

Letter of Findings: 04-20200338
Use Tax
For the Tax Years 2016-2018

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 This document is effective as of its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

Corporation's lowboy trailer, purchased in 2017, is subject to Indiana use tax because it was only used to transport production equipment and is not itself production equipment.

ISSUE

I. Use Tax - Manufacturing Exemption.

Authority: IC § 6-2.5-3-2; IC § 6-8.1-5-1; *Indiana Dept. of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dept. of State Revenue*, 867 N.E.2d 289 (Ind. Tax Ct. 2007); *Dept. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Merch. Warehouse Co. v. Indiana Dep't of State Revenue*, 87 N.E.3d 12, (Ind. 2017); *Indiana Dep't of State Revenue v. Cave Stone, Inc.*, 457 N.E.2d 520, (Ind. 1983); *Dep't of Revenue v. U. S. Steel Corp.*, 425 N.E.2d 659 (Ind. Ct. App. 1981); *State, Dep't of Revenue v. Calcar Quarries, Inc.*, 394 N.E.2d 939 (1979); [45 IAC 2.2-3-4](#); [45 IAC 2.2-5-4](#); [45 IAC 2.2-5-6](#); [45 IAC 2.2-5-8](#).

Taxpayer protests the imposition of use tax on the purchase of a lowboy trailer.

STATEMENT OF FACTS

Taxpayer is a trucking and excavating company based in Indiana. As the result of an audit, the Indiana Department of Revenue ("Department") assessed use tax on several items purchased by Taxpayer. The Department therefore issued proposed assessments for use tax for the years 2016-2018. Taxpayer only protested the use tax assessed on the purchase of a lowboy trailer. The Department held an Administrative hearing and this Letter of Findings results. Further facts will be provided as necessary.

I. Use Tax - Manufacturing Exemption.

DISCUSSION

Taxpayer protests the Department's proposed assessment of use tax for a lowboy trailer. Taxpayer uses the trailer to transport Taxpayer's wood grinder to local sawmills and other sites where the grinding process for mulch production begins. Taxpayer grinds the logs down to large chips and then the chips are hauled back to Taxpayer's facilities. The grinder never leaves the lowboy and cannot be transported to the sawmills and other sites without the lowboy. In the audit, the Department reasoned that Taxpayer only used the lowboy to transport the wood grinder and it is neither directly involved in the manufacturing process nor does it have an immediate effect in the direct production of mulch or wood chips. Put simply, the Department determined that the lowboy does not do the grinding or change the product's physical nature.

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 shall be entitled to deference.

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, the purchase and/or use of tangible personal property is subject to sales or use tax unless an applicable exemption exists.

[45 IAC 2.2-5-8](#) in relevant parts provided:

(a) In general, all purchases of tangible personal property by persons engaged in the direct production, manufacture, fabrication, assembly, or finishing of tangible personal property are taxable. The exemption provided in this regulation [[45 IAC 2.2](#)] extends only to manufacturing machinery, tools, and equipment directly used by the purchaser in direct production. It does not apply to material consumed in production or to materials incorporated into tangible personal property produced.

(b) The state gross retail tax does not apply to sales of manufacturing machinery, tools, and equipment to be directly used by the purchaser in the direct production, manufacture, fabrication, assembly, or finishing of tangible personal property.

(c) The state gross retail tax does not apply to purchases of manufacturing machinery, tools, and equipment to be directly used by the purchaser in the production process provided that such machinery, tools, and equipment are directly used in the production process; i.e., *they have an immediate effect on the article being produced. Property has an immediate effect on the article being produced* if it is an essential and integral part of an integrated process which produces tangible personal property.

(d) Pre-production and post-production activities. "Direct use in the production process" begins at the point of the first operation or activity constituting part of the integrated production process and ends at the point that the production has altered the item to its completed form, including packaging, if required.

(f) Transportation equipment.

(1) Tangible personal property used for moving raw materials to the plant prior to their entrance into the production process is taxable.

(2) Tangible personal property used for moving finished goods from the plant after manufacture is subject to tax.

(3) Transportation equipment used to transport work-in-process or semi-finished materials to or from storage is not subject to tax if the transportation is within the production process.

(4) Transportation equipment used to transport work-in-process, semi-finished, or finished goods between plants is taxable, if the plants are not part of the same integrated production process.

(g) "Have an immediate effect upon the article being produced": Machinery, tools, and equipment which are used during the production process and which have an immediate effect upon the article being produced are exempt from tax. Component parts of a unit of machinery or equipment, which unit has an immediate effect on the article being produced, are exempt if such components are an integral part of such manufacturing unit. *The fact that particular property may be considered essential to the conduct of the business of manufacturing because its use is required either by law or by practical necessity does not itself mean that the property "has*

an immediate effect upon the article being produced". Instead, in addition to being essential for one of the above reasons, the property must also be an integral part of an integrated process which produces tangible personal property.

(Emphasis added).

[45 IAC 2.2-5-8\(a\)](#) provides that, generally, purchases of tangible personal property by persons engaged in the direct production of tangible personal property are taxable. However, transactions of equipment directly used by the purchaser in the direct production or of tangible personal property is not subject to tax. The question is whether Taxpayer uses it in the direct production of the mulch. The phrase "directly used in direct production" means that the property must be integral and essential to the production process. The Court in *Merch. Warehouse Co. v. Indiana Dep't of State Revenue* explained that, "[C]onsidering Indiana law comprehensively, we distill that 'direct production' involves those essential and integral steps necessary to transform tangible personal property into a distinct marketable good, i.e., the good actually marketed to the consumer." *Merch. Warehouse Co. v. Indiana Dep't of State Revenue*, 87 N.E.3d 12, 18 (Ind. 2017). In addition, a test for directness which requires the equipment to have an immediate link with the product being produced. *Dep't of Revenue v. U. S. Steel Corp.*, 425 N.E.2d 659, 662 (Ind. Ct. App. 1981). Taxpayer argues that lowboy is essential and integral, the grinder cannot be used without it and thus the trees cannot be ground.

There is further guidance in determining whether the transportation by the lowboy is an integral part of the production or processing of the mulch. The Court in *Indiana Dep't of State Revenue v. Cave Stone, Inc.*, 457 N.E.2d 520, (Ind. 1983) held that the truck at issue in that case was directly used by the taxpayer in the direct production, manufacture, mining, processing or finishing of tangible personal property. The transportation equipment was essential to the achievement of a transformation of the crude stone into aggregate stone because it was transporting "in process" materials. *Id at 524.*

State, Dep't of Revenue v. Calcar Quarries, Inc., helps to explain when transportation equipment is exempt. In that decision, the court explained the application of the manufacturing exemption, holding that equipment (1) used in an integrated operation (stone, concrete, and asphalt operations), (2) to transport unfinished work in process (stone), (3) from one production step to another (from quarry to stockpiles to crusher to a hot asphalt plant or a ready mix concrete facility) is exempt. *State, Dep't of Revenue v. Calcar Quarries, Inc.*, 394 N.E.2d 939, 941 (1979).

Here, the lowboy is not used to transport the unfinished product. While it does transport a machine that is integral to the production product, the lowboy itself has no direct impact on the mulch being produced. The truck in *Cave Stone* was moving the product from one production stage to another, thus having some sort of direct immediate impact. The lowboy is equipment used by the purchaser but not directly used in the direct production of the mulch as required in [45 IAC 2.2-5-8\(b\)](#). Although the lowboy may be essential, the lowboy does not have an immediate effect on the mulch and is not an integral part of an integrated process which produces tangible personal property as required in [45 IAC 2.2-5-8\(g\)](#) and explained in *Cave Stone* and *Calcar Quarries, Inc.* Taxpayer has not met its burden under IC § 6-8.1-5-1(c).

FINDING

Taxpayer's protest is denied.

February 23, 2021

Posted: 04/28/2021 by Legislative Services Agency
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