INDIANA DEPARTMENT OF ENVIRONMENTAL MANAGEMENT

Title: Excess Liability Trust Fund/Risk Integrated System of Closure
Identification Number: WASTE-0039-NPD
Date Originally Adopted: February 10, 2000
Dates Revised: December 14, 2000, March 20, 2001
Other Policies Repealed or Amended: None
Brief Description of Subject Matter: This document will address whether the Excess Liability Trust Fund (ELTF) will reimburse eligible parties for the costs incurred in implementing a corrective action plan using the Risk Integrated System of Closure (RISC).
Citations Affected: IC 13-23-8, IC 13-23-9, 328 IAC 1-3-5

This nonrule policy document is intended solely as guidance and does not have the effect of law or represent formal Indiana Department of Environmental Management (IDEM) decisions or final actions. This nonrule policy document shall be used in conjunction with applicable laws. It does not replace applicable laws, and if it conflicts with these laws, the laws shall control. A revision to this nonrule policy document may be put into effect by IDEM thirty (30) days after the revised nonrule policy document is made available for public inspection and comment and is presented to the Financial Assurance Board. IDEM will submit revisions to the Indiana Register for publication.

Excess Liability Trust Fund/Risk Integrated System of Closure

The IDEM will be issuing a policy regarding the cleanup of sites using a risk based system [Risk Integrated System of Closure (RISC)]. This policy will replace the current policy for the remediation of leaking underground storage tanks, contained in the 1994 Underground Storage Tank Manual. Upon implementation of the RISC policy, there will be a transition period during which responsible parties will have to choose which policy they want to proceed under. This decision will be required on all sites undergoing corrective action. After the implementation of the RISC policy, responsible parties reporting releases must develop corrective action in accordance with the RISC policy.

There have been questions regarding whether the Excess Liability Trust Fund (ELTF) will reimburse responsible parties for corrective action costs under RISC and if so, under what conditions. IDEM does not intend to promulgate rules for this transition period because IDEM believes that the current rules are flexible enough to provide for reimbursement under RISC, as long as the responsible party has an approved Corrective Action Plan (CAP). Also, as the RISC policy is expected to be implemented in the second half of 2000, rules could not be promulgated quickly enough. Therefore, IDEM is issuing this nonrule policy document to explain how it intends to interpret the laws and rules concerning ELTF reimbursement.

IC 13-23-8-4(a)(5) requires that the responsible party have an approved CAP to be eligible for reimbursement from ELF. The CAP must be developed in accordance with the Underground Storage Tank Guidance Manual, ***including the department's risk-based corrective action plan standards when the standards become effective.*** Thus, IDEM has the authority to require and approve CAPs that are developed in accordance with IDEM's policies.

To ensure the solvency of the ELTF, IDEM will require owners/operators to submit a cost comparison to show the cost benefit of changing a site currently undergoing remediation under the 1994 Underground Storage Tank Guidance to a RISC based clean-up approach. IDEM will review the comparison and make a determination as to which method of remediation would be most cost effective.

Schedule for the ELTF reimbursement of LUST costs for sites during the transition to the RISC Policy.

Eligible Costs

Costs incurred ***before the implementation and transition period of the RISC policy,*** including:
9 Costs incurred in the implementation of an approved CAP that is consistent with the 1994 Underground Storage Tank Manual.
9 Costs associated with the collection of data that will be used in a decision as to which policy the responsible party wishes to use.

Costs incurred ***throughout the transition period for the RISC policy****, including:*
9 If the responsible party has an approved Corrective Action Plan (CAP), costs incurred for corrective action, regardless of whether the CAP is developed under the current guidance or under the RISC Guidance would be eligible.
9 Costs associated with transitioning a site from the 1994 policy to the RISC policy.
9 Costs associated with the collection of data necessary to make an informed decision as to which policy to proceed under.
9 Costs incurred in acquiring environmental notices (these costs will be considered third party claims and will be processed in accordance with IC 13-23-9-3).

Costs incurred once the RISC policy ***transition period has ended,*** *including:*
9 Costs incurred for corrective action at leaking underground sites which have approved CAPs.
9 Costs incurred in acquiring environmental notices(these costs will be considered third party claims and will be processed in accordance with IC 13-23-9-3).

Ineligible Costs

Costs not reimbursable under any circumstance:
9 Costs that are not eligible under 328 IAC 1-3-5.
9 Costs that do not fall within the reasonable cost range established under 328 IAC 1-3-5.
9 Costs associated with the development of a CAP under the RISC policy before the policy has been implemented, other than those costs associated with the collection of data which will be used in a decision as to which policy the responsible party wishes to use.
9 Costs associated with transitioning a site to RISC, if, through a cost comparison, IDEM determines that the cost to complete the remediation using RISC would be greater than that of completing the remediation using the 1994 Underground Storage Tank Guidance.

INDIANA DEPARTMENT OF ENVIRONMENTAL MANAGEMENT

Title: Voluntary Remediation Program Community Relations Plan
Identification Number: WASTE-0049-NPD
Date Originally Adopted: April 20, 2001
Dates Revised: None
Other Policies Repealed or Amended: Amends the Community Relations Section (8.0) of the Remediation Work Plan Requirements found in the Voluntary Remediation Program's Resource Guide (July 1996) and supplements the Voluntary Remediation Program Chapter (4) of the Risk-Integrated System of Closure User's Guide (February 2001)
Brief Description of the Subject Matter: This document addresses community relations activities necessary for inclusion in and approval of a Voluntary Remediation Program Remediation Work Plan.
Citations Affected: IC 13-25-5-7; IC 13-25-5-11

This nonrule policy document is intended solely as guidance and does not have the effect of law or represent formal Indiana Department of Environmental Management ("IDEM") decisions or final actions. This nonrule policy document shall be used in conjunction with applicable laws. It does not replace applicable laws, and if it conflicts with these laws, the laws shall control. A revision to this nonrule policy document may be put into effect by IDEM thirty (30) days after the revised nonrule policy document is made available for public inspection and comment and is presented to the Solid Waste Management Board. IDEM will submit revisions to the Indiana Register for publication.

Policy Statement

The Voluntary Remediation Program ("VRP") requires the submittal of a proposed Remediation Work Plan for IDEM approval. This plan must include a Community Relations Plan as stated in IC 13-25-5-7. The requirements of the Community Relations Plan were previously issued as part of the Voluntary Remediation Program Resource Guide (latest update - July 1996). As part of the ongoing evaluation of IDEM's remediation programs, especially with respect to IDEM's upcoming risk based remediation policy, and public information concerns, the VRP's Community Relations Plan requirements are being revised. This revision will replace the Community Relations Plan requirements last addressed in the July 1996 Resource Guide and will supplement the Voluntary Remediation Program Chapter of the Risk-Integrated System of Closure User's Guide (February 2001). The new basic components take a more proactive approach to making sure that neighboring residents, businesses and institutions are informed of VRP site remediation activities.

Community Relations Plan Requirements

Community education and participation is a necessary component of all VRP projects. Therefore, the Remediation Work Plan is required to contain a Community Relations Plan. The minimum requirements of a Community Relations Plan are stipulated below. These requirements apply to all VRP applications approved after the effective date of this policy. Participants are also encouraged to inform the community about their project by utilizing communication methods beyond the minimum requirements listed in this document. For example, many VRP participants find that informal informational meetings and discussions are effective in preventing

project complications sometimes caused by having an uninformed public. Such meetings are especially appropriate for neighbors and sensitive community institutions. Other effective means of community relations communication can include, but are not limited to, canvassing the neighborhoods door-to-door, and mass mailings. Regardless of the communication methods used, participants should formulate a Community Relations Plan in conjunction with their IDEM Voluntary Remediation Project Manager that best addresses the needs of the participant and the community.

Listed below are the basic components that a Community Relations Plan must include.

The Community Relations Plan shall:

1. Identify all property owners and property occupants, which include property owners or occupants affected or likely to be affected by the contamination that is the subject of the proposed Voluntary Remediation Project and all owners or occupants of adjacent or closely proximate land.
2. Identify all known or registered neighborhood organizations serving the location of the Voluntary Remediation Project, if any.
3. Identify all known or reasonably apparent sensitive community institutions within two (2) miles, including, but not limited to schools, health care facilities, child care facilities, senior citizen residential or care facilities and the administrative office or owner of parks and playgrounds.
4. Include a sample of a written notice to be sent to the property owners and property occupants, neighborhood organizations, and sensitive community institutions, which shall include:
    a. the following paragraph: "This notice is being provided to inform you of the presence of a site in your neighborhood that has been accepted into IDEM's Voluntary Remediation Program. This notice is a requirement of a Community Relations Plan which has been developed by the Applicant and is a component of the Remediation Work Plan that is available for review at the repository listed below. The Community Relations Plan includes provisions for notifying all neighboring property owners and occupants, neighborhood organizations and other local entities. In addition, the Community Relations Plan may require the applicant to post an informational sign at the subject property. For additional information about the Community Relations Plan and the Remediation Work Plan please review the documents in the repository or contact the IDEM Project Manager at (317) 234-0973.";
    b. a short description of the work to be performed;
    c. information concerning the public comment period, including the time period and procedures for public comment, and the address to which comments are to be directed. (The sample need not include the dates of the public comment period, as they will not be known when the Remediation Work Plan is drafted; however, the actual notices that are sent out must include these dates.); and
    d. the location of the record repository where the Remediation Work Plan has been placed.
5. Provide the name(s) and mailing address(es) of all affected local governmental units with jurisdiction within one (1) mile of the property affected by the proposed Remediation Work Plan.

IDEM will notify the affected local government units about the VRP Project and the anticipated remediation at the time IDEM signs the Voluntary Remediation Agreement. In addition, local government units that are affected by the proposed VRP Project will be notified by IDEM of the Remediation Work Plan and the beginning of the public comment period as soon as an internal review of the document has been completed. These local government units will include government units located in the county of the project as well as those within one (1) mile of the project but in another county. The Participant should also include a listing of any other governmental units that they wish to have notified of the project.

6. Provide the name(s) and mailing address(es) of the newspaper(s) or other appropriate circulars in which notice of the public comment period will be published.
7. Identify the location of the public library and other public repositories in which a copy of the proposed Remediation Work Plan will be placed. The proposed Remediation Work Plan must be placed in the public library closest to the site and in the county or counties affected by the project. If more than one repository is selected, the participant shall provide one additional copy of the proposed Voluntary Remediation Work Plan for each additional repository.
8. In addition, VRP Participants shall post a sign that:
    a. identifies the location as a Voluntary Remediation Program cleanup site;
    b. gives the IDEM VRP site number, the VRP phone number and the VRP web site address;
    c. shall meet the following criteria:
        1) be visible/readable from 20 feet;
        2) be in English and the language predominantly used in the neighborhood if other than English; and
        3) place one sign per site access point; and
    d. shall be posted starting with the end of the public comment period for the Remediation Work Plan, before any work begins and remain posted until the Covenant Not To Sue has been issued.

The VRP Participant shall identify all posting locations and the text of the information to be included on the sign in the Community Relations Plan.

Exceptions to Section 8 (above) will be considered by IDEM on a site-specific basis if there is a compelling reason for not posting a sign and it is stated in the Remediation Work Plan. Examples of potential exceptions are:

a. the site already meets targeted cleanup objectives;
b. no active remediation is occurring or the cleanup is of short duration;
c. The VRP participant has made a reasonable effort to notify affected parties in some other acceptable manner such as but not limited to, certified mail, door-to-door canvassing, or a well-publicized informational meeting open to the public;
d. public display of a sign would negatively impact a retail business by keeping customers/visitors away (this impact must be demonstrable);
e. The site is located in an area where passers by could not see the sign or the site is otherwise inaccessible;
f. there are no residents within one quarter (1/4) mile of the boundaries of the site;
g. soil at the site is not being disturbed, and pits and piles are not created; or
h. the site is secured (monitored, patrolled, adequately fenced) or operational at all hours of the day.

To implement the Community Relations Plan, IDEM will:

a. place a copy of the Remediation Work Plan at the public library and any other repositories specified in the Community Relations Plan;
b. notify the Affected Governments;
c. publish a notice requesting comments; and
d. set a public comment period of at least thirty (30) days.

Before the comment period begins, the Participant must mail, or otherwise provide in writing, the written notice as provided above, to all:

a. property owners;
b. property occupants;
c. neighborhood organizations;
d. sensitive community institutions; and
e. others requesting notification.

The participant must confirm in the VRP Completion Report that all the property owners, property occupants, neighborhood organizations, sensitive community institutions, and those requesting notification were sent the written notice of the public comment period.
(Note: For definitions of the terms, facility, site and area please refer to the RISC Technical and User Guides)

INDIANA STATE DEPARTMENT OF HEALTH
MONTHLY CALCULATION
March 2001
INCOME ELIGIBILITY GUIDELINES FOR THE MCH / CSHCS / HOOSIER HEALTHWISE PROGRAMS
BASED ON HEALTH AND HUMAN SERVICES POVERTY INCOME GUIDELINES
PROGRAM IMPLEMENTATION DATES LISTED BELOW:
CSHCS / February 16, 2001 MCH / HOOSIER HEALTHWISE / April 1, 2001

The following information must be used by all MCH funded projects, CSHCS programs, and Hoosier Healthwise (HH) recorded on the appropriate enrollment forms. Guidelines for use of this form are as follows: (all calculations are calculated from HCFA income guidelines).

MCH: The payment level for MCH Services is at the bottom of the form. It ranges from no charge at or below 100% of federal poverty guidelines to patients being charged the full cost of service (100%) at greater than 250% of federal poverty guidelines. Assignment of an MCH payment level category is based on the participant's annual family/household (economic unit) gross income and size with regard for extenuating circumstances (i.e., substantial financial debt, family members with extraordinary medical bills). The participant's payment level category must be updated annually. This payment level is for persons without insurance to cover services.

CSHCS: To be financially eligible for CSHCS, the gross household income must be less than or equal to 250% of the federal poverty income guidelines. Household means a group of related or non-related individuals who are not residents of an institution, but who are living as one economic unit. The applicant must also be medically eligible to receive services. MCH and Hoosier Healthwise define a pregnant woman as two family members. CSHCS defines a pregnant woman as one family member.

HH: For a pregnant woman and/or child 0-19, to be financially eligible for package A and B Hoosier Healthwise, the gross economic unit income must be less than or equal to 150% of the federal poverty income. Children 0-19 are eligible for Package C (required variable premium payment) up to 200% of federal poverty income guidelines.

HOUSEHOLD SIZE:	100% MONTHLY Income Starting At	HH A & B 150% MONTHLY Income Equal To Or Less Than	HH Partial Premium Package C 175% MONTHLY Income Equal To Or Less Than	HH Full Premium Package C 200% MONTHLY Income Equal To Or Less Than	CSHCS 250% MONTHLY Income Equal To Or Less Than	250% + MONTHLY Income Greater Than
1	$716	$1,074	$1,253	$1,432	$1,790	$1,790
2	$968	$1,452	$1,694	$1,935	$2,419	$2,419
3	$1,220	$1,829	$2,134	$2,439	$3,048	$3,048
4	$1,471	$2,207	$2,574	$2,942	$3,678	$3,678
5	$1,723	$2,584	$3,015	$3,445	$4,307	$4,307
6	$1,975	$2,962	$3,455	$3,949	$4,936	$4,936
7	$2,226	$3,339	$3,896	$4,452	$5,565	$5,565
8	$2,478	$3,717	$4,336	$4,955	$6,194	$6,194
9	$2,730	$4,094	$4,777	$5,459	$6,823	$6,823
10	$2,981	$4,472	$5,217	$5,962	$7,453	$7,453
11	$3,233	$4,849	$5,657	$6,465	$8,082	$8,082
12	$3,485	$5,227	$6,098	$6,969	$8,711	$8,711
Each additional member add:	$252					
*MCH	0%	**1-24%	25%	50%	75%	100%

Base Poverty Level is: $8,590. Federal Register Vol. 66, No. 33, February 16, 2001

*MCH Percentage used to calculate MCH charges.

**Clinic choice 1-24% for the cost of service except those covered by HH.

ANNUAL CALCULATION

March 2001

INCOME ELIGIBILITY GUIDELINES FOR THE WIC / MCH / CSHCS / HOOSIER HEALTHWISE PROGRAMS BASED ON HEALTH AND HUMAN SERVICES POVERTY INCOME GUIDELINES

PROGRAM IMPLEMENTATION DATES LISTED BELOW:

CSHCS / February 16, 2001 MCH / HOOSIER HEALTHWISE / April 1, 2001 WIC / May 1, 2001

The following information must be used by all MCH funded projects, WIC programs, CSHCS programs, and Hoosier Healthwise (HH) recorded on the appropriate enrollment forms. Guidelines for use of this form are as follows: (all calculations other than 185% are calculated from HCFA income guidelines).

MCH: The payment level for MCH Services is at the bottom of the form. It ranges from no charge at or below 100% of federal poverty guidelines to patients being charged the full cost of service (100%) at greater than 250% of federal poverty guidelines. Assignment of an MCH payment level category is based on the participant's annual family/household (economic unit) gross income and size with regard for extenuating circumstances (i.e., substantial financial debt, family members with extraordinary medical bills). The participant's payment level category must be updated annually. This payment level is for persons without insurance to cover services.

WIC: Please note that there is no charge for WIC services and WIC income eligibility cannot exceed 185% of the poverty income levels. Proof of income is required to receive WIC benefits. No allowances for extenuating circumstances can be made. Total household income (gross) must be used; except for self-employed persons, such as a farmer or a small business owner. For this special group use gross income less business expenses. Household consists of a group of related or non-related individuals who are not residents of an institution but who are living as one economic unit.

CSHCS: To be financially eligible for CSHCS, the gross household income must be less than or equal to 250% of the federal poverty income guidelines. Household means a group of related or non-related individuals who are not residents of an institution, but who are living as one economic unit. The applicant must also be medically eligible to receive services. MCH and Hoosier Healthwise and WIC define a pregnant woman as two family members. CSHCS defines a pregnant woman as one family member.

HH: For a pregnant woman and/or child 0-19, to be financially eligible for package A and B Hoosier Healthwise, the gross economic unit income must be less than or equal to 150% of the federal poverty income. Children 0-19 are eligible for

Package C (required variable premium payment) up to 200% of federal poverty income guidelines.

HOUSEHOLD SIZE:	100% ANNUAL Income Starting At	HH A & B 150% ANNUAL Income Equal To Or Less Than	HH Partial Premium Package C 175% ANNUAL Income Equal To Or Less Than	USDA / WIC Standard 185% ANNUAL Income Equal To Or Less Than	HH Full Premium Package C 200% ANNUAL Income Equal To Or Less Than	CSHCS 250% ANNUAL Income Equal To Or Less Than	250% + ANNUAL Income Greater Than
1	$8,590	$12,885	$15,033	$15,892	$17,180	$21,475	$21,475
2	$11,610	$17,415	$20,318	$21,479	$23,220	$29,025	$29,025
3	$14,630	$21,945	$25,603	$27,066	$29,260	$36,575	$36,575
4	$17,650	$26,475	$30,888	$32,653	$35,300	$44,125	$44,125
5	$20,670	$31,005	$36,173	$38,240	$41,340	$51,675	$51,675
6	$23,690	$35,535	$41,458	$43,827	$47,380	$59,225	$59,225
7	$26,710	$40,065	$46,743	$49,414	$53,420	$66,775	$66,775
8	$29,730	$44,595	$52,028	$55,001	$59,460	$74,325	$74,325
9	$32,750	$49,125	$57,313	$60,588	$65,500	$81,875	$81,875
10	$35,770	$53,655	$62,598	$66,175	$71,540	$89,425	$89,425
11	$38,790	$58,185	$67,883	$71,762	$77,580	$96,975	$96,975
12	$41,810	$62,715	$73,168	$77,349	$83,620	$104,525	$104,525
Each additional member add:	$3,020			$5,587			
*MCH	0%	**1-24%	25%	25%	50%	75%	100%

Base Poverty Level is: $8,590. Federal Register Vol. 66, No. 33, February 16, 2001
Federal Register Vol. 66, No. 50, March 14, 2001
WIC cannot exceed 185% and there is no charge for WIC services.
*MCH Percentage used to calculate MCH charges. **Clinic choice 1-24% for the cost of service except those covered by HH.

DEPARTMENT OF STATE REVENUE
AUDIT-GRAM NUMBER IR-017
February 27, 2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

Corporate Partner Distributions – Adjusted Gross Income Tax

Authority: IC 6-3-1-19; IC 6-3-4-10; IC 6-3-4-11; 45 IAC 3.1-1-106; 45 IAC 3.1-1-153; Hunt Corp., Ind. Tax Court (1999)

IC 6-3-4-10. Partnership returns.

(a) [E]very partnership doing business in this state… and every partnership which has gross income derived from sources within this state, shall make a return for each taxable year… [1963]

IC 6-3-4-11. Partnerships not subject to tax.

(a) A partnership… shall not be subject to the adjusted gross income tax… [C]orporations carrying on business as partners shall be liable for the adjusted gross income tax… (based on)… each partner's… distributive share… [1980]

45 IAC 3.1-1-153. Taxation of a corporate partner.

(a) A corporate partner's share of profit or loss from a partnership will be included in its federal taxable income and therefore generally subject to the same rules as any other adjusted gross income. [1993]

I. GENERAL STATEMENT

A partnership doing business in Indiana is not subject to adjusted gross income tax but must file an information return reporting the proportionate share of profit or loss distributed to each partner. Each partner receiving a distribution from a partnership doing business in Indiana must file an adjusted gross income tax return and pay the tax calculated thereon less any tax withheld [FN 1]

by the partnership at time of distribution.

The method of calculating a resident or a nonresident corporate partner's Indiana adjusted gross income is determined by the partner's business relationship with the partnership.

II. PARTNERSHIP DISTRIBUTIONS TO CORPORATE MEMBERS

A. Unitary Business Relationship 45 IAC 3.1-1-153(b)

If a corporate partner and its partnership maintain a unitary business relationship, the partnership distribution shall be distributed to the partner without any prior apportionment by the partnership. If the partner derives income from sources both within and without Indiana and is required to apportion its income, the partner's apportionment factors shall include the partner's proportionate share of the respective partnership factors.

B. Non-Unitary Business Relationship 45 IAC 3.1-1-153(c); (e)

If a corporate partner and its partnership do not maintain a unitary business relationship, the partnership distribution shall be distributed to the partner after any required apportionment by the partnership. The distribution, once apportioned to Indiana by the partnership, may not be included in any further apportionment calculations required on the partner's return.

III. UNITARY BUSINESS RELATIONSHIP [FN 2]

"Unitary business" means business activities or operations that are of mutual benefit, dependent upon, or contributory to one another in transacting business between a partnership and its corporate partners.

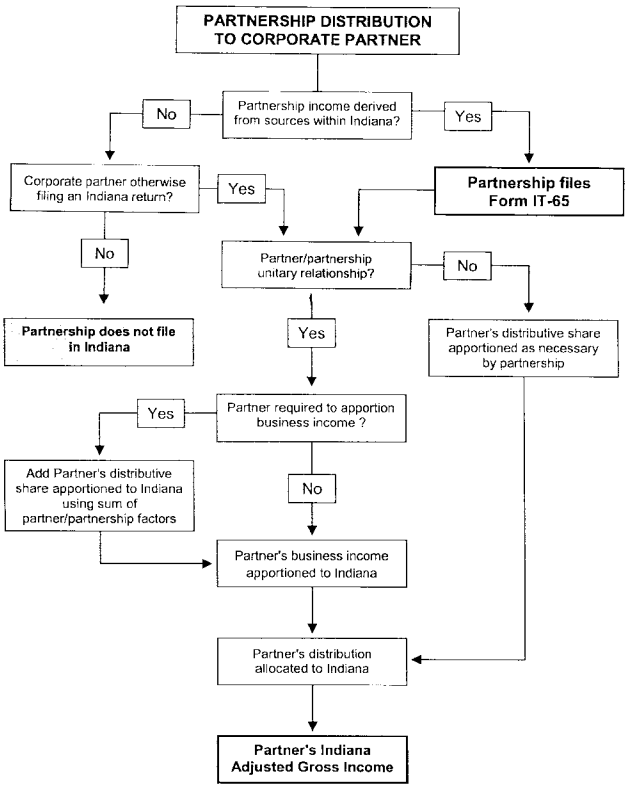
Unity may be established whenever there is unity of operation and use evidenced by centralized management or executive force, centralized purchasing, advertising, accounting, or other controlled interaction between a partnership and its corporate partners.

When evaluating the existence of a partner/partnership unitary business relationship, the percentage of individual partner ownership is not relevant.

[FN 1] 45 IAC 3.1-1-107(a)(2)

[FN 2] For purposes of this document, refer to IC 6-5.5-1-18(a) and (b) for additional explanation.

IV. PARTNERSHIP DISTRIBUTION TO CORPORATE PARTNER



DEPARTMENT OF STATE REVENUE
AUDIT-GRAM NUMBER IR-018
March 26, 2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

Packaging and Wrapping Materials and Equipment.

Authority: IC 6-2.5-5-3, 5.1, 6; IC 6-2.5-5-9(d); 45 IAC 2.2-5-8(d); 45 IAC 2.2-5-16

IC 6-2.5-5-9. Wrapping material.

(d) Sales of wrapping material(s)… are exempt from the state gross retail tax if the person acquiring the material(s)… acquires them for use as nonreturnable packages for selling the contents that he adds. [1980]

45 IAC 2.2-5-8. Sales of manufacturing machinery, tools and equipment used in direct production…

(d) Pre-production and post-production activities. "Direct use in the production process" begins at the point of the first operation or activity constituting part of the integrated production process and ends at the point that the production has altered the item to its completed form, including packaging, if required. [1987]

I. PRODUCING AND SHIPPING A COMPLETED PRODUCT

A. Producing a Completed Product

1. Purchases of machinery, tools, equipment, and supplies directly used [FN 1] or consumed [FN 2] in producing a packaged completed product for sale to a final consumer are exempt from Sales Tax.

2. Purchases of materials, including packaging materials [FN 3], incorporated [FN 4] into a packaged completed product for sale to a final consumer are exempt from Sales Tax.

B. Shipping a Completed Product

1. Purchases of tangible personal property to be used as wrapping materials for a packaged completed product during shipment to any buyer are exempt from Sales Tax.

2. Purchases of machinery, tools, equipment, and supplies used or consumed in producing or applying wrapping materials to a packaged completed product are subject to Sales Tax.

II. DEFINITIONS

A. "Packaged completed product" is that tangible personal property which is the fundamental product available for sale to a final consumer and includes any required packaging materials.

B. "Packaging materials" includes those materials incorporated as a material part of a completed product, the application of which constitutes the final step in an integrated production process. The term does not include "wrapping materials".

C. "Wrapping materials" means materials used to enclose, surround, or contain a packaged completed product or products during shipping to any buyer providing such materials are not customarily returned by the buyer to the seller for reuse by the seller. The term does not include material used to protect the packaged completed product during storage unless the materials are subsequently sold.

D. "Final consumer" means the final purchaser (in a possible series of purchasers) who ultimately consumes or uses the product for its intended purpose. "Final consumer" does not include a person acting as a wholesaler, retailer, or in a similar capacity.

The seller is deemed to have sold a packaged completed product to a final consumer if the seller is required to collect Sales Tax from the buyer. If the seller secures from the buyer an Exemption Certificate, Form ST-105, indicating any reason except "Resale Only", the seller is deemed to have sold a packaged completed product to a final consumer.

[FN 1] IC 6-2.5-5-3(b) Manufacturing machinery, tools, and equipment…
[FN 2] IC 6-2.5-5-5.1(b) Consumed in direct production…
[FN 3] 45 IAC 2.2-5-8(d) Production process… including packaging…
[FN 4] IC 6-2.5-5-6 Incorporation as a material part…

DEPARTMENT OF STATE REVENUE
INFORMATION BULLETIN NO. 68
Sales Tax
January 1998

Disclaimer: Information bulletins are intended to provide nontechnical assistance to the general public. Every attempt is made to provide information that is consistent with the appropriate statutes, rules and court decisions. Any information that is not

consistent with the law, regulations or court decisions is not binding on either the Department or the taxpayer. Therefore, the information provided herein should serve only as a foundation for further investigation and study of the current law and procedures related to the subject matter covered herein.

SUBJECT: State Educational Institutions

AUTHORITY: IC 6-2.5-4-6; IC 6-2.5-4-8; IC 6-2.5-5-16; IC 6-2.5-5-22; IC 6-2.5-5-24; IC 6-2.5-6-1; 45 IAC 2.2-5-24; 45 IAC 2.2-5-25; 45 IAC 2.2-5-46; 45 IAC 2.2-5-58.

INTRODUCTION

This information bulletin is directed to those colleges and universities which are recognized as governmental agencies and were created by an Indiana statute.

ACTIVITIES OF STATE COLLEGES OR UNIVERSITIES

Indiana Code, 6-2.5-4-8, provides, in relevant part, that:

An Indiana governmental entity, agency, instrumentality, or political subdivision (including a state college or university) is a retail merchant making a retail transaction when it performs private or proprietary activities that would constitute retail transactions under this article if those activities were performed by a retail merchant.

This section specifies that state colleges and universities act as retail merchants in respect to receipts derived from the conduct of private or proprietary activities.

For the purposes of this bulletin, the term "proprietary activities" is defined as activities generating revenues for state colleges or universities from the general public that are both customarily associated with the conduct of a private business enterprise, and are outside the scope of activities of governmental and educational functions as defined for state colleges or universities. Examples of proprietary activities include, but are not limited to, the following:

1) sales of merchandise, cards, clothing, toiletries, and other goods typically purchased in retail stores;
2) sales of textbooks by college and university bookstores;
3) sales of computer hardware, software and peripherals to the general public;
4) sales of athletic apparel and merchandise at intercollegiate athletic events and in retail operations;
5) sales of catering and food services provided to the general public; and
6) operation of hotels or other places of accommodations available to non-students.

The purpose for which state colleges and universities are granted exemption fall into four primary categories:

A) Teaching and instruction which involves educating citizens, businesses and institutions of the state through the use of conventional and electronic classroom facilities to provide:

1) courses which grant credit toward the attainment of an undergraduate or graduate degree;
2) post-graduate practical training and instruction in academic disciplines offered by state universities;
3) continuing education courses (non-credit);
4) professional development activities;
5) educational conferences, seminars and training meetings.

B) Research which includes expanding the knowledge base of the citizens, businesses and institutions of the state of Indiana through scientific inquiry and dissemination of scholarly information. Activities associated with the fulfillment of this function include participation in laboratory and field research, the development and distribution of educational or research related tools or materials that are published, copyrighted or patented by a state college or university.

C) Public service which includes activities that are consistent with other governmental and educational functions served by the state of Indiana, and other charitable, not-for-profit purposes for which the universities are granted exemption from Indiana gross income tax and federal income tax.

D) Other university activities that are customarily undertaken in the conduct of governmental functions and which include:

1) sponsoring continuing education activities;
2) operating the county extension service for the state;
3) providing public access to intercollegiate athletic functions;
4) providing public access to recreational and physical fitness facilities;
5) providing public access to musical, theatrical, and artistic performances;
6) providing access to informational and cultural events and productions; and
7) recruiting and development activities including recruiting of students and faculty.

SALES BY STATE COLLEGES OR UNIVERSITIES

The following are examples of sales made by colleges or universities that are predominantly for educational purposes and are not subject to sales tax.

1. Indiana Code 6-2.5-5-22 exempts the sale of food by not-for-profit colleges or universities if the purchaser is a student at the college or university. The sale of food by third parties (private caterers, restaurants, licensees or other lessees operating on the campuses of the college or university) to students do not qualify for exemption as such sales are not made by a qualified not-for-

profit educational organization. However, if the third parties are acting in agency capacity on behalf of the college or university, the exemption is applicable. The contracts with the third parties (private caterers, restaurants, licensees or other lessees operating on the campuses of the college or university) must specifically designate the third party as an agent on behalf of the college or university. Furthermore, the third party food provider must be subject to the control of the university in connection with the selling of food to students. Sale of food to members of the faculty or other employees are subject to Indiana sales tax. Sales of food to non-students of that college or university do not qualify for exemption. Example: Sale of food to a Ball State student visiting an Indiana University facility. Sales of food to elementary or secondary school students are subject to tax as IC 6-2.5-5-22 requires that the food be sold by the elementary school on its premises in order to qualify for the exemption.

For the purposes of this bulletin, the term "student" is defined to mean an individual enrolled or registered in courses which grant credit toward the attainment of an undergraduate or graduate degree or who is enrolled in an elementary or secondary school. Example: A high school student who is enrolled as a participant in a summer conference on a college or university campus is exempt from sales tax on meals provided to that student by the university or its agent on the campus premises. The term student includes any individual enrolled in remedial courses which are certified by the college or university.

Sales of educational materials, excluding books, stationery, or supplies, are exempt if sold to students as these sales are primarily intended to further the educational purpose of the college or university (Indiana Sales/Use Tax Regulation 45 IAC 2.2-5-58). The sale of cartographic, demographic or topographical maps or surveys required as part of the college or university's operation of the "county extension service" is exempt from Indiana sales/use tax. The sale of such educational material if sold to the general public is subject to tax as these items would be taxable if sold by a retail merchant. Example: Sales of the Indiana Law Review to members of the faculty, staff and the general public are subject to tax. However, these sales may still be exempt as sales in interstate commerce or where the purchaser is entitled to an exemption of its own (e.g. governmental entity [public library]). If the purchaser is entitled to an exemption, the purchaser must supply the educational institution with a valid exemption certificate.

For the purposes of this bulletin, the term "educational materials" means materials which communicate information, graphic images or sound, that are utilized in teaching, instruction, or research. Educational materials may be in various forms of media, including but not limited to:

1) scholarly and professional journals, reviews, and papers;
2) research reports, papers, surveys, polling data and summaries;
3) books, guides, and other printed instructional materials;
4) instructional audio and video materials; and
5) instructional software and computerized research tools.

The following are examples of sales made by colleges or universities that are subject to Indiana sales tax.

1. Sale of books, stationery, haberdashery, supplies or other property by an accredited college or university.

2. Sale of computers, software and related peripherals would be subject to tax unless sold to students and required to be purchased as part of an accredited curriculum.

3. Sale of food and drink at athletic, theatrical, artistic, cultural or informational events.

4. Receipts from the rental of accommodations for periods of less than thirty days to non-students are subject to Indiana sales tax and, if applicable, the county innkeepers tax. The term "accommodations" includes any room or rooms, lodgings in any commercial hotel, motel, inn, university memorial union, university residence hall, tourist camp or tourist cabin. The tax does not apply to any student renting lodging in a university residence hall while participating in a course of study for college credit at the college or university.

5. Sale of abandoned personal property if the property was not originally used in connection with the state educational institution's educational purpose.

PURCHASES BY STATE COLLEGES AND UNIVERSITIES

Transactions involving tangible personal property or service are exempt from sales tax if the person acquiring the property or service is a not-for-profit organization, primarily uses the property or service to carry on or to raise money to carry on its not-for-profit purpose, and is not an organization operated predominantly for social purposes. Furthermore, state colleges and universities are recognized as governmental agencies that qualify for the exemption under IC 6-2.5-5-16.

The following is an example of a purchase qualifying for exemption under the governmental exemption.

1. The purchase of food and beverage used predominantly in the performance of a governmental function such as recruiting students and faculty for a state educational institution if the purchase of food and beverage meets the following three requirements:

(a) The purchase must be invoiced directly to the state educational institution;
(b) The purchase must be paid for via government funds (a check issued by the respective state university); and
(c) The purchase must be for a governmental function as described above.

TELECOMMUNICATIONS

Indiana Code 6-2.5-4-6, as amended effective July 1, 1993, provides that a person is a retail merchant making a retail transaction when such person furnishes or sells an intrastate telecommunication service.

State educational institutions would be required to collect Indiana sales tax when they furnish or sell an intrastate telecommunication service to students, members of the faculty or staff.

An example of this transaction would be the educational institution billing students and members of the faculty and staff for their respective long distance intrastate phone calls. Any charges billed directly to students or members of the faculty and staff for "local service charges" would also be subject to the collection of Indiana sales tax.

GENERAL INFORMATION

Indiana state educational institutions are required to remit any sales tax collected in accordance with the reporting periods discussed in IC 6-2.5-6-1.

Where the sales and use tax remitted in the prior calendar year does not exceed $10 per month, the Indiana sales tax may be remitted annually.

Where the sales and use tax remitted in the prior calendar year does not exceed $25 per month, the Indiana sales tax may be remitted semi-annually.

Where the sales and use tax remitted in the prior calendar year does not exceed $75 per month, the Indiana sales tax may be remitted quarterly.

A retail merchant using a reporting period, other than monthly, must file the sales/use tax return and pay the tax not later than the last day of the month following the close of that reporting period.

Where the sales and use tax remitted in the prior calendar year does not exceed $1,000 per month, the Indiana sales tax must be remitted not more than 30 days after the end of the liability month.

Where the sales and use tax remitted in the prior calendar year exceeds $1,000 per month, the Indiana sales tax must be remitted not more than 20 days after the end of the liability month.

Where the sales and use tax remitted in the prior calendar year exceeds $10,000, (effective January 1, 1998) the retail merchant shall pay the sales/use tax by electronic fund transfer (as defined in IC 4-8.1-2-7) or by delivering in person or by overnight courier a payment by cashier's check, certified check, or money order to the department not later than 20 days after the end of the liability month.

STUDENT ORGANIZATIONS AT STATE COLLEGES AND UNIVERSITIES

Student organizations are informal student clubs, whose membership consists of students who share a common interest in the particular cause or activity that the organization exists for, promotes or furthers. To be exempt from sales tax the student organization must be recognized by the college university, connected with the state college or university and under the supervision of the college or university. Furthermore, the student organization's records must be maintained by the university as an "agency" account.

A student organization that is registered with and under the control of the college or university will not be required to register with the Indiana Department of Revenue as a not-for-profit organization. It will be considered a part of the college or university.

Kenneth L. Miller
Commissioner

DEPARTMENT OF STATE REVENUE

02960591.LOF

LETTER OF FINDINGS NUMBER: 96-0591 ITC
Adjusted Gross Income Tax
For Years 1991, 1992, and 1993

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Adjusted Gross Income Tax – Foreign Dividend Deduction

Authority: IC 6-3-2-12

The taxpayer protested the auditor's adjustments adding back taxpayer's Federal foreign dividend expense deductions to taxpayer's foreign dividend income deduction when calculating Adjusted Gross Income.

II. Tax Administration – Waiver of Penalty

Taxpayer seeks waiver of the penalties because the tax liabilities were due to reasonable cause and not due to willful neglect.

STATEMENT OF FACTS

Taxpayer calculated taxable income in a different way for each of three audit years. For the years 1991 and 1993, the taxpayer calculated the Adjusted Gross Income as being reduced by the foreign source dividend on the federal return without reducing the

foreign source dividend by the expenses taken as deductions to it on the federal return. The 1992 return was calculated with the Adjusted Gross Income being reduced by both the foreign source dividend and expenses. Taxpayer protests additional assessments based on Audit's addback of expenses associated with these foreign source dividends.

I. Adjusted Gross Income Tax – Foreign Dividend Deduction

DISCUSSION

In calculating its Indiana tax liabilities, taxpayer, pursuant to IC 6-3-2-12, deducted foreign source dividend income from its Indiana adjusted gross income. Audit, however, disagreed with taxpayer's calculus. Re-calculation by Audit resulted in an increase in taxpayer's Indiana adjusted gross income and tax. Proposed assessments of Indiana adjusted gross income tax followed.

Taxpayer, in response, directs the Department's attention to the language of IC 6-3-2-12(b), which states:

A corporation that includes any foreign source dividend in its adjusted gross income for a taxable year is entitled to a deduction from that adjusted gross income. The amount of the deduction equals the product of:

the amount of the foreign source dividend included in the corporation's adjusted gross income for the taxable year; multiplied by the percentage prescribed in subsection (c), (d), or (e), as the case may be.

The aforementioned subsections (c), (d), and (e) allow corporate taxpayers to receive a one hundred percent (100%) deduction for foreign source dividends received from corporations in which a taxpayer has an eighty percent (80%) or larger ownership interest; an eighty-five percent (85%) deduction for dividends received from corporations in which a taxpayer has a fifty to seventy-nine percent (50%-79%) percent ownership interest; and a fifty percent (50%) deduction for dividends received from corporations in which a taxpayer has less than a fifty percent (50%) ownership interest. IC 6-3-2-12(c)-(e).

This statutory language is cogent and clear. IC § 6-3-2-12 authorizes pro rata deductions (based on the percentage ownership of the payor by the payee) of certain foreign source dividend income. In this instance, taxpayer has followed the statutory prescriptions in calculating its foreign source dividend deductions.

FINDING

Taxpayer's protest is sustained.

II. Tax Administration – Waiver of Penalty

DISCUSSION

The prior finding renders this issue moot.

FINDINGS

The taxpayer's appeal is sustained.

DEPARTMENT OF STATE REVENUE

02970064.LOF

LETTER OF FINDINGS NUMBER: 97-0064
Indiana Corporation Income Tax
For Tax Year Ending March 31, 1994

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of the document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Disallowance of Taxpayer's Nonbusiness Income Deduction on Indiana Corporation Income Tax Return – Litigation Settlement Income Characterized as Business or Nonbusiness Income

Authority: IC 6-3-1-3.5(b); IC 6-3-1-20; IC 6-3-1-21; IC 6-3-2-2(a); IC 6-3-2-2(b); IC 6-3-2-2(g)-(k); 45 IAC 3.1-1-29

Taxpayer protests the Department's determination that certain of taxpayer's income, received as the result of a litigation settlement, should be classified as apportionable business income. The taxpayer maintains that the income derived from an activity not normally undertaken by the taxpayer but was attributable to another company's negligence. Therefore, according to the taxpayer, in determining the taxpayer's adjusted gross income tax the income should be allocated as nonbusiness income to the taxpayer's home state.

STATEMENT OF FACTS

The taxpayer is incorporated and commercially domiciled in a state other than Indiana. The taxpayer operates helicopters in various states including Indiana. The taxpayer's helicopters are powered by engines produced by a manufacturer. Taxpayer brought a lawsuit against the manufacturer. Subsequently, taxpayer and manufacturer reached and concluded a settlement agreement whereby manufacturer paid a settlement to the taxpayer. The settlement amount was included within the taxpayer's federal income tax returns. The Department determined that the settlement income was properly characterized as "business income" and, as a result, was subject

to the three-factor formula for apportioning business income. The taxpayer protested that determination, but waived its right to an administrative hearing. Taxpayer's representative was asked to supply information regarding the nature of the settlement amount. In the Department's correspondence, taxpayer's representative was asked whether the settlement awarded taxpayer consisted of compensation for lost business revenues or compensation for faulty equipment. The taxpayer declined to respond or to provide additional information. Accordingly, this Letter of Findings has been prepared on the basis of the information contained within the Department's file and upon the basis of the taxpayer's written protest letter dated December 17, 1996.

DISCUSSION

I. Disallowance of Taxpayer's Nonbusiness Income Deduction on Indiana Corporation Income Tax Return

Taxpayer protests the Department's determination that income, derived from a settlement agreement, constitutes business income and is subject to the three-factor apportionment set out in IC 6-3-2-2(b). Nonbusiness income is allocated to specific jurisdictions pursuant to IC 6-3-2-2(g)-(k). Business income apportioned to the state of Indiana, plus nonbusiness income allocated to Indiana, plus certain modifications required by IC 6-3-1-3.5(b), determines the total of the taxpayer's net income subject to the state's adjusted gross income tax. Taxpayer argues that the litigation award was acquired outside the regular course of its business and that the award should be directly allocated to its home state.

Under Indiana law, corporate adjusted gross income derived from sources within Indiana is reported as either business or nonbusiness income. IC 6-3-2-2(a). Under IC 6-3-1-20, business income is defined as "income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitutes integral parts of the taxpayer's regular trade or business." Nonbusiness income is defined in the negative and "means all income other than business income." IC 6-3-1-21.

Regulation 45 IAC 3.1-1-29 defines business income as that "income from transactions and activity in the regular course of the taxpayer's trade or business including income from tangible and intangible property if the acquisition, management, or disposition of the property are integral parts of the taxpayer's regular trade or business." That same regulation goes on to state that "[t]he classification of income by the labels occasionally used, such as manufacturing income, compensation for services, sales income, interest, dividends, rents, royalties, gains, operating income, non-operating income, etc., is of no aid in determining whether income is business or nonbusiness income. Income of any type or class and from any source is business income if it arises from transactions and activity occurring in the regular course of a trade or business. Accordingly, the critical element in determining whether income is 'business income' or 'nonbusiness income' is identification of the transactions and activity which are the elements of particular trade or business." Id.

In determining the nature of income, states have employed one of two tests based upon the previous language. The regulatory phrase, "income from transactions and activity in the regular course of the taxpayer's trade or business..." has led to the formulation of the "transactional test." Id. Under this test, the nature of the particular transaction is critical in determining the nature of the income in question. The second test is the "functional test" and is derived from the language which states that "income from tangible and intangible property [represents business income] if the acquisition, management, or disposition of the property are integral parts of the taxpayer's regular trade or business." Id. In this second test, the particular use or function of the asset -- to which the income at issue is attributable -- within the taxpayer's regular trade or business is used to categorize the income as either business or nonbusiness.

Taxpayer argues that the settlement agreement income should be classified as nonbusiness income because the income derives from an activity not normally undertaken by the taxpayer and because the income was not derived from its tangible or intangible property. Taxpayer maintains that it is in the business of providing transportation services and is not in the business of suing manufacturers. According to the taxpayer, the settlement agreement income is attributable not to any activity of, or asset belonging to, the taxpayer but is entirely attributable to the manufacturer's negligence.

Taxpayer oversimplifies the issues and errs in its analysis. Taxpayer would have the Department conclude that the settlement agreement income arose in a vacuum entirely independent of and distinct from the taxpayer's activities and assets. Clearly, the facts indicate otherwise. Taxpayer's aircraft are central to the taxpayer's business operations. Presumably, it was the purported deficiencies of taxpayer's aircraft, critical to taxpayer's business activities, which led taxpayer to seek compensation. Although taxpayer has declined to discuss in detail the basis for the action it brought against manufacturer or the basis for the settlement determination, it may be safely presupposed that taxpayer's lawsuit was predicated upon the impact those deficiencies had upon its business activities and upon its physical assets. Similarly, it may be presumed that the amount of the settlement agreement was not determined capriciously. Whether based on the taxpayer's lost business opportunities, damages sustained by its equipment, or the added expenses incurred by the taxpayer in maintaining the aircraft, the settlement agreement was inextricably linked to both taxpayer's business activities and business assets.

FINDING

Taxpayer's protest is respectfully denied.

DEPARTMENT OF STATE REVENUE

04980011.LOF

LETTER OF FINDINGS NUMBER: 98-0011
Sales and Use Tax
For the Periods: 12/31/94 through 12/31/96

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Sales and Use Tax – Simulcast Services
Authority: IC 6-2.5-2-1; IC 6-2.5-4-10; IC 6-2.5-4-6; IC 6-2.5-1-1; IC 6-2.5-2-2
The taxpayer protests the assessment of gross retail tax on telecommunication services.

II. Sales and Use Tax – Decoder Rental
Authority: IC 6-2.5-2-1(b)
The taxpayer protests the assessment of gross income tax on decoder rental.

III. Sales and Use Tax – Totalisator Services
Authority: IC 6-2.5-2-1; 45 IAC 2.2-4-27(d)(3)(B)
The taxpayer protests the assessment of gross retail tax on totalisator services.

IV. Sales and Use Tax – Laundry Services
Authority: IC 6-2.5-2-1
The taxpayer protests the assessment of gross retail tax on laundry services.

STATEMENT OF FACTS

The taxpayer is in the business of operating and maintaining a pari-mutuel racetrack. The taxpayer also has three satellite locations in Indiana. In addition to live racing, the taxpayer broadcasts other races. The taxpayer also offers off track betting at its satellite locations.

I. Sales and Use Tax – Simulcast Services

DISCUSSION

In 1994 the taxpayer entered into a contract with "S" to provide television production equipment and services at its various locations. As part of the contract "S" agreed to provide for the design, installation, operation, and maintenance of closed circuit television systems and other systems and services including equipment, personnel, and supervision to produce and display television programs. "S" utilized specialized equipment owned by it to fulfill the contract and included the equipment costs as part of the total price for services rendered. "S" then charged the taxpayer based upon several factors including the number and types of races produced and the number of hours required to produce the races.

Retail transactions made in Indiana are subject to sales tax. IC 6-2.5-2-1. The rental of tangible personal property is defined as a retail transaction. IC 6-2.5-4-10. Sales of services, except for some specifically enumerated services, are not retail transactions and are not subject to sales tax. Transactions furnishing both tangible personal property and services pursuant to a single contract for a total combined price are unitary transactions. IC 2.5-1-1. Sales tax is imposed on unitary transactions. IC 6-2.5-2-2.

State gross retail tax was assessed against the taxpayer on the services it purchased from "S" as one of the taxable enumerated services defined at IC 6-2.5-4-6:

(a) As used in this section, "telecommunication services" means the transmission of messages or information by or using wire, cable, fiber optics, laser, microwave, radio, satellite, or similar facilities. The term does not include value added services in which computer processing applications are used to act on the form, content, code, or protocol of the information for purposes other than transmission.
(b) A person is a retail merchant making a retail transaction when the person:
(1) furnishes or sells an intrastate telecommunication service; and
(2) receives gross retail income from billings or statements rendered to customers.

"S" provides services and equipment to Taxpayer at three Indiana locations. Each of these locations is staffed by "S" employees. These employees provide services including the production of a daily television racing program taped using several different cameras, race officials' replays and slow motion replays. For a full day of simulcasting and an evening of live racing at Taxpayer's facility, one operator and one supervisor from "S" control the simulcasting. For a full day of live racing, "S" provides three operators, four camera operators, one uplink operator and one supervisor. These employees have the specific expertise and skill to install, operate, maintain and service the equipment on a daily basis. In this case the taxpayer purchases services and equipment which include more than the intrastate transfer of information.

The transaction is, however, a unitary transaction furnishing both tangible personal property and services, both taxable and exempt, for a single price pursuant to a contract. Therefore the sales tax properly applies in this situation.

FINDING

The taxpayer's protest is denied.

II. Sales and Use Tax – Decoder Rental

DISCUSSION

In order to receive satellite transmissions from other racing facilities the taxpayer rented decoders. The decoders decipher the transmissions and allow the taxpayer's patrons to view other races. The taxpayer rented decoders from various vendors with property located in Indiana. The taxpayer protests the assessment of gross retail tax on the rental of these decoders.

The taxpayer contends that it cannot pay the gross retail tax directly to the state because retail merchants have the obligation to collect the tax pursuant to the following provisions of IC 6-2.5-2-1(b):

> The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state.

In this case, the taxpayer acquired the property in a retail transaction and is therefore liable for the tax. The fact that the agent, the retail merchant, did not collect the tax as the agent for the state does not take the authority to collect the tax away from the principal, the state.

FINDING

The taxpayer's protest is denied.

III. Sales and Use Tax – Totalisator Services

DISCUSSION

During 1994, the taxpayer entered into contracts with "UT" for the provision of totalisator services. As part of the contract, "UT" was responsible for automatically registering and totaling the amount wagered on both live and simulcast races and then issuing daily summaries of the wagering activities at each of the taxpayer's locations. At all times, "UT" retained ownership of and insured the equipment used to provide the services. "UT" always exercised control over the computers used in providing the totalisator service. "UT" has a system manager responsible for the Indiana service area. "UT" charged for its services based upon a percentage of all pari-mutuel wagers and the number of racing days. In mid 1995, "UT" began charging and collecting sales tax on the total contract price. The taxpayer protests the assessment of tax prior to mid 1995.

The issue to be determined is whether this represents a lease of tangible personal property, which is taxable pursuant to IC 6-2.5-2-1, or the provision of a nontaxable service.

This issue is addressed at 45 IAC 2.2-4-27(d)(3)(B) as follows:

> The rental of tangible personal property together with an operator as part of a contract to perform a specific job in a manner to be determined by the owner of the property or the operator shall be considered the performance of a service rather than a rental or lease provided the lessee cannot exercise control over such property and operator.

The taxpayer contends that the situation fits within this definition of a service. The taxpayer does lease the tangible personal property, the totalisator computers. According to the contract, "UT" services and maintains the computer system and trains the taxpayer's employees to operate the equipment and sets up the operation protocols. The contract further states that the taxpayer will furnish the necessary staff of tellers and mutuel department employees and that they will be supervised by employees of the taxpayer. The taxpayer therefore exercises significant control and does not qualify for exemption pursuant to 45 IAC 2.2-4-27(d)(3)(B).

FINDING

The taxpayer's protest is denied.

IV. Sales and Use Tax – Laundry Services

DISCUSSION

The taxpayer's employees are required to wear uniforms. The taxpayer pays a per pound charge to a laundry service for the laundering of the uniforms. The gross retail tax is on retail transactions transferring tangible personal property. IC 6-2.5-2-1. Unless the provision of a service is specifically defined as a retail transaction, it is not subject to the gross retail tax. The provision of laundry services is not defined as a retail transaction. Therefore, it is a nontaxable service.

FINDING

The taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

04980184P.LOF

LETTER OF FINDINGS NUMBER: 98-0184P
Use Tax
Calendar Year 1996

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE(S)

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2

Taxpayer protests the penalty assessed.

STATEMENT OF FACTS

Taxpayer, a banking entity, is a Delaware corporation conducting various types of mortgage services in Indiana. A sales and use tax audit was completed on February 9, 1998. The taxpayer was assessed use tax on several items including purchases of computer supplies, brochures, magazines, and other miscellaneous items. A hearing was scheduled for September 28, 1999; however, the taxpayer asked the department to write its Letter of Finding based upon a brief dated April 15, 1998.

Taxpayer failed to remit use tax on clearly taxable purchases although it had a use tax accrual system in place.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer protests the imposition of a ten percent (10%) negligence penalty. Taxpayer states that the penalty was based on the use tax assessed in the audit and the use tax liability resulted from vendors failing to charge sales tax to the taxpayer. The taxpayer also states that it has implemented changes in its procedures to ensure adherence to Indiana tax law in the future. Taxpayer requests a penalty waiver.

A review of the audit indicates that the purchases for which no use tax was accrued or paid amounted to fifty-two percent (52%) of the use tax due for calendar year 1996. Taxpayer did not provide reasonable cause to allow a waiver of the penalty.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

02980242.LOF

LETTER OF FINDINGS NUMBER: 98-0242
Indiana Corporation Income Tax
For Years 1992, 1993, 1994, and 1995

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Negative Nonbusiness Income Claimed by the Taxpayer – Net Expenses Resulting from Aircraft Accident

Authority: IC 6-3-1-20; IC 6-3-1-21; IC 6-3-2-1(b); IC 6-3-2-2(a); Atlantic Richfield Co. v. State, 601 P.2d 628 (Colo. 1979); 45 IAC 3.1-1-62

Taxpayer protests the auditor's determination that a certain loss experienced by taxpayer at its Indiana business site constituted negative "business income" and should have been included within the apportionment formula. Taxpayer asserts that the casualty loss should not be apportioned because it was unique to Indiana, was the result of an unusual and unpredictable event, and because the loss directly impacted the financial results of the Indiana business site.

II. Apportionment of Partnership Income – Inclusion of Joint Ventures' Gross Receipts in the Sales Factor

The taxpayer has protested the decision by the auditor to correct the amount reported by the taxpayer for the sales within Indiana and sales everywhere components of the sales factor. The taxpayer argues that gross sales everywhere needs to be corrected for tax years 1993 and 1995.

III. Abatement of Ten Percent Negligence Penalty

Authority: IC 6-8.1-10-2.1(a); IC 6-8.1-10-2.1(b)(2), (4); 45 IAC 15-11-2(b); 45 IAC 15-11-2(c)

The taxpayer has protested the auditor's determination recommending a ten-percent negligence penalty against all the years of assessment. The taxpayer argues that the penalty should not have been assessed because it fully disclosed and properly determined Indiana adjusted gross income during all relevant tax years.

STATEMENT OF FACTS

Taxpayer is in the hotel and lodging business. Taxpayer operates hotels in various states including a hotel Indiana. The taxpayer's headquarters is located in Missouri.

DISCUSSION

I. Negative Nonbusiness Income Claimed by the Taxpayer

In February of 1992, the taxpayer's Indiana business location was the site of a military airplane crash resulting in substantial damage to the taxpayer's property. After the taxpayer completed repairs to its business property and after the taxpayer recovered all related insurance

proceeds from the government, the taxpayer sustained a net loss of approximately $491,000. This amount represents the difference between the amount of insurance recovery and the amount the taxpayer spent repairing and rebuilding its Indiana hotel business.

Initially the taxpayer claimed the $491,000 as "negative non-business" income. The auditor found that this decision was erroneous because, according to the auditor, the $491,000 constituted "negative business income" (loss). The taxpayer argues that this particular loss, because it was unusual and unpredictable, occurred at the taxpayer's Indiana location, and because the loss impacted the financial results of the taxpayer's Indiana business site, should not be included in the apportionment formula but should be allocated exclusively to the state of Indiana. According to the taxpayer, the application of the standard three-factor apportionment formula to the loss would result in an unfair tax to the taxpayer's Indiana site when calculating the taxpayer's adjusted gross income tax. Further, the taxpayer argues that applying the standard three-factor apportionment creates an arbitrary division of income and effects an unfair hardship and injustice upon the taxpayer.

Indiana levies adjusted gross income tax on corporate income attributable to Indiana. In order to determine what corporate income is attributable to Indiana, it must first be determined whether the income is business or non-business income. IC 6-3-2-2(a). Under IC 6-3-1-20, "'business income' means income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitutes integral parts of the taxpayer's regular trade or business operations." In contrast, non-business income is defined in the negative and "means all income other than business income." IC 6-3-1-21.

The taxpayer predicates its assertion, that the $491,000 loss should be allocated exclusively to its Indiana business location, upon the unique circumstances under which the loss was incurred. However, under the first of the two tests, which the Department employs to distinguish business and non-business income – the functional test and the transactional test – "the extraordinary nature or the infrequency of the transactions is irrelevant." Atlantic Richfield Co. v. State, 601 P.2d 628, 631 (Colo. 1979). Separated from the unique circumstances under which the loss occurred, the taxpayer's $491,000 loss is ordinary business income analogous to the proceeds attributable to any ordinary insurance recovery. Separated from the unique circumstances under which the loss occurred, the $491,000 represents a loss directly attributable to the reconstruction of one of the taxpayer's business locations and falls within the classification of income "arising from the taxpayer's trade or business." IC 6-3-1-20. Therefore, the $491,000 loss is properly classified as ordinary business income.

Having made the threshold determination that taxpayer's 1992 loss is ordinary business income, that income becomes subject to the apportionment formula set out in IC 6-3-2-1(b). Specifically, the taxpayer may not adopt a reporting methodology that, in effect, provides for a "separate accounting" of its Indiana operation. Under 45 IAC 3.1-1-62, the Department will allow the taxpayer to "depart from use of the standard formula only if the use of such formula works a hardship or injustice upon the taxpayer, results in an arbitrary division of income, or in other respects does not fairly attribute income to this state or other states." Such a departure is warranted only "in limited and unusual circumstances (which ordinarily will be unique and nonrecurring) when the standard apportionment provisions produce incongruous results." Id.

FINDING

The taxpayer's protest is respectfully denied.

DISCUSSION

II. Apportionment of Partnership Income

Taxpayer operates its business on a calendar year basis with an annual audit prepared and concluded in early May of each year. Thereafter, all state income tax returns -- including taxpayer's Indiana returns -- are filed in advance of the taxpayer's final audited statements and in advance of the final Federal 1120. The data used for taxpayer's state income tax returns are the taxpayer's final numbers pending the annual audit and the final Federal 1120. The auditor, aware of the taxpayer's financial practices, adjusted the taxpayer's state figures to conform with the information on the taxpayer's federal returns as filed. The taxpayer has set forth a generalized argument that the auditor, in adjusting the Indiana returns, erred by failing to include certain receipts derived from hotels in which taxpayer participated as a joint equity partner. Subsequent review of the taxpayer's state and federal returns raises questions concerning the proper characterization of the taxpayer's partnership income and the computation of the taxpayer's sales factor. Given the absence of information which supports a decision to either exclude or include the taxpayer's partnership income, the Department must ask audit to revisit the taxpayer's state and federal returns.

FINDING

Audit is requested to make the aforementioned determinations consistent with the language of this Letter of Findings.

DISCUSSION

III. Abatement of Ten Percent Negligence Penalty

Taxpayer requests that the 10% negligence penalty, imposed under the authority of IC 6-8.1-10-2.1(a), be abated. IC 6-8.1-10-2.1(a)(3) imposes on the taxpayer a penalty for a "deficiency that is due to negligence." The penalty is limited to ten-percent of the amount of the tax that was not timely remitted. IC 6-8.1-10-2.1(b)(2), (4). The standards under which negligence is determined and the penalty imposed is found at 45 IAC 15-11-2(b) which states that "'[n]egligence' on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result

from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations." The regulation goes on to state that the Department shall determine negligence "on a case by case basis according to the facts and circumstances of each taxpayer." Id.

The Department is authorized to waive the penalty "if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence." 45 IAC 15-11-2(c). The regulation provides a non-exclusive list of factors, which go toward establishing reasonable cause, but concludes that "[r]easonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case." Id.

Taxpayer requests abatement of the negligence penalty because it feels it made a good faith effort to accurately file its tax returns. The taxpayer asserts that the calculation of its tax liabilities, given certain unique factual and business circumstances, fairly and accurately reflects its Indiana income.

Taxpayer requests abatement of the negligence penalty based upon general equitable principles. However, absent concrete and specific factual indicia upon which to substantiate the taxpayer's request, the Department must decline the opportunity to abate the assessed penalties.

FINDING

Taxpayer's protest is respectfully denied.

DEPARTMENT OF STATE REVENUE

02980457.LOF

LETTER OF FINDINGS NUMBER: 98-0457
State Corporate Income Tax
For 1989, 1990, 1991, 1992, and 1993

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Income Tax – Foreign Source Dividends/Expense Deduction

Authority: Ind. Code § 6-3-2-12

Taxpayer protests the reduction of the foreign source dividend deduction by related expenses.

STATEMENT OF FACTS

Taxpayer is engaged in multinational operations. The Department visited taxpayer and conducted an audit for tax periods ending in 1988 to 1993. This audit resulted in additional proposed assessments of Indiana adjusted gross income tax. Taxpayer now protests these assessments.

I. Income Tax – Foreign Source Dividends/Expense Deduction

DISCUSSION

In calculating its Indiana tax liabilities, taxpayer, pursuant to IC 6-3-2-12, deducted foreign source dividend income from its Indiana adjusted gross income. Audit, however, disagreed with taxpayer's calculus. Re-calculation by Audit resulted in an increase in taxpayer's Indiana adjusted gross income and tax. Proposed assessments of Indiana adjusted gross income tax followed.

Taxpayer, in response, directs the Department's attention to the language of IC 6-3-2-12(b), which states:

A corporation that includes any foreign source dividend in its adjusted gross income for a taxable year is entitled to a deduction from that adjusted gross income. The amount of the deduction equals the product of:

(1) the amount of the foreign source dividend included in the corporation's adjusted gross income for the taxable year; multiplied by

(2) the percentage prescribed in subsection (c), (d), or (e), as the case may be.

The aforementioned subsections (c), (d), and (e) allow corporate taxpayers to receive a one hundred percent (100%) deduction for foreign source dividends received from corporations in which a taxpayer has an eighty percent (80%) or larger ownership interest; an eighty-five percent (85%) deduction for dividends received from corporations in which a taxpayer has a fifty to seventy-nine percent (50%-79%) percent ownership interest; and a fifty percent (50%) deduction for dividends received from corporations in which a taxpayer has less than a fifty percent (50%) ownership interest. IC 6-3-2-12(c)-(e).

This statutory language is cogent and clear. IC § 6-3-2-12 authorizes pro rata deductions (based on the percentage ownership of the payor by the payee) of certain foreign source dividend income. In this instance, taxpayer has followed the statutory prescriptions in calculating its foreign source dividend deductions.

FINDING

Taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

04980491.LOF

LETTER OF FINDINGS NUMBER: 98-0491
State Gross Retail and Use Taxes
For Years 1994, 1995, and 1996

NOTICE: Under 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Sales/Use Tax Assessment – Applicability of the Gross Retail Tax to Purchases of UPC/Bar Code Labels Affixed to Taxpayer's Nonreturnable Containers

Authority: IC 6-2.5-5-6; 45 IAC 2.2-5-14; 45 IAC 2.2-5-14(e)(1); 45 IAC 2.2-5-14(e)(3)

The taxpayer protests the auditor's determination that use tax should be assessed on certain labels affixed to non-returnable containers. The auditor determined that the labels were taxable because they were not incorporated by the taxpayer as a material or integral part of tangible personal property produced for resale. The taxpayer argues that the labels, which display UPC or bar codes, are items directly used in the direct production of finished goods and are, therefore, exempt.

II. Sales/Use Tax Assessment on Electrical Consumption – Results of Energy Consumption Audit

Authority: IC 6-2.5-4-5(c)(3); IC 6-8.1-5-1(b); 45 IAC 2.2-4-13(e)

The taxpayer protests the auditor's determination that a portion of taxpayer's electrical consumption during the year 1996 was subject to sales tax because the percentage of exempt usage for the year 1996, as determined by an on-site utility study, failed to reach the 50% threshold necessary to qualify for the "predominant use" exemption. The taxpayer argues that the electric utility study employed an incorrect method to determine the electrical consumption of certain items of taxpayer's non-exempt equipment. Purportedly, the use of this particular method resulted in an energy audit that substantially overstated the amount of taxpayer's non-exempt electric usage.

III. Sales/Use Tax Assessment on Certain Equipment – Manufacturing Equipment Used in the Direct Production of Taxpayer's Tangible Personal Property

Authority: IC 6-2.5-5-3(b); IC 6-8-5-1(b); 45 IAC 2.2-5-8; 45 IAC 2.2-5-8(a); 45 IAC 2.2-5-8(b); 45 IAC 2.2-5-8(c); 45 IAC 2.2-5-8(d); 45 IAC 2.2-5-10; 45 IAC 2.2-5-10(c); 45 IAC 2.2-5-16; 45 IAC 2.2-5-17

The taxpayer protests the auditor's determination that various items of equipment did not qualify for the manufacturing exemption because they lacked an essential and integral relationship with the taxpayer's manufacturing process. The taxpayer maintains that certain of these items – in particular label printers, die cut stencils, tape dispensers, coil straighteners – are equipment that does play a vital role in the manufacturing of taxpayer's final product and, therefore, qualify for the manufacturing exemption.

IV. Sales and Use Tax Assessment on Packaging Materials – Packing Materials Placed Within Shipping Enclosures

Authority: IC 6-2.5-5-3; IC 6-2.5-5-9(d); General Motors Corp. v. Dept. of State Revenue, 578 N.E.2d 399 (Ind. Tax Ct. 1991); 45 IAC 2.2-5-16; 45 IAC 2.2-5-16(a); 45 IAC 2.2-5-16(c)(1); 45 IAC 2.2-5-16(d)(1); 45 IAC 2.2-5-16(e)(2)

The taxpayer protests the auditor's determination that specific packing materials, placed within or used to enclose the taxpayer's shipping containers, are subject to the use tax because, according to the auditor, these items do not in any way qualify for an exemption. The taxpayer maintains that these packing materials – corrugated pads, partitions, spacers, separators, stuffing materials, filling materials, stretch film, strapping materials, sealing tape, top caps – are necessary to protect the packaged goods from harm and to provide the taxpayer's customers with undamaged, marketable goods.

V. Abatement of the Ten Percent Negligence Penalty

Authority: IC 6-8.1-10-2.1; IC 6-8.1-10-2.1(d); 45 IAC 15-11-2(b); 45 IAC 15-11-2(c)

The taxpayer maintains that, based upon the its diligent good faith efforts to comply with the state's tax regulations, the ten-percent negligence penalty should be entirely abated.

STATEMENT OF FACTS

The taxpayer is a manufacturer of a variety of automobile safety equipment including marker lights, reflectors, turn signals, and rear view mirrors. The taxpayer manufactures the component parts in Indiana. Some of the component parts are then assembled at the Indiana site into finished products. The other components are packed, shipped, and then assembled at the taxpayer's assembly facility located in Mexico. The finished goods are shipped by common carrier to distribution centers and automobile manufacturers throughout the world.

I. Sales/Use Tax Assessment – Applicability of the Gross Retail Tax to Purchases of UPC/Bar Code Labels Affixed to Taxpayer's Nonreturnable Containers

DISCUSSION

The taxpayer has protested the auditor's determination that its purchase of certain labels is subject to sales tax. These labels,

which display UPC / Bar Code information, are affixed to the outside of non-returnable containers. Inside these closed containers are multiple packages of either the taxpayer's individual finished goods or component parts. The UPC / Bar Code labels provide coded information which identifies the contents of the package and the product quantity. According to the taxpayer, the UPC / Bar Code labels are required by taxpayer's customers and are used by the customers for inventory control purposes.

The auditor determined that the labels were subject to the Indiana gross sales tax because the taxpayer did not incorporate the labels as a material or integral part of tangible personal property, produced for resale, as specified in 45 IAC 2.2-5-14. Instead, the auditor determined that the UPC / Bar Code labels served a dual function. The coded labels were used by the taxpayer as part of its own warehouse management system. The auditor found that the labels were used by the taxpayer to determine the quantity of items available and to locate particular items within the taxpayer's warehouse without having to open and inspect the contents of each container. In addition, the auditor found that the coded labels were used to facilitate the tracking of taxpayer's goods during and after the production process.

The purchase of labels is exempt from the gross retail tax to the extent that the labels are incorporated into other property which is itself exempt. IC 6-2.5-5-6, provides that "[t]ransactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for incorporation as a material part of other tangible personal property which the purchaser manufactures... for sale in his business." 45 IAC 2.2-5-14(e)(1) provides that in order for the exemption to take effect, "[t]he material must be physically incorporated into and become a component part of the finished product."

Taxpayer's Bar Code / UPC labels, affixed to the outside of taxpayer's containers are not incorporated into the taxpayer's finished product and, consequently, the purchase of those labels – or materials used to produce the labels – is not exempt from the imposition of the gross retail tax. 45 IAC 2.2-5-14 exempts those labels which are affixed to a finished product which is itself "produced for sale by the purchaser." 45 IAC 2.2-5-14(e)(3). The taxpayer is in the business of manufacturing, as a finished product, various automobile parts. In facilitating that manufacturing process, the taxpayer has adopted a sophisticated labeling, tracking, and inventory control system. This integrated system, of which the labels are simply the most conspicuous component, is intended for the benefit of the taxpayer. Once the labels leave taxpayer's control, the label's utility is over and their continued presence, as part of the product packaging, is an irrelevancy. When the downstream consumer acquires one of taxpayer reflectors, lights, or other safety devices, the Bar Code / UPC label has long since served its purpose and has been discarded along with the shipping container in which the individual items were originally packaged and shipped.

Because taxpayer's Bar Code / UPC labels are not incorporated into the tangible personal property taxpayer produces for resale, because the labels do not become a material part of the item purchased by consumer, and because the labels are used by taxpayer for its own inventory and record keeping purposes, the purchase of the labels is entirely subject to the imposition of the state's gross retail tax.

FINDING

Taxpayer's protest is respectfully denied.

II. Sales/Use Tax Assessment on Electrical Consumption – Results of Energy Consumption Audit

DISCUSSION

At the request of the taxpayer, the Department provided assistance in the preparation of a utility study. One portion of that audit, the electric utility study, conducted with the assistance of Department of Revenue personnel, resulted in a determination that taxpayer's 1996 electrical consumption was less than 50% attributable to the taxpayer's manufacturing process. Specifically, the electric utility study concluded that 44.1% of taxpayer's electrical consumption could be attributed to exempt purposes. The 1996 results differed from determinations made for 1994 and 1995 in which the predominant use exemption (45 IAC 2.2-4-13(e)) was applicable because more than 50% of taxpayer's electrical usage was attributable to excepted purposes.

Under IC 6-2.5-4-5(c)(3), the sale of electricity used for the purpose of manufacturing is exempt from sales or use tax. However, because taxpayer's electrical service is metered from a single source and is used for both manufacturing and non-manufacturing purposes, taxpayer's entire electrical bill is subject to tax. Taxpayer can claim a "predominant use" exemption under the provisions of 45 IAC 2.2-4-13(e), if "more than fifty percent (50%) of [taxpayer's] utility services... are consumed for excepted use."

The utility study employed the following methodology. All of taxpayer's electrical equipment was sorted into production and non-production categories. The electrical consumption for non-production equipment was determined by reading the "face plate" of each item of equipment. The annual electrical consumption for each non-exempt piece of equipment was calculated by multiplying the power rating by the number of hours of daily operation by the number of days of operation each year. The total electrical consumption, attributable to non-exempt purposes, was subtracted from the actual amount of electricity consumed during the year as established by the taxpayer's electric utility bills.

The taxpayer argues that, in conducting the electric utility study, the Department erred in its methodology of determining the electrical rating for individual items of equipment. Taxpayer maintains that determining the electrical rating for individual items of equipment by reading the "face plate" rating inflates the amount of actual electrical usage. In refuting the Department's calculations, the taxpayer randomly chose six items of equipment, asked an electrical contractor to meter the actual electrical consumption of that

equipment, and compared those results with the results obtained by the Department in the original study. The taxpayer maintains that the results of its own testing demonstrates that the electrical consumption of the six selected items is approximately 80% less than the figure determined in the original audit.

The sample of six items of equipment represents a very small sampling of the hundreds of items listed within the original energy audit. While a comparison of the Department's estimated consumption rates and the taxpayer's measured rates reveals some substantial differences, it would be inappropriate to extrapolate the consumption rates determined by the taxpayer's sampling method to the hundreds of items listed on the seventeen pages of the original utility study. The taxpayer has failed to overcome the presumption of correctness afforded the auditor's original determination as provided under IC 6-8.1-5-1(b).

However, the taxpayer has raised substantive issues – supported by independent, quantitative measurements – such that it would be appropriate for the Department to revisit the issue and to conduct a supplemental audit of the taxpayer's utility usage. This recommendation is supported by the fact that the conclusions reached in the original utility study were exclusively based upon readings taken from the taxpayer's non-production equipment. Therefore, it is requested that a supplemental utility usage audit encompassing taxpayer's 1996 tax year be conducted.

FINDING

Taxpayer's protest is sustained subject to audit review.

III. Sales/Use Tax Assessment on Certain Equipment – Manufacturing Equipment Used in the Direct Production of Taxpayer's Tangible Personal Property

DISCUSSION

The taxpayer protests the auditor's determination that four items of equipment do not qualify for the manufacturing exemption available under 45 IAC 2.2-5-10 because the equipment does not have an essential and integral relationship with the taxpayer's manufacturing process. The four items of equipment are label printers, die cut stencils, tape dispensers, and coil straighteners.

IC 6-2.5-5-3(b) provides that "[t]ransactions involving manufacturing machinery, tools, and equipment are exempt from the state gross retail tax if the person acquiring that property acquires it for direct use in the direct production, manufacture, fabrication, assembly, extraction, mining, processing, refining, or finishing of other tangible personal property." 45 IAC 2.2-5-10(c) amplifies that code section by stating that, in order for the equipment to be considered "directly used," the item of equipment must "have an immediate effect on the tangible personal property being processed or refined. The property has an immediate effect on the article being produced if is an essential and integral part of an integrated process which processes or refines the tangible personal property." Id.

The label printer does not meet the statutory requirement. It is used by the taxpayer to produce UPC / Bar Code labels affixed to the outside of the taxpayer's product containers. These labels are used by the taxpayer for the purpose of warehouse tracking and inventory control. The labels provide information concerning the quantity and identity of the items contained within the product containers. The label printer does not act upon, have an effect on, or play an essential and integral part in the production of taxpayer's automotive and safety equipment.

Taxpayer pays the cost of certain "die cut stencils." From taxpayer's description, it would appear that these stencils are used in the preparation and fabrication of the custom designed cardboard containers taxpayer uses in shipping manufactured components and finished products. The cost of the stencils, the actual dies, and other associated costs is initially incurred by taxpayer's supplier and is then passed along to the taxpayer. Taxpayer maintains that the die cut stencils are entitled to the manufacturing exemption available under 45 IAC 2.2-5-8. That regulation exempts from the gross retail tax the purchase of "tangible personal property by persons engaged in the direct production, manufacture, fabrication, assembly, or finishing of tangible personal property..." 45 IAC 2.2-5-8(a). The purchase of the equipment is exempt when it is "directly used by the purchaser" in an "integrated process which produces tangible personal property." 45 IAC 2.2-5-8(b), (c). The taxpayer misapprehends the applicability of the regulation. Even if it could be demonstrated that the die cut stencils were used in directly producing the cardboard shipping containers, it is the manufacturer of the containers – not taxpayer – which is entitled to the exemption. The exemption is clearly available to the manufacturer of tangible personal property and not the downstream user of that property. Taxpayer is in the business of producing automobile accessories and components and not cardboard containers.

However, the cost of the die cut stencils -- passed along to the taxpayer as a serverable charge distinct from the price of the cardboard containers produced by those stencils -- should have been included as part of the integral cost of the cardboard containers. Accordingly, to the extent the cardboard containers are exempt as non-returnable packaging under 45 IAC 2.2-5-16, the apportionable cost of the die cut stencils is also exempt.

The third category of equipment at issue consists of tape dispensers, which the taxpayer maintains are used in its manufacturing process. The tape dispensers are used to dispense a protective film-like tape. This tape serves two purposes. The tape holds plastic reflective lenses in position until a frame is placed around the lens. The tape is used to protect the surface of the lens during handling and shipping. After the lens reaches the ultimate consumer, the protective tape is normally removed. Taxpayer maintains that the tape dispensers qualify for the manufacturing exemption provided under 45 IAC 2.2-5-8. Taxpayer errs. In order for the exemption to apply, the equipment at issue must be used by the purchaser "in the direct production, manufacture, fabrication, assembly, or

finishing of tangible personal property." 45 IAC 2.2-5-8(b). Taxpayer has failed to establish a sufficient factual basis upon which to determine if the tape dispensers are "directly used in the [taxpayer's] production process." IC 2.2-5-8(c). Accordingly, that portion of the taxpayer's protest regarding its tape dispensers must be denied.

Finally, taxpayer seeks a sales tax exemption for the purchase of coil straighteners. During the taxpayer's manufacturing process, coils of metal (various steel alloys, brass, etc.) are positioned near or above the production equipment. As production takes place, the coiled metal is fed into these machines. However, the coiled metal has an acquired and inherent "coil set" which prevents the metal from being directly used by the production machinery. Taxpayer Memo, Eng'g Dep't, Sept. 29, 2000. The "coil set" is an innate curvature of the metal somewhere between perfectly flat and the degree of curvature as defined by the outside coil circumference. Id. The amount and degree of "coil set" is dependent on the type of metal, hardness, temper, and other physical properties of the metal. Id. The coil straighteners act upon the metal as it is fed into the production machinery in such a way as to insure that the "coil set" is removed and the metal is correctly aligned. Without the coil straighteners, the "coil set" would prevent proper alignment of the metal, production machinery would not function properly, and the taxpayer's products would consist of, to use the taxpayer's words, "complete scrap." The auditor determined that the coil straighteners were non-production equipment that did not warrant exemption from the sales tax because the coil straighteners did not have an effect on the taxpayer's products. Instead, the auditor found that, because the straighteners'' only function was to straighten and align the coiled metal, the straightener had no immediate effect on the taxpayer's products and, in fact, was used prior to the actual manufacturing process.

Taxpayer employs two types of coil straighteners. The first is a "pull through" straightener that is built into and is an integral part of the metal feeder attached to the production machinery. This type is used for lighter gauge coiled metals. The second type of coil straightener is an independent, stand-alone model located immediately between the uncoiler system (supporting the coiled metal) and the metal feeder. Both types of straightener consist of an array of five, seven, or nine adjustable rollers through which the metal is passed. The rollers alternately work the metal up and down – to varying degrees – with the result that the metal emerges from the straightener with the inherent curvature of the metal having been removed.

45 IAC 2.2-5-8 allows the taxpayer to purchase machinery, tools, and equipment without paying the gross retail tax when the equipment is used in the direct production of tangible personal property. 45 IAC 2.2-5-8(a) specifies that the exemption is limited to that equipment "used by the purchaser in direct production." 45 IAC 2.2-5-8(c) specifies that "directly used" means that the equipment has "an immediate effect on the article being produced." Refining the definition one further step, the regulation states that "[p]roperty has an immediate effect on the article being produced if it is an essential and integral part of an integrated process which produces tangible personal property." Id.

The taxpayer's coil straighteners fall within the exemption provided under 45 IAC 2.25-8 because the straighteners act in such a way as to have an effect on the tangible personal property being produced by the taxpayer and because the coil straighteners are within the taxpayer's production process. The coil straighteners are more than simple transport devices used to facilitate the transfer of the raw metal from the coil reel to the first production machine. Instead, the coil straightener acts upon the metal to change the metals' inherent structure in the same manner that a punch press, a lathe, or cutting torch act upon raw metals. After the metal has gone through the coil straightener, the metal that is dispensed is different from the metal originally on the metal coil having been physically transformed in an initial step of taxpayer's production process.

FINDING

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

IV. Sales and Use Tax Assessment on Packaging Materials – Packing Materials Placed Within Shipping Enclosures

DISCUSSION

Taxpayer protests the assessment of the gross retail tax on the purchase of certain packing materials. These materials consist of corrugated pads, partitions, spacers, separators, stuffing materials, filling materials, stretch film, strapping materials, sealing tape, and top caps. The taxpayer argues that its customers expect their delivered products to arrive in pristine condition. Therefore, according to the taxpayer, these particular packaging materials are exempt under the provisions of 45 IAC 2.2-5-16 because, without the packaging material, the products would not arrive at the end user in a usable condition.

Taxpayer sets forth a secondary argument. Some of these same materials are also used for making interdivisional transfers of work-in-progress from the taxpayer's Indiana site to its assembly site in Mexico. According to the taxpayer, as materials used to facilitate the interdivisional shipment of work-in-progress, the packing materials are exempt under the terms of the decision reached by the Tax Court in General Motors Corp. v. Dept. of State Revenue, 578 N.E.2d 399 (Ind. Tax Ct. 1991).

The auditor determined that the packaging materials did not qualify for an exemption under 45 IAC 2.2-5-16.

The taxpayer's use of these particular packing materials falls within two general categories and is addressed as such.

A. Packing Materials Used in Making Interdivisional Transfers.

The taxpayer argues that its purchase of certain packing materials, used to protect component parts during transfer from its primary manufacturing plant to the taxpayer's final assembly plant in Mexico, is exempt from the gross retail tax. Taxpayer asserts its claim under the principles set forth in General Motors Corp. v. Indiana Dept. of State Revenue, 578 N.E.2d 399 (Ind. Tax Ct. 1991). Accordingly, the relevant authority for taxpayer's claim is based on IC 6-2.5-5-3(b) which states that "[t]ransactions involving

manufacturing machinery, tools, and equipment are exempt from the state gross retail tax if the person acquiring that property acquires it for direct use in the direct production, manufacture, fabrication, assembly, extraction, mining, processing, refining, or finishing or other tangible personal property." Superficially, the taxpayer's status (and the legitimacy of its claim to the tax exemption) is similar to that of the automobile manufacturer in General Motors.

In General Motors, the automobile manufacturer shipped component parts to its assembly plants and, as taxpayer here has done, claimed an exemption for the packaging materials used to protect the component parts during those inter-divisional transfers. The court held that the automobile manufacturer's packing materials were part of the integral process whereby the manufacturer produced its finished product. Therefore, the automobile manufacturer's packing materials were exempt under IC 6-2.5-5-3. The court came to its determination after finding that the automobile manufacturer's widely separated production facilities formed a cohesive, singular production unit in which the claimant's "manufacture of finished marketable automobiles [was] accomplished by one continuous integrated production process within which the transport of parts from component plants to assembly plants [was] an essential and integral part." General Motors, 578 N.E.2d at 414. The court's holding, finding that the packing materials used in interdivisional transfers were exempt from the gross retail tax, included such "expendable packing materials, [] as corrugated cardboard cartons, separators, liners, pads, wrapping paper, plastic plugs, pallets, and other items to protect the parts during shipment to assembly plants...." Id. at 399. Similarly, the taxpayer is making interdivisional transfers of partially completed work in progress with the intent of producing its most marketable finished good. Similarly, taxpayer seeks an exemption for a variety of packing materials used in those interdivisional transfers. Similarly, at the completion of its manufacturing process, taxpayer has a goal of producing its most marketable finished good.

However, the analogy between the automobile manufacturer claimant in General Motors and taxpayer breaks down upon closer examination. The tax court in General Motors allowed the automobile manufacturer the exemption because the court found that the automobile manufacturer's "integrated production process terminates the production of the most marketable finished product, e.g., the product actually marketed." Id. at 404. Essentially, the General Motors court redefined the various far-flung automobile manufacturing facilities as *one continuous, integrated, manufacturing process* such that the automobile manufacturer's purchase of packing materials, used to facilitate the transfer of unfinished goods within that integrated production process, was essential and integral to the taxpayer's manufacturing process and, thereby, was entitled to the manufacturing exemption available under IC 6-2.5-5-3. Among the evidence cited as relevant in determining that automobile manufacturer operated a continuous, integrated, manufacturing process, the court found that automobile manufacturer's personnel, located at its various plants, together collaborated to develop new products, together designed and engineered new parts and packing materials, together planned the production processes for new parts, and together mutually solved problems and ensured product quality. Id. at 403 n.3. In addition, the court held that the "continuity of production exist[ed] between [automobile manufacturer's] different plants [was] demonstrated by the standard practice of shifting certain production operations back and forth between component and assembly plants when necessary for more efficient operation." Id.

Taxpayer has failed to demonstrate that it is entitled to the manufacturing exemption available under IC 6-2.5-5-3. In seeking the exemption, the taxpayer "has the burden of showing the burden of showing the terms of the exemption statute are met." Id. at 404. In contrast to the burden of proof established by the automobile manufacturer in General Motors, the taxpayer has not demonstrated that its manufacturing plant and its assembly plant are operated as one continuous and integral operation. Taxpayer does not come within the purview of General Motors because it fails to demonstrate that the manufacturing work taking place at its Indiana facility and its Mexican facility constitutes "one continuous integrated production process." Id. at 404. Accordingly, the taxpayer is not entitled to an exemption from the state's gross retail tax for the purchase of packing materials used to protect interdivisional shipments of partially finished goods between its primary manufacturing facility and its Mexican assembly plant. The Department must decline the opportunity to expand the holding in General Motors beyond the unique factual setting of that particular case.

B. Packing Materials Used in Shipping Finished Goods to Taxpayer's Intermediate Distributors.

IC 6-2.5-5-9(d) provides that "[s]ales of wrapping materials and empty containers are exempt from the state gross retail tax if the person acquiring the material or containers acquires them for use as non-returnable packages for selling the contents that he adds." The applicable companion regulation is found at 45 IAC 2.2-5-16(a) which states that "[t]he state gross retail tax shall not apply to sales of non-returnable wrapping materials and empty containers to be used by the purchaser as enclosures or containers for selling contents to be added." The regulation goes on to state that, in order to qualify for the exemption, "non-returnable wrapping materials and empty containers must be used by the purchaser in the following way: (A) The purchaser must add contents to the containers purchased; and (B) The purchaser must sell the contents added." 45 IAC 2.2-5-16(d)(1).

Certain of the taxpayer's packaging materials are inserted into non-returnable containers as protection for the enclosed products. Those materials include corrugated pads, partitions, cardboard separators, spacers, styrofoam packing peanuts, stuffing materials, filling materials, and molded forms. Because these materials are used to physically separate and protect the taxpayer's products from damage, they are exempt from the gross retail tax.

The taxpayer's purchase of strapping materials is exempt from the gross retail tax under 45 IAC 2.2-5-16(c)(1) which states that "[n]onreturnable containers and wrapping materials including steel strap...." are exempt from state gross retail tax.

Taxpayer describes "top caps" as paper skid sheets used to stabilize packaging configurations for shipment to... customers." Taxpayer Memo, October 9, 2000. Accordingly, the top caps constitute non-returnable wrapping materials destined for the taxpayer's customer the purchase of which is exempt from the sales tax under 45 IAC 2.2-5-16. Therefore, to the extent that taxpayer's top caps, stretch film, and sealing tape constitute non-returnable wrapping materials destined for the taxpayer's customers, the taxpayer's purchase of these items is exempt from the imposition of the state's gross retail tax.

FINDING

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

V. Abatement of the Ten Percent Negligence Penalty

DISCUSSION

The taxpayer has requested that the ten-percent negligence penalty, assessed by the auditor under authority of IC 6-8.1-10-2.1, be abated. The taxpayer argues that it acted in good faith and with reasonable diligence in determining the taxability of those items addressed within its protest. In addition, the taxpayer maintains that the fact that it has policies and practices in place to resolve tax issues, is a further demonstration of its good faith and diligence.

The Department determined that imposition of the negligence penalty was appropriate because the taxpayer was inconsistent in its coding and accrual of use tax, failed to have exemption certificates on file with its utility providers, and because the taxpayer had remitted less than one-half of its use tax.

The Department's regulations provide guidance in determining those instances in which imposition of the ten-percent negligence penalty is appropriate. 45 IAC 15-11-2(b) defines negligence as "the failure to use reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." The taxpayer's negligence may be inferred from its "carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations." Id. IC 6-8.1-10-2.1(d) requires that the Department waive the penalty upon a showing that the taxpayer's failure to pay the tax delinquency was due to "reasonable cause and not due to willful neglect." In order to establish "reasonable cause," 45 IAC 15-11-2(c) requires that the taxpayer demonstrate that it "exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed...."

The taxpayer has failed to demonstrate that, in those areas of concern raised by the auditor, it exercised the degree of reasonable care required to justify waiving the ten-percent negligence penalty. Although some of the questions raised by the taxpayer involve technical issues of interpretation and applicability, given the totality of the circumstances, waiver of the penalty is nonetheless inappropriate.

FINDING

Taxpayer's protest is respectfully denied.

DEPARTMENT OF STATE REVENUE

02990188P.LOF

LETTER OF FINDINGS NUMBER: 99-0188P
Income Tax
Calendar years 1994 and 1996, Short Years June 30, 1995 and December 31, 1995

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2

The taxpayer protests the penalty assessed.

STATEMENT OF FACTS

Taxpayer, in a letter dated April 12, 1999, protests the negligence penalty related to an audit performed for the calendar years 1994 and 1996 and the short years June 30, 1995 and December 31, 1995.

The taxpayer produces automobile heaters and air conditioners for automobile manufacturers.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer protests the negligence penalty assessed by the Department for the taxpayer's failure to report throwback sales from Ohio. The taxpayer argues that the penalty should be waived as the taxpayer did not act with willful intent to evade tax.

The taxpayer's support for this position is the taxpayer mistakenly underreporting a Federal Net Operating Loss. The Department agrees the taxpayer did not act with willful intent to evade tax; however, the Department believes the taxpayer was inattentive to tax duties.

45 IAC 15-11-2(b) states, "Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer."

As inattention is negligence and negligence is subject to penalty, the penalty protest is denied.

FINDING

The taxpayer's penalty protest is denied.

DEPARTMENT OF STATE REVENUE

03990203.LOF

LETTER OF FINDINGS NUMBER: 99-0203
Withholding Tax
For Tax Years 1995 through 1997

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Withholding – Nonresident Shareholders
Authority: IC 6-3-4-13

Taxpayer protests the formula used to arrive at the apportionment factor for corporate withholding tax assessment.

STATEMENT OF FACTS

Taxpayer, a Kentucky S corporation, operates a farm in Indiana. There were two shareholders for the tax years in question. Those shareholders lived in Kentucky. The Department of Revenue conducted an investigation and issued assessments for corporate withholding taxes for nonresident shareholders. Taxpayer protested that the Department did not use a proper apportionment formula.

I. Withholding – Nonresident Shareholders

DISCUSSION

Taxpayer operates a farm in Indiana. The Department reviewed its records for the tax years in question and was unable to find any nonresident shareholder withholding tax remittances from taxpayer. Under IC 6-3-4-13, taxpayer is required to withhold Indiana adjusted gross income tax on distributions to all nonresident shareholders regardless of their individual filing requirement and status. IC 6-3-4-13 states in part:

(a) Every corporation which is exempt from tax under IC 6-3 pursuant to IC 6-3-2-2.8(2) shall, at the time that it pays or credits amounts to any of its nonresident shareholders as dividends or as their share of the corporation's undistributed taxable income, withhold the amount prescribed by the department. Such corporation so paying or crediting any nonresident shareholder:

(1) shall be liable to the state of Indiana for the payment of the tax required to be withheld under this section and shall not be liable to such shareholder for the amount withheld and paid over in compliance or intended compliance with this section;

Taxpayer, an S-Corporation with Indiana income, failed to withhold taxes on distributions made to nonresident shareholders. Audit, therefore, made withholding tax adjustments based on returns filed by taxpayer. Taxpayer paid one third (1/3) of these assessments, but rather than contesting its withholding duties, taxpayer protested that the Department did not use the proper apportionment formula in determining these assessments. In the course of this protest, taxpayer submitted information relating to the apportionment formula used to determine the percentage of income and tax to be paid to Indiana.

In a letter to the Department accompanying some of the documentation submitted for this protest, taxpayer explained that it had paid tax to the Kentucky Revenue Cabinet on the income in question. Despite this, the withholding requirement of IC 6-3-4-13 does subject taxpayer to taxation in Indiana. Indiana cannot waive a valid tax on the basis that a taxpayer sent payment to another state.

Under IC 6-3-4-13, taxpayer is required to withhold Indiana adjusted gross income tax on distributions to nonresident

shareholders. Taxpayer failed to withhold these taxes. However, the Audit division will review taxpayer's returns and the submitted documentation to determine taxpayer's proper Indiana apportionment factors.

FINDING

Taxpayer's protest is denied. The Audit division will review and verify the information related to income apportionment.

DEPARTMENT OF STATE REVENUE

02990376.LOF

LETTER OF FINDINGS NUMBER: 99-0376
Corporate Income Tax
For Tax Periods: 1995-1997

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

1. Adjusted Gross Income Tax – Net Operating Loss
Authority: 26 U.S.C.A. 172; IC 6-3- 2-2.6

The taxpayer protests the Indiana Department of Revenue treatment of the net operating loss.

STATEMENT OF FACTS

The taxpayer is a manufacturer of doors. After an audit for the tax period 1995-1997, the taxpayer was assessed additional adjusted gross income tax. The taxpayer timely protested Audit's treatment of the net operating losses and a hearing was subsequently held. Further facts will be provided as necessary.

1. Adjusted Gross Income Tax – Net Operating Loss

DISCUSSION

During calendar years 1988 and 1989, the taxpayer incurred net operating losses ("NOLs") of $374,350 and $340,434 respectively. These NOLs were carried back to offset income earned in 1986 and carried forward to offset income earned in 1990. The taxpayer contends the remaining NOLs for l988 and l989 should have been carried forward to offset income earned in 1997. Audit, however, has determined that if the taxpayer had properly applied these NOLs to offset prior year's income, then the NOLs would have been exhausted by 1992. The taxpayer now protests Audit's conclusions. The taxpayer now asks the Department for permission to carry forward its remaining 1988 and 1989 NOLs to offset income earned in 1997.

Indiana treatment of net operating losses is governed by the provisions of the federal law concerning corporate net operating losses. IC 6-3-2-2.6. The carry back and carry forward provisions of the federal law are found at 26 U.S.C.A. Sec. 172. These provisions require that any corporate net operating loss must first be carried back three years before the loss can be carried forward, unless the taxpayer has elected to forego the three year carry back.

For the years at issue, any eligible loss not applied in the three preceding years may be carried forward up to fifteen years. 26 U.S.C.A. Sec. 172(b)(1)(A)(ii). However, such losses "shall be carried to the earliest of the taxable years to which... such loss may be carried." 26 U.S.C.A. Sec. 172(b)(2).

The taxpayer failed to apply its NOLs to the earliest eligible tax years. The taxpayer should have applied its 1988 and 1989 NOLs to offset income earned in 1990 and 1992. Had the taxpayer properly applied these NOLs, the taxpayer would not have had any remaining NOLs from 1988 and 1989 to utilize in 1997. The taxpayer, therefore may not carry forward its unused 1988 and 1989 NOLs to offset income earned in 1997.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04990454P.LOF

LETTER OF FINDINGS NUMBER: 99-0454P
Sales and Use Tax
Calendar Years of 1994, 1995, and 1996

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana

Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2

The Taxpayer protests the penalty assessed.

STATEMENT OF FACTS

Taxpayer, In a letter dated April 12, 1999, protests the negligence penalty related to an audit performed for the calendar years 1994, 1995, & 1996.

The taxpayer produces automobile heaters and air conditioners for automobile manufacturers. All items are for resale.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer protests the negligence penalty assessed by the Department on taxable missing invoices. The taxpayer states the loss of the invoices was the result of a couple of plant moves and not the result of willful negligence. The Department agrees the taxpayer did not act with willful intent to evade tax; however, the Department believes the taxpayer was inattentive to tax duties.

45 IAC 15-11-2(b) states, "Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer."

As inattention is negligence and negligence is subject to penalty, the penalty protest is denied.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

03990522P.LOF

LETTER OF FINDINGS NUMBER: 99-0522P
Withholding Tax
Calendar Year 1996

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE(S)

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2

Taxpayer protests the penalty assessed.

II. Tax Administration – Interest

Authority: IC 6-8.1-10-1

Taxpayer protests the interest assessed.

STATEMENT OF FACTS

Taxpayer filed its WH-3 late and was assessed ten dollars ($10) for each late filed W-2.

Taxpayer protests the penalty and interest assessed due to its filing a criminal suit against its former secretary for embezzlement and the neglecting of her duties.

I. Tax Administration – Penalty

DISCUSSION

Taxpayer requests the department waive the penalty for its failure to file information returns timely.

Taxpayer's payment history indicates it has had numerous late payment penalties since July 1993. Taxpayer only states it has filed criminal action against its former secretary but did not provide reasonable cause to allow the department to waive the late filing penalty.

FINDING

Taxpayer's protest is denied.

II. Tax Administration – Interest

DISCUSSION

Taxpayer protests the interest assessed.

Under IC 6-8.1-10-1(e) the department may not waive the interest imposed.

FINDING

Taxpayer's protest is denied.

CONCLUSION

Taxpayer's protest is denied for issues I and II.

DEPARTMENT OF STATE REVENUE

03990523P.LOF

LETTER OF FINDINGS NUMBER: 99-0523
Withholding Tax
Calendar Year 1996

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE(S)

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2

Taxpayer protests the penalty assessed.

II. Tax Administration – Interest

Authority: IC 6-8.1-10-1

Taxpayer protests the interest assessed.

STATEMENT OF FACTS

Taxpayer filed its WH-3 late and was assessed ten dollars ($10) for each late filed W-2.

Taxpayer protests the penalty and interest assessed due to its filing a criminal suit against its former secretary for embezzlement and the neglecting of her duties.

I. Tax Administration – Penalty

DISCUSSION

Taxpayer requests the department waive the penalty for its failure to file information returns timely.

Taxpayer's payment history indicates it has had numerous late payment penalties since April 1990. Taxpayer only states it has filed criminal action against its former secretary but did not provide reasonable cause to allow the department to waive the late filing penalty.

FINDING

Taxpayer's protest is denied.

II. Tax Administration – Interest

DISCUSSION

Taxpayer protests the interest assessed.

Under IC 6-8.1-10-1(e) the department may not waive the interest imposed.

FINDING

Taxpayer's protest is denied.

CONCLUSION

Taxpayer's protest is denied for issues I and II.

DEPARTMENT OF STATE REVENUE

28990648.LOF

LETTER OF FINDINGS NUMBER: 99-0648 CSET
Controlled Substance Excise Tax
For Tax Periods: 1998

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana

Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

1. Controlled Substance Excise Tax – Imposition

Authority: IC 6-7-3-5; IC 6-8.1-5-1(b); Hurst v. Department of Revenue, 720 N.E.2d 370 (Ind. Tax. 1999); Hall v. Department of Revenue, 720 N.E.2d 1287 (Ind. Tax 1999)

Taxpayer protests the imposition of the Controlled Substance Excise Tax.

STATEMENT OF FACTS

On September 23, 1998, a marijuana growing operation was discovered on a farm in Indiana. The marijuana was cut down and seized by the Indiana State Police and National Guard. Taxpayer was not arrested. On October 4, 1999, the county prosecutor of the county where the outdoor grow was located sent the Indiana Department of Revenue a letter stating that he would not press criminal charges against Taxpayer concerning the marijuana discovered on the farm. The Indiana Department of Revenue issued a Record of Jeopardy Finding, Jeopardy Assessment, Notice and Demand on December 1, 1999 in a base tax amount of $317,520.00. Taxpayer filed a protest to the assessment. A hearing on the protest was held on August 23, 2000. Further facts will be provided as necessary.

1. Controlled Substance Excise Tax – Imposition

DISCUSSION

IC 6-7-3-5 imposes the Controlled Substance Excise Tax on the possession of marijuana in the State of Indiana. Indiana Department of Revenue assessments are presumed to be correct and Taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1 (b). Possession of the marijuana can be either actual or constructive. Hurst v. Department of Revenue, 720 N.E.2d 370 (Ind. Tax. 1999), Hall v. Department of Revenue, 720 N.E.2d 1287 (Ind. Tax 1999). Although both direct and circumstantial evidence may prove constructive possession, proof of presence in the vicinity of drugs, presence on property where drugs are located, or mere association with the possessor is not sufficient. Hurst at 374-375. To prove constructive possession, there must be a showing that Taxpayer had not only the requisite intent but also the capability to maintain dominion and control over the substance. Hurst at 374.

In the Hall case, the Indiana Department of Revenue assessed Controlled Substance Excise Tax on a husband and wife. The couple owned and lived together in a residence. The marijuana was grown in a basement room with a locked door. Only the husband had a key to the room. Although the wife co-owned the house, lived in the house, did laundry in the room adjacent to the room which housed the marijuana, and the smell of marijuana permeated the house; the Court found that the wife did not have the capability to maintain dominion and control over the marijuana. Therefore she did not constructively possess the marijuana and the Controlled Substance Excise Tax was improperly imposed against the wife.

The issue to be determined in this case is whether or not Taxpayer had constructive possession of the marijuana. The farm had belonged to Taxpayer's deceased mother. A bank held legal title to the farm. Although Taxpayer and his brother lived in other residences, they cared for the farm. A tenant farmer did the actual farming. The marijuana was found in fields some distance from the house and yard. At the time the police arrived, Taxpayer was in his own house across the street. There were some paths from the corner of the farmhouse lawn to the fields and marijuana residue and rolling papers were found in the kitchen of the farmhouse. This is, however, significantly less circumstantial evidence than existed in the Hall case. This evidence does not support a finding that Taxpayer had the intent and capability to maintain dominion and control over the marijuana growing in the fields.

FINDING

Taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

2820000034.LOF

LETTER OF FINDINGS NUMBER: 00-0034 CSET
Controlled Substance Excise Tax
For Tax Period: 1998

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Controlled Substance Excise Tax – Imposition

Authority: IC 6-7-3-5; IC 6-8.1-5-1(b); Hurst v. Department of Revenue, 720 N.E.2d 370 (Ind. Tax. 1999); Hall v. Department of Revenue, 720 N.E.2d 1287 (Ind. Tax. 1999)

Taxpayer protests the imposition of the Controlled Substance Excise Tax.

STATEMENT OF FACTS

On September 23, 1998, a marijuana growing operation was discovered on a farm in Indiana. The marijuana was cut down and seized by the Indiana State Police and National Guard. Taxpayer was arrested at the scene for public intoxication. On October 4, 1999, the county prosecutor of the county where the outdoor grow was located sent the Indiana Department of Revenue a letter stating that he would not press criminal charges against Taxpayer concerning the marijuana discovered on the farm. The Indiana Department of Revenue issued a Record of Jeopardy Finding, Jeopardy Assessment, Notice and Demand on December 1, 1999 in a base tax amount of $317,520.00. Taxpayer filed a protest to the assessment. A hearing on the protest was held on August 23, 2000. Further facts will be provided as necessary.

I. Controlled Substance Excise Tax – Imposition

DISCUSSION

IC 6-7-3-5 imposes the Controlled Substance Excise Tax on the possession of marijuana in the State of Indiana. Indiana Department of Revenue assessments are presumed to be correct and Taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1 (b). Possession of the marijuana can be either actual or constructive. Hurst v. Department of Revenue, 720 N.E.2d 370 (Ind. Tax. 1999), Hall v. Department of Revenue, 720 N.E.2d 1287 (Ind. Tax 1999). Although both direct and circumstantial evidence may prove constructive possession, proof of presence in the vicinity of drugs, presence on property where drugs are located, or mere association with the possessor is not sufficient. Hurst at 374-375. To prove constructive possession, there must be a showing that Taxpayer had not only the requisite intent but also the capability to maintain dominion and control over the substance. Hurst at 374.

In the Hall case, the Indiana Department of Revenue assessed Controlled Substance Excise Tax individually on a husband and wife. The couple owned and lived together in a residence. The marijuana was grown in a basement room with a locked door. Only the husband had a key to the room. Although the wife co-owned the house, lived in the house, did laundry in the room adjacent to the room which housed the marijuana and the smell of marijuana permeated the house; the Court found that the wife did not have the capability to maintain dominion and control over the marijuana. Therefore she did not constructively possess the marijuana and the Controlled Substance Excise Tax was improperly imposed against the wife.

The issue to be determined in this case is whether or not Taxpayer had constructive possession of the marijuana. The farm had belonged to Taxpayer's deceased mother. A bank held legal title to the farm. Although Taxpayer and his brother had other residences, they cared for the farm. A tenant farmer did the actual farming. The marijuana was found in fields some distance from the house and yard. At the time the police arrived, Taxpayer was walking away from the farmhouse to his brother's house across the street. There were some paths from the corner of the lawn to the fields and marijuana residue and rolling papers were found in the kitchen. This is, however, significantly less circumstantial evidence than existed in the Hall case. This evidence does not support a finding that Taxpayer had the intent and capability to maintain dominion and control over the marijuana growing in the fields.

FINDING

Taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

0420000193.LOF

LETTER OF FINDINGS NUMBER: 00-0193
Use Tax
Calendar Years 1996, 1997, 1998, and 1999

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE(S)

I. Gross Retail Tax – Remittance
Authority: IC 6-2.5-2-1

Taxpayer protests the audit assessment.

II. Tax Administration – Penalty
Authority: IC 6-8-10-1-2.1; 45 IAC 15-11-2

The Department addresses the penalty.

STATEMENT OF FACTS

Taxpayer failed to show for a hearing scheduled for Tuesday, February 6, 2001. The determination is made based upon

information contained in the audit file and taxpayer's protest letter dated March 16, 2000. The Department has allowed the taxpayer ample time to provide information.

Taxpayer operates an asphalt-manufacturing plant in Indiana. The taxpayer maintained a seasonal filing status with the Department for the periods April through October and is a non-filer for the periods 5/96, 7/96, 8/96, 9/96, 10/96, and 4/97 through 10/97. The taxpayer paid system-generated billings (SBIA's) in lieu of the actual sales tax liability incurred for these periods. The taxpayer was allowed credit for all payments made during the audit period. In addition, taxpayer failed to file returns and remit sales/use tax as required for tax year ended 12/31/98 and the pre-petition bankruptcy period.

Taxpayer collected sales tax on asphalt sold at retail but failed to file ST-103's and remit the tax collected to the department with the exception of June 1996. The taxpayer did not provide the auditor with complete sets of sales journals and invoice registers; consequently additional taxable sales represents the total gross receipts as reported on the federal income tax returns (Form 1120) less Department issued (BIA) billings paid by the taxpayer.

I. Gross Retail Tax – Remittance

DISCUSSION

Taxpayer's letter dated March 16, 2000 states it does not owe tax for Government/Municipal sales, non-collectable sales and year-end write-offs, and previously paid tax assessments. Taxpayer provided several ST-105's and AD-70's that were not taken into consideration at audit.

Audit is instructed to adjust for the correct exemption certificates presented with the taxpayer's protest letter. Additional adjustments can not be made for the write-offs or previously paid tax assessments as no proof nor detail has been provided.

FINDING

Taxpayer's protest is partially denied and partially sustained.

II. Tax Administration – Penalty

DISCUSSION

Although the taxpayer did not specifically protest the penalty assessed, the department addresses the penalty. Taxpayer failed to file ST-103's returns, collect and remit sales tax.

Taxpayer has not provided reasonable cause for the failure to collect and remit sales tax.

FINDING

Taxpayer's protest is denied.

CONCLUSION

Taxpayer's protest is partially denied and partially sustained for issue I and denied for issue II.

DEPARTMENT OF STATE REVENUE

0120000297.LOF

LETTER OF FINDINGS NUMBER: 00-0297
Individual Income Tax
Calendar Year 1999

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE(S)

I. Adjusted Gross Income – Credit for Local Taxes Paid Outside Indiana

Authority: IC 6-3.5-1.1-6

Taxpayer protests a reduction of its refund for the disallowance of tax paid to a locality outside of Indiana.

STATEMENT OF FACTS

Taxpayer failed to attend a hearing scheduled for Wednesday, September 6, 2000. Taxpayer protests the reduction of a refund. Taxpayer is a resident of Indiana who works in Kentucky.

Taxpayer took a credit for Owensboro, Kentucky local income tax on its Indiana full year resident tax return in the amount of $1,288.30. The department reduced the refund to disallow the credit.

I. Adjusted Gross Income – Credit for Local Taxes Paid Outside Indiana

DISCUSSION

At issue is whether the taxpayer is allowed to take credit for taxes paid to a county outside the state of Indiana.

IC 6-3.5-1.1-6 explains "Credit for taxes imposed by governmental entities outside of state" as follows:

a) Except as provided in subsection (b), if for a particular taxable year a county taxpayer is liable for an income tax imposed by a county, city, town, or other local governmental entity located outside of Indiana, that county taxpayer is entitled to a credit against his county adjusted gross Income liability for that same taxable year. The amount of the credit equals the amount of tax imposed by the other governmental entity on income derived from sources outside Indiana and subject to the county adjusted gross income tax. However, the credit provided by this section may not reduce a county taxpayer's county adjusted gross income tax liability to an amount less than would have been owed if the income subject to taxation by the other governmental entity had been ignored.

Persons claiming a county credit for taxes paid to out-of-state localities must add the deduction taken for non-Indiana locality earnings back to their state taxable income before arriving at their county taxable income. In addition, the allowable credit is equal to the lessor of:

c) The amount of county tax due on the Indiana return.

Page 24 of the instruction booklet, Indiana Credits: Form IT-40, Schedule 2, Line 1 clearly states that "The credit can be used against the Indiana county tax figured if the tax is the County Adjusted Gross Income Tax (CAGIT) or County Option Income Tax (COIT). This credit **cannot** be claimed against the County Economic Development Income Tax (CEDIT)."

Taxpayer did not pay CAGIT or COIT. Taxpayer paid CEDIT for which a credit against it cannot be claimed.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0120000366.LOF

LETTER OF FINDINGS NUMBER: 00-0366
Individual Income Tax
Calendar Years 1998 and 1999

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE(S)

I. Prison Investment Credits – Application
Authority: IC 6-3.1-6-2; Information Bulletin #59

Taxpayer protests the disallowance of the Prison Investment Credit.

II. Tax Administration – Penalty
Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2

Taxpayer protests the penalty assessed.

STATEMENT OF FACTS

Taxpayer protests the disallowance of the Prison Investment Credit that was passed through to him from an S-corporation. PIC is a nonrefundable credit which means the credit allowed is only up to the tax due amount. S-Corporations have no tax due and IC 6-3.1-6 allows no credit to the individual.

Taxpayer states its company is a subchapter S Corporation licensed to do business in Indiana and used prisoners for its assembly work beginning in 1998. Taxpayer further states that the S corporation has complied with all rules and filings regarding the Indiana Prison Investment Credit (IC 6-3.1-6) and flowed the credits through to its shareholders according to the Indiana S corporation instructions.

I. Prison Investment Credits – Application

DISCUSSION

Taxpayer took an investment credit on his individual income tax returns for 1998 and 1999 for the Prison Investment paid by an S-Corporation.

PIC is a non-Refundable Credit, which means the credit allowed is only up to the amount of tax due. The S-Corporation had no tax due and the S-Corporation is allowed only a deduction on its return. There is no provision in the Indiana Code or Regulations that allows credit to flow through to the shareholder.

FINDING

Taxpayer's protest is denied.

II. Tax Administration – Penalty

DISCUSSION

Taxpayer was assessed a penalty after the department made adjustments to the returns for the Prison Investment Credit. The Department believes the Taxpayer had reasonable cause to believe it could take a credit.

FINDING

Taxpayer's protest is sustained.

CONCLUSION

Taxpayer's protest is denied in Issue I and sustained in Issue II.

DEPARTMENT OF STATE REVENUE

2820000433.LOF

LETTER OF FINDINGS NUMBER: 00-0433 CSET
Controlled Substance Excise Tax
For Tax Periods: 2000

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

1. Controlled Substance Excise Tax – Imposition
Authority: IC 6-7-3-5; IC 6-8.1-5-1(b)

Taxpayer protests the assessment of Controlled Substance Excise Tax.

STATEMENT OF FACTS

Taxpayer was arrested for possession of marijuana. The Indiana Department of Revenue issued a Record of Jeopardy Finding, Jeopardy Assessment Notice and Demand on October 17, 2000, in a base tax amount of $4228.14. Taxpayer filed a protest to the assessment. A hearing on the protest was held by telephone on January 25, 2001. Further facts will be provided as necessary.

1. Controlled Substance Excise Tax – Imposition

DISCUSSION

IC 6-7-3-5 imposes the Controlled Substance Excise Tax on the possession of marijuana in the State of Indiana. Taxpayer bears the burden of proving that the assessment of tax is incorrect. IC 6-8.1-5-1(b). During a flyover, officers in an Indiana State Police helicopter saw several plants of marijuana with two men standing nearby. After landing, the officers saw twenty-nine marijuana plants. Eighteen plants were in black plastic pots and eleven had been planted in the ground. There was a foot path and a vehicle path from the marijuana patch to Taxpayer's yard. After obtaining a search warrant, the officers found a grow operation indoors, marijuana and marijuana smoking equipment in Taxpayer's bedroom and marijuana in Taxpayer's automobile. Taxpayer argues that he did not possess the marijuana because he did not own the house, and he wasn't charged criminally for possession of the marijuana and he is disabled.

The evidence indicates that the house belonged to Taxpayer's brother who was living in California at the time. Taxpayer had occupied the house for several months and allowed another person to live there with him. This indicates that Taxpayer was in control of the property at the time of the arrest. The marijuana was clearly linked with Taxpayer since it was found in his bedroom, in his car and at the end of a path from the yard. At hearing, Taxpayer did not sustain his burden of proving that the assessment was incorrect.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0220000484P.LOF

LETTER OF FINDINGS NUMBER: 00-0484P
Gross and Adjusted Gross Income Tax
Fiscal Years Ended April 1, 1994, March 31, 1995, March 29, 1996, March 28, 1997, and April 3, 1998

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana

Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE(S)

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2

Taxpayer protests the penalty assessed.

STATEMENT OF FACTS

Taxpayer is incorporated in Nevada and has no Indiana business locations. Upon audit it was discovered that the taxpayer failed to correctly report its gross income for three years of the audit. Taxpayer provides customers in Indiana computer hardware, software, software services, support/maintenance, consulting, leasing, and miscellaneous undefined services. Taxpayer underreported its receipts in two of the audit years and reported its product sales as service receipts in two of the audit years. The auditor adjusted the receipts to the correct tax rate and included all revenues from Indiana sources. In addition, the sales factor numerator was adjusted to agree with the amount of Indiana receipts as shown on the sales by state analysis and the gross income shown in the audit report.

Taxpayer protests the penalty and states that it has made an honest attempt to correctly report its liabilities and has a history of paying its tax liabilities timely. It has made necessary changes to insure it does not happen in the future.

I. Tax Administration – Penalty

DISCUSSION

Taxpayer was assessed a negligence penalty for failure to correctly report receipts in gross income, various errors in the apportionment factor and failure to correctly report business income. Taxpayer paid 70.7%, 94.5%, and 85.7% of the tax due for calendar years 1996, 1997, and 1998 respectively.

Taxpayer states that it receives an analysis from six related companies that include consulting fees, leases, and undefined sales. Taxpayer states it allowed the auditor to include the undefined sales in high rate income when it likely could be low rate. Taxpayer should have made itself aware of the type of income it received from the related companies. Taxpayer further states that it has made an honest attempt to correctly report its tax liabilities, and has made necessary changes to insure these errors are corrected in the future.

Taxpayer also made errors in various areas of its tax return that should have been verified before filing. Taxpayer has not provided reasonable cause to allow the department to waive the negligence penalty.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420010007P.LOF

LETTER OF FINDINGS NUMBER: 01-0007P
Use Tax
Calendar Years 1997, 1998, and 1999

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ISSUE(S)

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2

Taxpayer protests the penalty assessed.

STATEMENT OF FACTS

Taxpayer manufactures, distributes, and markets high-quality ceramic tile products. At audit, it was determined that the taxpayer did not have a use tax accrual system in place for 1997 and failed to pay tax on fixed assets and miscellaneous expense items.

Taxpayer failed to remit use tax on clearly taxable purchases although it had a use tax accrual system in place for two of the audited years.

I. Tax Administration – Penalty

DISCUSSION

Taxpayer's audit report revealed that it failed to remit use tax on clearly taxable purchases.

Taxpayer states that it continually strives to comply with all state and local tax requirements. Taxpayer believes that its error ratios were not significant due to its significant turnover in the tax and accounting area as well as system conversions. Taxpayer states it has introduced procedures and trained field personnel in order to reduce future errors.

A review of the audit indicates the taxpayer remitted no use tax in 1997, seventy-nine percent (79%) in 1998 and thirty-four percent (34%) in 1999. Taxpayer did not provide reasonable cause to allow a waiver of the penalty.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420010030P.LOF

LETTER OF FINDINGS NUMBER: 01-0030P
Use Tax
Calendar Years 1996, 1997, and 1998

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE(S)

I. Tax Administration – Penalty
Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2

Taxpayer protests the penalty assessed.

STATEMENT OF FACTS

Taxpayer is a wholesale distributor of drain and storm pipes. At audit, it was determined that the taxpayer did not have a use tax accrual system in place and failed to obtain valid exemption certificates for all of its sales.

I. Tax Administration – Penalty

DISCUSSION

Taxpayer's audit report revealed that it failed to remit use tax on clearly taxable purchases and had no use tax accrual system in place. Taxpayer failed to collect sales tax on all of its sales

Taxpayer states that it did not intentionally withhold the sales tax and the Indiana auditors had its full cooperation in completing the audit. Taxpayer further states that due to the length of time in completing the audit, which was out of its control, it requests an abatement of the penalties assessed.

A review of the audit indicates the taxpayer had no use tax accrual system in place although it is registered with the Department. Its reasoning, that the audit took too long, does not affect taxpayer's noncompliance in remitting its use tax and failing to obtain exemption certificates. Taxpayer did not provide reasonable cause to allow a waiver of the penalty.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0220010033P.LOF

LETTER OF FINDINGS NUMBER: 01-0033P
Gross and Adjusted Gross Income Tax
Calendar Years 1995, 1996, 1997, and 1998

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE(S)

I. Tax Administration – Penalty
Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2

Taxpayer protests the penalty assessed.

STATEMENT OF FACTS

Taxpayer is incorporated in Delaware and manufactures industrial gases.

At audit it was determined that the taxpayer failed to include in gross receipts its Indiana destination sales, failed to add back state income and property taxes, and include the sales of Indiana assets.

Taxpayer protests the penalty and states it did everything a reasonable person would do when filing its tax returns. Taxpayer states it immediately sent payment, based on a Preliminary Audit Summary, in good faith even though the audit was not finalized. Taxpayer further states it had many internal changes including a hundred percent turnover in manpower in the tax department.

I. Tax Administration – Penalty

DISCUSSION

Taxpayer was assessed a negligence penalty for failure to report its gross proceeds from the sale of Indiana assets and Indiana destination sales. Taxpayer failed to addback State income and property taxes, failed to file amended returns to report changes to federal taxable income resulting from RAR adjustments for 1995 and 1996 as required by 45 IAC 3.1-1-94, and made other errors. Taxpayer has been audited previously.

Taxpayer, in a letter dated December 8, 2000 protested penalties assessed due to its good faith with the Department and circumstances beyond its control.

Taxpayer, however, failed to report RAR adjustments as required under 45 IAC 3.1-1-94 and failed to properly report its income and addback taxes.

Taxpayer has not provided reasonable cause for its failure to report the RAR adjustments, its failure to include all of its gross income, its failure to addback taxes. In addition the audit indicated other areas of noncompliance. The taxpayer failed to remit 27%, 34%, 55%, and 55% in 1995, 1996, 1997, and 1998 respectively. The Department finds that a negligence penalty is proper.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

2920010037.LOF

LETTER OF FINDINGS NUMBER: 01-0037 CG

Denial of Indiana Charity Gaming Application

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Charity Gaming – Operator Membership Requirement

Authority: IC 4-32-9-28

The Petitioner, Love All Ministries, Inc., protests the Department's denial of its Indiana Charity Gaming Application.

II. Charity Gaming – Management and Conduct of Events

Authority: IC 4-32-9-15

The Petitioner protests the Department's denial of its Indiana Charity Gaming Application.

III. Charity Gaming – Grounds for Penalties

Authority: IC 4-32-12-2

The Petitioner protests the imposition of civil penalties.

IV. Charity Gaming – Additional Penalties

Authority: IC 4-32-12-3

The Petitioner protests the three (3) year prohibition on associating with charity gaming in Indiana.

STATEMENT OF FACTS

The Petitioner's organization was formed in December of 1993, and was incorporated in October of 1995. Petitioner received its federal exemption on February 21, 1996. The Petitioner obtained a certificate of assumed name from the Indiana Secretary of State's Office on December 8, 1997. The Petitioner was then certified by the Indiana Secretary of State to use the name Models for Christ, Inc. On or about November 6, 2000 the Petitioner applied for an Indiana charity gaming license. The Petitioner's application was completed by its attorney and signed by the Pastor on September 1, 2000. The Department instituted an investigation, and as a result of that investigation denied Petitioner's application, imposed civil penalties, and prohibited several individuals from associating with Indiana charity gaming for a period of three (3) years on January 18, 2001. The Petitioner filed a formal protest on January 23, 2001. An administrative hearing in the above referenced matter was held on January 25, 2001. The hearing was

conducted pursuant to IC 6-8.1-5-1 et seq. See, Portland Summer Festival v. Department of Revenue, 624 N.E. 2d 45 (Ind. App. 5 Dist. 1993).

I. Charity Gaming – Operator Membership Requirement

DISCUSSION

The Department's investigation revealed that the proposed operators, "are not now nor have ever been members" of the Petitioner's organization. IC 4-32-9-28 states, "An operator must be a member in good standing of the qualified organization that is conducting the allowable event for at least one (1) year at the time of the allowable event." The Annual Bingo License Application (CG-2) contains the following language directly above the signature of the Pastor, "We certify under penalty of perjury that the organization applying is a qualified organization, and there are no misrepresentations or falsifications in the information stated. We understand false or misleading statements will cause rejection of this application or revocation of future license(s)…". During the Department's investigation, and again at hearing, the Petitioner's Pastor reiterated that he did not know the operators whose names appeared on the form CG-2, and in fact stated under oath, "…They are not actual members of Love All People Ministry….". (Record at 54). Petitioner's counsel called as a witness the organization's attorney who had filled out the form CG-2. Petitioner's attorney, who was under oath stated, "…something that would have obviously made this a lot more unconfusing [sic] is if we would have just proceeded with this application process under Models for Christ, but unfortunately Models for Christ is a subsidiary of – well, our position is that it's a subsidiary auxiliary or affiliated group, therefore, we could not have – there's no way that they would have met the criteria as far as documentation that is required by the Department of Revenue situation… ". (Record at 103).

It is clear from the testimony at hearing that the Petitioner's attorney was the one who filled out the CG-2, even though the application was signed by the Pastor. The Petitioner's Pastor assumed that the application was in order since it was completed by their attorney. The Petitioner's reliance upon its counsel's expertise contributed to this controversy. As it turns out, the Petitioner's attorney's knew all three operators. One of the proposed operators was his secretary. He stated that he had a personal relationship with another proposed operator and he knew the third for about five years. (Record at 89). The operators were alleged to have been members of the organization Models for Christ, Inc. which was the assumed business name of the Petitioner. An organization operating under an assumed business name is legally the same entity. However, it is clear from the testimony given at the hearing that the members of Petitioner's organization and Model's for Christ were different. (See Department's Exhibits D & E). Acting under an assumed business name the two organizations should be the same entity. In this case, the list of members were different, the criteria to become a member was separate and distinct and the members of Model's for Christ did not even have to be a member of the Petitioner's organization. (Record at 54, 70, 71, 77, 78, 91 92, 102, 103). It is clear that the two entities were treated by the Petitioner as two distinct entities.

FINDING

The Petitioner's protest is denied.

II. Charity Gaming – Management and Conduct of Events

DISCUSSION

The Department's investigation alleges that the proposed operators were recruited to specifically work for the Petitioner as part of a contract to operate the gaming events. IC 4-32-9-15 provides that a qualified organization may not contract or otherwise enter into an agreement with an individual, a corporation, a partnership, a limited liability company, or other association to conduct an allowable event for the benefit of the organization. A qualified organization shall use only operators and workers meeting the requirements of this chapter to manage and conduct an allowable event.

Pursuant to IC 6-8.1-5-1, the Department's findings constitute prima facie evidence that the Department's findings are valid. The burden of proving that the findings are wrong rests with the person against whom the findings are made. See Portland Summer Festival v. Department of Revenue, 624 N.E.2d 45 (Ind.App. 5 Dist. 1993).

Prima facie evidence is evidence, which, if unexplained or uncontradicted, is sufficient to sustain a judgment in favor of the issue, which it supports, but which may be contradicted by other evidence. Of course, the Department's assertions must be made based on a reasonable belief, based upon the best information available to the Department. Here, the Department's assertion that the Petitioner contracted with the operators to conduct charity gaming is based upon the fact that the operators' names appear as operators for several other entities, and that Petitioner's attorney was the owner of the property where the charity gaming was to be conducted. (Record at 90). This evidence does not constitute prima facie evidence.

FINDING

The Petitioner's protest is sustained.

III. Charity Gaming – Grounds for Penalties

DISCUSSION

Pursuant to IC 4-32-12-2, "The department may impose upon a qualified organization or an individual the following civil penalties: (1) Not more than one thousand dollars ($1,000) for the first violation…". The Petitioner's protest of Issue I was denied. The violation of IC 4-32-9-28 by the Petitioner constitutes a violation subjecting the Petitioner to a civil penalty; therefore, the imposition of the civil penalty is well within the Department's authority pursuant to IC 4-32-12-2.

FINDING

The Petitioner's protest is denied.

IV. Charity Gaming – Additional Penalties

DISCUSSION

Additionally, the Department prohibited the Petitioner's Pastor and the three (3) proposed operators from associating with charity gaming for a period of three (3) years. IC 4-32-12-3(3) provides, "In addition to the penalties described in section 2 of this chapter, the department may do all or any of the following: …(3) Prohibit an operator or an individual who has been found to be in violation of this article from associating with charity gaming conducted by a qualified organization…"

Pursuant to IC 6-8.1-5-1, the Department's findings are prima facie evidence that the Department's claim is valid. The burden of proving that the findings are wrong rests with the person against whom the findings are made. See Portland Summer Festival v. Department of Revenue, 624 N.E.2d 45 (Ind.App. 5 Dist. 1993). In this case, the three (3) operators did not show nor did the Petitioner provide any evidence supporting its proposition that the operator's were not in violation of Title 4 Article 32.

FINDING

The Petitioner's protest is sustained as to its Pastor; However, the three (3) operators are hereby prohibited from associating with charity gaming for a period of three (3) years from the date of this opinion.

CONCLUSION

Upon payment of the civil penalty, the Petitioner may reapply for an Indiana charity gaming license provided the proposed operators and workers comport to the provisions of IC 4-32-9-28, & 29.

DEPARTMENT OF STATE REVENUE

02940893.SLOF

SUPPLEMENTAL LETTER OF FINDINGS NUMBER: 94-0893 ITC
Gross Income Tax
For Tax Periods: 1985 and 1988 through 1992

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Gross Income Tax – Receipts from Retail Sales

Authority: IC 6-2.1-2-1

Taxpayer protests assessments of Indiana gross income tax on sales of tangible personal property from inventory.

II. Gross Income Tax – Receipts from "Remanufacturing" Activities

Authority: IC 1-1-4-1; IC 6-2.1-2-1; IC 6-2.5-4-2; IC 6-6-2.5-12; 45 IAC 1.1-1-23; 45 IAC 2.2-5-10; *Jefferson Smurfit v. Indiana Department of State Revenue,* 681 N.E.2d 806 (Ind.Tax 1997); *Chrome Deposit v. Indiana Dept. of State Revenue,* 557 N.E.2d 1110 (Ind.Tax 1990); *State v. Apex Steel & Supply Company*, 375 N.E.2d 598 (Ind.App. 1978); *Oster v. Department of Treasury*, 37 N.E.2d 528 (Ind. 1941)

Taxpayer protests assessments of Indiana gross income tax on receipts derived from "remanufacturing" activities.

III. Gross Income Tax – Interstate Sales

Authority: IC 6-2.1-3-3; IC 6-8.1-5-1; 45 IAC 1-1-119

Taxpayer protests the characterization of its "out-of-state sales" as Indiana gross income.

STATEMENT OF FACTS

Taxpayer is incorporated and domiciled in Indiana. For tax years 1985 and 1988 through 1992, Audit proposed assessments of Indiana gross income tax. Taxpayer protested these assessments. The Department held an administrative hearing and a Letter of Findings (LOF) was subsequently issued. As Taxpayer was not sustained on all protested issues, Taxpayer timely requested, and the Department granted, a rehearing.

I. Gross Income Tax – Receipts from Retail Sales

DISCUSSION

Among its business activities, Taxpayer *remanufacturers* certain types of rings. Remanufacturing activities require Taxpayer to obtain a supply of used rings. Taxpayer may purchase used rings from third parties. Taxpayer may accept used rings from customers which are given as "trade-ins" towards the purchase of new or remanufactured rings; or Taxpayer may receive used rings from its customers, not as trade-ins, but with instructions to "remanufacture" and return the originally supplied rings.

Taxpayer's original protest focused on whether, for gross income tax purposes, receipts from remanufacturing activities should

have been taxed at the high rate (as service sales) or at the low rate (as retail or wholesale sales).

In the original letter of findings ("LOF"), the Department concluded that Taxpayer's sale of remanufactured rings *from inventory* qualified for low rate treatment because the receipts were derived from selling at retail. The Department explained:

> Consistent with the…language [found in IC 6-2.1-2-1(b)(1)], **taxpayer's sale of remanufactured rings *from inventory* qualifies as selling at retail.**
>
> Conversely, the Department also stated:
>
> *[But] when taxpayer's customers send in used rings and receive, in return, their original, remanufactured rings, receipts from these sales are not derived from "selling at retail."* Absent from these transactions is the requisite exchange of tangible personal property.

To summarize, the Department concluded that Taxpayer's sales of remanufactured rings *from inventory* qualified for low rate treatment while receipts from "sales" of remanufactured rings owned by its customers were to be taxed at the high rate. The Department denied Taxpayer's protest.

Taxpayer asks the Department to clarify the scope of its original findings. Specifically, Taxpayer is concerned that despite the language used in the original LOF, the unconditional denial of Taxpayer's protest results in additional gross income tax assessments, at the high rate, for receipts derived from sales of remanufactured rings from inventory.

Taxpayer points to the Department's own language in the original LOF:

> Audit classified taxpayer's remanufacture of jet engine rings as a service activity. Consequently, **Audit assessed all income received from these remanufacturing activities at the high rate for gross income tax purposes** (emphasis added).

Taxpayer contends the aforementioned language, coupled with language found in the auditor's report, indicates that all receipts derived from remanufacturing activities—whether from sales of remanufactured rings from inventory, or from "sales" of remanufactured rings owned by its customers—were classified by Audit as service income.

Taxpayer's point is well taken. The language used by Audit does suggest that all receipts from Taxpayer's remanufacturing activities were characterized as high rate service income—a result at odds with the conclusions reached by the Department. The proposed assessments, therefore, will be adjusted to the extent Taxpayer's retail sales (i.e., sales from inventory) were mistakenly characterized as service income.

FINDING

Taxpayer's protest is sustained.

II. Gross Income Tax – Receipts from "Remanufacturing" Activities

In the original protest, Taxpayer argued that its remanufacturing activities should have been characterized, for gross income tax purposes, as industrial processing—with receipts taxed at the low rate. Taxpayer, in support of its position, directed the Department's attention to IC 6-2.1-2-1(c)(1)(D)(ii), which broadened the statutory definition of wholesale sales to include:

> (D) Receipts from industrial processing or servicing, including:
>
> (i) tire retreading; and
>
> (ii) the enameling and plating of tangible personal property which is owned and is **to be sold** by the person for whom the servicing or processing is done, either as a complete article or incorporated as a material, or as an integral or component part of tangible personal property **produced for sale** by such person in the business of manufacturing, assembling, constructing, refining, or processing (emphasis added).

The court in *Jefferson Smurfit v. Indiana Department of State Revenue,* 681 N.E.2d 806 (Ind.Tax 1997), limited application of the industrial processing resale requirement (i.e., the "to be sold" and "produced for sale" language) to only those engaged in "enameling and plating" activities. Given this "limitation," Taxpayer believed its remanufacturing activities fell within the industrial processing classification.

The Department disagreed, and explained:

> [R]egardless of moniker used – whether taxpayer rebuilds, repairs, refurbishes, or remanufactures – taxpayer's customers are not engaged in activities contemplated by the concept, or definition, of "industrial processing." **Implicit in the concept of industrial processing is the notion that the owners of the processed property (i.e., taxpayer's customers) are engaged in manufacturing, processing, or similar activities**. In this instance, taxpayer's customers—commercial airlines—are not engaged in these types of activities. Rather, taxpayer's customers are service providers (emphasis added).

Taxpayer asks the Department to reconsider its interpretation of "industrial processing" in light of the *Jefferson Smurfit* decision. Taxpayer provides the following rationale:

> As the Jefferson Smurfit court dictates, subsections of IC 6-2.1-2-1(c)(1)(D) must be read independently. Borrowing from the rationale of the Jefferson Smurfit court, a similar conclusion is reached regarding the "by such person in the business of manufacturing, assembling, constructing, refining, or processing" requirement contained in subparagraph (ii). This requirement may not be expanded beyond the parameters of (ii). If the restrictions in (ii) do not apply to (i), they certainly do not apply to subsection (D) in general….Only "industrial processing or servicing" that involves enameling and plating, and which falls under Ind. Code Ann. 6-2.1-2-1(c)(1)(D)(ii), may have a "by such person in the business of manufacturing, assembling,

constructing, refining, or processing" requirement. Therefore, [Taxpayer], whose industrial processing or servicing does not involve enameling or plating, has no "such person in the business of manufacturing, assembling, constructing, refining, or processing" requirement for the years in question, 1990-1992.

In other words, Taxpayer argues that since the "to be sold" and "produced for sale" language (aka the "resale" requirement) applies only to those engaged in "the enameling and plating of tangible personal property," so too should the phrase "by such person in the business of manufacturing, assembling, constructing, refining, or processing."

The Department disagrees with Taxpayer's conclusions and therefore, declines the invitation to revise its post-*Jefferson Smurfit* interpretation of IC 6-2.1-2-1(c)(1)(D)(ii). If, as Taxpayer contends, the logic used by the *Jefferson Smurfit* court to limit the resale requirement to only those "engaged in enameling and plating of tangible personal property" can be used to similarly limit the rest of the requirements listed in IC 6-2.1-2-1(c)(1)(D)(ii), then what remains of the concept "industrial processing?"

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While the term is not ubiquitous, a discussion (however brief) of "industrial processing" appears in enough Indiana authorities—e.g., statutes, regulations, and court cases—to indicate the term's ongoing relevance and importance. The term "industrial processing" is explicitly mentioned in **four (4) Indiana court cases**—*Jefferson Smurfit, Chrome Deposit v. Indiana Dept. of State Revenue,* 557 N.E.2d 1110 (Ind.Tax 1990), *State v. Apex Steel & Supply Company*, 375 N.E.2d 598 (Ind.App. 1978), and *Oster v. Department of Treasury*, 37 N.E.2d 528 (Ind. 1941)—**three (3) statutes**—IC 6-2.1-2-1 (imposition of gross income tax), IC 6-2.5-4-2 (state gross retail and use taxes, "wholesale sales"), and IC 6-6-2.5-12 (definition of "heating oil")—and **two (2) regulations**—45 IAC 1.1-1-23 (gross income tax, "wholesale sale" defined) and 45 IAC 2.2-5-10 (sales and use tax exemptions).

However, after *Jefferson Smurfit*, who may call themselves "industrial processors" except those engaged in enameling and plating activities? Do the following requirements of IC 6-2.1-2-1(c)(1)(D)(ii), as Taxpayer argues, now apply only to this select subset of "industrial processors" and not to those who have traditionally been characterized as "industrial processors?" Taxpayer wishes to limit the following language:

1. the tangible personal property being processed must be owned "by the person for whom the servicing or processing is done;"
2. the tangible personal property being processed or serviced must either represent **(a)** a complete article or **(b)** one incorporated as a material, or **(c)** integral, or **(d)** component part of tangible personal property; and
3. the owner of the property (i.e., the "industrial processor's customer) must be in the business of **(a)** manufacturing, **(b)** assembling, **(c)** constructing, **(d)** refining, or **(e)** processing.

At first blush, parity of reasoning suggests Taxpayer may be correct. But absent a statutory definition of "industrial processing," how can the Department properly administer the statute?

****

Without a definition of "industrial processing," only those engaged in enameling and electroplating could qualify for low rate treatment. IC 6-2.1-2-1. All others (including Taxpayer) would, by default, be characterized as "service providers"—an absurd result clearly at odds with and "plainly repugnant" to the intent of the Legislature as evidenced by the aforementioned authorities.

Therefore, absent a statutory definition of "industrial processing"—a conclusion reached if Taxpayer's post-*Jefferson Smurfit* interpretation is correct—the term "industrial processing" must be given its "plain and ordinary meaning." (See IC 1-1-4-1 and *Apex Steel.*) To obtain such meaning, the Department must turn to other sources.

The court in *Apex Steel* was required to define "processing" and "servicing" as the words were used in a previously codified version of the statute defining "wholesale sales." The court stated:

> At issue is the interpretation of IC 6-2-1-3, and in particular subparagraphs (a)(4) and (g). Subparagraph (a)(4) provides a tax rate of ½% upon wholesale sales. "Wholesale sales" are then specially defined in seven (7) categories. Category (4) consists of,
>
> > [r]eceipts received from the business of industrial **processing** or **servicing** including but not limited to enameling and plating of any tangible personal property…(emphasis added).

Apex Steel at 598.

> The court, interpreting the words "servicing" and "processing" as used in IC 6-2-1-3(a)(4), adopted the following definition: As Apex's expert witness in linguistics testified at trial, "processing" and "servicing" in their plain and commonly understood meaning refer to *performing some act upon a material in order to render it in a condition for further use, or for sale or into a finished state* (emphasis added).

Id. at 600.

However, our lexical analysis is not complete as both "processing" and "servicing" are modified by "industrial." The Department references a popular English language dictionary—*The American Heritage Dictionary of the English Language* (Third Edition, 1992)—in its search for the "plain and ordinary meaning" of "industrial." As an adjective, "industrial" means "relating to, or resulting from industry: *industrial development; industrial pollution*." *Id.* at 922. The first three (3) definitions for "industry" read as follows:

1. Commercial production and sale of goods. **2.** A specific branch of manufacture and trade: *the textile industry.* See synonyms at **business. 3.** The sector of an economy made up of manufacturing enterprises: *government regulation of industry.*

Id.

As "industry" refers to those engaged in production or manufacturing activities, so too must "industrial." Even absent a statutory definition of "industrial processing," its plain and common meaning suggests a reference to one who performs "some act upon [tangible personal property] in order to render it in a condition for further use, or for sale or into a finished state" for another who is engaged in production or manufacturing activities. The "by such person in the business of manufacturing, assembling, constructing, refining, or processing" requirement of IC 6-2.1-2-2(c)(1)(D)(ii) is consistent with this "plain and ordinary" meaning.

Not only is the "plain and ordinary meaning" consistent with commonsense perceptions of "industrial processing," it is consistent with the term as it is used in the context of a statutory subset of "wholesale sales." Recall, IC 6-2.1-2-1(c)(1) states in part:

"Wholesale sales" means any sale described in this subsection in which the purchaser is not a division, subdivision, agency, instrumentality, unit, or department of government:

(C) Sales of tangible personal property to be incorporated as a material or integral part of *tangible personal property produced by a purchaser in the business of manufacturing, assembling, constructing, refining, or processing.*

(Emphasis added.)

Clearly, the concept of "wholesale sales" anticipates the production of tangible personal property by one claiming the "wholesale sales" exemption. The inclusion of the debated language of IC 6-2.1-2(c)(1)(D)(ii)—i.e., "by such person in the business of manufacturing, assembling, constructing, refining, or processing"—is also consistent with this notion. The Department, therefore, will not exclude the "manufacturing, assembling, refining, or processing" requirement from its definition of "industrial processing."

FINDING

Taxpayer's protest is denied.

III. Gross Income Tax – Interstate Sales

DISCUSSION

Taxpayer classified sales of computer software maintenance agreements as interstate sales. These sales were excluded by Taxpayer from its Indiana gross income. Proposed assessments resulted.

In the original LOF, the Department concluded, relying on IC 6-2.1-3-3 and 45 IAC 1-1-119, that Taxpayer's sales represented sales "made in interstate commerce;" as such, the sales should not have been included in Taxpayer's Indiana gross income. Taxpayer now asks the Department to clarify the scope of its findings. Taxpayer explains:

Although the "Discussion" [from the original LOF] squarely addresses the issue, the "Discussion" and "Finding" do not exactly address all years for which adjustments are necessary…. 1991 was the only year the taxpayer classified these sales as sales made in interstate commerce. <u>In fiscal years 6/30/90 and 6/30/92 the taxpayer erroneously did not exclude any of these sales [from its Indiana gross income] as sales made in interstate commerce.</u>

* * * * * * * * * * * * * *

We, therefore, request a rehearing to incorporate into the "Discussion" and "Findings"…adjustments…to taxable gross receipts for fiscal years 6/30/90 and 6/30/92 [in order] to exclude the gross receipts from sales of computer software maintenance contracts made in interstate commerce (emphasis added).

The Department, pursuant to IC 6-8.1-5-1, conducts hearings on timely filed protests of proposed assessments—as was the case for 1991. However, no proposed assessments were made in 1990 and 1992 because Taxpayer included these "interstate" sales in its Indiana gross income. Concomitant with its protest of these proposed assessments, Taxpayer requested a refund for taxes "erroneously" paid in 1990 and 1992. In other words, the 1990 and 1992 claims were based on overpayments of tax, not on proposed assessments. Given the statutory mandate regarding the conduct of hearings, the Department will not expand the language of its LOF to incorporate overpayments made in 1990 and 1992.

Taxpayer, however, is not without a remedy. Taxpayer's refund request will be evaluated consistent with the Department's previous findings; but any refund amounts approved may only be used to offset Taxpayer's outstanding tax liabilities (based on assessments) for 1990 and 1992.

FINDING

Audit did not propose assessments of sales/use tax on Taxpayer's interstate sales of computer software maintenance agreements in 1990 and 1992. Consequently, Taxpayer lacks an issue to protest. Findings, therefore, are not required.

DEPARTMENT OF STATE REVENUE

04990634.SLOF

SUPPLEMENTAL LETTER OF FINDINGS NUMBER: 99-0634
Sales and Use Tax
For Tax Periods: 1996-1997

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

1. Sales and Use Tax – All Terrain Vehicles

Authority: IC 6-2.5.5-2; IC 6-8.1-5-1(b); IC 6-2.5-3-2(a)(3); 45 IAC 2.2-5-3(e)(3); 45 IAC 2.2-5-1(c)(3); 45 IAC 2.2-5-1(a); 45 IAC 2.2-5-1(a); Gross Income Tax Division v. National Bank and Trust Co., (1948) 226 Ind. 298, 79 N.E. 2d 651

Taxpayer protests the assessment of gross retail tax on purchases of two all terrain vehicles.

STATEMENT OF FACTS

Taxpayer is a Kentucky tree, grain and cattle farmer. In 1996 and 1997 he bought all terrain vehicles from an Indiana dealership. After an audit of the Indiana dealership, the Indiana Department of Revenue assessed gross retail tax on Taxpayer's purchases of the all terrain vehicles. Taxpayer protested the assessment. A hearing was held and Letter of Findings was issued on September 1, 2000. A rehearing was requested and granted. More facts will be provided as necessary.

1. Sales and Use Tax

DISCUSSION

Pursuant to IC 6-2.5-3-2 (a), Indiana imposes an excise tax on tangible personal property stored, used, or consumed in Indiana. A number of exemptions are available from use tax. All exemptions must be strictly construed against the party claiming the exemption. Gross Income Tax Division v. National Bank and Trust Co., (1948) 226 Ind. 298, 79 N.E. 2d 651. Taxpayer contends that the purchases of the all terrain vehicles qualify for exemption pursuant to the agricultural exemption found at IC 6-2.5-5-2 as follows:

> (a) Transactions involving agricultural machinery, tools, and equipment are exempt from the state gross retail tax if the person acquiring that property acquires it for his direct use in the direct production, extraction, harvesting, or processing of agricultural commodities.

This exemption applies to "those persons occupationally engaged in producing food or agricultural commodities for sale." 45 IAC 2.2-5-1 (a). Taxpayer is engaged in the growing of grain, cattle and oak trees for sale. Therefore, Taxpayer is one of the persons who can purchase equipment which qualifies for this exemption. The statute states that the exemption applies to machinery that is directly used in the direct production of agricultural commodities. To qualify for this exemption, the equipment "must have an immediate effect on the article being produced." 45 IAC 2.2-5-1 (a). Machinery meets this test "if it is an essential and integral part of an integrated process which produces food or an agricultural commodity." 45 IAC 2.2-5-1 (a). If equipment is used in both an exempt and non exempt manner, it qualifies for exemption in proportion to the amount of exempt use. 45 IAC 2.2-5-1 (c) (3). The issue to be determined is whether any or all of the use of the all terrain vehicles qualifies for exemption.

The first all terrain vehicle was purchased to replace a tractor. The second all terrain vehicle was purchased to replace the first all terrain vehicle after it was of no further use. The all terrain vehicles look like golf carts. They have no cab, turn signals or brake lights. They cannot legally be driven on the public highways.

Taxpayer provided the Department with a breakdown of the various uses of the all terrain vehicles and the percentage of time the all terrain vehicles were used in each of the functions. First, the all terrain vehicles are used twenty percent (20%) of the time to clear new growth and weeds from the edges of fields. The field edges are not used to produce food. Therefore, this use does not qualify for exemption from the sales and use tax.

Taxpayer used the all terrain vehicles another twenty percent (20%) of the time during the planting and fertilizing process. Therefore, this use qualifies for the agricultural exemption from sales and use tax.

Two to three times per growing season Taxpayer used the all terrain vehicles to spray crops with chemicals to eliminate weeds. This twenty percent (20%) use of the all terrain vehicles qualifies for exemption.

Taxpayer also used the all terrain vehicles ten percent (10%) to clear new growth and weeds from the edges of pastures. The edges of the pastures are not used to produce food. Therefore, this use does not qualify for exemption.

Ten percent (10%) of the time, Taxpayer used the all terrain vehicles to transport tools, fuel and parts. This is clearly a taxable use of the vehicles since it does not directly affect the process of growing trees, cattle and grain.

Taxpayer also used the all terrain vehicles to construct and check fencing. The exempt use of fencing is clarified at 45 IAC 2.2-5-3 (e) (3) as follows:

> Fences, fencing materials, gates, posts, and electric fence chargers are exempt only if the same are purchased for use in confining livestock during the production processes of breeding, gestation, farrowing, calving, nursing, or finishing... Fencing

materials are also taxable if the fence is used only as a partition fence between adjoining landowners or as a means to keep wildlife, stray animals, or trespassers from entering cropland or farm premises.

In this case Taxpayer used the fencing ten percent (10%) of the time to keep cattle in the appropriate areas for their growth. Pursuant to the Regulation, this use of fencing qualifies for exemption. Taxpayer also used the all terrain vehicles five percent (5%) of the time to run fence around the property lines to keep animals out of the woods. Pursuant to the Regulation, this is a taxable use of fencing.

Taxpayer's final use of the all terrain vehicles was to run the timber grounds to keep timber thieves at bay. This five percent (5%) use of the all terrain vehicles is not directly related to the direct production of agricultural products and does not qualify for exemption.

FINDING

Taxpayer's protest is sustained for fifty percent (50%) of the use of the all terrain vehicles and denied for fifty percent (50%) of the use of the all terrain vehicles.

DEPARTMENT OF STATE REVENUE
REVENUE RULING #2001-04 IT
February 19, 2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

Adjusted Gross Income Tax – Attribution of Nonresident Partners' Distributive Shares of Partnership Income, Gain, Loss and Deduction to Sources Within Indiana

Authority: Rule 45 IAC 3.1-1-105; Rule 45 IAC 3.1-1-106

The taxpayer requests the Department to rule whether or not portfolio interest, net Internal Revenue Code Section 1231 loss, long-term capital gain from the sale of securities and long-term capital gain attributable to the sale or exchange of goodwill and going concern value are subject to apportionment or direct allocation for nonresident non-corporate partners.

Further, if the above items are subject to apportionment the taxpayer requests the Department to rule whether or not the items are apportioned at the entity or partner level.

The taxpayer, also, requests the Department to rule, if the above items are subject to direct allocation, to where and on what basis are the items allocated and is such allocation determined at the entity or partner level.

STATEMENT OF FACTS

The taxpayer is a limited liability partnership. The taxpayer entered into several transactions throughout the past year which resulted in long-term capital gains. In addition, the taxpayer generated portfolio interest from short-term investment of its working capital. The management activity with respect to such investments takes place outside of Indiana and the underlying intangibles have a situs wholly outside Indiana. Also during the year, the taxpayer generated a net Internal Revenue Code Section 1231 loss from the sale of tangible personal property used in the ordinary conduct of its business operations and having a situs at various taxpayer operating offices throughout the United States.

DISCUSSION

Rule 45 IAC 3.1-1-105 provides that a partnership must file an annual return with the Department disclosing each partner's distributive share of partnership income. Rule 45 IAC 3.1-1-105, further, provides that, "As used in this section "partner's distributive share" means the amount determined under Section 704 of the Internal Revenue Code and its prescribed regulations before any modifications required by Indiana tax statutes." Rule 45 IAC 3.1-1-106, addressing individual nonresident partners' distributive shares, states that, "The distributive share of a nonresident partner will be reported after apportionment to determine the partnership income derived from sources within Indiana. This determination will be accomplished by use of the apportionment formula described in IC 6-3-2-2(b)."

It is clear from the above regulations that <u>all</u> of a partnership's income is subject to apportionment. Portfolio interest, net Internal Revenue Code Section 1231 loss, long-term capital gain from the sale of securities and from the sale or exchange of goodwill and going concern value, as components of partnership income, therefore, are subject to apportionment at the partnership level.

RULING

The Department rules that portfolio interest, net Internal Revenue Code Section 1231 loss, long-term capital gain from the sale of securities and long-term capital gain attributable to the sale or exchange of goodwill and going concern value are subject to apportionment at the partnership level for nonresident non-corporate partners.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated herein, are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling, a change in statute, regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

DEPARTMENT OF STATE REVENUE
Revenue Ruling #2001-06 IT
March 13, 2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

Adjusted Gross Income Tax – Prison Investment Credits
Authority: IC 6-3.1-6; IC 6-3.1-1-1; IC 6-3-1-14; IC 6-3-1-15

The taxpayer requests the Department to rule whether or not an individual taxpayer is entitled to prison investment credits if the individual taxpayer satisfies all requirements found In IC 6-3.1-6.

STATEMENT OF FACTS

The taxpayer, an individual, contracted with a corporation to supplement his business operations. The taxpayer engaged the corporation to facilitate the manufacture of circuit boards and other electronic devices. The corporation facilitates the manufacture of circuit boards and other electronic devices through its relationship with Pen Products and/or the Indiana Department of Correction.

DISCUSSION

IC 6-3.1-6 does not provide a definition of "taxpayer". IC 6-3.1-1-1, however, states:

Except as otherwise provided in this article, the definitions contained in IC 6-3-1 apply throughout this article.

IC 6-3-1-14 defines "person" as an individual, trust or estate: Provided, that no corporation shall be considered to be a person. IC 6-3-1-15 defines "taxpayer" as any person or any corporation subject to taxation under IC 6-3. A person is subject to taxation under IC 6-3-2-1. IC 6-3.1-6-2 provides that a "taxpayer" who satisfies the requirements of IC 6-3.1-6 is entitled to receive prison investment credits. It is clear then, a taxpayer is not precluded from entitlement to prison investment credits by virtue of being an individual.

RULING

The Department rules that an individual taxpayer is entitled to prison investment credits if the individual taxpayer satisfies all the requirements found in IC 6-3.1-6.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated herein, are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling, a change in a statute, regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.