

**Memorandum of Decision 04-20221056**  
**Gross Retail Tax**  
**for the Year 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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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 Memorandum of Decision.

**HOLDING**

The Department erred in its analysis of Boat Manufacturer's request seeking a refund of use tax paid on its purchase of "materials and tools"; the Department erroneously evaluated the refund based on the credit provided against Indiana's income tax while Boat Manufacturer based its claim on the research and development sales tax exemption.

**ISSUE**

**I. Gross Retail Tax - Research and Development Property.**

**Authority:** IC §§ 6-2.5-5 et seq.; IC § 6-2.5-5-40; IC § 6-3-1-1; IC §§ 6-3.1-4-1 et seq.; IC § 6-3.1-4-1; [45 IAC 2.2-3-14](#); [45 IAC 2.2-5-3](#); [45 IAC 2.2-5-6](#); [45 IAC 2.2-5-8](#); [45 IAC 2.2-5-9](#); [45 IAC 2.2-5-10](#); Sales Tax Information Bulletin 75 (April 2017).

Taxpayer argues it was not required to pay sales or use tax on the purchase of certain equipment and supplies on the ground that the items qualify for the research and development sales tax exemption.

**STATEMENT OF FACTS**

Taxpayer is an Indiana company in the business of designing, building, and selling recreational boats. Taxpayer submitted a refund request by means of the Department of Revenue's ("Department") form GA-110L. Taxpayer requested a refund of approximately \$6,300 in Indiana's sales/use tax on the ground that Taxpayer had erroneously self-assessed tax on purchases of various items. Taxpayer explained:

Taxpayer incorrectly self-assessed use tax on purchases of research development property - IC § 6-2.5-5-40. Amended Returns Copies of the Use Tax Accruals and Refund Spreadsheet attached. Invoices will be sent electronically via pdf upon request.

The Department reviewed the request and, in a letter dated June 7, 2021, denied the refund explaining as follows:

[T]axpayer is requesting a refund for use tax paid on materials and tools utilized in its research in its research and development of new and improved pontoons.

[M]ost of the purchases are indicative of a new prototype that is soon to be manufactured once it's past testing. However, a purchase of a competitor's pontoon boat would be exclusive from being a qualified supply.

Thereafter, the June 7 letter cited to IC § 6-3.1-4 and I.R.C. § 174 as authority for denying the refund. The letter explained:

Treasury Regulation § 174 which would disallow this as the purchaser of a competitor's model would not be a qualified supply. The same regulations apply to Indiana, more information will be needed before I can complete the claim. The taxpayer had purchased a console from a competitor to take apart and review how it was made. Additionally other items such as packing supplies, and boat covers which would not be afforded the exemption since they are not part of the pontoon.

Taxpayer disagreed with the Department's decision denying the refund and submitted a protest to that effect. An

administrative hearing was conducted by telephone during which Taxpayer's representative explained the basis for the protest. This Memorandum of Decision results.

## I. Gross Retail Tax - Research and Development Property.

### DISCUSSION

The issue is whether the Department erred in its evaluation of both Taxpayer's refund request and the grounds under which the refund was originally requested.

According to Taxpayer, it incorrectly self-assessed use tax on the acquisition of items which qualified as "purchases of research and development property. . . ." Specifically, Taxpayer cited to the exemption provided under IC § 6-2.5-5-40.

At the outset and as a general rule, all purchases of tangible personal property - including parts used to build boats - are subject to sales or use tax unless specifically exempted by statutes or regulations. [45 IAC 2.2-5-3\(b\)](#); [45 IAC 2.2-5-6\(a\)](#); [45 IAC 2.2-5-8\(a\)](#); [45 IAC 2.2-5-9\(a\)](#); [45 IAC 2.2-5-10\(a\)](#). Various sales tax exemptions are outlined in IC §§ 6-2.5-5 et seq. which are also applicable to use tax. [45 IAC 2.2-3-14\(2\)](#).

In this case, Taxpayer relies on the exemption found at IC § 6-2.5-5-40 which states:

(a) As used in this section, "research and development activities" includes design, refinement, and testing of prototypes of new or improved commercial products before sales have begun for the purpose of determining facts, theories, or principles, or for the purpose of increasing scientific knowledge that may lead to new or enhanced products. The term does not include any of the following:

- (1) Efficiency surveys.
- (2) Management studies.
- (3) Consumer surveys.
- (4) Economic surveys.
- (5) Advertising or promotions.
- (6) Research in connection with nontechnical activities, including literary, historical, social sciences, economics, humanities, psychology, or similar projects.
- (7) Testing for purposes of quality control.
- (8) Market and sales research.
- (9) Product market testing, including product testing by product consumers or through consumer surveys for evaluation of consumer product performance or consumer product usability.
- (10) The acquisition, investigation, or evaluation of another's patent, model, process, or product for the purpose of investigating or evaluating the value of a potential investment.
- (11) The providing of sales services or any other service, whether technical or nontechnical in nature.

(b) As used in this section, "research and development equipment" means tangible personal property that:

- (1) consists of or is a combination of:
  - (A) laboratory equipment;
  - (B) computers;
  - (C) computer software;
  - (D) telecommunications equipment; or
  - (E) testing equipment;
- (2) has not previously been used in Indiana for any purpose; and
- (3) is acquired by the purchaser for the purpose of research and development activities devoted directly to experimental or laboratory research and development for:
  - (A) new products;
  - (B) new uses of existing products; or
  - (C) improving or testing existing products.

(c) As used in this section, "research and development property" means tangible personal property that:

- (1) has not previously been used in Indiana for any purpose; and
- (2) is acquired by the purchaser for the purpose of research and development activities devoted to experimental or laboratory research and development for:
  - (A) new products;
  - (B) new uses of existing products; or
  - (C) improving or testing existing products.

(d) For purposes of subsection (c)(2), a research and development activity is devoted to experimental or laboratory research and development if the activity is considered essential and integral to experimental or

laboratory research and development. The term does not include activities incidental to experimental or laboratory research and development.

(e) For purposes of subsection (c)(2), an activity is not considered to be devoted to experimental or laboratory research and development if the activity involves:

- (1) heating, cooling, or illumination of office buildings;
- (2) capital improvements to real property;
- (3) janitorial services;
- (4) personnel services or accommodations;
- (5) inventory control functions;
- (6) management or supervisory functions;
- (7) marketing;
- (8) training;
- (9) accounting or similar administrative functions; or
- (10) any other function that is incidental to experimental or laboratory research and development.

(f) A retail transaction:

- (1) involving research and development equipment; and
- (2) occurring after June 30, 2007, and before July 1, 2013; is exempt from the state gross retail tax.

(g) A retail transaction:

- (1) involving research and development property; and
- (2) occurring after June 30, 2013;

is exempt from the state gross retail tax.

(h) The exemption provided by subsection (g) applies regardless of whether the person that acquires the research and development property is a manufacturer or seller of the new or existing products specified in subsection (c)(2).

The Department's evaluation of Taxpayer's request was based on IC §§ 6-3.1-4-1 et seq. which provides a research and development ("R&D") credit "against any tax otherwise due and payable under [IC 6-3](#)." IC § 6-3.1-4-1. The reference to "[IC 6-3](#)" describes Indiana's "Adjusted Gross Income Tax." IC § 6-3-1-1.

In this particular case, the Department and Taxpayer were talking past each other. Taxpayer sought a refund of sales/use tax, but the Department responded by addressing whether or not the items were or were not entitled to a R&D credit against Indiana's adjusted gross income tax provisions. The Department's Sales Tax Information Bulletin 75 (April 2017), 20170726 Ind. Reg. 045170335NRA, explains as follows:

[T]he rules applicable to the sales tax exemption for research and development property and the rules applicable to the credit for increasing research expenses under [IC 6-3.1-4](#) are not identical. While some categories of expenses would qualify for both, the sales tax exemption and income tax credit *have somewhat different provisions which may permit qualification for either the exemption or the credit but not both.* (*Emphasis added*).

Taxpayer purchased and presumably self-assessed use tax on "materials and tools" such as:

Prototype Fuel Tank Tester  
Hose, T-Bolt, Coupling  
Center Counsel R&D  
Tooling Charges  
52 Gal. FL MFT Port Side/Sample

Despite both Taxpayer and the Department's best intentions to the contrary, this MOD has no basis on which to determine whether or not these and numerous other "materials and tools" are or are not entitled to the IC § 6-2.5-5-40 sales tax exemption. The Department did not render a decision addressing the question Taxpayer presented but denied the refund based upon an incorrect application of Indiana law.

On the sole issue of whether or not the Department's decision denying the refund - based upon the grounds Taxpayer presented - was correct, Taxpayer's protest is sustained.

### FINDING

For the specific reasons noted above, Taxpayer's protest is sustained.

*Posted: 04/26/2023 by Legislative Services Agency*  
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