

Memorandum of Decision 04-20231386
Indiana Gross Retail Tax
For the Years 2019 to 2022

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 Memorandum of Decision.

HOLDING

Indiana Research Company was entitled to an additional refund of sales tax paid on purchases of equipment and supplies essential and integral to Company's research. Company was not entitled to a refund of sales tax paid on the purchase of generic office furniture, household extension cords, and routine office supplies.

ISSUE

I. Gross Retail and Use Tax - Equipment and Items Integral to Taxpayer's Research and Development Activities.

Authority: [IC 1-1-4-1](#); [IC 6-2.5-1-27](#); [IC 6-2.5-2-1](#); [IC 6-2.5-3-1](#); [IC 6-2.5-3-2](#); [IC 6-2.5-5-3](#); [IC 6-2.5-5-40](#); *Conklin v. Town of Cambridge City*, 58 Ind. 130 (1877); *Indiana Dep't of State Rev. v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138 (Ind. Tax Ct. 2010); *Rhoades v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044 (Ind. Tax Ct. 2002); *Mynsberge v. Dep't of State Revenue*, 716 N.E.2d 629 (Ind. Tax Ct. 1999); *Tri-States Double Cola Bottling Co. v. Dep't of State Revenue*, 706 N.E.2d 282 (Ind. Tax Ct. 1999); *Leehaug v. State Bd. of Tax Comm'rs*, 583 N.E.2d 211 (Ind. Tax Ct. 1991); *General Motors Corp. v. Indiana Dept. of State Revenue*, 578 N.E.2d 399 (Ind. Tax Ct. 1991); *Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96 (Ind. Ct. App. 1974); [45 IAC 2.2-5-10](#); Sales Tax Information Bulletin 75 (January 2023); Sales Tax Information Bulletin 75 (April 2017); BLACK'S LAW DICTIONARY (11th ed. 2019).

Taxpayer argues that the Department made a mistake when it denied a portion of its originally requested sales tax refund.

STATEMENT OF FACTS

Taxpayer is an Indiana company in the business of conducting chemical and pharmaceutical analyses and providing its customers development and intellectual property support.

Taxpayer submitted a claim for a refund of sales tax paid on the purchase of tangible personal property used in research and development of Taxpayer's products. Taxpayer sought a refund of approximately \$210,000.

The Indiana Department of Revenue ("Department") reviewed the refund request. As a result of that review, the Department agreed that Taxpayer was entitled to a refund of approximately \$165,000 but denied the remaining \$45,000 refund amount.

In a letter dated October 2022, the Department explained why the \$45,000 refund was denied.

Denied portion for 2019, 2020, 2021, and 2022 is due to tangible personal[] property not being essential or integral to the research and development process per [IC 6-2.5-5-40](#). A portion of the 2019 amount was due to the inclusion of invoices from 2018 which is out of statute. There were also duplicate invoices found in 2020. It was also agreed upon that the computers and computer equipment are 95[percent] exempt, 5[percent] taxable.

Taxpayer disagreed with the Department on the grounds that it was entitled to the entire amount originally requested. Taxpayer submitted a protest to that effect. An administrative hearing was scheduled to permit Taxpayer to explain the basis for its protest.

In response to Taxpayer's protest, the Department issued a Final Order Denying Refund (August 16, 2023). The Department reviewed the items under consideration, the exemption statute, and the standard under which

exemptions are implemented. The ODR denied Taxpayer the additional refund amount concluding as follows:

[T]he Department is unable to agree that Taxpayer has established that the extension cords, desks, filing equipment and the like are essential and integral in conducting research. The Department does agree that these items are useful and necessary; researchers need desks, chairs, and filing cabinets but that does not necessarily mean that they qualify for the exemption.

Taxpayer asked for and was granted a rehearing on the matter. An administrative hearing was conducted by video conference, and this Memorandum of Decision results.

I. Gross Retail and Use Tax - Equipment and Items Integral to Taxpayer's Research and Development Activities.

DISCUSSION

The issue is whether Taxpayer has established that the Department was wrong when it granted Taxpayer less than 100 percent of the originally requested sales tax refund because the disputed items were essential and integral to its research activities.

A. Indiana's Sales and Use 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 person who acquires property in a retail transaction (a "retail purchaser") is liable for the tax on the transaction. [IC 6-2.5-2-1\(b\)](#). 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 Rev. v. Caterpillar, Inc.*, 15 N.E.3d 579, 583 (Ind. 2014).

In general, purchases of tangible personal property are subject to sales tax. [45 IAC 2.2-5-10\(a\)](#). Tangible personal property means personal property that: (1) can be seen, weighed, measured, felt, or touched; or (2) is in any other manner perceptible to the senses. [IC 6-2.5-1-27](#). Tangible personal property also includes electricity, water, gas, steam, and prewritten computer software. *Id.*

Indiana also imposes a complementary excise tax called "the use tax" 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." [IC 6-2.5-3-2\(a\)](#). Use means the "exercise of any right or power of ownership over tangible personal property." [IC 6-2.5-3-1\(a\)](#).

In effect and practice, the use tax is generally equivalent to the sales tax. See *Rhoads v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044, 1047 (Ind. Tax Ct. 2002).

B. Research and Development Sales Tax Exemption.

[IC 6-2.5-5-40](#) (effective January 1, 2016) provides a sales tax exemption for research and development ("R&D") property. The current version of [IC 6-2.5-5-40](#) provides that certain activities are not considered qualifying R&D activities and clarifies that certain activities are considered simply incidental to R&D activities. Sales Tax Information Bulletin 75 (January 2023), 20230125 Ind. Reg. 045230020NRA, explains:

[T]he property must be acquired by the purchaser for the purpose of research and development activities devoted to experimental or laboratory research and development for new products, new uses of existing products, or improving or testing existing products. See also Sales Tax Information Bulletin 75 (April 2017), 20170726 Ind. Reg. 045170335NRA.

[IC 6-2.5-5-40\(g\)](#) explains that a taxpayer is entitled to purchase certain items of tangible personal property without paying the gross retail tax when the property is utilized in qualifying R&D activities in the manner and to the extent provided in the law. In full, the exemption is set out in [IC 6-2.5-5-40](#) as follows:

(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). **(Emphasis added).**

C. Weighing Taxpayer's Arguments and Explanations.

[IC 6-2.5-5-40](#), like all tax exemption provisions, is strictly construed against exemption from the tax. *Tri-States Double Cola Bottling Co. v. Dep't of State Revenue*, 706 N.E.2d 282, 283 (Ind. Tax Ct. 1999); *Mynsberge v. Dep't of State Revenue*, 716 N.E.2d 629, 636 (Ind. Tax Ct. 1999). Indiana law has long held that "[W]here [] 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." *Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96, 101 (Ind. Ct. App. 1974). (Citing *Conklin v. Town of Cambridge City*, 58 Ind. 130, 133 (1877)).

Nevertheless, the Department is also aware of the countervailing rule that a "statute must not be construed so narrowly that it does not give effect to legislative intent because the intent of the legislature embodied in a statute constitutes the law." *General Motors Corp. v. Indiana Dept. of State Revenue*, 578 N.E.2d 399, 404 (Ind. Tax Ct. 1991).

D. Taxpayer's Supplemental Refund Request.

Taxpayer maintains that the Department made a mistake when it denied a refund of sales tax paid on purchases of items such as file organizers, desktop file sorters, extension cords, desk chairs, shelves, and task chairs. Taxpayer explains that these items are essential and integral in performing its research activities. For example, Taxpayer explains:

The extension cords are "used to power the computers and other items. Without power, the computers and lab equipment will not work."

The filing aids are used by "scientist[s] to organize findings from experiments." Without these filing aids, "[P]aperwork would be misconstrued [sic] and lead to test results that are not accurate."

These two arguments are offered to explain the basis for much of its protest argument. Taxpayer essentially relies on a "but for" analysis. If Taxpayer did not have this extension cord, it would not be able to continue its research activity. If Taxpayer's scientists and its technicians did not have chairs, those scientists would not be able to continue conducting research. If Taxpayer's scientists did not have "filing aids," the scientists could not conduct their research.

Bearing in mind that the Department is required to "strictly construe" exemption statutes, [IC 6-2.5-5-40](#) the Department is unable to agree that the exemption is quite as inexact as that proposed by Taxpayer. [IC 6-2.5-5-40\(b\)](#) allows the exemption for laboratory equipment, computers, telecommunications equipment, testing equipment, and the like. It allows the exemption for items which are "essential and integral to experimental or laboratory research and development."

However, [IC 6-2.5-5-40\(d\)](#) excludes items which are "incidental to experimental or laboratory research and development."

In this instance, the Department will bear in mind that statutory interpretation begins with "plain and ordinary meaning of the language used." *Leehaug v. State Bd. of Tax Comm'rs*, 583 N.E.2d 211, 212 (Ind. Tax Ct. 1991). In implementing this state's statute, [IC 1-1-4-1\(1\)](#) requires that "[w]ords and phrases shall be taken in their plain, or ordinary, and usual sense."

As such, the Department will assume that when the legislature adopted the "essential and integral" standard, that it chose words which mean what they say. "Essential" is defined as "[o]f the utmost importance; basic and necessary" while "Incidental" is defined as "having a minor role." BLACK'S LAW DICTIONARY (11th ed. 2019). However, the Department also acknowledges that [IC 6-2.5-5-40](#) did not impose a stringent "double direct" standard such as found in Indiana's "manufacturing exemption." [IC 6-2.5-5-3](#).

The Department agrees that Taxpayer has met its burden of establishing that the following items meet the "essential and integral standard."

- Market Lab Fireproof box and Waterproof Box
- Global Industrial Flammable Cabinet
- Battery Backup & Surge Protector
- All-Star Electronic Security Systems
- Telecommunications Equipment (Phone) Purchases Amazon

The Department initially found that a number of refund requests were outside the statute of limitations because the invoices were dated 2018. As far as relevant here, the Department agrees with Taxpayer "that payment was made in 2019, therefore the line items [are] still in statute."

Taxpayer's protest is denied in part and sustained in part. The Department agrees that security system equipment, telecommunications equipment, specialized storage devices, and combination back-up surge protectors are essential and integral to Taxpayer's research activities. The Department does not agree that generic office furniture, household extension cords, and miscellaneous office supplies are anything more than incidental to those research activities.

FINDING

To the extent specified in this Memorandum of Decision, Taxpayer's protest is sustained in part and denied in part.

November 29, 2023

Finding Replaces: new

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