

Letter of Findings: 04-20231276
Gross Retail and Use Tax
For the Years 2018 to 2020

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

Combination Convenience Store/Gas Station met its burden of establishing that the Department's audit assessment of sales tax should be adjusted to reflect the amount of exempt purchases recorded on its convenience store register.

ISSUE

I. Gross Retail and Use Tax - Convenience Store and Fast-Food Restaurant Sales.

Authority: [IC 6-2.5-1-2](#); [IC 6-2.5-2-1](#); [IC 6-2.5-3-2](#); [IC 6-2.5-4-1](#); [IC 6-2.5-5](#) et seq.; [IC 6-2.5-5-34](#); [IC 6-2.5-9-3](#); [IC 6-8.1-5-1](#); [IC 6-8.1-5-4](#); *Dep't. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289 (Ind. Tax Ct. 2007); [45 IAC 15-5-1](#); *Indiana Tax Handbook for New and Small Business Owners*, <https://www.in.gov/dor/files/new-small-business-handbook.pdf>.

Taxpayer argues that the Department's assessment of additional sales tax is excessive on the ground that the Department's Audit misunderstood the financial relationship between its convenience store sales and its restaurant sales.

STATEMENT OF FACTS

Taxpayer is an Indiana business operating a combined convenience/gas station store (hereinafter "Convenience Store") and fast-food restaurant. The Convenience Store and restaurant conduct business under the same roof. Taxpayer's customers move freely between the Convenience Store and the restaurant and conduct business in both venues. The Convenience Store sells motor fuel, accepts food stamps, sells lottery tickets, sells cigarettes, items which are subject to sales tax, and items which are exempt from sales tax.

The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayer's business records including federal and state income tax returns, bank statements, purchase invoices, cash register tapes, "cash paid out" slips, and the financial reports provided by Taxpayer's accountant.

Pursuant to the audit, the Department assessed additional sales tax. Taxpayer disagreed with the assessment and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representative explained the basis for the protest. This Letter of Findings results.

I. Gross Retail and Use Tax - Convenience Store and Fast-Food Restaurant Sales.

DISCUSSION

The issue is whether Taxpayer has met its burden of establishing that the Department made a mistake when it calculated the amount of exempt Convenience Store sales, and - because of that mistake - the sales tax assessment is wrong.

For clarity's sake, the Department here points out that the amount of restaurant sales is not at issue and is irrelevant except for the necessity of excluding restaurant sales from sales which were recorded at and included in the Convenience Store's register.

A. Taxpayer's Burden of Proof.

As a threshold issue, it is the Taxpayer's responsibility to establish that the sales 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 Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463, 466 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't 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. The Department points out that, "[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.'" *Dep't. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579, 583 (Ind. 2014). Thus, interpretations of Indiana tax law contained within this decision, as well as the preceding audit, are entitled to deference.

B. Indiana's Sales and Use Tax.

Pursuant to [IC 6-2.5-2-1](#), a sales tax, known as state gross retail tax, is imposed on retail transactions made in Indiana unless a valid exemption is applicable. [IC 6-2.5-5](#) et seq. Retail transactions involve the transfer of tangible personal property. [IC 6-2.5-1-2](#); [IC 6-2.5-4-1](#).

A retail merchant - such as a convenience store - is required to "collect the tax as agent for the state." [IC 6-2.5-2-1\(b\)](#). The retail merchant "holds those taxes in trust for the state and is personally liable for the payment of those taxes" [IC 6-2.5-9-3](#).

A complementary 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. [IC 6-2.5-3-2](#).

C. Taxpayer's Record Keeping Responsibility.

Taxpayers are required to keep and maintain business records. "Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for tax by reviewing those books and records." [IC 6-8.1-5-4\(a\)](#). In addition, [IC 6-8.1-5-4\(c\)](#) provides that, "A person must allow inspection of the books and records and returns by the department or its authorized agents at all reasonable times."

In the absence of contemporaneous records, the Department is required by law to issue an assessment based upon whatever alternative means may be available. [IC 6-8.1-5-1\(b\)](#) provides in relevant part that "[i]f the [D]epartment reasonably believes that a person has not reported the proper amount of tax due, the [D]epartment shall make a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the [D]epartment." (*Emphasis added*). See also [45 IAC 15-5-1](#).

D. Audit Findings and Assessment Based on the Information Available.

The Department's audit report indicates that Taxpayer reports Convenience Store and restaurant total sales on the same form ST-103 but "keeps separate books and bank accounts for [the] fast food restaurant and convenience store sales."

The Department's audit concluded that "[a] review of the [T]axpayer's sales tax register reports for the [Convenience Store] indicated that the [T]axpayer's point-of-sale system was not reliable when identifying the correct break-out of taxable versus non-taxable sales."

The Department's audit found that the records presented "were not reliable" for the following reason: Taxpayer operated one cash register in the convenience store and another in the restaurant. The distinction between restaurant transactions and convenience store sales was not readily apparent because Taxpayer operated multiple cash registers and intermingled exempt and non-exempt transactions.

The Department's audit report describes more fully the apparent difficulty.

When a customer purchases a [restaurant] sandwich and also another item from the convenience store, the

[T]axpayer enters the [restaurant] sale in the [restaurant] register and provides a ticket to the customer to pay at the convenience store. The [customer] pays for the total transaction at the convenience store register. Due to the fact [that restaurant] sales were enter[ed] in the [restaurant] register, the [restaurant] sales paid for at the convenience store are treated as exempt sales.

Taxpayer reported its combined total sales on form ST-103 (Indiana Sales and Use Tax Voucher). That form contains a line which reflects "gross sales." In Taxpayer's case, the line reflected the combined Convenience Store sales and restaurant sales. The audit's task was to first review Convenience Store sales and differentiate the amount of taxable Convenience Store sales and the amount of exempt Convenience Store sales. The audit report explains how the audit arrived at that distinction.

The auditor calculated the [Convenience Store] receipts as follows: [Restaurant] sales and Negative [Restaurant] sales were subtracted from the reported gross receipts on ST-103, line 1. This resulted in an increase in [Convenience Store] sales.

After that calculation was made, the audit then proceeded to determine the amount of exempt and taxable Convenience Store sales. To make that distinction, the Department reviewed vendor purchases, financial reports, and annual point-of-sale register detail. As a result, "the audit was able to determine non-taxable sales from reviewing invoices from [food vendors]."

The exempt food purchases were then "adjusted with a cost of sales percentage of 76.43[percent] to calculate the non-taxable grocery sales." The audit referred to "Biz Stats" and that source's "Biz Stats Cost of Goods Sold Ratio." Having done so, the Department's audit concluded that 9.57 percent of the Convenience Store's 2018 sales were exempt. As to the other years under the audit's consideration, "[T]his same percentage was then applied to calculate the exempt sales for 2019 and 2020."

E. Taxpayer's Protest.

1. Restaurant Sales and Total Convenience Store Sales.

Taxpayer challenges the Department's attempt to calculate and differentiate the restaurant sales and taxable Convenience Store sales. Taxpayer explained how it accounted for its restaurant sales and for its Convenience Store sales.

[Taxpayer] has two separate cash registers, one for [the restaurant] and one for the [Convenience Store]. If the customer is only buying [from restaurant], they pay at that register. If they are buying other [Convenience Store] items, they are given a ticket and that is run through the [Convenience Store] register with their other items and they pay there.

Taxpayer explained the reason for maintaining two cash registers and - in some instances - ringing up a restaurant sale twice; a restaurant sale may be recorded on the restaurant's register and once on the Convenience Store's register.

[Franchiser] requires all [restaurant] sales be run through a single register for reporting purposes. This is for franchise fees, royalties, and advertising fees.

Taxpayer explains: "For example, if the [Convenience Store] register has \$500 of sales and the [Restaurant] register has \$100 in [Restaurant] sales and \$50 of those were paid at the [Convenience Store] register, here is how the total sales (line 1, ST-103) and [Convenience] sales *should* be calculated."

Convenience Store Register	\$500
Restaurant Register	\$100
Negative Restaurant Sales	-\$50
Total Sales	\$550

(Thereafter)

Total Sales	\$550
Restaurant Register	-\$100
Total Convenience Sales	\$450

As Taxpayer's objections are considered, it bears repeating how the audit calculated Convenience Store's gross sales amount and then the amount of exempt sales: (1) first distinguish the restaurant proceeds from the Convenience Store proceeds to accurately determine only the proceeds received in and recorded by the Convenience Store; (2) once the amount of Convenience Store proceeds is determined, calculate the amount of taxable Convenience Store transactions and the amount of exempt Convenience Store proceeds. The audit report explained:

The auditor calculated the [Convenience Store] receipts as follows: [Restaurant] sales and Negative [Restaurant] sales were subtracted from the reported gross receipts on ST-103, line 1. This resulted in an increase in [Convenience Store] sales.

The total restaurant sales were relevant for sales tax purposes but only to the extent that exempt restaurant sales must be removed from the reported total sales reported on Taxpayer's sales tax return. That "removal" is necessary because, in some cases, a customer purchased restaurant food (recorded on the restaurant's register) but then paid for that food at the Convenience Store register. That customer was purchasing food and also purchasing Convenience Store items.

Taxpayer states that the Department's audit mistakenly determined the amount of its Convenience Store sales and provides the following illustration. In this illustration its two-step calculation arrives at, in this instance, \$450 in total Convenience Store sales. "Negative Restaurant Sales" refers to an amount "double counted" in the two cash registers.

Convenience Store Register	\$500
Restaurant Register	\$100
Negative Restaurant Sales	-\$50
Total Sales	\$550

(Thereafter)

Total Sales	\$550
Restaurant Register	-\$100
Total Convenience Sales	\$450

In contrast, Taxpayer explains what it believes is the calculation the Department's audit mistakenly employed. This calculation arrives at - in Taxpayer's opinion - an erroneous \$400 in convenience store sales. According to Taxpayer, the convenience store sales were \$450.

Total Sales	\$550
Restaurant Register	-\$100
Negative Restaurant Sales	-\$50
Total Convenience Sales	\$400

Taxpayer explains that the audit's mistake "causes the [Convenience Store] sales to be understated in the audit results. In the audit, the auditor reduced the wrong amount to calculated total [Convenience Store] sales. In [Taxpayer's] new calculation, [Taxpayer] removed the negative subways sales from the calculation."

2. Convenience Store Exempt Lottery Sales.

Taxpayer next maintains that the Department's audit failed to properly account for exempt Convenience Store lottery sales. The Department explains that "[s]ales tax is not collected on the following items . . . Lottery tickets." [IC 6-2.5-5-34](#); *Indiana Tax Handbook for New and Small Business Owners*, <https://www.in.gov/dor/files/new-small-business-handbook.pdf>. (Last visited May 27, 2023).

Taxpayer points out that "[i]ts lottery sales are included in line 1 and should be considered when estimating taxable [Convenience Store] sales." Presumably Taxpayer's reference to "line 1" refers to Taxpayer's as-filed ST-103 sales tax returns.

Taxpayer suggests two alternative approaches as follows:

Deduct lottery sales from Line 1 (Total Sales) and use the auditors exempt percentage to get to total [Convenience Store] or included lottery sales in the calculation of exempt [percentage].

Taxpayer believes that the audit did it wrong and, as a result, the audit understated the 9.57 percent exempt sales amount. As a result:

[T]his greatly overstates taxable sales and increases sales tax due. It also creates additional "unreported income" that the auditor claims is subject to income tax.

Taxpayer's reference to "unreported income" refers to the results of a separate audit of the business income received by Taxpayer's sole shareholder. The shareholder's income tax issues are addressed in a separate Letter of Findings.

F. Analysis and Conclusion.

The Department agrees with Taxpayer that it has established that the sales tax assessment should be adjusted in part. Following review of the extensive documentation and analysis provided, the Department agrees that the Taxpayer's treatment of the "negative" restaurant sales is correct, and that the Department should recalculate the sales tax liability to reflect that interpretation.

However, the lottery sale issue remains unresolved. That issue stems from Taxpayer's sale of lottery tickets which are, of course, not subject to sales tax. If Taxpayer can establish that lottery sales were included in Line 1 on its sales tax returns, that amount should be deducted *before* calculating exempt and non-exempt sales.

The Department here notes that it is not enough to simply document its lottery sales. That number is presumably available. However, if as Taxpayer suggests the Department erred in its treatment of lottery sales, Taxpayer will need to establish that those sales were inadvertently included in income reported on the ST-103s. That information, if available, should be forwarded to the Department within 30 days of the date this decision is issued, at which point it will be included in the Department's revised calculations. If such documentation is not provided in that timeframe, the Department will revise its calculations without adjusting the lottery sales numbers.

FINDING

Taxpayer's protest sustained in part and denied in part.

August 23, 2023

Finding Replaces: New

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An [html](#) version of this document.