

**Final Order Denying Refund: 04-20200319**  
**Gross Retail and Use Tax**  
**For the Years 2016, 2017, and 2018**

**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**

The Department disagreed with Retailer that it was entitled to a refund of sales tax paid on the purchase, delivery, and installation of a warehouse conveyor system; the conveyor system consisted of tangible personal property purchased and paid for on a time-and-material basis, and there was not sufficient evidence to grant a refund on any of the contractor's exempt engineering services or installation costs.

**ISSUES**

**I. Gross Retail Tax - Purchase and Installation of a Warehouse Conveyor System.**

**Authority:** IC § 6-2.5-2-1; IC § 6-2.5-4-1; IC § 6-2.5-4-9; *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); [45 IAC 2.2-3-8](#); [45 IAC 2.2-3-9](#); [45 IAC 2.2-4-2](#); [45 IAC 2.2-4-3](#); [50 IAC 4.2-4-10](#); Sales Tax Information Bulletin 92 (December 2019); Sales Tax Information Bulletin 60 (July 2021); Sales Tax Information Bulletin 60 (October 2020); Sales Tax Information Bulletin 60 (November 2017).

Taxpayer argues that the Department erred in denying it a refund of sales tax paid on the purchase, delivery, and installation of a warehouse conveyor system.

**STATEMENT OF FACTS**

Taxpayer is an out-of-state company which operates retail stores in Indiana and other states. Taxpayer operates a distribution center in Indiana. Taxpayer hired a company to remove the center's existing conveyor system and install a replacement conveyor system along with the necessary control devices. Taxpayer submitted a refund claim (Form GA-110L) for approximately \$540,000. Taxpayer argued that it should not have paid sales tax on the cost of the conveyor system because the completed installation was an addition to its distribution center building and because Taxpayer, as the purchaser, could have purchased the conveyor exempt.

The Indiana Department of Revenue ("Department") reviewed Taxpayer's refund request and issued an "Explanation of Adjustments" granting a refund of approximately \$46,000 but denying the remaining \$494,000. The Department denied the majority of the refund on the ground that Taxpayer's distribution center was not a manufacturing facility.

Taxpayer disagreed with the Department's decision and submitted a protest to that effect. An administrative hearing was conducted by video conference during which Taxpayer's representatives explained the basis for the protest.

**I. Gross Retail Tax - Purchase and Installation of a Warehouse Conveyor System.**

**DISCUSSION**

Taxpayer argues in its protest it is entitled to a refund of sales tax paid on the purchase of the conveyor system on the ground that it entered into a "lump sum" contract with the conveyor company ("Contractor"). Taxpayer explains:

The charges relate directly to the installation [of] a custom conveyor installed in [Taxpayer's distribution center] . . . [Taxpayer's] agreement with [Contractor] was for a lump sum contract that included engineering, manufacturing and installation services, and materials. A construction contractor is liable for sales and use

tax on construction materials purchased under a lump sum contract. A lump sum contract is a contract in which all charges are quoted as a single price. [Taxpayer] has provided the contract and pricing breakdown as evidence that these are transactions [that] are related to a lump sum contract.

In addition, Taxpayer argues that the conveyor system was exempt because it was an improvement to real property. As explained by Taxpayer:

Indiana exempts purchases involved in improvements made to real property by contractors. Improvements include new installations and repair or improvements to real property. Indiana considers construction materials that are affixed to land (e.g., electrical equipment, garage doors, doors, disposal systems, carpeting, fencing, HVAC) to be real property. Under this analysis, the entire conveyor project was done specifically to [Taxpayer's] requirements and [Taxpayer] was the owner of materials the entire time the project was underway.

Taxpayer offers an alternative argument stating that a substantial portion of the cost paid its Contractor was for installation and other exempt services. Under Taxpayer's analysis, because services are not subject to Indiana's sales tax, it should receive any sales tax paid for those services.

### **A. Taxpayer's Burden in Claiming a Refund**

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).

### **B. 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). A retail transaction occurs when a retail merchant, in the ordinary course of his regularly conducted trade or business, "(1) acquires tangible personal property for the purpose of resale; and (2) transfers that property to another person for consideration." IC § 6-2.5-4-1(a). The purchaser of the tangible personal property is liable for the sales tax. IC § 6-2.5-2-1(b).

At the outset, the Department takes note - and Taxpayer agrees - that the conveyor system does not qualify for the manufacturing exemption under IC § 6-2.5-4-9 and [45 IAC 2.2-3-8](#) because the conveyor system is not used in direct production, does not have an immediate effect on the items being transported within the warehouse, and is not part of an integrated production process.

### **C. Sales Tax Exemption for the Purchase of Materials Incorporated into Real Property.**

Taxpayer primarily argues that tangible personal property (the conveyor system) incorporated into real property (the distribution center) is not subject to sales/use tax in Indiana. Indiana law and the Indiana Administrative Code address this issue. IC § 6-2.5-4-9 provides 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.
- (c) Notwithstanding subsections (a) and (b), a transaction described in subsection (a) or (b) is not a retail transaction if the ultimate purchaser or recipient of the property to be added to a structure or facility would be exempt from the state gross retail and use taxes if that purchaser or recipient had directly purchased the property

from the supplier for addition to the structure or facility. (Effective January 1, 2010).

In addition, [45 IAC 2.2-3-8](#) provides:

(a) In general, all sales of tangible personal property are taxable, and all sales of real property are not taxable. The conversion of tangible personal property into realty does not relieve the taxpayer from a liability for any owing and unpaid state gross retail tax or use tax with respect to such tangible personal property.

(b) All *construction material* purchased by a contractor is taxable either at the time of purchase, or if purchased exempt (or otherwise acquired exempt) upon disposition unless the ultimate recipient could have purchased it exempt. (*Emphasis added*).

"Construction material" is explained at Sales Tax Information Bulletin 60 (July 1, 2021), [20210728-IR-045210297NRA](#), which states the "construction material" includes:

[A]ny tangible personal property to be converted into real property. Examples of construction material that may be converted into real property through incorporation or installation include, but are not limited to: doors, garage doors, windows, cabinets, garbage disposals, water heaters, water softeners, alarms, furnaces, central air conditioning units, gutters, carpeting and other flooring materials, drywall, lumber, asphalt, concrete, fencing, trees, shrubbery, and pre-fabricated construction material.

The Bulletin further explains:

Construction material has been converted into real property when it has been attached to or incorporated into real property in such a way that would lead one to reasonably believe the construction material has been *permanently affixed to the real property*. Construction material incorporated into real property becomes part of and *indistinguishable from the real property* into which it has been incorporated. *Id.* (*Emphasis added*),

(See also Sales Tax Information Bulletin 60 (October 2020), 20201202-Ind. Reg.-045200596NRA and Sales Tax Information Bulletin 60 (November 2017), 20180131 Ind. Reg. 045180051NRA).

#### **D. Real Property Contracts.**

Taxpayer cites to [50 IAC 4.2-4-10\(c\)](#) for its definition of "real property" contracts. The regulation explains in small part that:

The use of a unit of machinery, equipment, or a structure determines its classification as real or personal property. If the unit is directly used for manufacturing or a process of manufacturing, it is personal property. If the unit is a land or building improvement, it is real property.

The regulation thereafter stipulates that "retaining walls," "wharves and docks," and railroad "bridges and trestles" are defined as "real property." "Real property," according to the regulation, includes building foundations, walls, floors, roofs, air conditioning, and elevators. On the issue of "conveyors," the regulation is less than helpful; some conveyors are real property, and some are personal property.

Finally, the property tax regulations are irrelevant in resolving what is purely an Indiana sales tax issue. The property tax regulations and definitions are - at most - informative.

#### **E. Analysis and Conclusion.**

The first issue is whether the "tangible personal property" (wires, rollers, belts, motors, etc.) used to construct the conveyor system is or is not subject to sales tax. Both the Department and Taxpayer agree that the completed conveyor system is not easily moved and that it was custom designed and built to perform very specific functions at a very specific location. However, it is also fair to note that the distribution center's previous conveyor system was removed and - given the passage of time and technology - the current system may well also be replaced without necessarily changing or disturbing the distribution building itself.

The contract between Contractor and Taxpayer is not a lump sum contract. If it were a lump sum contract, Contractor would have been paying sales tax on each nut, bolt, and roller it purchased. In addition, the contract and "statement of work" speaks for themselves on this issue by differentiating prices Contractor charged for such line items as "mechanical equipment," "control[] equipment," "mechanical engineering," and "project management."

The Department's regulation, [45 IAC 2.2-3-8](#) is clear on the issue stating that "the conversion of tangible personal property into realty does not relieve the taxpayer from a liability for . . . unpaid state gross retail tax or use tax." The regulation provides either a vendor or its customer pays the tax on purchases of non-exempt tangible personal property.

[45 IAC 2.2-3-9\(d\)](#) is also relevant in part providing:

A contractor-retail merchant has the responsibility to collect the state gross retail tax and to remit such tax to the Department of Revenue whenever he disposes of any construction material in the following manner:

- (1) Time and material contract. He converts the construction material into realty on land he does not own and states separately the cost for the construction material and the cost for the labor and other charges (only the gross proceeds from the sale of the construction materials are subject to tax), or
- (2) Construction material sold over the counter. Over the counter sales of construction materials will be treated as exempt from the state gross retail tax only if the contractor receives a valid exemption certificate issued by the person for whom the construction is being performed or by the customer who purchases over the counter, or a direct pay permit issued by the customer who purchases over the counter.

Even if one were to accept Taxpayer's argument that the conveyor system has become part-and-parcel with - and is now indistinguishable from the distribution building - "tangible personal property" incorporated into realty is subject to Indiana's sales/use tax laws unless Taxpayer - as the ultimate recipient - could have purchased the property exempt.

The second issue is whether Taxpayer is entitled to a partial refund because Taxpayer was paying for exempt services or installation charges.

[45 IAC 2.2-4-2](#) contains a provision exempting the purchase of services from sales 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.*

The Department classifies "installation" costs as exempt services. Sales Tax Information Bulletin 92 (December 2019), 20200401-Ind. Reg.-045200169NRA, provides:

Separately stated charges for installation that occurs after delivery and transfer of the tangible personal property are not subject to sales tax. Installation charges that are not separately stated from the selling price of an item or the delivery charge for an item are subject to sales tax.

However, [45 IAC 2.2-4-3\(a\)](#) distinguishes "delivery" services.

Separately stated delivery charges are considered part of selling at retail and subject to sales and use tax if the delivery is made by or on behalf of the seller of property not owned by the buyer.

Assuming that - as Taxpayer explains - it "owned the property prior to installation," Taxpayer would have owed sales tax on those charges but not for charges which are distinguishable as exempt "professional services."

A review of the individual vendor invoices is not particularly helpful because the invoices simply list undifferentiated charges for such items as "Engineering & Manufacturing" and "Installation & Manufacturing." It is not possible to distinguish exempt engineering services or exempt installation charges. The Department agrees that payments for services are not subject to sales tax; the Department agrees that charges for installation costs are not subject to sales tax. However, given the manner in which Taxpayer and Contractor entered into the agreement and the manner in which Taxpayer was billed, the Department finds itself unable to agree that Taxpayer has clearly established the purchase of the tangible personal property was exempt from tax and unable to agree that there is sufficient evidence establishing that any particular portion of the tax was clearly attributable to exempt "services" or "installation."

## FINDING

Taxpayer's protest is respectfully denied.

October 14, 2021

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