

**Letter of Findings: 04-20231821
Gross Retail (Sales) and Use Tax
For the Years 2018, 2019, and 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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

Retailer provided some verifiable documents to support that the assessment was overstated. As such, Retailer was responsible for a reduced amount.

ISSUE

I. Sales and Use Tax - Burden of Proof.

Authority: [IC 6-2.5-1-2](#); [IC 6-2.5-1-5](#); [IC 6-2.5-1-6](#); [IC 6-2.5-1-24](#); [IC 6-2.5-1-27](#); [IC 6-2.5-2-1](#); [IC 6-2.5-3-2](#); [IC 6-2.5-4-1](#); [IC 6-2.5-8-8](#); [IC 6-2.5-9-3](#); [IC 6-8.1-3-12](#); [IC 6-8.1-5-1](#); [IC 6-8.1-5-4](#); *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138 (Ind. Tax Ct. 2010); *Indiana Dep't of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96 (Ind. Ct. App. 1974); *Indiana Dep't of State Revenue v. Kimball Int'l Inc.*, 520 N.E.2d 454 (Ind. Ct. App. 1988); [45 IAC 2.2-2-1](#); American Heritage College Dictionary (3d ed. 1997); PC Magazine, <https://www.pcmag.com/encyclopedia>.

Taxpayer protested the audit assessment claiming that the assessment was overstated.

STATEMENT OF FACTS

Taxpayer is a retail merchant in the business of selling new and used video games, consumer electronics, and gaming merchandise. Taxpayer operates various retail stores located in Indiana. Taxpayer files Indiana tax returns and remits taxes to Indiana.

The Indiana Department of Revenue ("Department") audited Taxpayer's business records and tax returns for the 2018, 2019, and 2020 tax years. Taxpayer and the Department agreed to utilize a statistical sample methodology to project the audit result. Pursuant to the audit, the Department determined that Taxpayer did not correctly collect sales tax on certain retail transactions that were subject to Indiana sales tax. In addition, the Department found that Taxpayer purchased tangible personal property to be used to conduct its business in Indiana without paying sales tax or remitting use tax. As a result, the Department assessed Taxpayer additional tax plus interest. The Department nonetheless waived the penalty.

Taxpayer protested the sales tax assessment only. A hearing was held. This Letter of Findings results. Additional facts will be provided as necessary.

I. Sales and Use Tax - Burden of Proof.

DISCUSSION

Pursuant to the audit, the Department assessed Taxpayer additional sales tax. Taxpayer disagreed, claiming that the assessment was overstated. Therefore, the issue is whether Taxpayer provided verifiable documents sufficient to support that the audit assessment was overstated.

Indiana mandates that every person who is subject to a listed Indiana tax must keep books and records, including all source documents, "so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records." [IC 6-8.1-5-4\(a\)](#). "The [D]epartment may audit any returns with respect to the listed taxes using statistical sampling." [IC 6-8.1-3-12\(b\)](#). "If the taxpayer and the [D]epartment agree to a sampling method to be used, the sampling method is binding on the taxpayer and the [D]epartment in determining

the total amount of additional tax due" *Id.*

Under [IC 6-8.1-5-1\(b\)](#), if the Department "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." All tax assessments are *prima facie* evidence that the Department's claim for the unpaid tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. [IC 6-8.1-5-1\(c\)](#). The taxpayer is required to provide documentation explaining and supporting its challenge that the Department's assessment is wrong. 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). 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).

A. The Department's Initial Audit

During the initial audit review, pursuant to [IC 6-8.1-3-12](#), both Taxpayer and the Department entered into a binding agreement, under which the Department used a sampling method to determine the total amount of additional tax due. For sales tax, the audit noted, in part, the following:

Audit Adjustment 1: Projection - Sales Tax - [] Card

[Taxpayer] accepts [] exchanges (trade in) for gaming equipment such as gaming systems, video games, video game accessories and video game software. When a customer trades in their gaming equipment the trade in price is deducted (credited) from the total sales price of new video equipment that are being purchased. When the sales transaction total exceeds the trade in credit, the customer pays sales tax on the net amount due only. If the total cost of the new gaming items is less than the trade in credit amount [a] Card is issued to the customer in the amount of the excess balance to use on a later purchase.

The customer returns to [Taxpayer] after the initial trade in transaction to purchase additional gaming equipment. [The customer is allowed to] use the [] Card balance as partial or full payment for the new gaming equipment. Sales tax is only applied and collected by [Taxpayer] for the gross amount of the total transaction less the [] Card credit (net amount) on taxable items. This procedure of not taxing the [] Card amount on taxable items is done in error.

. . .

The customer using the [] Card, no longer owns the property that was originally exchanged. The customer can use the [] Card to purchase anything in the store. . . . The [] Card is used as a form of payment in the subsequent transaction. This transaction also does not specify the units or quantity of property being exchange[d]. Only the amount of the [] Card is listed in the payment section of the invoice. The [] Card is used in the same manner as a gift card. The sales tax on the monetary value of a gift card is charged when the recipient ultimately uses the card to make purchases. . . .

Audit Adjustment 2: Projection - Sales Tax - Like Kind Exchange

The initial sales transaction with a [trade in] sometimes include an exchange of gaming equipment for general merchandise such as t-shirts, trading cards, stuffed animals and figures. These items are not the same as gaming equipment. . . .

The audit concluded that Taxpayer did not properly collect sales tax on the transactions, which did not qualify as a "like kind exchange" under [IC 6-2.5-1-6](#). To qualify as a "like kind exchange," the trade in property must be for "like kind" property. Based on the sample projection, the audit assessed additional sales tax accordingly.

B. Taxpayer's Protest

Taxpayer initially protested the audit assessments on sales involving discount adjustments, POSA Gift Card sales, and trade-in credits. Subsequently after the hearing, Taxpayer withdrew its protest on the issue of discount adjustments. Taxpayer continued its protest of the remainder: (1) additional sales tax on sales of POSA Gift Cards and (2) additional sales tax on transactions which did not qualify "like kind exchange."

Taxpayer first asserted that the audit erred in assessing additional sales tax on sales of POSA Gift Cards, which

were non-taxable items. In addition, Taxpayer maintained that the audit erred in assessing additional tax on transactions which "trade-in" credits were applied because they qualified as a "like kind exchange." Taxpayer stated, in part:

[Taxpayer] is [a] video game retailer of new and pre owned video gaming consoles, software, and accessories, digital products, collectible pop culture themed products, accessories, and consumer electronics.

[Taxpayer] categorizes its products into [] several categories, [including] the category of Hardware and Accessories. The Hardware and Accessories category offers new and preowned video game platforms from the major console and PC manufacturers. . . .

[Taxpayer] has traditionally considered consoles and games as the same character of personal gaming devices and are essentially seen as just extensions of the consoles. Sales of consoles and games are very closely tied to one another as many are specifically made for these consoles and games (and in some cases sold together as a bundle.)

. . .

The Trade In Program allows customers the opportunity to trade in their pre-owned video game products in store in exchange for cash or in store credits which can be applied towards the purchase of other products, usually of the same character. This ability to accept trade ins gives [Taxpayer] a strategic advantage over its competitors and gives customers the best overall value and shopping experience. . . .

Referencing several of the Department's publications, Taxpayer argued that games and consoles are "same kind or character" because "both used together [for] 'gaming'." Taxpayer thus claimed, "if a customer purchases a [Sony PlayStation 5 ("PS5")], the customer will also need to purchase PS5 games in order to experience and use the personal gaming device." Taxpayer maintained that a customer "cannot have one without the other to experience personal gaming entertainment. A console without a game does nothing, and likewise a game without a console is useless." To support its protest, Taxpayer provided an Excel summary, a statement, and transaction details.

C. The Law

Indiana imposes an excise tax called "the state gross retail tax" ("sales tax") on retail transactions made in Indiana and "use tax" on a person's storage, use, or consumption of tangible personal property in Indiana. [IC 6-2.5-2-1\(a\)](#); [IC 6-2.5-3-2\(a\)](#); [IC 6-2.5-1-24](#); [IC 6-2.5-1-27](#); [45 IAC 2.2-2-1](#). A retail transaction is a transaction made by a retail merchant that constitutes "selling at retail." [IC 6-2.5-1-2\(a\)](#). Selling at retail occurs when a person "(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\(b\)](#). A person who acquires tangible personal property in a retail transaction (a "retail purchaser") is liable for the sales tax on the transaction. [IC 6-2.5-2-1\(b\)](#). The purchaser in general "shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction." *Id.* "The retail merchant shall collect the tax as agent for the state." *Id.*

The amount of sales tax is calculated based on the "gross retail income received by a retail merchant in a retail unitary or bundled transaction[.]" [IC 6-2.5-2-2\(a\)](#). "Gross retail income" generally is "the total amount of consideration, including cash, credit, property, and services, for which tangible personal property is sold, leased, or rented, valued in money, whether received in money or otherwise . . ." [IC 6-2.5-1-5\(a\)](#). The "gross retail income" does not include "the value of any tangible personal property received in a like kind exchange in the retail transaction, if the value of the property given in exchange is separately stated on the invoice, bill of sale, or similar document given to the purchaser." [IC 6-2.5-1-5\(b\)\(1\)](#).

[IC 6-2.5-1-6](#) provides:

(a) "Like kind exchange" means the reciprocal exchange of personal property between two (2) persons, when:

- (1) the property **exchanged is of the same kind or character, regardless of grade or quality**; and
- (2) the persons exchanging the property both own the property prior to the exchange.

(b) A "like kind exchange" may be a part of a transaction involving additional consideration other than the exchanged property.

(c) Notwithstanding subsection (a), a "like kind exchange" does not occur when:

- (1) the transaction involves more than two (2) persons; or
- (2) one (1) party to the transaction, through agreement or negotiation with the second party, acquires personal property for the primary purpose of exchanging that property for like kind property held by the second party.

(Emphasis added).

[45 IAC 2.2-1-1](#) further explains, in part:

(j) Like Kind Exchange: **Additional Consideration. Non-taxability extends only to the amount of value of the property received. Any additional consideration, commonly known as "boot", received either in cash or property of unlike kind, must be reported for taxation at actual value. However, when any property is clearly used as a medium of exchange in lieu of cash, the element of taxable exchange will be present.**

(k) Like Kind Exchange: Limited to Two Parties. Non-taxable "exchanges" include only transactions for a swap or barter of property between two parties. Property received in an exchange transaction in which a third party is involved, with or without property, is subject to gross retail tax. This rule is not meant to deny non-taxability of exchanges where one or both of the parties in a two-party exchange employ an agent in carrying out the agreement.

(l) Like Kind Exchange: Property to be Owned by Parties at Time of Exchange. **Non-taxable "exchanges" include only transactions in which the property exchanged is owned by the parties thereto at the time the exchange agreement is entered into. Transactions in which the property to be exchanged is acquired by one party after the agreement to exchange has been arranged are taxable. The exchange agreement must specify the definite units or quantity of property to be exchanged.** However, "retail merchants" are allowed to consider as non-taxable the full value of tangible personal property of like kind received in allowable exchanges, even though ownership of the property received is encumbered by a conditional sales contract, retail installment contract, or a chattel mortgage.

(Emphasis added).

In addition, when a purchaser claims the purchase "is exempt from the state gross retail [] tax[], the purchaser may issue an exemption certificate to the seller instead of paying the tax." [IC 6-2.5-8-8\(a\)](#). The "seller accepting a proper exemption certificate under [\[IC 6-2.5-8-8\]](#) has no duty to collect or remit the state gross retail [] tax on that purchase." *Id.* Otherwise, as an agent for the State of Indiana, the seller "holds those taxes in trust for the state and is personally liable for the payment of those taxes, plus any penalties and interest attributable to those taxes, to the state." [IC 6-2.5-9-3](#). A statute which provides a tax exemption is strictly construed against the taxpayer. *Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96, 97 (Ind. Ct. App. 1974). "[W]here such an exemption is claimed, the party claiming the same must show a case, by sufficient evidence, which is clearly within the exact letter of the law." *Id.* at 101 (internal citations omitted). In applying any tax exemption, the general rule is that "tax exemptions are strictly construed in favor of taxation and against the exemption." *Indiana Dep't of State Revenue v. Kimball Int'l Inc.*, 520 N.E.2d 454, 456 (Ind. Ct. App. 1988).

D. Hearing Analysis

Taxpayer in this case claimed that the assessment was overstated because (1) sales of POSA Gift Cards were not subject to sales tax and (2) the audit erred in assessing additional sales tax on transactions qualified "like kind exchange."

As stated above, both Taxpayer and the Department entered into a binding agreement to use the statistical sampling method to project the audit result. Therefore, Taxpayer is prohibited from disputing the sampling methodology pursuant to [IC 6-8.1-3-12](#). Nonetheless, under the agreed sampling methodology, Taxpayer is allowed to provide additional verifiable source documents to substantiate that taxes were correctly remitted within the sample.

1. Sales of POSA Gift Cards

Taxpayer's documents demonstrated that it regularly sells POSA Gift Cards - as a form of pre-paid credit - to customers, which could be used in future transactions in store or otherwise. Taxpayer documented that these cards are required to be activated at the initial point of sale to record the pre-paid credit after customers paid for them. Based on the additional documentation provided, the Department is prepared to agree that sales of POSA Gift Cards were not subject to sales tax at the initial point of sale when Taxpayer activated these cards to record the pre-paid credit for future use.

Accordingly, based on the additional supporting documentation, a supplemental review will be performed to verify these transactions. As such, Taxpayer's protest is sustained pending the result of the supplemental review. To the extent that the supplemental review results in reducing the assessment, Taxpayer's protest is sustained; otherwise, Taxpayer's protest of this issue is respectfully denied.

2. Like Kind Exchange

To qualify as a non-taxable exchange under Indiana law, the exchange must be the reciprocal exchange of personal property between two (2) persons and must qualify "like kind exchange." That is, the property to be exchanged must be "of the same kind or character, regardless of grade or quality []." [IC 6-2.5-1-6\(a\)](#). "Any additional consideration [] received either in cash or property of unlike kind, must be reported for taxation at actual value." [45 IAC 2.2-1-1\(j\)](#).

The audit in this case assessed additional sales tax under two separate instances involving "trade-in" credits where Taxpayer did not properly collect sales tax on the transactions in question. They were: (1) "trade-in" credits from gaming equipment that were applied to sales of "merchandise such as t-shirts, trading cards, stuffed animals and figures"; and (2) "trade-in" credits that were given in the form of Cards (as in-store credits or like gift cards), which were used in future purchases, as separate transactions.

Taxpayer, to the contrary, argued that consoles and games are like kind property because "[s]ales of consoles and games are very closely tied to one another as many are specifically made for these consoles and games (and in some cases sold together as a bundle[]).]" Taxpayer contended that "like kind exchange" should apply to "gaming" broadly which includes "game for console" and "console for game."

Upon review, however, the Department is not able to agree. A video game is "an electronic or computerized game played by manipulating images on a display screen." American Heritage College Dictionary 1505 (3d ed. 1997). Publicly available information describes a video game as "[i]nteractive software that is used for entertainment, role playing and simulation. Video games are played on a Windows PC, mobile device or specialized gaming console such as an Xbox or PlayStation." PC Magazine, available at <https://www.pcmag.com/encyclopedia> (last visited September 28, 2023). In other words, video games are software programs and are not of "the same kind" as consoles, which are electronic devices or hardware. Taxpayer in this case may strategically market consoles and games together as a bundle to be sold. Such strategy logically could improve its sales, but a console exhibits a distinct character, which a video game does not have. Selling consoles and games together as a bundle does not change the character of consoles or the character of video games. Likewise, consoles cannot replace games or vice versa; they are not of the same character. In short, consoles and games are not "like kind." The transactions in question therefore did not qualify as a "like kind exchange" and were subject to sales tax.

To conclude, the Department is prepared to agree that Taxpayer partially met its burden of proof demonstrating that the audit assessment was incorrect. Sales of POSA Gift Cards were not subject to sales tax at the initial point of sale when Taxpayer activated these cards to record the pre-paid credit for future use. Taxpayer, however, failed to meet its burden of proof concerning "like kind exchange" pursuant to the above-referenced Indiana law.

FINDING

Taxpayer's protest is sustained in part, and respectfully denied in part. Taxpayer's protest is subject to the Department's supplemental audit review. To the extent that the Department's supplemental review results in reducing the assessment, Taxpayer's protest is sustained; otherwise, Taxpayer's protest is respectfully denied.

October 5, 2023

Finding Replaces: New

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