1-10-2.1(a)(2); IC § 6-8.1-10-2.1(a)(3); IC § 6-8.1-10-2.1(d); [45 IAC 15-11-2\(b\)](#); [45 IAC 15-11-2\(c\)](#).

Taxpayer argues that the Department should exercise its authority to abate the ten-percent negligence penalty.

STATEMENT OF FACTS

Taxpayer is an out-of-state company, with locations in Indiana, in the business of providing services to medical care providers. Taxpayer sells its customers business forms, document management services, and various imaging and packaging services.

The Indiana Department of Revenue ("Department") conducted a sales and use tax audit of Taxpayer's business records, tax returns, and transaction records. The Department found that Taxpayer should have paid sales tax or self-assessed use tax on various transactions which took place during the years under audit. The audit resulted in the 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. Gross Retail and Use Tax - Exempt Transactions.

DISCUSSION

Taxpayer argues that it was not required to pay sales tax or self-assess use tax on six separate transactions for the reasons outlined below.

A. Service Only Transactions.

Taxpayer states it was not required to pay tax on a specific transaction on the ground that the transaction was one for services only and not for the purchase of tangible personal property.

1. Taxpayer's Burden.

Under IC § 6-8.1-5-1(c), "The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." Moreover, when a taxpayer challenges taxability in a specific instance, the taxpayer is required to provide documentation explaining and supporting its challenge. 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). When an agency is charged with enforcing a statute, the jurisprudence defers to the agency's reasonable interpretation of that statute "over an equally reasonable interpretation by another party." *Indiana Dep't of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579, 583 (Ind. 2014).

2. Indiana's Gross Retail Tax.

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). "When the product is received by the purchaser at a business location of the seller, the sale is sourced to that business location." IC § 6-2.5-13-1(d)(1). "When the product is not received by the purchaser at a business location of the seller, the sale is sourced to the location where receipt by the purchaser . . . occurs" IC § 6-2.5-13-1(d)(2).

3. Indiana's Complementary Use Tax.

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). "Use" means the "exercise of any right or power of ownership over tangible personal property." IC § 6-2.5-3-1(a).

In effect and practice, the use tax is generally functionally equivalent to the sales tax. See *Rhoads v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044, 1047 (Ind. Tax Ct. 2002). However, Indiana's use tax - not sales tax - allows an exemption for the "temporary storage" of tangible personal property delivered into Indiana but destined for use outside the state. IC § 6-2.5-3-2(e).

4. Exempt Services.

Taxpayer relies on [45 IAC 2.2-4-2](#) as authority for its position that these purchases are exempt from sales/use tax.

[45 IAC 2.2-4-2](#) provides as follows:

- (a) Professional services, personal services, and services in respect to property not owned by the person rendering such services are not "transactions of a retail merchant constituting selling at retail", and are not subject to gross retail tax. Where, in conjunction with rendering professional services, personal services, or other services, the serviceman also transfers tangible personal property for a consideration, this will constitute a transaction of a retail merchant constituting selling at retail unless:
 - (1) The serviceman is in an occupation which primarily furnishes and sells services, as distinguished from tangible personal property;
 - (2) The tangible personal property purchased is used or consumed as a necessary incident to the service;
 - (3) The price charged for tangible personal property is inconsequential (not to exceed 10[percent]) compared with the service charge; and
 - (4) The serviceman pays gross retail tax or use tax upon the tangible personal property at the time of acquisition.
- (b) Services performed or work done in respect to property and performed prior to delivery to be sold by a retail merchant must however, be included in taxable gross receipts of the retail merchant.
- (c) Persons engaging in repair services are servicemen with respect to the services which they render and retail merchants at retail with respect to repair or replacement parts sold.

(d) A serviceman occupationally engaged in rendering professional, personal or other services will be presumed to be a retail merchant selling at retail with respect to any tangible personal property sold by him, whether or not the tangible personal property is sold in the course of rendering such services. If, however, the transaction satisfies the four (4) requirements set forth in 6-2.5-4-1(c)(010), paragraph (1) [subsection (a) of this section], the gross retail tax shall not apply to such transaction.

The regulation on which Taxpayer depends, [45 IAC 2.2-4-2](#), contains a provision exempting the purchase of services from sales and use tax. [45 IAC 2.2-4-2\(a\)](#) states that, "Professional services, personal services, and services in respect to property not owned by the person rendering such services are not transactions of a retail merchant constituting selling at retail, and are not subject to gross retail tax." However, "Where, in conjunction with rendering professional services . . . the serviceman also transfers tangible personal property for a consideration, this will constitute a transaction of a retail merchant constituting selling at retail . . ." *Id.*

After reviewing the information provided, the Department is prepared to agree that Taxpayer has established it was not required to collect taxes on the following transaction. In this case, Taxpayer was selling its customer computer programming services not subject to sales tax.

- Lincoln National Life Insurance Co., \$1,100 Invoice 44637182

B. Improvements to Realty.

Taxpayer hired a Kentucky contractor to perform installation and maintenance work at one of its Indiana locations. The contractor charged Taxpayer for the labor costs and for the material costs on invoices which separately stated those two expenses. The Department assessed use tax on the material charges listed on the invoices.

Taxpayer argues that it is not required to pay sales or self-assess use tax on purchases of tangible personal property from the Kentucky vendor because the Kentucky vendor was required to pay tax to that state at the time it originally purchased the items. According to Taxpayer, the Department's assessment "would result in double taxation of those materials, and taxation of non-taxable labor."

IC § 6-2.5-4-9 provides in relevant part as follows:

- (a) A person is a retail merchant making a retail transaction when the person sells tangible personal property which:
- (1) is to be added to a structure or facility by the purchaser; and
 - (2) after its addition to the structure or facility, would become a part of the real estate on which the structure or facility is located.
- (b) A contractor is a retail merchant making a retail transaction when the contractor:
- (1) disposes of tangible personal property; or
 - (2) converts tangible personal property into real property;
- under a time and material contract. As such a retail merchant, a contractor described in this subsection shall collect, as an agent of the state, the state gross retail tax on the resale of the construction material and remit the state gross retail tax as provided in this article.

Sales Tax Information Bulletin 60 (November 2017, Retroactive eff. Jan. 1, 2010), [20180131-IR-045180051NRA](#), explains further:

Under Indiana law, contractors are retail merchants selling construction material when they (1) dispose of, or (2) convert construction material into real property under a time and material contract. Time and material contracts are contracts in which the cost of construction material and the cost of labor or other charges are stated separately. Because all sales of tangible personal property, including sales of construction material, are taxable, contractors converting construction material into real property under a time and material contract must collect and remit sales tax on the material portion of their contracts.

In this case, Indiana law required that the contractor collect Indiana sales tax on the enumerated sales of tangible personal property sold pursuant to a time and materials construction contract. Because the contractor failed to do so, the Department's audit was correct in assessing Indiana's complimentary use tax. The fact that a different but separate tax was imposed on upstream transactions relieves neither the contractor nor Taxpayer of their responsibility.

C. Exemption Certificates.

Taxpayer sold tangible personal property to two Indiana public health Departments. The Department assessed tax because "[T]axpayer did not have a valid exemption certificate on file." IC § 6-2.5-8-8(a) provides:

A person, authorized under subsection (b), who makes a purchase in a transaction which is exempt from the state gross retail and use taxes, may issue an exemption certificate to the seller instead of paying the tax. The person shall issue the certificate on forms and in the manner prescribed by the department. A seller accepting a proper exemption certificate under this section has no duty to collect or remit the state gross retail or use tax on that purchase.

In this case, Taxpayer provided exemption certificates for the two public health entities. The Department agrees that there is sufficient information to establish that Taxpayer's transactions with the Marshal and Randolph County health departments were exempt from sales tax.

FINDING

Taxpayer's sales to Lincoln National Life Insurance and to the Marshal and Randolph County health departments were exempt and Taxpayer's protest of the Department's assessment of tax is sustained. In all other respect, Taxpayer's protest is denied.

II. Gross Retail and Use Tax - Negligence Penalty.

DISCUSSION

Taxpayer states that it is entitled to abatement of the Department's ten-percent "negligence" penalty. Taxpayer points to its "compliant filing and payment history."

IC § 6-8.1-10-2.1(a)(3) requires that a ten-percent penalty be imposed if the tax deficiency results from the taxpayer's negligence. IC § 6-8.1-10-2.1(a)(2) requires a ten-percent penalty if the taxpayer "fails to pay the full amount of tax shown on the person's return on or before the due date for the return or payment."

IC § 6-8.1-10-2.1(d) states that, "If a person subject to the penalty imposed under this section can show that the failure to . . . pay the full amount of tax shown on the person's return . . . or pay the deficiency determined by the department was due to reasonable cause and not due to willful neglect, the department shall wave the penalty."

Departmental regulation [45 IAC 15-11-2](#)(b) defines negligence as "the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." Negligence is to "be determined on a case-by-case basis according to the facts and circumstances of each taxpayer." *Id.*

Departmental regulation [45 IAC 15-11-2](#)(c) requires that in order to establish "reasonable cause," the taxpayer must demonstrate that it "exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed"

Under IC § 6-8.1-5-1(c), "The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." An assessment - including the negligence penalty - is presumptively valid.

The Department believes that taxpayer erred in determining its sales and use tax liability. However, there is little indication that Taxpayer's determinations were so egregious as to constitute "willful neglect." Based on a "case-by-case" analysis and after reviewing "the facts and circumstances of each taxpayer" the Department agrees that the ten-percent negligence penalty should be abated.

FINDING

Taxpayer's protest is sustained.

SUMMARY

Taxpayer's challenge to the assessment of tax on payments for the exempt service transactions and sales to the two health departments is sustained as set out in Part I above. The Department agrees that the ten-percent

negligence penalty should be abated. The remaining portion of Taxpayer's protest is respectfully denied.

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