ALCOHOL AND TOBACCO COMMISSION
DOCUMENT #17

Date: August 16, 2001
Subject: Alcohol and Tobacco Commission application of Statute and rule regarding issuance of permits to premises in proximity to churches and schools.
Affected: IC 7.1-3-21-11; IC 6-1.1-10-16
1. IC 7.1-3-21-11 states as follows:
(a) As used in this section, "wall" means a wall of a building. The term does not include a boundary wall.
(b) Except as provided in subsection (c), the commission shall not issue a permit for a premises if a wall of the premises is situated within two hundred (200) feet from a wall of a school or church, if no permit has been issued for the premises under the provisions of Acts 1933, Chapter 80.
(c) This subsection applies to a county having a population of more than one hundred eight thousand nine hundred fifty (108,950) but less than one hundred twelve thousand (112,000). The commission shall not issue a permit for a premises if a wall of the premises is situated within two hundred (200) feet from a wall of a school or church unless:
(1) the permit is a beer dealer or wine dealer permit for a grocery store;
(2) the main entrance of the grocery store and the main entrance of the school or church face different streets or roads;
(3) there is a physical barrier between the grocery store and the school or church that prevents a person from moving between the two (2) properties; and
(4) a wall of the grocery store is not situated within one hundred (100) feet from a wall of the school or church.
2. IC 6-1.1-10-16(a) states as follows:
(a) All or part of a building is exempt from property taxation if it is owned, occupied, and used by a person for educational, literary, scientific, religious, or charitable purposes.
3. The term "church" shall include: Temple, Synagogue, Mosque, or any similarly situated building of religious worship.
4. The qualifications for the exception listed in IC 7.1-3-21-11(b), are as follows:
(a) the church must meet the qualifications listed in paragraph 3 immediately above;
(b) it must apply for the property tax exemption from the Indiana Department of Revenue for religious institutions; and,
(c) the building used as a church and for which the exception in IC 7.1-3-21-11(b) is sought is in fact exempt from property taxation, must be owned, occupied and used by a person for educational, literary, scientific, religious or charitable purposes.
5. Further, the measurement under IC 7.1-3-21-11(b) shall take place from the wall of the church nearest the permit premise that qualified under a-c above, to either:
l. the nearest two walls of each, if the permit premises and the church face the same street; or,
2. the nearest church wall and the nearest point of the permit premise facing the street upon which the permit premises is located if the permit premises and the church face different streets.
Analysis and Conclusion: In order for the Alcohol and Tobacco Commission to apply IC 7.1-3-21-11, a building must meet the definition of IC 6-1.1-10-1 6(a) as to churches and schools. If the building does not meet this definition, then the provisions of IC 7.1-3-21-ll shall not apply. If the building does meet the definition in IC 6-1.1-10-16(a), the determination of the buildings proximity in feet to the permit premises or proposed permit premises shall be made by a qualified member of the Indiana State Excise Police or the appropriate local board applying the provisions of 5 herein.

DEPARTMENT OF STATE REVENUE
INFORMATION BULLETIN #15
Income Tax
September 2001
(Replaces Information Bulletin #15, dated July 1986)

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 inconsistent with the law, regulations, or court decisions is not binding on either the Department or the taxpayer. Therefore, information provided in this Bulletin should only serve as a foundation for further investigation and study of the current law and procedures related to its subject matter.
SUBJECT: EXTENSION OF TIME TO FILE INDIANA CORPORATION INCOME TAX RETURNS AND RECOGNITION OF THE FEDERAL EXTENSION OF TIME TO FILE INDIANA CORPORATION INCOME TAX RETURNS
REFERENCES: IC 6-8.1-6-1; IC 6-8.1-10-2.1
INTRODUCTION:
The purpose of this Bulletin is to explain the steps necessary to get a valid Indiana extension to file an Indiana corporate income tax return.

I. EXTENSION OF TIME TO FILE

The Indiana Department of Revenue accepts the approved federal Form 7004 (Application for Automatic Extension of Time to File Corporation Income Tax Return). It is not necessary to request a separate extension of time to file for Indiana filing purposes if a federal extension has been approved. The Indiana corporation income tax return will be accepted as timely filed if it is filed within thirty (30) days after the expiration date of the federal extension. The federal extension is automatically an extension for six months. A copy of the approved Federal Extension Application must be attached to the return.

If an extension of time to file is not being requested from the Internal Revenue Service, or if an extension is being sought for a period in excess of the thirty (30) days past the expiration date of a federal extension, a special extension of time to file must be requested. The written request for a special extension of time to file must be made prior to the original due date or before the current extension of time expires. This request should contain an explanation as to why the extension is being sought and for what period. The request for a special extension of time to file should be sent to:

Indiana Dept. of Revenue
Corporation Income Tax Section
Returns Processing Center
100 N. Senate Avenue
Indianapolis, IN 46204-2253

The Corporation Income Tax Section will issue a letter of approval or denial.

A corporation must pay, by the original due date for filing its return, at least 90% of the tax that is reasonably expected to be due. Any amount due should be sent to the Corporation Income Tax Section as a fifth quarter estimated payment on Form IT-6.

II. PENALTIES

A ten percent (10%) penalty will be assessed against a taxpayer who files his Indiana corporation income tax returns past the due date of the return and does not attach a valid extension of time to file or have not prepaid at least ninety percent (90%) of the tax reasonably expected to be due by the original due date. The penalty is imposed under IC 6-8.1-10-2.1.

III. INTEREST

Any tax that remains unpaid during an extension period accrues interest in accordance with IC 6-8.1-6-1(d). The rate at which interest accrues depends upon the rate in effect during the extension period as determined in IC 6-8.1-10-1.

- 1992 – 8%
- 1993 – 7%
- 1994 – 7%
- 1995 – 6%
- 1996 – 7%
- 1997 – 7%
- 1998 – 7%
- 1999 – 7%
- 2000 – 7%
- 2001 – 8%

Any interest accrued should be paid with the remittance accompanying the tax return.

Kenneth L. Miller
Commissioner

DEPARTMENT OF STATE REVENUE
INFORMATION BULLETIN #18
Income Tax
September 2001
(Replaces Information Bulletin #18, dated December 1987)

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

SUBJECT: INSTRUCTIONS FOR OBTAINING EXTENSIONS OF TIME TO FILE INDIANA INDIVIDUAL INCOME TAX RETURNS

REFERENCE: IC 6-8.1-6-1; IC 6-8.1-10-2.1

INTRODUCTION:

This bulletin outlines the procedures for obtaining an extension of time to file the Indiana individual income tax return, (Form IT-40 or Form IT-40PNR).

I. AUTOMATIC EXTENSION OF TIME TO FILE, NOT TO EXCEED SIXTY (60) DAYS

Form IT-9, (Application for Automatic Extension of Time to File Indiana IT-40 or IT-40PNR), is used to obtain an automatic sixty (60) day extension of time to file the Indiana resident or nonresident return. Any taxpayer who wishes to request an extension of time to file, and who expects a payment to be due with their Indiana return, must complete and file the Form IT-9 voucher on or before the original due date of the Indiana individual tax return. If an application for extension is filed, at least ninety percent (90%) of the state and/or county tax due for the entire tax year must be paid with the application.

The payment made with Form IT-9 should be claimed as an estimated tax credit at the time of filing Form IT-40 or Form IT-40PNR. This is only an extension of time for filing your return. *This is not an extension of time to pay any state and/or county tax due.*

Form IT-9 is not required to be filed if there is no tax due on the Indiana individual income tax return.

If you file a federal extension, the Indiana Department of Revenue will accept the extension if a copy is attached to your return at the time of filing. You will have thirty (30) days beyond the federal extension period in which to file your Indiana return.

II. PENALTY AND INTEREST CHARGES

Form IT-9 or a federal extension does not extend the due date for the payment of the tax. A penalty may be assessed on any state or county tax paid after the due date of the return. However, a penalty will not be assessed if the balance due on the tax return is:

1. not in excess of ten percent (10%) of the amount of state and county tax due on the tax return, and;
2. paid with the return.

If a penalty is due with your return, it is calculated at ten percent (10%) of the tax that is owed with the return (excluding the first quarter installment of estimated tax) or $5.00, whichever is greater. Any penalty due with the return should be reported on the Form IT-40.

Interest will be charged on any amount due with your late filed return and should be calculated from the original due date of the return until the tax is paid. Interest is charged even though an extension has been granted. The interest rate changes annually. Please refer to Departmental Notice # 3. The interest should be added to the amount shown as due on the tax return.

Copies of returns and schedules are available on the Department's web site at www.in.gov/dor/taxforms

Kenneth L. Miller
Commissioner

INDIANA DEPARTMENT OF STATE REVENUE
INFORMATION BULLETIN #55
Income Tax
September 2001
(Replaces Information Bulletin # 55, dated April 1988)

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 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: DETERMINATION OF RESIDENCE FOR INDIVIDUALS LEAVING INDIANA FOR EMPLOYMENT IN A FOREIGN COUNTRY

REFERENCES: IC 6-3-1-11; IC 6-3-1-12; IC 6-3-4-4.1; 45 IAC 3.1-1-22

INTRODUCTION:

The purpose of this Bulletin is to briefly summarize the responsibilities for an individual who is working in a foreign country and still maintains his residency and domicile in Indiana.

I. RESIDENT DEFINED

The term "resident" means (a) any individual who was domiciled in Indiana during the taxable year; (b) any individual who maintains a permanent place of residence in Indiana and spends more than one hundred eighty three (183) days of the taxable year in Indiana; (c) any estate of a deceased person defined in (a) or (b); or (d) any trust which has a situs in Indiana.

II. DOMICILE DEFINED

A person has only one domicile at a given time even though that person maintains more than one residence at that time. Once a domicile has been established, it remains until the conditions necessary for a change of domicile occur.

In order to establish a new domicile, the person must be physically present at a place, and must have the simultaneous intent

of establishing a home at that place. It is not necessary that a person intend to remain there until death; however, if the person, at the time of moving to the new location, has definite plans to leave that new location, then no new domicile has been established.

The determination of a person's intent in relocating is necessarily a subjective determination. There is no one set of standards that will accurately indicate the person's intent in every relocation. The determination must be made on the facts presented in each individual case. Relevant facts in determining whether a new domicile has been established include: (1) purchasing or renting residential property; (2) registering to vote; (3) filing a resident state income tax return; (4) receiving public assistance; (5) titling and registering a motor vehicle; or (6) preparing a last will and testament which includes the state of domicile.

III. RESIDENT STATUS AND DOMICILE

You may be a resident of Indiana for income tax purposes even though you were living, working, or studying abroad during the taxable year.

To determine your resident status for income tax purposes, you must consider where you were domiciled and where you maintained a permanent place of abode during the taxable year.

If you are a United States citizen domiciled in Indiana, and you go to a foreign country for a limited amount of time because of an assignment by your employer, or for study, research or any other purpose, you do not lose or change your Indiana domicile unless you can clearly show that you intend to remain in that foreign country permanently and that you do not plan to return to Indiana.

IV. TAXABILITY OF INCOME EARNED IN A FOREIGN COUNTRY

If you are a United States citizen domiciled in Indiana while in a foreign country, you must file your Indiana individual income tax return as a resident, (Form IT-40). As an Indiana resident, you are subject to tax on income you received from all sources, including income earned in a foreign country that was included in your federal adjusted gross income.

If you are domiciled in Indiana and then go to a foreign country and clearly show your intent to establish your domicile outside of Indiana, then you must file your Indiana individual income tax return as a part-year resident, (Form IT-40PNR). As a part-year resident you are subject to tax on all your income from all sources for the part of the year you were an Indiana resident, and on any business income from Indiana for the part of the year you were a nonresident of Indiana.

V. FOREIGN TAX CREDIT

If you are entitled to a credit for taxes paid to a foreign country on your federal return, you may also be allowed a credit for Indiana income tax purposes. The computation of this credit is the same as computing the credit for taxes paid to other states. The credit is the lesser of (a) an amount equal to the Indiana tax rate multiplied by the income subject to tax in both Indiana and the foreign country; or (b) the actual amount of tax paid to the foreign country. This credit cannot exceed your Indiana adjusted gross income tax.

In order to be allowed a credit for tax paid to a foreign country you must attach a copy of Federal Form 1116, (Computation of Foreign Tax Credit), to your Indiana tax return.

VI. EXTENSION OF TIME TO FILE

If you are a United States citizen traveling, living or studying in a foreign country at the time your federal personal income tax is due, you qualify for an automatic two-month extension for filing your federal return. If you qualify for this federal extension, you are automatically entitled to the same extension plus thirty days for filing your Indiana personal income tax return. You do not have to request or apply for the Indiana extension as long as you attach to your Indiana return a statement that you qualify for the federal extension.

Also, if you receive an extension beyond the two-month period for filing your federal return, you are again automatically entitled to a similar extension for filing your Indiana return. Attach a copy of your approved federal extension to your Indiana return.

This is an extension of time to file and not an extension of time to pay. If a remittance is due, Form IT-9, (Indiana Department of Revenue Extension of Time to File), should be filed and payment made on or before the due date of the tax return.

VII. COUNTY TAX

If your county of residence was an adopting county on January 1 of the tax year, you are subject to county income tax. If you are an Indiana resident you must have an Indiana county as your county of residence, even though you may be in a foreign country at the time. The county tax is computed on Schedule CT-40 (County Tax Schedule for Indiana Residents) located in the Indiana individual income tax booklet.

VIII. PAYMENT OF ESTIMATED TAX

A taxpayer who expects to owe four hundred dollars ($400) or more in Indiana adjusted gross income tax and/or four hundred dollars ($400) or more in county income tax after subtracting all credits against the tax, is required to pay estimated tax. If you are paying estimated tax for the first time, you should mail Form ES-40 to the Department. You can make the first installment on the tax return. Mailing the Form ES-40 will ensure that you receive the estimated income tax voucher booklet for the remaining installments.

A ten percent (10%) penalty will be assessed for underpayment of estimated taxes. For further information, you may request Information Bulletin #3 from the Department or through its website at www.in.gov/dor/publications/bulletin/index.html

Kenneth L. Miller
Commissioner

DEPARTMENT OF STATE REVENUE
INFORMATION BULLETIN #73
Income Tax
September 2001
(Replaces Information Bulletin #73, dated March 1988)

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

SUBJECT: TAXABILITY OF NOT-FOR-PROFIT WATER, OR SEWAGE, CONSERVANCY, AND SOLID WASTE DISTRICTS

REFERENCE: IC 6-2.1-3-33; IC 13-21; IC 13-26; IC 14-33

INTRODUCTION:

Conservancy districts, regional water, or sewage solid waste districts, and certain not-for-profit corporations are exempt from the Indiana Gross Income Tax as provided under IC 6-2.1-3-33.

I. CONSERVANCY DISTRICTS

A conservancy district established under IC 14-33-20 (or under IC 13-3-4 before July 1, 1995) is exempt from Indiana gross income tax. A circuit court judge establishes a conservancy district after a petition has been presented and hearings held concerning the planned district. After the circuit court judge establishes the conservancy district, a plan for the district must be submitted to the Natural Resources Commission for approval.

Conservancy districts claiming an exemption should attach to their Indiana income tax return a copy of the circuit court order that established the district. The circuit court order will serve as verification that the taxpayer qualifies as a conservancy district.

II. REGIONAL WATER OR SEWAGE DISTRICTS:

A regional water or sewage district established under IC 13-26, (or IC 13-3-2 before July 1, 1995) is exempt from the Indiana gross income tax. A petition to establish a regional water or sewage district must be filed with the county executive of each governmental entity having territory within the district. The Indiana Department of Environmental Management must issue final approval.

Districts claiming an exemption should attach to the income tax return, a statement indicating whether they are a water or sewage district, as well as a copy of the approval letter issued by the Department of Environmental Management. The approval letter will serve as verification that the taxpayer qualifies as a regional water or sewage district.

III. SOLID WASTE MANAGEMENT DISTRICTS

A county solid waste management district or a joint solid waste management district established under IC 13-21 (or IC 13-9.5-2 before July 1, 1995) is exempt from the Indiana gross income tax. A district generally consists of one county, or multiple counties can become joint solid waste management districts.

IV. NOT-FOR-PROFIT WATER CORPORATIONS

A corporation formed solely for the purpose of providing water to the public is exempt from the Indiana gross income tax. The corporation must qualify for exemption from income tax under Section 501 of the Internal Revenue Code and be registered as a not-for-profit corporation with the Indiana Department of Revenue.

V. REGISTRATION AS A NOT-FOR-PROFIT

To be registered as a not-for-profit organization in Indiana, a corporation must submit an application to file as a not-for-profit organization, Form IT-35A. A copy of the articles of incorporation, a copy of the federal determination letter, and a Federal Form 990 must accompany the Indiana application. The application and requested attachments should be directed to the Not-For-Profit Section, Compliance Division, Indiana Department of Revenue, Room N203, Indiana Government Center North, Indianapolis, IN 46204. After an application has been reviewed, the Department will notify taxpayers regarding the not-for-profit status. If not-for-profit status is granted, the taxpayer will be required to file Form IT-35 AR (Not-For-Profit Organization's Annual Gross Income Tax Exemption Report).

Kenneth L. Miller
Commissioner

DEPARTMENT OF STATE REVENUE
INFORMATION BULLETIN #87A
Income Tax
September 2001

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

SUBJECT: RESIDENTIAL HISTORIC REHABILITATION CREDIT

REFERENCE: IC 6-3.1-22

INTRODUCTION:

Effective for taxable years beginning after December 31, 2001, there is an income tax credit available for the rehabilitation of historic residential property.

I. QUALIFIED TAXPAYERS

A qualified taxpayer is an individual filing a single return, or a husband and wife filing a joint return. If the husband and wife file a separate return, they may take the credit in equal shares, or one spouse may take the whole credit.

II. QUALIFIED EXPENDITURES

Qualified expenditures means expenditures for preservation or rehabilitation of a structure that enables the structure to be principally used and occupied by the taxpayer as the taxpayer's residence. The term does not include costs that are incurred to do the following:

- Acquire a property or an interest in a property.
- Pay taxes due on a property.
- Enlarge an existing structure.
- Pay realtor's fees associated with a structure or property.
- Pay paving and landscaping costs.
- Pay sales and marketing costs.

III. QUALIFICATION FOR THE TAX CREDIT

A taxpayer qualifies for the credit if all the following conditions are met.

The historic property is located in Indiana, is at least fifty years old, and is owned by the taxpayer.

1. The division of historic preservation and archeology of the department of natural resources (division) certifies that the historic property is listed in the register of Indiana historic sites and historic structures.
2. The division certifies that the taxpayer submitted a proposed preservation or rehabilitation plan to the division that complies with the standards of the division.
3. The division certifies that the preservation or rehabilitation work that is subject of the credit substantially complies with the proposed plan.
4. The preservation or rehabilitation work is completed in not more than two years, or five years if the preservation or rehabilitation plan indicates that the preservation or rehabilitation is initially planned for completion in phases.
5. The historic property is principally used and occupied by the taxpayer as the taxpayer's residence.

IV. LIMITATION OF THE TAX CREDIT

The qualified expenditures for preservation or rehabilitation of the historic property must exceed ten thousand dollars ($10,000). The tax credit is equal to twenty percent (20%) of the qualified expenditures that the taxpayer makes for the preservation or rehabilitation of the historic property. The total amount of all credits for all taxpayers may not exceed two hundred fifty thousand dollars ($250,000) in a state fiscal year.

V. PROCEDURE TO CLAIM THE CREDIT

The taxpayer shall claim the credit on the taxpayer's annual state income tax return. The taxpayer shall submit to the Department the certifications approved by the division.

If the credit exceeds the taxpayer's state income tax liability for the taxable year for which the credit is first claimed, the excess may be carried over to succeeding taxable years and used as a credit during those taxable years. The credit may be carried forward and applied to succeeding taxable years for fifteen taxable years following the unused credit year. A taxpayer is not entitled to a refund or carry back of any unused credit.

VI. RECAPTURE OF CREDIT CLAIMED

The Residential Historic Building Tax Credit shall be recaptured from the taxpayer if the property is transferred less than five years after completion of the certified preservation or rehabilitation work. The credit will also be recaptured if, less than five years after the completion of the certified preservation or rehabilitation, additional modifications to the property are undertaken that do not meet the standards of the division.

If the recapture of a credit is required, an amount equal to the credit recaptured shall be added to the tax liability of the taxpayer for the taxable year during which the credit is recaptured.

Kenneth L. Miller
Commissioner

DEPARTMENT OF STATE REVENUE
INFORMATION BULLETIN #91
Income Tax
September 2001

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SUBJECT: REREFINED LUBRICATION OIL FACILITY TAX CREDIT

REFERENCE: IC 6-3.1-22.2

INTRODUCTION:

This Bulletin is intended to summarize the tax credit available for property tax paid for an oil rerefining facility. The credit is applicable for tax years beginning after December 31, 2000.

I. REREFINED LUBRICATION OIL

Rerefined lubrication oil is base oil manufactured from at least ninety-five percent (95%) used oil, and uses not more than two percent (2%) previously unused oil in a refining process that effectively removes physical and chemical impurities and spent and unspent additives to the extent that the base oil is capable of meeting industry standards for engine oil.

II. ELIGIBLE ENTITIES AND TAXES APPLIED AGAINST

A taxpayer is an individual or entity that has state tax liability, including pass through entities.

The tax credit can be applied against the following taxes:

- Gross Income Tax
- State Gross Retail and Use Tax
- Adjusted Gross Income Tax
- Supplemental Corporate Net Income Tax
- Financial Institutions Tax
- Insurance Premiums Tax

III. QUALIFICATION FOR THE CREDIT

A person is entitled to a credit against their state tax liability in a taxable year for a percentage of the ad valorem property taxes paid in the taxable year for: real property on which a facility that processes rerefined lubrication oil is located; and personal property used in the processing of rerefined lubrication oil, including personal property used in the transportation of rerefined lubrication oil to and from the processing facility.

IV. CALCULATION OF THE CREDIT

The amount of the credit to which a taxpayer is entitled equals the product of:

The amount of ad valorem property taxes paid by the taxpayer in a taxable year; multiplied by the percentage that corresponds to the tax year listed below.

YEAR	PERCENTAGE OF CREDIT
2001	100%
2002	80%
2003	60%
2004	40%
2005	20%

A taxpayer is entitled to a carry-forward of any unused credit for a period not to exceed two years. However, no unused credit may be carried forward to a tax year beginning after December 31, 2007.

A taxpayer must request the Department of Commerce to determine if the taxpayer is entitled to the credit.

Kenneth L. Miller
Commissioner

DEPARTMENT OF STATE REVENUE

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LETTER OF FINDINGS NUMBER: 97-0442
State Cigarette Tax
For 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.

ISSUE

I. Cigarette Tax – Imposition

Authority: IC § 6-7-1-1; IC § 6-8.1-5-4; *Indiana Eby-Brown Co. v. Indiana Department of Revenue*, 648 N.E.2d 401 (Ind. Tax 1995)

Taxpayer protests the imposition of cigarette tax on cigarettes taxpayer reported exported from Indiana.

STATEMENT OF FACTS

Taxpayer is an Indiana Corporation that distributes cigarettes, tobacco products, and sundry items throughout Indiana and 3 other states, including Kentucky. During the audit period the Department inspected taxpayer's monthly cigarette tax returns and determined that the number of cigarettes reported exported to Kentucky on the Indiana cigarette returns was greater than the number of cigarettes reported imported, taxed, and sold on taxpayer's Kentucky cigarette returns for 1993, 1994, and 1995. The audit attributed the missing cigarettes to Indiana and assessed Indiana cigarette tax on them. Taxpayer is protesting this adjustment.

I. Cigarette Tax – Imposition

DISCUSSION

The overlying issue for the taxpayer's protest is the audit's assessment of tax based on inferences drawn from taxpayer records and tax returns from both Indiana and Kentucky. Taxpayer contends that the inferences resulting in assessment were not properly drawn. This issue revolves around the burden of proof in an audit situation, which IC § 6-8.1-5-4 defines as:

> Every person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records. The records in this subsection include *all source documents necessary to determine the tax*, including invoices, register tapes, receipts, and canceled checks. *(Emphasis added)*

Taxpayer does not cite any statute, regulation, or case law for the proposition that the auditor was required to accept assertions as to the nature of the transactions based solely on the returns taxpayer filed in Indiana. Taxpayer's assertion that the auditor was required to ignore conflicting documentation is not sustainable.

Taxpayer next argues that the discrepancy in the number of cigarettes reported shipped from Indiana and the number of cigarettes reported delivered to Kentucky is irrelevant to the Indiana audit, and that by implication the cigarettes 'disappeared' in interstate commerce and were thus not subject to taxation. The cigarette tax is imposed by IC § 6-7-1-1, which provides:

> It is the intent and purpose of this chapter to levy a tax on all cigarettes sold, used, consumed, handled, or distributed within this state, and to collect the tax from the person who first sells, uses, consumes, handles, or distributes the cigarettes. It is further the intent and purpose of this chapter that whenever any cigarettes are given for advertising or any purpose whatsoever, they shall be taxed in the same manner as if they were sold, used, consumed, handled, or distributed within this state. Notwithstanding any other provisions contained in this chapter. The liability for the excise taxes imposed by this chapter shall be conclusively presumed to be on the retail purchaser or ultimate consumer, precollected for convenience and facility only. When such taxes are paid by any other person, such payment shall be considered as an advance payment and shall be added to the price of the cigarettes and recovered from the ultimate consumer or user.

The Indiana Tax court addressed a challenge to the scope of this law, focusing on the issue of "shrinkage," which both parties stipulated to mean:

> Theft and shrinkage, prevalent problems in the cigarette industry, "occur through the complicity of the employees of the distributors and … prevail even though many precautionary methods are installed by distributors, such as surveillance cameras, tight entrance and exit security requirements, locked cages for storing cigarettes, periodic lie detector tests, anti-theft devices, more frequent inventory taking, etc." *Joint Stipulation* at ¶6. *Indiana Eby-Brown Co. v. Indiana Department of Revenue*, 648 N.E.2d 401 (Ind. Tax 1995) at 402

After review of the IC § 6-7-1-1 the court determined in *Indiana Eby-Brown Co. v. Indiana Department of Revenue*, 648 N.E.2d 401 (Ind. Tax 1995) at 406:

> For the foregoing reasons, this court holds that it is the legislature's intent to tax all cigarettes to be "sold, used, consumed, handled, or distributed" within the state,. Accordingly, the Department properly assessed to Eby-Brown a cigarette tax on cigarettes lost, stolen, or otherwise missing from its possession. Thus, the Department's final determination is AFFIRMED.

Taxpayer fails to address the chronology of these 'disappearances' in the protest. The cigarettes 'disappeared' totaled 97,825 in 1993, 516,050 in 1994, and 468,785 in 1995. This fivefold increase in annual losses after 1993 is not explained by taxpayer. Indeed, the only event of significance that occurred in 1993 related to this issue was a Letter of Finding issued to this taxpayer requiring the payment of cigarette tax on cigarettes that disappeared due to shrinkage, said interpretation of the law later being sustained in *Eby-Brown*.

As *Eby-Brown* holds, cigarettes consumed or distributed in this state, regardless of the circumstances surrounding their consumption, are taxable by this state. If 1,082,660 cigarettes disappear, shrinkage was involved. If the cigarettes last reported location was Indiana; then they were consumed or distributed in Indiana. Taxpayer's effort to transfer the shrinkage totals to interstate commerce is not sustained.

FINDING

Taxpayer protest denied.

DEPARTMENT OF STATE REVENUE

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LETTER OF FINDINGS NUMBER 97-0614
Responsible Officer
Sales Tax and Withholding Tax
For Tax Periods: 1993-1997

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 specific issues.

ISSUES

Sales and Withholding Tax – Responsible Officer Liability

Authority: IC 6-2.5-9-3, IC 6-3-4-8 (f), IC 6-8.1-5-1 (b), Indiana Department of Revenue v. Safayan, 654 N.E. 2nd 270 (Ind.1995) at page 273

The taxpayer protests the assessment of responsible officer liability for unpaid corporate sales and withholding taxes.

STATEMENT OF FACTS

The taxpayer was president of a corporation that did not remit the proper amount of sales and withholding taxes to Indiana. The taxpayer was personally assessed for the taxes and protested these assessments. A hearing was scheduled for May 15, 2001. Neither the taxpayer nor his representative appeared. Therefore, this decision is based upon the evidence in the file. More facts will be provided as necessary.

Sales and Withholding Tax – Responsible Officer Liability

DISCUSSION

The proposed sales tax liability was issued under authority of IC 6-2.5-9-3 that provides as follows:

An individual who:

(1) is an individual retail merchant or is an employee, officer, or member of a corporate or partnership retail merchant; and

(2) has a duty to remit state gross retail or use taxes to the department;

holds those taxes in trust for the state and is personally liable for the payment of those taxes, plus any penalties and interest attributable to those taxes, to the state.

The proposed withholding taxes were assessed against Taxpayer pursuant to IC 6-3-4-8(f), which provides that "In the case of a corporate or partnership employer, every officer, employee, or member of such employer, who, as such officer, employee, or member is under a duty to deduct and remit such taxes shall be personally liable for such taxes, penalties, and interest."

Indiana Department of Revenue assessments are prima facie evidence that the taxes are owed by the Taxpayer who has the burden of proving that assessment is incorrect. IC 6-8.1-5-1 (b).

Pursuant to Indiana Department of Revenue v. Safayan 654 N.E. 2nd 270 (Ind.1995) at page 273: "The statutory duty to remit trust taxes falls on any officer or employee who has the authority to see that they are paid. The factors considered to determine whether a person has such authority are the following:

1. The person's position within the power structure of the Corporation;
2. The authority of the officer as established by the Articles of Incorporation, By-laws or employment contract; and
3. Whether the person actually exercised control over the finances of the business including control of the bank account, signing checks and tax returns or determining when and in what order to pay creditors.

Id. At 273.

The taxpayer was the president of the corporation at the time of its incorporation. He contends, however, that he resigned as president on September 23, 1993. In support of this contention, the taxpayer submitted a copy of a letter to the Board of Directors of the corporation that informed them that he resigned his "positions as officer and director" of the corporation. Other documentation presented by the taxpayer, however, contradicts his claim that he resigned the presidency of the corporation. For example, the file includes a "Bill of Sale" dated February 18, 1997 with a notarized signature of the taxpayer as president of the corporation. The hearing officer finds that the notarized representation of the taxpayer as the president of the corporation on February 18, 1997 more credible than the self-serving and self-authenticated document wherein the taxpayer allegedly resigns the presidency.

The Secretary of State's office provided a copy of the Articles of Incorporation. Those Articles listed the taxpayer as the registered agent of the corporation. There was no listing of officers or designation of duties of the various officers. No copy of the corporate By-laws was available. The Indiana Department of Revenue must consider that presidents generally have the ultimate control and responsibility for any corporation.

The final indicia concerns the actual control over the finances of the corporation. A letter in the file and a Bill of Sale indicate that the taxpayer sold the corporation. The ability to sell the corporation indicates that the taxpayer had actual control over the financial aspects of the corporate activity.

Finally, the taxpayer alleges that another officer was actually the officer responsible for the remittance of taxes. The law does not require, however, that only one person be considered the person with a duty to remit taxes to the state. In the Safayan case, the corporate president was held to be a responsible person even though the day to day operations were specifically delegated to a vice-president in his employment contract as manager. "A party may be liable for trust taxes without having exclusive control over the corporation's funds." Safayan at 274. Another officer's possible responsibility for the remittance of taxes does not absolve the taxpayer from responsible officer liability.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04980187.LOF

LETTER OF FINDINGS NUMBER: 98-0187
Use Tax
For the Tax Periods: 1993, 1994, 1995, 1996

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ISSUE

I. Use Tax – Purchases

Authority: IC 6-2.5-3-2, IC 6-2.5-5-13, IC 6-8.1-5-1

The Taxpayer protests the Department's assessment of use tax on parts and equipment associated with its communications tower.

STATEMENT OF FACTS

Taxpayer owns large transmission towers in Indiana and leases space on them to communication providers. More facts supplied as necessary.

I. Use Tax – Purchases

DISCUSSION

Audit assessed use tax on parts and equipment purchased and then used by Taxpayer to construct, improve, and maintain a radio communications tower. Pursuant to IC 6-2.5-3-2(a), "[a]n excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana, if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction."

Taxpayer contends that its tower and component parts are not subject to tax because the tower is a fixture. The Department agreed that the tower represents a fixture, however, such characterization alone does not warrant exempt treatment. Pursuant to IC 6-2.5-3-2(c):

> The use tax is imposed on the addition of tangible personal property to a structure or facility, if, after its addition, the property becomes part of the real estate on which the structure is located. However, the use tax does not apply to additions of tangible personal property described in this subsection, if;
>
> (1) the state gross retail or use tax has been previously imposed on the sale or use of that property; or
>
> (2) the ultimate purchaser or recipient of that property would have been exempt from the state gross retail and use taxes if that purchaser or recipient had directly purchased the property from the supplier for addition to the structure or facility.

Taxpayer contends the tower qualifies for the sales/use exemption of IC 6-2.5-3-2(c)(2). Taxpayer, however, qualifies for no exemption. Specifically, IC 6-2.5-5-13 states that transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property furnishes or sells intrastate telecommunication service in a retail transaction. However, Taxpayer is not a telecommunications provider. Taxpayer merely leases space on his tower to the communications companies. Consequently, as no exemption applies, Taxpayer should have paid sales tax, or self-assessed use tax, on its purchase of parts and equipment intended for its communications tower. Insufficient documentation was submitted by Taxpayer to show the use tax was in fact paid.

FINDING

The Taxpayer's protest is respectfully denied.

DEPARTMENT OF STATE REVENUE

02980480.LOF

LETTER OF FINDINGS NUMBER: 98-0480
Adjusted Gross Income Tax – Unitary (Combined) Filing Status
Fiscal Years 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.

ISSUES

Adjusted Gross Income Tax – Unitary (Combined) Filing Status

Authority: *Mobil Oil Corporation v. Commissioner of Taxes of Vermont*, 445 U.S. 425, 100 S.Ct. 1223 (1980); *Exxon Corp. v. Department of Revenue of Wisconsin*, 447 U.S. 207, 100 S.Ct. 2109 (1980); *ASARCO, Inc. v. Idaho State Tax Commission*, 458 U.S. 307, 102 S.Ct. 3103 (1982); *F.W. Woolworth v. Taxation and Revenue Department of New Mexico*, 458 U.S. 354, 102 S.Ct. 3128 (1982); *Allied-Signal, Inc. v. Director, Division of Taxation*, 504 U.S. 768, 112 S.Ct. 2251 (1992); *Container Corp. v. Franchise Tax Board*, 463 U.S. 159, 180, n. 19, 103 S.Ct. 2933, 2948, n. 19 (1983); IC 6-3-2-2(l); IC 6-3-2-2(p); IC 6-3-2-2(q); 35 ILCS 5/1501(a)(27); Tenn.Code Ann. § 67-4-2004(25)(B)

Taxpayer protests the Audit Division's subsequent disallowance of unitary combined filing status, for purposes of the taxpayer's combined adjusted income tax return reporting for fiscal years 1995 and 1996, on the basis that the combined return inaccurately reported taxpayer's Indiana income.

STATEMENT OF FACTS

Taxpayer's parent corporation (hereinafter, "Parent") develops and manufactures electronic parts and assemblies. At the time of the audit, Parent maintained subsidiary manufacturing service centers in several locations in the United States and Canada, which included subsidiaries in Michigan and Indiana. The Michigan and Indiana subsidiaries were an automotive unit which produced shifter systems, parking-brake mechanisms, brake pedals, underbody spare-tire carriers, and airbag components. The "taxpayer" in the instant case is the Indiana subsidiary.

In July of 1995, Parent filed a petition for permission to file Indiana unitary combined returns with the Indiana and Michigan subsidiaries for the fiscal year 1995 and subsequent tax years. In its petition, Parent maintained that both the Michigan and Indiana subsidiaries were one hundred percent (100%) owned by Parent; that operationally, the Michigan and Indiana subsidiaries were one entity; that the administration and management of the two subsidiaries were located at the offices of the Michigan subsidiary; that all decisions regarding the operations of both subsidiaries were made at the Michigan subsidiary's offices in Michigan; and, that the subsidiaries shared officers and a board of directors.

In a letter dated August 30, 1995, and based upon the information submitted by Parent, the Indiana Department of Revenue granted Parent's request to file unitary combined returns in Indiana for fiscal year 1995 forward. Specifically, the Department found that Parent and its Michigan and Indiana subsidiaries met the unity requirements through its unity of ownership, centralized management, and centralized financial, administrative and operational services. (*See Department of Revenue-Tax Policy Division Letter* dated August 30, 1995, page 2). The Department further found that Parent and its subsidiaries met the "best method for reporting adjusted gross income" test through its shared industry impact on Indiana adjusted gross income, its interdependency of operation, and its coordination of the production process and production facilities. (*See Department of Revenue-Tax Policy Division Letter* dated August 30, 1995, page 3). Nevertheless, the Department reserved the right to revoke its grant of permission for unitary combined filing in the event that, *inter alia*, the facts subsequently established by the Department disclosed material error or misrepresentation of the facts set forth in Parent's original petition. (*See Department of Revenue-Tax Policy Division Letter* dated August 30, 1995, page 3).

Subsequent to its determination in its August 30, 1995 letter, the Department conducted an audit of Parent's Indiana subsidiary (*i.e.*, taxpayer) for the fiscal years 1995 and 1996. The Department's auditor determined that the unitary combined returns should not have been allowed because taxpayer was unable to prove that the combined return reporting method more fairly represented the adjusted gross income attributable to Indiana. According to the auditor, the Indiana adjusted gross income is more fairly represented by filing separate company returns.

Adjusted Gross Income Tax – Unitary (Combined) Filing Status

DISCUSSION

The taxpayer (*i.e.*, the Indiana subsidiary) protests the auditor's determination that it may not file unitary combined returns for the fiscal years in question. Taxpayer argues that the combined reporting is the only filing method that fairly represents the flow of value from functional integration, centralized management, and economies of scale, present between taxpayer and the Michigan subsidiary. According to taxpayer, because the Michigan and Indiana subsidiaries operate as one operating entity, the filing of separate company returns would result in an unfair and distorted apportionment of income to Indiana.

Before we address whether the Audit Division erred in determining that taxpayer may not file unitary combined returns, we

first address whether the Department may retroactively withdraw permission to file unitary combined returns. Taxpayer questions the Department's ability to challenge its earlier grant of permission to file combined returns without a finding of some material misstatement of fact.

On August 30, 1995, the Department granted taxpayer the right to file combined returns in a letter, stating in pertinent part: "Permission is hereby granted to [taxpayer and the Michigan subsidiary, and required of Parent], to file combined/unitary returns for adjusted gross income and supplemental net income tax effective for tax year ended June 30, 1995." (*See Department of Revenue-Tax Policy Division Letter* dated August 30, 1995, page 3). The statute applicable to the permission issue is found in IC 6-3-2-2 which states in pertinent part that:

> IC 6-3-2-2 Corporations and nonresidents; "adjusted gross income derived from sources in state" defined...
>
> (l) If the allocation and apportionment provisions of this article do not fairly represent the taxpayer's income derived from sources within the state of Indiana...
>
> (q)... taxpayers may petition the department... for permission to file a combined income tax return for a taxable year. The petition to file a combined income tax return must be completed and filed with the department not more than thirty (30) days after the end of the taxpayer's taxable year.

(*See Department of Revenue-Tax Policy Division Letter* dated August 30, 1995, page 3).

The Department's grant of permission to file combined returns was a determination, based upon the facts available to the Department at the time, upon which taxpayer could rely. However, the Department did reserve the right to revoke the grant of permission if, *inter alia*, "the facts subsequently established by the Department disclose material error or misrepresentation to the facts set forth in this petition." (*See Department of Revenue-Tax Policy Division Letter* dated August 30, 1995, page 3). This right of revocation was clearly set forth in the letter to taxpayer. And, the language of the letter clearly warned taxpayer that should a subsequent audit reveal a misrepresentation of the facts set forth originally, permission to file combined returns would be revoked. The Audit Division performed an audit for the years in question and determined that the combined filing method did not fairly reflect taxpayer's Indiana income and issued an assessment against taxpayer. We find nothing in the rules or statutes that prohibits the Department from determining whether taxpayer's assertions, in light of more contemporary audit findings, rise to the level of material error or misrepresentation of fact such that taxpayer's combined filing status should be revoked.

We now turn to the question of whether the Audit Division erred in determining that taxpayer's combined filing status should be disallowed on the basis that the combined return inaccurately reported taxpayer's Indiana income. In addressing this question, we examine: (1) whether a unitary relationship actually exists between Parent and taxpayer; and (2) whether filing a combined return would more fairly represent the Parent's and taxpayer's Indiana income.

The Supreme Court over the years has developed a three-part test in determining whether a unitary relationship exists: common ownership, common management, and common use or operation. *See*, *e.g.*, *Mobil Oil Corporation v. Commissioner of Taxes of Vermont*, 445 U.S. 425, 100 S.Ct. 1223 (1980); *Exxon Corp. v. Department of Revenue of Wisconsin*, 447 U.S. 207, 100 S.Ct. 2109 (1980); *ASARCO, Inc. v. Idaho State Tax Commission*, 458 U.S. 307, 102 S.Ct. 3103 (1982); *F.W. Woolworth v. Taxation and Revenue Department of New Mexico*, 458 U.S. 354, 102 S.Ct. 3128 (1982); *Allied-Signal, Inc. v. Director, Division of Taxation*, 504 U.S. 768, 112 S.Ct. 2251 (1992). The first item to be considered under this three-part test is common ownership. As a general rule, at least fifty percent (50%) of a corporation's stock must be commonly owned (either directly or indirectly) in order for a corporation to be considered part of a unitary business. *See*, *i.e.*, 35 ILCS 5/1501(a)(27) and Tenn.Code Ann. § 67-4-2004(25)(B). The information in taxpayer's file shows that during the audit period Parent owned one hundred percent (100%) of the stock of taxpayer. The evidence of file is sufficient to establish common ownership.

The second criteria to be considered is common management. Common management is shown when the parent corporation provides a management role that is grounded in the parent's own operation expertise and overall operational strategy. *See*, *e.g.*, *Container Corp. V. Franchise Tax Board*, 463 U.S. 159, 180, n. 19, 103 S.Ct. 2933, 2948, n. 19 (1983).

Here, the taxpayer has supplied evidence which shows that Parent exercised control and influence over it and the Michigan subsidiary. Parent, through Parent's finance division, consisted of six (6) officers, Chairman, President, Vice President-Secretary, Vice President-Treasurer, Vice President-General Counsel, and Assistant Treasurer; and two (2) professional staff, the Director of Employee Benefits and the Director of Corporate Communications. Each one of Parent's subsidiary groups was headed by a Vice President-General Manager (VP-GM). (Taxpayer and the Michigan subsidiary together comprised one subsidiary group (hereinafter referred to together as, the "Group")). Parent's board of directors controlled all of the subsidiaries. The VP-GM's of the subsidiary groups reported directly to the executive officers of the finance division. To obtain operating funds, the VP-GM's were required to send a request to the finance division treasurer. All excess funds were remitted to the finance division to reduce the line of credit. Additionally, Corporate Counsel routinely reviewed the subsidiary groups from the standpoint of insuring both compliance with applicable laws and regulations, as well as the practice of preventative law. We find that common management existed between Parent and Group.

The third test is that of common operation or use. Evidence of a common operation exists where certain functions are performed for the group by the parent (such as purchasing, financing, advertising, marketing, research, tax compliance, insurance, and pension plan management) which independent companies would perform for themselves.

In the taxpayer's case, information was supplied which shows that many of the administrative, management, and financing functions for the Parent's subsidiaries were centralized. All short-term financing, income tax return filing, legal support, and insurance coverage for the Group and the other subsidiaries was provided by Parent's finance division. Parent's finance division provided administrative and management assistance to the Group and the other subsidiaries with their respective defined benefit plans and worker's compensation claims. The finance division reviewed the marketing information prepared by the management units of the subsidiaries before the printing and distribution of said marketing materials. The finance division also supervised the commercial preparation of most preprinted marketing information, and arranged photograph sessions and commercial printer selection.

On the basis of these facts, we cannot say that the Department's finding that taxpayer enjoyed a unitary relationship with Parent and the Michigan subsidiary was against the weight of the evidence of file. There exists the elements of common ownership and management, and a modicum flow of value between the members of the business group. Using Parent's staff to provide services for taxpayer and the Michigan subsidiary that said taxpayer and subsidiary could have provided for themselves, resulted in common operation.

We now turn to the next point of analysis and the question of whether requiring taxpayer to use a standard apportionment or separate company filing method, instead of combined return filing, would result in a distortion of the income Parent reported as Indiana source income. Ultimately, this question requires us to determine whether, under all of the circumstances of the unitary relationship between Parent and the Michigan and Indiana subsidiaries, standard apportionment fulfills the statutory purpose of avoiding distortion of and realistically portraying Indiana source income. *See* IC 6-3-2-2(p).

Although IC 6-3-2-2(q) allows a parent corporation to petition the Department to file a combined return, it also incorporates by reference the restrictions imposed on alternative methods of reporting adjusted gross income by subsection (l) of that same section. Subsection (l) states in pertinent part:

> If the allocation and apportionment provisions of this article do not fairly represent the taxpayer's income derived from sources within the state of Indiana, the taxpayer may petition for or the department may require, in respect to all or any part of the taxpayer's business activity, if reasonable:
>
> ...
>
> (4) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

It is clear from the language in subsection (l) that the standard apportionment and the separate accounting filing methods are the preferred methods of representing a taxpayer's income derived from Indiana sources. Other methods of income allocation and apportionment (including the combined reporting method) should only be allowed when those provided for by IC 6-3-2-2 do not fairly reflect a taxpayer's Indiana income. As stated in a more concise manner, if the Indiana source income in the instant case can be fairly represented on the basis of standard apportionment or separate accounting, then such filing methods should be used.

The foundation of much of taxpayer's argument rests upon its assertions that it is impossible and inequitable to attribute Indiana income to it on a separate accounting basis since, due to the unitary nature of the relationship between Parent, taxpayer and the Michigan subsidiary, the production processes of taxpayer and the Michigan subsidiary were so interdependent that taxpayer's Indiana income could not be separately determined. However, despite the finding of a unitary relationship between Parent, taxpayer and the Michigan subsidiary, and despite the relationship between taxpayer's and the Michigan subsidiary's business operations, it does not appear that the operations of the businesses were so integrated to the point where the filing of separate returns would lead to a distortion of income.

Taxpayer would have us believe that it was nothing more than a corporate shell for identical business operations conducted directly by the Michigan subsidiary; and, that no value could be assigned to the products produced at the Indiana facility. However, the Department determined that Parent operated a unitary business where each operation contributed to the business as a whole, and that the income-producing activities and sources within Indiana could be differentiated from the income-producing activities and sources outside of Indiana. Taxpayer had its own employees that performed the work assigned to the facility. Taxpayer received orders and completed the production cycle of raw material to finished product within its facility. The production of product at taxpayer's facility was "self-contained" and not linked with the production that occurred at the Michigan facility.

Notwithstanding the foregoing, we do not believe that the Audit Division's subsequent revocation of the Department's determination that taxpayer could file combined tax returns was due to a material error or misrepresentation. The original approval letter specifically stated that combined filing status would be revoked if a material error or misrepresentation was discovered. However, through its examination of the books, records, and property of taxpayer, and its determination that separate filing best represented the taxpayer's Indiana income, Audit did not appear to discover any material error or misrepresentation on the part of taxpayer.

Upon review of the instant case, the Department concludes that the original approval letter granting taxpayer permission to file combined tax returns is in error, but was not the result of a material error or misrepresentation on the part of taxpayer in the application process. Therefore, the appropriate remedy is for taxpayer's combined filings for the years in question to be allowed.

FINDING

Taxpayer's protest is sustained. Taxpayer's combined returns for tax years in question will be allowed. However, taxpayer's permission to file combined tax returns is revoked for tax years beginning after the date of the audit report.

DEPARTMENT OF STATE REVENUE

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LETTER OF FINDINGS NUMBER: 98-0568
Indiana Corporate Income Tax
For the 1994, 1995, and 1996 Tax Years

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.

ISSUES

I. Foreign Currency Rate Exchange Gain

Authority: I.R.C. § 988; 45 IAC 3.1-1-8; IC 6-3-1-3.5(b)

Taxpayer argues that, for purposes of calculating its adjusted gross income tax liability, it should not be required to include foreign currency exchange rate gain realized by the taxpayer, within the numerator of the sales factor.

II. Applicability of the Throw-Back Rule

Authority: 45 IAC 3.1-1-53; 45 IAC 3.1-1-64; IC 6-3-1-25; IC 6-3-1-25; IC 6-3-2-2(n)(2); Indiana Dept. of State Revenue v. Continental Steel Corp., 399 N.E.2d 754 (Ind. Ct. App. 1980); Wisconsin Dept. of Revenue v. William Wrigley, Jr., Co., 112 S.Ct. 2447 (1992); PL 86-272 (15 U.S.C.S. § 381)

Taxpayer argues that, for purposes of calculating its adjusted gross income tax liability, it should not be required to throw-back sales made into Kentucky, Canada, and Japan.

III. Exclusion of Taxpayer's Out-Of-State Tooling from the Property Factor Based on a De Minimis Exception

Authority: 45 IAC 3.1-1-40; 45 IAC 3.1-1-41

Taxpayer argues that it was error to exclude from the property factor certain out-of-state tooling based upon a purported de minimis exception.

STATEMENT OF FACTS

Taxpayer is a manufacturer of automobile parts, is engaging in a joint venture with a Japanese partner, and is incorporated and headquartered in Indiana. Taxpayer manufactures exhaust systems, instrument panels, door impact beams, and stampings for engine and body parts. Taxpayer sells these parts to automobile manufacturers located in Kentucky, California, Canada, and Japan.

DISCUSSION

I. Foreign Currency Rate Exchange Gain

Taxpayer makes purchases from foreign vendor. At the time the purchases are made, taxpayer books the accrued liabilities in American dollars. When taxpayer makes the payments, the payments are made in foreign currency. As a result of the delay between accrual of the liabilities and the time payment is made, fluctuations in the foreign currency rate exchange may result in gains or losses. For example, taxpayer purchases $1,000 in goods from foreign vendor and books the $1,000 liability accordingly. By the time taxpayer makes payment in the appropriate foreign currency – and as the result of an intervening exchange rate fluctuation – taxpayer may find that it only needs to make a payment in $900 worth of American currency. Taxpayer protests the decision by audit to include these "gains," realized from the foreign currency rate fluctuations, within the numerator of the sales factor.

Under I.R.C. § 988, a gain or loss attributable to foreign currency exchange fluctuations involving either the sale or purchase of goods, is treated as "ordinary income or loss." I.R.C. § 988(a)(1)(A). When a U.S. taxpayer buys or sells to a foreign company, and the U.S. taxpayer agrees either to pay for the goods – or receive payment for the goods – in foreign currency units, this constitutes a foreign currency transaction from the point of view of the U.S. taxpayer. In these situations, the U.S. taxpayer has "crossed currencies" and has assumed the risk of fluctuating foreign exchange rates of the foreign currency units. This exposed currency risk may lead to recognition of foreign exchange gains or losses in the income of the U.S. taxpayer.

Taxpayer's transactional "gains" are considered "ordinary income or loss" under I.R.C. § 988. Pursuant to 45 IAC 3.1-1-8, Indiana uses the taxpayer's federal adjusted gross income as the starting point for calculating taxpayer's Indiana adjusted gross income. In the absence of any specific authority to deduct taxpayer's foreign currency gains from that federal starting point, audit correctly determined that taxpayer's foreign currency gains are part of Indiana's adjusted gross income tax calculus.

Taxpayer cites to the Department's past practices of treating foreign exchange gains in determining Indiana's gross income tax. However, in determining the taxpayer's *adjusted gross income tax*, the taxpayer's foreign exchange gains are properly included in the numerator of the sales factor. Those foreign exchange gains, included in taxpayer's federal adjusted gross income, are derived from taxpayer's regular business activities and are properly subject to the apportionment provisions of IC 6-3-1-3.5(b) and, consequently, properly included within the numerator of the sales factor.

FINDING

Taxpayer's protest is respectfully denied.

II. Applicability of the Throw-Back Rule

The audit determined that taxpayer's activities in Canada, Japan and Kentucky, did not go beyond the protection afforded under PL 86-272 (15 U.S.C.S. § 381). According to the audit, taxpayer's sales to Kentucky should be subject to the throw-back rule because taxpayer did not file tax returns in Kentucky from 1993 through 1995 and because the taxpayer did not have income producing property in Kentucky. The audit determined that taxpayer's sales to Canada should be subject to the throw-back rule because taxpayer does not maintain facilities within Canada and because taxpayer's contact with Canada was limited to sending personnel to address problems arising from one of the taxpayer's products. Similarly, the audit determined that taxpayer's sales to Japan should be subject to the throw-back rule because taxpayer's contact with Japan was limited to personnel visits to their joint-venture partner's headquarters in Japan.

15 U.S.C.S. § 381 (Public Law 86-272) prohibits states from imposing a net income tax on a foreign taxpayer if the foreign taxpayer's only business activity within that state is the solicitation of sales. A state may not impose an income tax on income derived from business activities within that state unless those activities exceed the mere solicitation of sales. 15 U.S.C.S. § 381(a), (c). The effect of the throw-back rule is to revert sales receipts back to the state from where the goods were shipped in those situations where 15 U.S.C.S. § 381 deprives the purchaser's own state of the power to impose a net income tax. 45 IAC 3.1-1-64. In effect, 15 U.S.C.S. § 381 permits Indiana to tax out-of-state business, without violating the Commerce Clause and without the possibility of subjecting taxpayer to double taxation, because Indiana's right to tax those out-of-state activities is derivative of the foreign state's own taxing authority. In every sales transaction, at least one state has the authority to tax income derived from the sale of the tangible personal property; if the state wherein the sale occurred is forbidden to do so by 15 U.S.C.S. § 381, then the income is "thrown-back" to the originating state.

For the purposes of determining whether a taxpayer is subject to the taxing jurisdiction of another state pursuant to 45 IAC 3.1-1-64, "[t]he term 'state' means any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States, and any foreign country or political subdivision thereof." IC 6-3-1-25. Accordingly, the jurisdictions at issue – Japan, Kentucky, and Canada – fall within the definition of a "state" and are properly considered as potentially subject to the throw-back rule. *See also* IC 6-3-1-25.

Taxpayer disputes audit's determination that its sales to Kentucky, Canada, and Japan should be thrown-back to Indiana. Taxpayer argues that its activities within those foreign jurisdictions exceed the "mere solicitation" 15 U.S.C.S. § 381 standard. Consequently, it is those foreign jurisdictions which have the right to impose the tax – not Indiana.

The Department must determine whether taxpayer's activities within the three foreign jurisdictions exceed the 15 U.S.C.S. § 381 benchmark of "mere solicitation." Indiana Dept. of State Revenue v. Continental Steel Corp., 399 N.E.2d 754 (Ind. Ct. App. 1980), defines those activities which do and do not exceed the "mere solicitation" standard. In that case, the court held that, "solicitation should be limited to those generally accepted or customary acts in the industry which lead to the placing of orders not those which follow as a natural result of the transaction, such as collections, servicing complaints, technical assistance and training...." Id. at 759. Further, "solicitation must be limited to those acts which lead to the placing of orders and does not include those acts which follow as a result of the transaction." Id. The court set out examples of activity which exceeded "mere solicitation" including "giving spot credit, accepting orders, collecting delinquent accounts and picking up returned goods within the taxing state, pooling and exchanging technical personnel in a complex mutual endeavor, maintaining personal property [] and associated local business activity for purposes not related to soliciting orders within the taxing state." Id.

In Continental, the court held that the taxpayer's activities within the foreign state exceeded solicitation because taxpayer's activities "[did] not lead to the placing of orders but follow[ed] as a natural result of transaction." Id. Those activities included the taxpayer's "salesmen making adjustment on complaints, [and] salesmen giving customers technical assistance...." Id.

The "mere solicitation" standard was refined by the Supreme Court in Wisconsin Dept. of Revenue v. William Wrigley, Jr., Co., 112 S.Ct. 2447 (1992). The Court concluded that "although solicitation covered more than what was strictly essential to making requests for purchases, the fact that an activity is performed by salespersons does not automatically convert that activity into solicitation." Id. at 2456-57. The Court held that whether the taxpayer's in-state activity was sufficiently de minimis to avoid the loss of taxpayer immunity, conferred by 15 U.S.C.S. § 381, depended on whether the activity establishes a "non-trivial additional connection with the taxing State." Id. at 2458. In Wrigley, the Court determined that the taxpayer's sales representatives' activities, consisting of replacing stale gum at retail locations, was an activity outside 15 U.S.C.S. § 381 immunity. Id. at 2458-59. The Court held that although the representatives' activity could be said to facilitate the sales, it did not facilitate the *requesting* of sales and was not ancillary to the solicitation of sales. Id. at 2459 (Emphasis added). Therefore, because taxpayer's practice of having its representatives rotate stocks of stale gum was an activity outside the solicitation of sales, taxpayer brought itself outside the scope of 15 U.S.C.S. § 381 immunity and subjected itself to the local net income tax. Id. at 2460.

Because the taxpayer has submitted separate information relevant to each of the three foreign jurisdictions at issue (Kentucky, Japan, Canada), those three jurisdictions will be addressed separately.

A. Kentucky

According to the taxpayer, its representatives spend very little of their time marketing products to its Kentucky customer. Taxpayer Letter, Feb. 22, 2001, p. 1. Rather the taxpayer characterizes the relationship between an automobile parts supplier and an automobile manufacturer, in today's "supplier environment," as more complex than the typical relationship between a vendor

and an industrial consumer. Taxpayer argues that it maintains an ongoing, day-to-day relationship with its Kentucky customer based upon a collaborative attempt to resolve production, quality, engineering, and sales issues. Taxpayer has submitted quantitative and narrative information in an attempt to describe its relationship to its Kentucky customer.

Four to five times each year, taxpayer's representatives meet with the Kentucky customer for "Data Exchange" sessions. These on-site sessions are conducted for the purpose of acquiring information on taxpayer's performance as a parts supplier. Id. at p. 2. The number of these Data Exchange sessions increases during the introduction of new customer products.

Four times each year, taxpayer's marketing managers, quality control representatives, and purchasing representatives meet with Kentucky customer to perform "Quarterly Reviews" of taxpayer's performance during the preceding quarter. Id. During these on-site Quarterly Reviews, taxpayer's and customer's representatives discuss the customer's quality, cost, and delivery standards.

Once each year, taxpayer's service teams and management meet with Kentucky customer to conduct an "Annual Review" for the purpose of discussing customer's expectations as well as taxpayer's achievements in the areas of cost, quality, and delivery. Id. Between 10 and 20 of taxpayer's employee's attend these meeting. The participants include taxpayer's president, vice-presidents, plant manager, plant coordinator, marketing manager, marketing coordinator, quality control manager, quality control coordinator, production control manager, and production control coordinator.

In addition, taxpayer's production and engineering personnel perform annual, on-site "Production/Engineering Reviews" to discuss production standards, discuss potential quality control problems, and determine means for minimizing those problems. Id.

Taxpayer's quality control personnel visit the Kentucky customer to conduct "Bi-Weekly Quality Control Visits." These visits are conducted for the purpose of identifying potential production problems. Taxpayer's and customer's representatives review new part design and alternative part designs. The representatives review customer's production problems, discuss delivery of non-conforming parts, evaluate sample parts, investigate warranted return parts, and perform on-site repairs of non-conforming parts.

Taxpayer maintains an on-site quality control team for one week during the time in which its Kentucky customer introduces a new product. Id. at p. 3.

In addition to the above narrative information, taxpayer has submitted quantitative information regarding the number of hours taxpayer's representatives spend at the Kentucky customer site. During the audit period, taxpayer's marketing personnel spent between 250 to 300 hours each year at the Kentucky customer site. During the audit period, taxpayer's quality control personnel spent 400 to 800 hours each year at the Kentucky customer site. During the audit period, taxpayer's production control personnel spent between 100 to 200 hours each year at the Kentucky customer site. Id.

Taxpayer has submitted information sufficient to establish that its Kentucky activities exceed the "mere solicitation" standard of 15 U.S.C.S. § 381, that the taxpayer is subject to Kentucky's net income tax, and that the income derived from taxpayer's Kentucky activities should not be thrown back to Indiana. Taken together, taxpayer's activities within Kentucky constitute a "non-trivial additional connection" with Kentucky over and above the solicitation of its automobile parts business. Wrigley, 112 S.Ct. at 2458. The issue of whether taxpayer does or does not file a Kentucky income tax return, does or does not pay Kentucky income taxes, is irrelevant and is of no concern to the state of Indiana. Continental, 399 N.E.2d at 758; IC 6-3-2-2(n)(2).

B. Canada

Taxpayer maintains that its relationship with its Canadian customer is similar to the relationship it has with its Kentucky customer. Taxpayer Letter, Feb. 22, 2001, p. 4. Although similar, taxpayer admits that its contacts with its Canadian customer are more limited than those it maintains with its Kentucky customer. Orders for parts destined for Canadian customer do not originate from the Canadian site. Taxpayer does not maintain its own tangible personal property at the Canadian site. Taxpayer does not send its own representatives to Canadian customer for regular quarterly meetings. In contrast to the regularly scheduled contacts taxpayer maintains with its Kentucky customer, taxpayer schedules its visits to Canadian customer – in which it provides services similar to those provided Kentucky customer – as Canadian customer requests.

In an attempt to quantify its contacts with Canadian customer, taxpayer estimates that its personnel, during the relevant 1994 to 1996 tax years, spent 1,700 hours at the Canadian site. During that time, taxpayer was called on to address specific product issues, assist with the receipt of parts, and sort replacement parts. Id.

From the information provided by the taxpayer, taxpayer's representatives performed activities in Canada that exceed the "solicitation of orders." Wrigley, 112 S.Ct. at 2455. Further, taxpayer's Canadian activities exceed the de minimis exception because the activities establish a "nontrivial additional connect with the taxing [jurisdiction]." Id. at 2458. The taxpayer's specific on-site activities – addressing quality issues, assisting in the receipt of taxpayer's parts, sorting replacement parts – served an "independent business function apart from their connection to the soliciting of orders." Id. at 2456.

Taxpayer has provided sufficient information to establish that its Canadian activities exceed the 15 U.S.C.S. § 381 "mere solicitation" standard, that the taxpayer has subjected itself to the jurisdiction's net income tax, and that the income derived from taxpayer's Canadian activities should not be thrown back to Indiana.

The existence of the Convention Between the United States of America and Canada With Respect to Taxes on Income and on Capital, Sept. 26, 1980, U.S.-Can., T.I.A.S. No. 11087, is an irrelevancy in determining the applicability of the throw-back rule to taxpayer's Canadian business activities. 45 IAC 3.1-1-64 states in relevant part:

In the case of any "State," as defined in IC 6-3-1-25, other than a state of the United States or political subdivision of such state, the determination of whether [a] "state" [as defined in IC 6-3-1-25] has jurisdiction to subject the taxpayer to a net income tax shall be made by application of the jurisdictional standards applicable to that state of the United States. If jurisdiction to tax is otherwise present, such "state' is not considered as being without jurisdiction to tax by reason of the provisions of a treaty between that state and the United States.

C. Japan

Taxpayer raises the identical issue with regards to income derived from its activities in Japan. Taxpayer maintains that sales made to its Japanese customer should not be thrown back to Indiana because taxpayer was not the "exporter of record." Taxpayer Letter, Sept. 16, 1998, p. 5. Goods destined for taxpayer's Japanese customer were not shipped by taxpayer but were picked up in the United States and exported to Japan by an independent entity. Id. at 3. Taxpayer maintains that its sales to Japan were classified as "Japanese sales" merely for its own accounting and tax administrative ease. Id. at 5.

Taxpayer makes a distinction without a difference. Taxpayer manufactured auto parts and sold those goods to its Japanese customer. The fact that an independent third-party shipped the goods is an irrelevancy. The regulation is quite clear. 45 IAC 3.1-1-53 provides that gross receipts from the sale of tangible personal property are deemed to be in Indiana "if the property is shipped from an office, store, factory, or other place of storage in this state, and the taxpayer is not taxable in the state of the purchaser."

Since taxpayer has not demonstrated that its Japanese activities exceeded the 15 U.S.C.S. § 381 benchmark, that taxpayer was not subject to the jurisdiction's net income tax, or that its Japanese activities were not merely ancillary to the solicitation of sales, the income derived from taxpayer's Japanese activities is subject to the throw-back rule under 45 IAC 3.1-1-53.

FINDING

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

III. Exclusion of Taxpayer's Out-Of-State Tooling from the Property Factor Based on a De Minimis Exception

Taxpayer maintains certain tangible personal property at its Kentucky customer's manufacturing facility. Taxpayer Letter, Feb. 22, 2001, p. 3. This equipment consists of gauges. The gauges are incorporated into tooling, used by a third-party vendor (sub-contractor), to manufacture integral component parts of the products taxpayer sells to Kentucky customer. The tooling is assigned to third-party vendor to assure that the parts produced by third-party vendor meet taxpayer's quality standards. Taxpayer maintains that this "tooling [gauges] is used to produce a component part of [taxpayer's] business inventory...." Taxpayer Letter, Sept. 16, 1998, p. 6. Taxpayer argues that the tangible personal property should be included in the property factor.

The audit disagreed and reduced "property everywhere" to reflect the value of the tangible personal property. The audit stated that "[t]he vendor tooling is de minimis in value and is not producing income."

45 IAC 3.1-1-41 states that "The property factor includes all property owned or rented by the taxpayer which is actually used or is available for or capable of being used to produce business income." Taxpayer states that the tooling is incorporated into equipment used to produce component automobile parts. Accordingly, the tooling falls within the 45 IAC definition of property used to produce business income. Therefore, the tooling should be included within taxpayer's property factor pursuant to 45 IAC 3.1-1-40 because the tooling is being used to produce business income. The fact that the value of the tooling, approximately $ 67,000, is de minimis in comparison to the value of taxpayer's total property in all states, is irrelevant in reaching that determination.

FINDING

Taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

04990046.LOF

LETTER OF FINDINGS NUMBER: 99-0046 ST
Sales and Use Tax
For Tax Periods: 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 specific issues.

ISSUES

1. Sales and Use Tax – Retail Sale

Authority: IC 6-2.5-2-1 (a), IC 6-2.5-3-2 (d), IC 6-2.5-1-2, IC 6-2.5-4-1, 45 IAC 2.2-5-54 (a), First National Leasing and Financial Corporation v. Indiana Department of State Revenue, 598 N.E.2nd 640, (Ind. Tax 1992)

Taxpayer protests the assessment of gross retail tax on the sale of catalogs.

2. Tax Administration – Penalty

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

Taxpayer protests the imposition of the penalty.

STATEMENT OF FACTS

The taxpayer is an Indiana partnership that produces catalogs for a direct mail order business. After an audit for the years 1995-1997, additional gross retail tax was assessed against the taxpayer. The taxpayer protested this assessment and a hearing was subsequently held. Further information will be provided as necessary.

1. Sales and Use Tax – Retail Sale

DISCUSSION

The taxpayer negotiates with various entities to secure design services, paper, printing, and mailing of the catalogs as directed by its customer, a mail order business. That business provides its customer lists to the taxpayer. The bulk of the catalogs are mailed directly to the direct mail order business' customers. Other catalogs are delivered to the Indiana location of the direct mail order business where they are inserted into packages of goods being sent to customers or sent to potential customers as advertising. Catalogs are also sent to the Indiana location where they are used as samples for management and by employees in various capacities including the order entry area. Catalogs are also sent to offices of companies around the country that are related to the direct mail order business.

The auditor assessed Indiana sales tax on catalogs delivered into Indiana that were used in the offices and ordering areas of the direct mail order business, that were mailed as advertising from the mail order business Indiana location to Indiana residents and that were inserted into the orders delivered from the mail order business Indiana location. The taxpayer protests these assessments.

Indiana imposes a sales tax on retail transactions made within the state. IC 6-2.5-2-1(a). IC 6-2.5.3-2(d). A "retail transaction" is defined at IC 6-2.5-1-2 as including a transaction of a retail merchant that constitutes "selling at retail" as described in IC 6-2.5-4-1. IC 6-2.5-4-1(b),(c) states:

(b) A person is engaged in selling at retail when, in the ordinary course of his regularly conducted trade or business, he:

(1) Acquires tangible personal property for the purpose of resale; and

(2) Transfers that property to another person for consideration.

(c) For purposes of determining what constitutes selling at retail, it does not matter whether:

(1) The property is transferred in the same form as when it was acquired;

(2) The property is transferred alone or in conjunction with other property or services; or

(3) The property is transferred traditionally or otherwise.

The taxpayer contends that its activities do not constitute a retail sale as defined by statute. Rather, the taxpayer contends that its activities are services that are not subject to the gross retail tax. The taxpayer produced a contract between itself and the mail order business dated August 30, 1993 that supports the taxpayer's contention that the taxpayer provided non-taxable services to the mail order business. The contract states at Section 8 as follows:

> Service. Except as expressly provided in this Agreement, neither [mail order business] nor [taxpayer] authorizes the transfer, use, consumption, control or right of use of the title or possession, whether actual or constructive, of tangible personal property in any manner or form pursuant to this Agreement. Tangible personal property owned or controlled by [mail order business] or [taxpayer] shall, at all times, remain in the sole control and possession of, respectively, [mail border business] or [taxpayer]. This Agreement provides for the provision of services only, except as expressly provided herein.

While the taxpayer may characterize activities as services, that does not change the fact that the taxpayer actually produces catalogs which it sells to the mail order business. It is established Indiana law that tax consequences are determined by the substance rather than the form of a transaction. First National Leasing and Financial Corporation v. Indiana Department of State Revenue, 598 N.E.2nd 640, (Ind. Tax 1992).

The catalogs are of value to the direct order mail business since they offer the products for sale. The direct mail order business provided the mailing lists for the catalogs. The direct mail order business determined how many catalogs would be delivered to and mailed from out of state drop mail points and how many would be delivered to the Indiana facility. This value of the catalogs to the direct order mail business and control over the product are further indications that the direct mail order business purchased the catalogs in a retail transaction. The substance of this transaction is that a transfer of control actually takes place and the catalogs are in the possession of the direct mail order business after the transfer. Therefore this transaction meets the definition of a retail transaction since tangible personal property is transferred for a consideration.

The remaining issue to be determined is whether or not the transaction is an Indiana transaction subject to the Indiana gross retail tax. Both the seller and buyer of the tangible personal property are Indiana business entities. Those sales that have nexus with Indiana are subject to the Indiana tax. 45 IAC 2.2-5-54 (a). The auditor only assessed sales tax on the sales with clear connections to Indiana. Many of the catalogs are sent from the printers directly to the taxpayer's customers in Indiana. Many of the catalogs are actually located in Indiana at the direct mail corporate headquarters. These catalogs are used in offices by executives and order takers in the phone ordering division. Other catalogs on which the auditor assessed sales tax are those catalogs that are accepted at the

direct mail order business at the Indiana location and mailed as advertising to potential Indiana customers. The remainder of the catalogs upon which the auditor assessed sales tax are those catalogs that are accepted at the Indiana location of the direct mail order business and included in packaged orders delivered to customers. Each of the assessed transactions clearly has adequate nexus with Indiana for the Indiana sales tax to apply. None of the assessed transactions qualify for any exemptions from the sales tax.

FINDING

Taxpayer's protest is denied.

2. Tax Administration – Penalty

DISCUSSION

Taxpayer's final point of protest concerns the imposition of the ten per cent negligence penalty pursuant to IC 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2 (b) clarifies the standard for the imposition of the negligence penalty as follows:

> 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 reach 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.

In this instance, Taxpayer failed to follow the instructions of the department in the way it reported its sales tax liability. This breach of its duty to properly report and remit sales taxes constitutes negligence.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420000001.LOF

LETTER OF FINDINGS NUMBER: 00-0001
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.

ISSUES

1. Sales and Use Tax – Riverboat Casino

Authority: IC 6-2.5-3-2(a)

The taxpayer protests the imposition of tax on its riverboat casino.

2. Sales and Use Tax – Computer Software

Authority: IC 6-2.5-3-2(a), Sales and Use Tax Information Bulletin #8, dated January 15, 1982; Revised May 23, 1983

The taxpayer protests the imposition of tax on computer software and licensing agreements.

3. Sale and Use Tax – Lump Sum or Time and Materials Contracts

The taxpayer protests the imposition of tax on materials used in improvements to the taxpayer's gaming vessel.

STATEMENT OF FACTS

The taxpayer operates a casino riverboat. The taxpayer opened its gaming boat in approximately June 1996 with a leased vessel and later purchased a new gaming vessel in 1997. The Indiana Department of Revenue audited the taxpayer and assessed additional sales and use tax. The taxpayer timely protested the assessment and a hearing was held.

1. Sales and Use Tax – Riverboat Casino

Pursuant to IC 6-2.5-3-2(a), Indiana imposes an excise tax on tangible personal property stored, used, or consumed in Indiana. In 1997 the taxpayer purchased a new riverboat casino which it operated in Indiana waters. In its audit, the Indiana Department of Revenue imposed use tax on the taxpayer's gaming vessel.

The taxpayer protests the assessment claiming that the riverboat casino is actually real estate and therefore not subject to the use tax which is only imposed on tangible personal property. The taxpayer bases its contention on the definition of real property found in the law governing the Indiana property tax, IC 6.1-1-15 as follows:

> "Real Property" means:
> (1) land located within this state;
> (2) a building or fixture situated on land located within this state;
> (3) an appurtenance to land located within this state;

(4) an estate in land located within this state, or an estate, right, or privilege in mines located on or minerals, including but not limited to oil or gas, located in the land, if the estate, right, or privilege is distinct from the ownership of the surface of the land; and

(5) notwithstanding IC 6–6-6-7, a riverboat licensed under the provisions of IC 4-33 for which the state board of tax commissioners shall prescribe standards to be used by township assessors.

The first four items in the property tax definition of real property are the commonly understood definitions of real property. The last item concerning the classification of riverboats such as the taxpayer's riverboat was added in 1995 to specifically denominate riverboat casinos as real property for purposes of the tax on real property. The fact that the legislature considered it necessary to specifically classify riverboats as real property for purposes of property tax when all other property in the state is classified pursuant to the first four items indicates that the classification is counterintuitive to the generally held understanding of a riverboat as tangible personal property. Although the Department may look to the classification of property for property tax purposes to assist in determining whether difficult to classify property is tangible personal property for sales tax purposes, it is not required to do so.

The issue to be determined is whether the taxpayer's gaming vessel is tangible personal property for sales and use tax purposes. "Tangible" is defined as "discernable by the touch or capable of being touched" in Webster's II New Riverside University Dictionary, The Riverside Publishing Company, 1988 at page 1182. The same dictionary at page 877 defines "personal property" as "temporary or movable property as distinguished real property." A gaming vessel is movable property that can be touched. The boat actually has a pilot and life preservers for travel in the water. It operates under authority of the U.S. Department of Transportation. It is not permanently attached to the land. Generally, then, the taxpayer's riverboat casino would be considered tangible personal property.

The Sales and Use Tax Regulations do not give a definition of tangible personal property for sales and use tax purposes. They do, however, refer to boats and watercraft as subject to the sales and use tax. 45 IAC 2.2-3-6 (a)(2) defines "watercraft" as

> a contrivance used or designed for navigation on water, including a vessel, boat, motor vessel, steam vessel, sailboat, vessel operated by machinery either permanently or temporarily affixed, scow, tugboat or any marine equipment that is capable of carrying passengers, except a ferry.

The taxpayer's riverboat casino clearly falls within the sales and use tax regulatory definition of "watercraft." 45 IAC 2.2-3-6(c)(2) specifically imposes use tax on Indiana watercraft purchased out of state. By these standards, the taxpayer's riverboat casino is tangible personal property and subject to the sales and use tax. Since there is a specific definition and imposition of sales and use tax on boats in the Sales and Use Tax Regulations, the Indiana Department of Revenue does not need to look to the property tax statute for assistance in classification of the gaming vessel as tangible personal property subject to the sales and use tax.

Alternatively, the taxpayer contends that if the Department finds that its gaming vessel is tangible personal property and qualifies for imposition of the sales and use taxes, then that gaming vessel qualifies for the public transportation exemption found at IC 6-2.5-5-27 as follows:

> Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property.

To bolster its argument that the riverboat casino qualifies for the provision of public transportation exemption, the taxpayer offers evidence that the vessel's operation is regulated by the U.S. Department of Transportation and that those regulations are enforced by the U.S. Coast Guard.

The only purpose of the taxpayer's gaming vessel is the provision of an opportunity for people to gamble legally. Persons seeking transportation in the state of Indiana do not consider the taxpayer's services. The previously cited sales and use tax regulation specifically states that a ferry would not be subject to the imposition of tax. The taxpayer's boat can not be considered a ferry in that it doesn't transport anyone from one point to another point. At most the boat moves people in Indiana waters so that they can gamble legally. The taxpayer's riverboat casino does not qualify for the public transportation exemption from the sales and use tax.

Finally, the taxpayer argues that the classification of the riverboat casino as real property for property tax purposes and tangible personal property for sales and use tax purposes violates the United States Constitution, Amendment 14 and Article I, Section 12 of the Indiana Constitution. An administrative hearing is not the proper forum for the determination of constitutional issues.

FINDING

The taxpayer's first point of protest is denied.

2. Sales and Use Tax – Computer Software

The taxpayer protests the imposition of use tax on its purchases of software and software licensing agreements. Examples of the software and licensing agreements purchased and used include a diskette software for a speaker phone, HR system software and IBM 16/4 Auto Tr Sa virus scan. The use tax was imposed pursuant to IC 6-2.5-3-2(a) which provides that "an excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction..." The taxpayer contends that the software and software licensing agreements are not subject to use tax because they are intangible personal property and the tax is only imposed on tangible personal property.

Sales and Use Tax Information Bulletin No. 8 dated January 15, 1982; Revised May 23, 1983 clarifies the Indiana Department

of Revenue position on software and software licensing systems. On Page 2 the Information Bulletin states as follows:

Pre-written programs, not specifically designed for one purchaser, developed by the seller for sale or lease on the general market in the form of tangible personal property and sold or leased in the form of tangible personal property are subject to tax irrespective of the fact that the program may require some modification for a purchaser's particular computer.

The programs and licensing agreements at issue in this audit are the type of canned software clarified as taxable in Sales and Use Tax Information Bulletin 8. The modifications necessary for the taxpayer were not sufficient to remove any of the items to the classification of custom software which would not be subject to the sales and use tax.

FINDING

This point of the taxpayer's protest is denied.

3. Sale and Use Tax – Lump Sum or Time and Materials Contracts

DISCUSSION

The taxpayer's final point of protest concerns the imposition of use tax on materials used in improving the taxpayer's gaming vessels pursuant to IC 6-2.5-3-2(a). The taxpayer contends that the contractors rather than the taxpayer are responsible for the remittance of sales and use tax on any materials used as part of the construction contracts. The taxpayer bases this contention of 45 IAC 2.2-3-9(d)(1) and 45 IAC 2.2-3-9(e)(3) which deal with construction contracts for the improvement of real estate. As discussed in the first issue of the taxpayer's protest, the gaming vessels are tangible personal property rather than real estate for sales tax purposes. Therefore the cited Sales and Use Tax Regulations do not apply in this instance and the taxpayer is subject to use tax on materials used in improving its riverboat casinos.

FINDING

The taxpayer's final point of protest is denied.

DEPARTMENT OF STATE REVENUE

0420000010.LOF

LETTER OF FINDINGS NUMBER: 00-0010

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.

ISSUES

1. Sales and Use Tax – Riverboat Casino

Authority: IC 6-2.5-3-2(a), IC 6.1-1-15, 45 IAC 2.2-3-6(a), IC 6-2.5-5-27

The taxpayer protests the imposition of tax on its riverboat casino.

2. Sales and Use Tax – Credits

Authority: IC 6-2.5-3-2

The taxpayer protests assessments on certain items.

3. Sales and Use Tax – Gaming Equipment

Authority: IC 6-2.5-1(b)

The taxpayer protests the assessment of tax on gaming equipment.

4. Sales and Use Tax – Kitchen Equipment

Authority: IC 6-2.5-5-3, Sales Tax Information Bulletin #11, Revised May, 1994.

The taxpayer protests the assessment of tax on kitchen equipment.

5. Tax Administration – Negligence Penalty

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

The taxpayer protests the imposition of tax on materials used in improvements to the taxpayer's gaming vessel.

STATEMENT OF FACTS

The taxpayer operates a casino riverboat. After an audit, the taxpayer was assessed additional use tax, interest and penalty. The taxpayer protested the assessment and a hearing was held.

1. Sales and Use Tax – Riverboat Casino

Pursuant to IC 6-2.5-3-2(a), Indiana imposes an excise tax on tangible personal property stored, used, or consumed in Indiana. In 1996 the taxpayer purchased a new gaming vessel which was constructed in Florida and delivered to Indiana. The taxpayer self-assessed use tax on $25,779,715. However, the total cost of the gaming vessel was $33,879,715. The audit assessed use tax on the difference of $8,100.000. The taxpayer protested this assessment and claimed a refund of the use tax previously paid. Only the

protest of the assessment will be addressed in this Letter of Findings.

The taxpayer protests the assessment claiming that the riverboat casino is actually real estate and therefore not subject to the use tax which is only imposed on tangible personal property. The taxpayer bases its contention on the definition of real property found in the law governing the Indiana property tax, IC 6.1-1-15 as follows:

"Real Property" means:

(1) land located within this state;

(2) a building or fixture situated on land located within this state;

(3) an appurtenance to land located within this state;

(4) an estate in land located within this state, or an estate, right, or privilege in mines located on or minerals, including but not limited to oil or gas, located in the land, if the estate, right, or privilege is distinct from the ownership of the surface of the land; and

(5) notwithstanding IC 6–6-6-7, a riverboat licensed under the provisions of IC 4-33 for which the state board of tax commissioners shall prescribe standards to be used by township assessors.

The first four items in the property tax definition of real property are the commonly understood definitions of real property. The last item concerning the classification of riverboats such as the taxpayer's riverboat was added in 1995 to specifically denominate riverboat casinos as real property for purposes of the tax on real property. The fact that the legislature considered it necessary to specifically classify riverboats as real property for purposes of property tax when all other property in the state is classified pursuant to the first four items indicates that the classification is counterintuitive to the generally held understanding of a riverboat as tangible personal property. Although the Department may look to the classification of property for property tax purposes to assist in determining whether difficult to classify property is tangible personal property for sales tax purposes, it is not required to do so.

The issue to be determined is whether the taxpayer's gaming vessel is tangible personal property for sales and use tax purposes. "Tangible" is defined as "discernable by the touch or capable of being touched" in Webster's II New Riverside University Dictionary, The Riverside Publishing Company, 1988 at page 1182. The same dictionary at page 877 defines "personal property" as "temporary or movable property as distinguished real property." A gaming vessel is movable property that can be touched. The boat actually has a pilot and life preservers for travel in the water. It operates under authority of the U.S. Department of Transportation. It is not permanently attached to the land. Generally, then, the taxpayer's riverboat casino would be considered tangible personal property.

The Sales and Use Tax Regulations do not give a definition of tangible personal property for sales and use tax purposes. They do, however, refer to boats and watercraft as subject to the sales and use tax. 45 IAC 2.2-3-6(a)(2) defines "watercraft" as

a contrivance used or designed for navigation on water, including a vessel, boat, motor vessel, steam vessel, sailboat, vessel operated by machinery either permanently or temporarily affixed, scow, tugboat or any marine equipment that is capable of carrying passengers, except a ferry.

The taxpayer's riverboat casino clearly falls within the sales and use tax regulatory definition of "watercraft." 45 IAC 2.2-3-6(c)(2) specifically imposes use tax on Indiana watercraft purchased out of state. By these standards, the taxpayer's riverboat casino is tangible personal property and subject to the sales and use tax. Since there is a specific definition and imposition of sales and use tax on boats in the Sales and Use Tax Regulations, the Indiana Department of Revenue does not need to look to the property tax statute for assistance in classification of the gaming vessel as tangible personal property subject to the sales and use tax.

Alternatively, the taxpayer contends that if the Department finds that its gaming vessel is tangible personal property and qualifies for imposition of the sales and use taxes, then that gaming vessel qualifies for the public transportation exemption found at IC 6-2.5-5-27 as follows:

Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property.

To bolster its argument that the riverboat casino qualifies for the provision of public transportation exemption, the taxpayer offers evidence that the vessel's operation is regulated by the U.S. Department of Transportation and that those regulations are enforced by the U.S. Coast Guard.

The only purpose of the taxpayer's gaming vessel is the provision of an opportunity for people to gamble legally. Persons seeking transportation in the state of Indiana do not consider the taxpayer's services. The previously cited sales and use tax regulation specifically states that a ferry would not be subject to the imposition of tax. The taxpayer's boat can not be considered a ferry in that it doesn't transport anyone from one point to another point. At most the boat moves people in Indiana waters so that they can gamble legally. The taxpayer's riverboat casino does not qualify for the public transportation exemption from the sales and use tax.

FINDING

The taxpayer's first point of protest is denied.

2. Sales and Use Tax – Credits

DISCUSSION

The use tax is imposed on an Indiana use of tangible personal property purchased in a retail transaction. IC 6-2.5-3-2. The taxpayer and the Indiana Department of Revenue are in agreement that tax on the use of the purchased items is due to the state. The tax should only, however, be imposed once on each item of property purchased in a retail transaction.

The taxpayer executed a voluntary disclosure agreement under which the taxpayer agreed to remit outstanding use tax related to its 1996 pre-opening expenses made prior to June l, 1996. The taxpayer contends that the audit did not give it credit for the $139,747.00 remitted with the 1996 IT-20. While it is true that the auditor did not give credit for taxes paid on the IT-20 return, the auditor also did not include those total taxable purchases in the audit. The auditor only assessed tax on additional purchases on which the sales tax was not paid by the taxpayer.

The taxpayer also contends that three purchases were listed twice in the audit. The taxpayer requests that one listing of each of the three purchases should be offset against the audit assessment.

FINDING

The taxpayer's protest concerning the credit for taxes paid on the IT-20 return is denied.

The taxpayer's protest concerning the purchases that were listed twice in the audit is sustained subject to audit verification.

3. Sales and Use Tax – Gaming Equipment

DISCUSSION

The taxpayer agrees that gross retail tax is due to the state on these items of gaming equipment. The taxpayer contends, however, that it has already paid the tax to the vendor as agent of the state. The law provides for the payment of gross retail tax at IC 6-2.5-2-1(b) as follows:

> 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.

The taxpayer provided a copy of the contract indicating that the total price of the gaming equipment included sales tax and a copy of a letter indicating the payments made. The Indiana Department of Revenue records indicate that the vendor was registered as a retail merchant with the Indiana Department of Revenue during the tax period and that the vendor actually remitted sales tax during that period to the state.

FINDING

The taxpayer's protest is sustained.

4. Sales and Use Tax – Kitchen Equipment

DISCUSSION

The taxpayer purchased kitchen equipment for the bars and restaurants on its riverboat. The taxpayer self assessed use tax on some of the equipment. In the audit, the Indiana Department of Revenue assessed use tax on several other pieces of equipment. The taxpayer protests a portion of these assessments.

Pursuant to IC 6-2.5-5-3, tangible personal property which is purchased "for direct use in the direct production... of other tangible personal property" qualifies for exemption from the use tax. Sales Tax Information Bulletin #11, revised May, 1994, clarifies the application of the manufacturing exemption to kitchen equipment in a bar or restaurant as follows:

> The purchase of tangible personal property that will act directly on the food during preparation are exempt from the sales tax. (For example, a fryer or broiler would be exempt. However, a refrigerator is taxable because it serves merely as an agent in the preservation of food and does not act directly on the food during preparation. [)]

The taxpayer protests the assessment of tax on a microwave oven and a hot dog bun warmer. These two items merely keep food warm and do not act directly on the food during preparation. Therefore, they do not qualify for the exemption.

The taxpayer protests the assessment of tax on an iced tea brewer, a coffee brewer, two hot dog grills and a four-slice toaster. These items of kitchen equipment act directly on the food during preparation by cooking it. Therefore, these pieces of equipment qualify for the exemption.

Finally, the taxpayer protests the assessment of tax on two ice machines. These machines act directly on water to freeze it into ice cubes. These machines qualify for exemption.

FINDING

The taxpayer's protest is sustained in part and denied in part.

5. Tax Administration – Negligence Penalty

DISCUSSION

Taxpayer's final point of protest concerns the imposition of the ten per cent negligence penalty pursuant to IC 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2(b) clarifies the standard for the imposition of the negligence penalty as follows:

> "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.

The audit assessed use tax on purchases in addition to those under protest. For example, the taxpayer failed to pay retail sales tax or remit use tax on many items clearly subject to the use tax such as umbrellas, business cards, greeting cards, housekeeping supplies and Indiana flags. The taxpayer's actions meet the requisite negligence standard.

FINDING

The taxpayer's final point of protest is denied.

DEPARTMENT OF STATE REVENUE

0420000022.LOF

LETTER OF FINDINGS NUMBER: 00-0022
Use Tax
For Tax Years 1996 through 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. Use Tax – Assets and Supplies

Authority: IC 6-8.1-5-1; 45 IAC 2.2-3-20

Taxpayer protests the imposition of use tax on certain purchases.

STATEMENT OF FACTS

Taxpayer performs services for utility companies. As the result of an audit, the Department of Revenue determined that taxpayer had not paid sales or use tax on some purchases for which sales or use tax was properly due. The Department issued assessments for the unpaid tax. Taxpayer protests that it does not owe the tax. Further facts will be supplied as needed.

I. Use Tax – Assets and Supplies

DISCUSSION

Taxpayer protests the imposition of use tax on some purchases it made. Taxpayer's protest states, in its entirety:

Please be informed that we protest the above mentioned assessments. It is our belief that the retailer is responsible to collect the consumer use taxes. The fact that this was not the case leads us to believe that no tax was or is due.

In the Audit Summary, the Department referred to 45 IAC 2.2-3-20, which states:

All purchases of tangible personal property which are delivered to the purchaser for storage, use, or consumption in the state of Indiana are subject to the use tax. The use tax must be collected by the seller if he is a retail merchant described in Reg. 6-2.5-3-6(b)(010) *[45 IAC 2.2-3-19]* or if he has Departmental permission to collect the tax. If the seller is not required to collect the tax or fails to do so, the purchaser must remit the use tax directly to the Indiana Department of Revenue.

Therefore, taxpayer is incorrect in assuming that merely because no sales or use tax was collected that none is due. 45 IAC 2.2-3-20 clearly states that if a seller fails to collect the tax, the purchaser (in this case, taxpayer) must remit the tax directly to the Department.

Taxpayer merely claimed that the tax was not due. IC 6-8.1-5-1(b) states in relevant part:

The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made.

Taxpayer incorrectly asserted that since no tax was collected, none was due. No other explanation or evidence was provided. Therefore, taxpayer has not met its burden of proving that the proposed assessments are wrong.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420000026.LOF

LETTER OF FINDINGS NUMBER: 00-0026
Use Tax – Packaging Supplies
For Tax Years 1996 through 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

Use Tax— Packaging Supplies

Authority: IC 6-2.5-3-2; IC 6-2.5-3-4(a)(2); IC 6-2.5-5-9(d); 45 IAC 2.2-5-16(d)(1); Sales Tax Information Bulletin #44

Taxpayer protests the imposition of use tax on packaging supplies.

STATEMENT OF FACTS

Taxpayer is a Minnesota corporation that manufactures and sells cabinets for use in the kitchen, laundry, and bathroom. Taxpayer sells the manufactured cabinets wholesale to retailers. When taxpayer ships the cabinets to its customers, it hand loads the cabinets onto semi-trailers in rows stacked close to the ceiling and walls. Airbags are placed between the product and the trailer ceiling and walls and inflated. The airbags compression fit the row of cabinets to prevent the cabinets from moving during their transportation. Once the cabinets reach their destination, the airbags are sliced open. This renders the airbags useless after one time of use. After the airbags are deflated, they are discarded.

The Department of Revenue conducted an audit for the years in question, and issued use tax assessments on taxpayer's use of the airbags. Although taxpayer wrote a letter to the Department protesting the proposed assessments, taxpayer failed to respond to the Department's letter of March 5, 2001, which requested that taxpayer schedule an administrative hearing with the Department. Using the best information available, efforts were made to contact taxpayer and taxpayer failed to respond. The Department issues this Letter of Finding based on its best understanding of the facts as provided by the auditor and the taxpayer's protest letter.

Use Tax— Packaging Supplies

DISCUSSION

IC 6-2.5-3-2 imposes "[a]n excise tax, known as the use tax,... on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction...." An exemption to this use tax is provided by IC 6-2.5-3-4(a)(2) if: "the property was acquired in a transaction that is wholly or partially exempt from the state gross retail tax under any part of IC 6-2.5-5,... and the property is being used, stored, or consumed for the purpose for which it was exempted."

At issue here are nonreturnable packaging materials used to transport the cabinets manufactured by taxpayer. In its protest letter, taxpayer protests use tax assessed on its purchases of nonreturnable packaging supplies, *i.e.*, airbags, used to secure the product during shipping.

The taxpayer cites Sales Tax Information Bulletin #44 as providing exemption for the protested items. However, the bulletin pertains only to containers and wrapping materials used by the purchaser as follows: the purchaser must add contents to the containers purchased; and, the purchasers must sell the contents added.

In this case, the taxpayer purchases airbags and uses them to secure the cabinets as they are transported to customers. No product is added to the airbags. According to IC 6-2.5-5-9(d), 45 IAC 2.2-5-16(d)(1), and Information Bulletin #44 the exemption is for nonreturnable wrapping material and empty containers to be used by the purchaser as enclosures or containers for selling contents sold in a sale constituting selling at retail. Taxpayer's airbags are not considered by the Department to constitute wrapping materials nor are they empty containers to be used as enclosures or containers. The airbags merely facilitate shipping.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0220000189.LOF

LETTER OF FINDINGS NUMBER: 00-0189
Adjusted Gross Income Tax
For the 1996, 1997, and 1998 Tax Years

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.

ISSUES

I. Applicability of the Adjusted Gross Income Tax to That Portion of Lease Payments Designated as Property Tax

Authority: IC 6-3-1-3.5(b); Cooper Industries, Inc. v. Indiana Dept. of State Revenue, 673 N.E.2d 1209 (Ind. Tax. Ct. 1996); 45 IAC 3.1-1-8(3)(b)

Taxpayer protests the decision to include that portion of lease payments – specifically designated as property tax payments – within the taxpayer's income subject to the state's adjusted gross income tax. Taxpayer maintains that the property tax payments should not be included as part of its gross receipts, that the taxpayer was acting merely as a fiduciary in collecting the property tax, and that the property tax receipts should not be added back as a modification to Indiana adjusted gross income.

II. Denial of Tax Refund for Calendar Year Ending June 30, 1995

Authority: IC 6-8.1-5-2; 45 IAC 3.1-1-94

Taxpayer argues that it is entitled to a tax refund for the financial year ending June 30, 1995. Because it is being assessed additional tax for the previous two years, taxpayer believes that it should not have been denied the tax refund for the tax year ending June 30, 1995.

III. Abatement of the 10-percent Negligence Penalty

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

Taxpayer maintains that the Department should exercise its discretionary authority to abate the 10-percent negligence penalty for all years included within the audit period. Taxpayer asserts that it acted in good faith and used reasonable care in filing its state income tax returns.

STATEMENT OF FACTS

Taxpayer is incorporated in and maintains its headquarters in California. Taxpayer leases and sells various computers, software, computer related equipment, and other items of personal property to customers located throughout the United States. Taxpayer leases equipment to customers located in Indiana and derives Indiana source income from that equipment. Taxpayer retains ownership of the equipment it leases. Taxpayer's leases are non-cancelable "net" leases for terms ranging from two to five years. The leases contain provisions which require the lessee (customer) to maintain and service the equipment, insure the equipment, and to pay all taxes on the equipment.

DISCUSSION

I. Applicability of the Adjusted Gross Income Tax to That Portion of Lease Payments Designated as Property Tax

Taxpayer is of the opinion that it should not be subject to Indiana adjusted gross income on that portion of lease payments which are designated as property tax. Taxpayer is the owner of the leased property and is responsible for the property tax on the leased equipment. Taxpayer maintains that it is simply conducting a "pass-through" transaction whereby it collects property taxes on behalf of the lessees and remits the property taxes to the proper taxing jurisdiction. Taxpayer's standard lease contract includes a provision stating that, "All fees, assessments and taxes... which may now or hereafter become due or are imposed upon the ownership, sale, possession and /or use of the Property are to be paid by Lessee. While Lessee will be responsible for payment of all personal property taxes, [taxpayer] will file all personal property tax returns."

Taxpayer maintains that its typical lease arrangement is one in which the lessee is billed either quarterly or monthly. However, the lessee is billed once each year for the amount of property tax attributable to the equipment held by the lessee. According to the taxpayer, this arrangement provides evidence that the property tax is severable from the lease payments, and that the receipt of the property tax is not a taxable receipt of lease payments.

IC 6-3-1-3.5(b) provides the starting point for determining taxpayer's taxable income stating that the term "adjusted gross income" shall mean, "In the case of corporations the same as 'taxable income' (as defined in Section 63 of the Internal Revenue Code...." The Department's Administrative Rules restates the basic principle at 45 IAC 3.1-1-8 stating that "'Adjusted Gross Income' with respect to corporate taxpayers is 'taxable income' as defined in Internal Revenue Code – section 63)...." In Cooper Industries, Inc. v. Indiana Dept. of State Revenue, 673 N.E.2d 1209 (Ind. Tax. Ct. 1996), the court held that the code provision was "plain and unambiguous." Id. at 1213. "Indiana adjusted gross income begins with federal taxable income as defined by I.R.C. § 63, not as reported by the taxpayer." Id.

In calculating the taxpayer's adjusted gross income, Indiana begins with the federal definition as found in I.R.C. § 63. Having defined the Indiana taxpayer's federal adjusted gross income, the regulations provide for certain adjustments one of which is relevant here. 45 IAC 3.1-1-8(3)(b) provides for the add back of "[p]roperty taxes levied by a political subdivision of any state...." The effect of the regulation is to subject property taxes, even if otherwise not subject to the federal adjusted gross income tax, to the state's adjusted gross income tax.

Taxpayer's receipt of payments – designated and segregated as payments for property taxes – falls squarely within the statutory definition of "taxable income." Taxpayer's efforts to characterize the receipt of these payments as pass-through events having no taxable effect, is unavailing. The property tax expenses are merely one of those numerous costs of conducting a leasing business which the taxpayer ultimately expects its customers – either directly or indirectly – to bear.

FINDING

Taxpayer's protest is respectfully denied.

II. Denial of Tax Refund for Calendar Year Ending June 30, 1995

Taxpayer argues that it should not have been denied a tax refund purportedly due for taxes paid during the tax year ending June 30, 1995. During the audit, taxpayer provided copies of the revenue agents reports (RAR) for certain federal audit periods but was advised that the time allowed for any refund had expired as to all tax years addressed within the RAR and that, accordingly, the amended returns adjustments were "out of statute."

Department regulation 45 IAC 3.1-1-94 sets out the procedural steps whereby a taxpayer is permitted to seek a refund upon a change in the taxpayer's federal return or federal liability. The regulation states that, "All taxpayers, except resident individuals, are required to file a notice with the Department within 120 days after a modification of a Federal income tax return or a modification of a Federal income tax liability explaining the modification." 45 IAC 3.1-1-94; *See also* IC 6-3-4-6.

There is apparently no dispute that taxpayer failed to file an amended return within the requisite 120 days. However, taxpayer sets out a general equitable argument stating that, because the Department has assessed taxes for two years *prior* to the tax year ending June 30, 1995, it is entitled to claim the refund.

45 IAC 3.1-1-94 provides the Department with no discretion in this matter. In the absence of any statutory or regulatory authority to do so, the Department must decline the opportunity to waive the 120-day filing requirement.

FINDING

Taxpayer's protest is respectfully denied.

III. Abatement of the 10-percent Negligence Penalty

Taxpayer has requested that the 10-percent negligence penalty, imposed under the authority of IC 6-8.1-10-2.1(a), be abated for the all of the taxpayer's income tax liabilities assessed during the years encompassed within the audit report. Taxpayer maintains that any mistakes it made were made in good faith and in the exercise of reasonable care.

IC 6-8.1-10-2.1(d) states that if a person, subject to the negligence penalty, imposed under IC 6-8.1-10-2(a), can show that the failure to file a return, pay the full amount of tax shown on the person's return, timely remit tax held in trust, or pay the deficiency determined by the Department, was due to reasonable cause and not due to willful neglect, the Department shall waive the penalty. 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. Negligence results from a taxpayer's carelessness, thoughtlessness, disregard, or inattention to duties placed upon the taxpayer by the Indiana Code or Department regulations. Id.

In order to waive the negligence penalty, the taxpayer must demonstrate that its failure to pay the full amount of tax was due to reasonable cause. 45 IAC 15-11-2(c). Taxpayer may establish reasonable cause by "demonstrat[ing] that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed...." Id. In determining whether reasonable cause exists, the Department may consider the nature of the tax involved, previous judicial precedents, previous Department instructions, and previous audits. Id.

Taxpayer has provided no substantive, statutory, or factual basis upon which the Department can justifiably be expected to find a reasonable cause for taxpayer's failure to pay the assessed tax deficiencies. The taxpayer various assertions and explanations – even taken together – do not rise to the level of "reasonable cause" sufficient to permit the Department to waive the negligence penalty assessed against an otherwise substantial and sophisticated taxpayer.

FINDING

Taxpayer's protest is respectfully denied.

DEPARTMENT OF STATE REVENUE

0220000214.LOF
0220000215.LOF

LETTERS OF FINDINGS NUMBERS: 00-0214 and 00-0215
Adjusted Gross Income Tax
For Years 1996 and 1997

NOTICE: Under Indiana Code § 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 – Add Back of State Income Taxes

Authority: IC § 6-2.1-1-2(a)(1); IC § 6-3-1-3.5; IC § 6-2.1-2-1; IC § 6-3-2-2; IC § 6-2.1-2-2; 45 IAC 3.1-1-8

Taxpayers, through parent corporation, protest the addback of state income taxes.

II. Tax Administration – Penalty

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2.1

Taxpayers, through parent corporation, protest the imposition of the 10% negligence penalty.

STATEMENT OF FACTS

Taxpayers are Indiana corporations, part of a nation-wide chain of restaurants. Taxpayers' parent corporation (not an Indiana taxpayer), files consolidated federal tax returns for all the individual restaurants, paying all state and federal taxes. The parent charges the tax back to each restaurant who then reimburses the parent through the payment of management and other administrative fees the parent charges as administrative costs.

The Department audited taxpayers for tax years 1996 and 1997. The Department assessed adjusted gross income tax for taxpayers' failure to add back the proper amount of taxes deducted on the federal return, and imposed the 10% negligence penalty. Taxpayers, through the parent, timely protested and a hearing was scheduled.

After the notice of hearing was issued and before the hearing was held, the parent, at the Department's request, sent in several sets of documents showing how the management fees were broken down, and how the federal returns for the two non-compliant restaurants were filled out. Based on the documents taxpayer sent, and a series of telephone conversations between the Hearing Officer and the parent, the Department and the parent concluded all information necessary to resolve taxpayers' protests had been produced. Therefore, this Letter of Findings is based on information contained in the files, taxpayer's additional documentation, and a series of telephone conversations. Further information will be provided as necessary.

I. Adjusted Gross Income Tax: Add-Back of State Income Taxes

DISCUSSION

The taxpayers, through the parent corporation, protest the add-back of state income taxes to their Indiana state income tax liability, taxes that were allegedly deducted in error on the consolidated federal returns by the parent corporation. The State of Indiana requires that all state income taxes based on income be added back to arrive at the state modified adjusted gross income tax for taxable income. See, IC § 6-3-1-3.5(b)(3). Taxpayers did not include the taxes paid to Indiana as an add-back.

Taxpayers, one located in Indianapolis and one in Evansville, are part of a nation-wide chain of restaurants. Both are incorporated in Indiana, but neither files a consolidated Indiana tax return with the parent. The parent pays the income, property, withholding, sales, and food and beverage taxes for all the subsidiaries (including taxpayers). The parent, to obtain discounts from vendors, makes bulk purchases of food sold by the restaurants. The parent also makes many of the operating decisions for the subsidiaries, including accounting functions. The subs are then charged management fees that cover the parent's costs.

The taxpayers deducted, through the parent, state income taxes on the consolidated federal income tax return. The parent files a consolidated federal tax return for all the subsidiaries and deducts the state income taxes on the federal 1120 form. However, when the two taxpayers' Indiana state income tax returns were prepared, the state income taxes paid were not shown as a deduction, nor were they added back to the adjusted gross income tax as required by Indiana's tax statutes and regulations. The parent claimed the deduction. The parent corporation did not include the state income taxes as an add-back to the adjusted gross income tax on the taxpayers' Indiana tax returns as required by Indiana's tax statutes and regulations. All taxes are shown on the parent's return, but none at the state level for the two taxpayers at issue.

The tax liability at issue belongs to the taxpayers; it is their responsibility and was therefore actually deductible by them. As all the restaurants file a consolidated federal income tax return, the issue of where the tax was deducted has no tax effect for federal purposes. The tax was in fact deducted on the federal return of the consolidated group. Either the parent erred in showing the tax as being deductible by the parent, or the parent was in fact reimbursed by the individual restaurants for the tax paid on their behalf through management fees or other intercompany transfers/eliminations. Regardless, the Department is correct in requiring taxpayers to add back the state income taxes deducted.

The taxpayers, through the parent's Letter of Protest, questioned the add-back of the management fees they paid to the parent, arguing that an error had been made in filling out the consolidated federal tax returns:

> The State of Indiana asserts that the taxpayers did not add back to taxable income, the State income taxes paid to the State of Indiana. The State correctly recognizes that the taxes were not "shown as a deduction" in the tax return but incorrectly suggests that the State income tax deductions are included in the management fees and that part of the deducted management fees paid to the to the [sic] Parent Corporation are "in lieu of the actual state income taxes."
>
> * * *
>
> In order to maintain some control over the State Income Tax payment process, the Parent Corporation also pays all of the State Income Taxes for the benefit of the taxpayers. On an estimated basis the taxpayers are charged for their share of the Federal Income Tax liability and for the estimated state income taxes.
>
> * * *
>
> Attached as Schedule 1 to this protest is a copy of page 4 of the taxpayer's Federal Income Tax Returns. As you will note in Schedule M-1 on line 2 there is an amount that is added back to the book income and accordingly not deducted at arriving at taxable income. While the notation in the return indicates that these amounts are "Federal income tax," in fact this notation

is incorrect. The numbers represent the taxpayer's estimated share of both Federal and State of Indiana income taxes and the total charge that they incurred for income taxes.

Pursuant to IC § 6-3-1-3.5(b)(3), taxpayers should have added back the amount of Indiana income tax the parent deducted on the consolidated federal tax return and then collected through management fees charged to the taxpayers:

When used in IC 6-3, the term "adjusted gross income shall mean the following:

(b) In the case of corporations, the same as "taxable income" (as defined in Section 63 of the Internal Revenue Code) adjusted as follows:

(3) Add an amount equal to any deduction or deductions allowed or **allowable** pursuant to Section 63 of the Internal Revenue Code for taxes based on or measured by income and levied at the state level by any state of the United States. (emphasis added)

Further, 45 IAC 3.1-1-8 provides:

Definition of adjusted gross income for corporations.

"Adjusted Gross Income" with respect to corporate taxpayers is "taxable income as defined in Internal Revenue Code section 63 with three adjustments:

(3) Add back deductions taken pursuant to Internal Revenue Code section 63 for:

(a) Taxes based on or measured by income and levied at the state level. For purposes of this subsection, the Indiana Gross Income Tax is a state tax measured by income and must be added back. (emphasis added)

Taxpayers' adjusted gross income tax deficiencies fall precisely within the ambit of the cited statutory and regulatory language. Audit initially based the amount of tax to be added back on the amount of estimated tax payments made by corporate headquarters on behalf of its subsidiaries (i.e., the restaurants). The amount of tax to be added back, however, should have been based on the subsidiaries' proportionate share of the consolidated federal deduction of state income tax.

FINDING

The taxpayers' protests concerning the add-back of taxes are denied. A supplemental audit should be completed to make the necessary corrections.

II. Tax Administration – Penalty

Taxpayers protest the Department's imposition of the 10% negligence penalty. Indiana Administrative Code, Title 45, Article 15, Rule 11-2(b) provides in pertinent part:

"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.

In determining whether or not to assess the 10% penalty, the Department looks for indicia of negligence as well as indicia of due diligence. The taxpayers, through the parent, were negligent because the parent failed to read and follow instructions on the Indiana tax returns. It does not matter that the returns are "pro forma." If taxpayers, through the parent, are going to rely on "pro forma" returns in fulfilling their statutory duties under Indiana's tax code and regulations, then the Department is fully justified in relying on "pro forma" returns in assessing tax deficiencies.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420000233.LOF

LETTER OF FINDINGS NUMBER: 00-0233
Sales and Use 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.

1. Sales and Use Tax – Unloaders

Authority: IC 6-2.5-3-2(a), IC 6-2.5-5-3(b), 45 IAC 2.2-5-8(c), Indiana Bell Telephone Co. v. Indiana Department of Revenue, 627 N.E. 2d 1386, Ind. Tax Court (1994)

Taxpayer protests the imposition of use tax on unloaders.

2. Sales and Use Tax – Scissors Lifts and Pallet Lifts

Authority: IC 6-2.5-5-3(b), 45 IAC 2.2-5-8(c)(2)(F), Indiana Department of Revenue v. United States Steel, 425 N.E. 2d, 659, Ind. App. (1981)

Taxpayer protests the imposition of use tax on scissors lifts and pallet lifts.

3. Sales and Use Tax – Stretch Wrap

Authority: IC 6-2.5-5-9(d), 45 IAC 2.2-5-16(c)

Taxpayer protests the imposition of use tax on stretch wrap.

4. Sales and Use Tax – Materials Purchased by Contractors

Authority: IC 6-2.5-2-1, IC 6-2.5-3-2(a), IC 6-2.5-2-1(b), IC 6-2.5-4-1(b), 45 IAC 2.2-4-22

Taxpayer protests the imposition of use tax on materials purchased by contractors.

5. Tax Administration – Penalty

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

Taxpayer protests the imposition of the penalty.

STATEMENT OF FACTS

The taxpayer is a corporation that produces toothpaste, cleanser and base material in Indiana. The base material is placed in containers and shipped to other facilities for completion. During the early portion of the audit, the taxpayer also produced shaving cream. After a routine audit, the Indiana Department of Revenue assessed additional sales and use tax, interest and penalty. The taxpayer protested the assessment and a hearing was held.

1. Sales and Use Tax – Unloaders

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. There are several statutory exemptions from the use tax. It is established law that all tax exemptions must be strictly construed against taxpayers. Indiana Bell Telephone Co. v. Indiana Department of Revenue, 627 N.E. 2d 1386, Ind. Tax Court (1994). Therefore, the taxpayer bears the burden of showing that any item meets the tests to qualify for exemption.

The taxpayer contends that the tube unloader qualifies for exemption from the use tax pursuant to the following provisions of IC 6-2.5-5-3(b):

> Transactions 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.

This exemption is clarified at 45 IAC 2.2-5-8(c):

> The state gross retail tax does not apply to purchases of manufacturing machinery, tools, and equipment to be directly used by the purchaser in the production process provided that such machinery, tools, and equipment are directly used in the production process; i.e., they have an immediate effect on the article being produced. Property 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.

The first items that the taxpayer contends qualifies for exemption as directly used in direct production are the tube unloaders. Empty toothpaste tubes are moved from the warehouse to the production line on a conveyer belt that the taxpayer agrees is subject to use tax. The tube unloaders move the empty toothpaste tubes from the conveyer belt to the point where they are filled with toothpaste. The process of moving the tubes to the point where the production process begins is not a use that has an immediate effect on the production of toothpaste. This use does not qualify for exemption.

FINDING

Taxpayer's protest is denied.

2. Sales and Use Tax – Scissors Lifts and Pallet Lifts

DISCUSSION

The taxpayer's second point of protest concerns the assessment of use tax on the scissors lifts and pallet lifts which are used to raise and lower the pallets to facilitate the loading of finished product onto the pallets prior to shipping. The scissors and pallet lifts raise and lower the pallets to levels that are a safe working height for the workers who hand stack the pallets. Therefore, the taxpayer contends that these lifts qualify for the directly used in direct production exemption as safety equipment. IC 6-2.5-5-3(b).

In support of its position, the taxpayer cites Indiana Department of Revenue v. U.S. Steel, 425 N.E.2d 659, Ind. App. (1981). In that case, the Court held that personal safety equipment used by U.S. Steel workers qualified for the directly used in direct production exemption as safety equipment. The exempt equipment included items such as safety eyeglasses, protective mittens, hardhats, goggles masks, hoods, heatshields, respirators and protective clothing. Without these personal safety items, the workers would not have been able to withstand the dangers of the environment and could not have produced the steel. The items that qualified for exemption were essential to the steel production. They were not merely items to make the work place more comfortable or convenient for the employees as in the case of the taxpayer's pallet lifts and scissors lifts.

45 IAC 2.2-5-8(c)(2)(F) provides an exemption for "safety clothing or equipment which is required to allow a worker to

participate in the production process without injury or to prevent contamination of the product during production." The scissors lifts and pallet lifts do not meet this regulatory test. They make it more convenient and comfortable for the workers to hand stack the pallets. They are not, however, necessary for a worker to stack the pallets. Therefore, they do not qualify for the safety equipment exemption to the use tax.

FINDING

Taxpayer's protest is denied.

3. Sales and Use Tax – Stretch Wrap

DISCUSSION

The taxpayer purchases stretch wrap that it uses in the packaging of its product. Specifically, the stretch wrap is used to wrap pallets of boxes of product for shipment to distribution warehouses. At these warehouses the stretch wrap is sometimes taken off the palletized product and the product is reorganized and re-shrink wrapped for smaller shipments. The audit assessed use tax on the twenty five per cent (25 %) of the stretch wrap that was replaced in this manner. The taxpayer protests this assessment.

The taxpayer contends that this stretch wrap qualifies for exemption pursuant to IC 6-2.5-5-9(d) as follows:

Sales of wrapping material and empty containers are exempt from the state gross retail tax if the person acquiring the material or containers acquires them for use as nonreturnable packages for selling the contents that he adds.

45 IAC 2.2-5-16(c) further clarifies this exemption as follows:

General rule. The receipt from a sale by a retail merchant of the following types of tangible personal property are exempt from state gross retail tax:

(1) Nonreturnable containers and wrapping materials including steel strap and shipping pallets to be used by the purchaser as enclosures for selling tangible personal property.

....

(d) Application of general rule.

(1) Nonreturnable wrapping material and empty containers. To qualify for this exemption, nonreturnable 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.

In this case, the taxpayer purchases shrink wrap, a nonreturnable wrapping material. The taxpayer wraps pallets containing tubes of toothpaste in the shrink wrap. The taxpayer then delivers the toothpaste to distribution centers where part of the shrink wrap is removed and the toothpaste is rewrapped. The taxpayer contends that this rewrapping always takes place after the toothpaste is sold to distribution centers that are not related to the taxpayer. The taxpayer did not, however, submit any evidence to substantiate its position that the distribution centers and warehouses are not owned or operated by the taxpayer and that the packages are rewrapped after the sale is consummated.

FINDING

The taxpayer's protest is denied.

4. Sales and Use Tax – Materials Purchased by Contractors

Indiana imposes a sales tax on retail transactions made in Indiana. IC 6-2.5-2-1. A retail transaction takes place when a retailer acquires tangible personal property and transfers it for a consideration in his ordinary course of business. IC 6-2.5-4-1(b). The purchaser of the tangible personal property in a retail transaction pays the tax to the seller as an agent for the state. IC 6-2.5-2-1(b).

A purchaser who acquires tangible personal property in a retail transaction without paying the sales tax is liable for the use tax when the purchaser uses the tangible personal property in Indiana. IC 6-2.5-3-2(a).

The application of the general rules to contractors is stated at 45 IAC 2.2-4-22 as follows:

(a) A contractor may purchase construction material exempt from the state gross retail tax only if he issues either an exemption certificate or a direct pay certificate to the seller at the time of the purchase.

....

(e) Disposition subject to the use tax. With respect to construction material a contractor acquired tax-free, the contractor is liable for the use tax and must remit such tax (measured on the purchase price) to the Department of revenue when he disposes of such property in the following matter.

....

(3) Lump sum contract. He converts the construction material into realty on land he does not own pursuant to a contract that includes all elements of cost in the total price.

The audit assessed additional tax on the materials portion of several invoices which the taxpayer claims were actually lump sum contracts and the contractors bear the responsibility for paying the sales or use tax. To substantiate its contention, the taxpayer submitted documentation for each of the contractors. That documentation included schedules of the invoices from each vendor, copies of the invoices, written assertions from most of the contractors indicating that the contractors deemed themselves to be entering into a lump sum contract with the taxpayer and that sales taxes were either paid at the time of purchase or use taxes were

paid when the materials were removed from tax-free inventory for use. The documentation presented sustains the taxpayer's burden of proving that it is not responsible for the sales or use tax on the lump sum contracts.

FINDING

The taxpayer's protest is sustained subject to audit verification.

5. Tax Administration – Penalty

DISCUSSION

Taxpayer's final point of protest concerns the imposition of the ten per cent negligence penalty pursuant to IC 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2(b) clarifies the standard for the imposition of the negligence penalty as follows:

> "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.

The audit assessed use tax on purchases in addition to those under protest. For example, the taxpayer failed to pay retail sales tax or remit use tax on the rental of forklifts and non-production computer equipment. The taxpayer's actions meet the requisite negligence standard.

FINDING

Taxpayer's final point of protest is denied.

DEPARTMENT OF STATE REVENUE

0420000238.LOF

LETTER OF FINDINGS NUMBER: 00-0238
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.

ISSUES

1. Sales and Use Tax – Riverboat Casino

Authority: IC 6-2.5-3-2(a)

The taxpayer protests the imposition of tax on its riverboat casino.

2. Sales and Use Tax – Printing and Duplication

Authority: IC 6-2.5-2-1(b)

The taxpayer protests the imposition of tax on purchases from a printing and duplication company.

3. Tax Administration – Negligence Penalty

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

The taxpayer protests the imposition of penalty.

STATEMENT OF FACTS

The taxpayer operates a casino riverboat. After an audit, the taxpayer was assessed additional use tax, interest and penalty. The taxpayer protested the assessment and a hearing was held.

1. Sales and Use Tax – Riverboat Casino

Pursuant to IC 6-2.5-3-2(a), Indiana imposes an excise tax on tangible personal property stored, used, or consumed in Indiana. In 1996 the taxpayer purchased a new gaming vessel which was constructed in Florida and delivered to Indiana. The taxpayer self assessed use tax on $25,779,715.00. However, the total cost of the gaming vessel was $33,879,715.00. The audit assessed tax on the difference of $8,100.000.00. The taxpayer protested this assessment and claimed a refund on the monies self assessed. Only the protest will be addressed in this Letter of Findings.

The taxpayer protests the assessment claiming that the riverboat casino is actually real estate and therefore not subject to the use tax which is only imposed on tangible personal property. The taxpayer bases its contention on the definition of real property found in the law governing the Indiana property tax, IC 6.1-1-15 as follows:

> "Real Property" means:
> (1) land located within this state;
> (2) a building or fixture situated on land located within this state;
> (3) an appurtenance to land located within this state;

(4) an estate in land located within this state, or an estate, right, or privilege in mines located on or minerals, including but not limited to oil or gas, located in the land, if the estate, right, or privilege is distinct from the ownership of the surface of the land; and

(5) notwithstanding IC 6–6-6-7, a riverboat licensed under the provisions of IC 4-33 for which the state board of tax commissioners shall prescribe standards to be used by township assessors.

The first four items in the property tax definition of real property are the commonly understood definitions of real property. The last item concerning the classification of riverboats such as the taxpayer's riverboat was added in 1995 to specifically denominate riverboat casinos as real property for purposes of the tax on real property. The fact that the legislature considered it necessary to specifically classify riverboats as real property for purposes of property tax when all other property in the state is classified pursuant to the first four items indicates that the classification is counterintuitive to the generally held understanding of a riverboat as tangible personal property. Although the Department may look to the classification of property for property tax purposes to assist in determining whether difficult to classify property is tangible personal property for sales tax purposes, it is not required to do so.

The issue to be determined is whether the taxpayer's gaming vessel is tangible personal property for sales and use tax purposes. "Tangible" is defined as "discernable by the touch or capable of being touched" in Webster's II New Riverside University Dictionary, The Riverside Publishing Company, 1988 at page 1182. The same dictionary at page 877 defines "personal property" as "temporary or movable property as distinguished real property." A gaming vessel is movable property that can be touched. The boat actually has a pilot and life preservers for travel in the water. It operates under authority of the U.S. Department of Transportation. It is not permanently attached to the land. Generally, then, the taxpayer's riverboat casino would be considered tangible personal property.

The Sales and Use Tax Regulations do not give a definition of tangible personal property for sales and use tax purposes. They do, however, refer to boats and watercraft as subject to the sales and use tax. 45 IAC 2.2-3-6(a)(2) defines "watercraft" as

a contrivance used or designed for navigation on water, including a vessel, boat, motor vessel, steam vessel, sailboat, vessel operated by machinery either permanently or temporarily affixed, scow, tugboat or any marine equipment that is capable of carrying passengers, except a ferry.

The taxpayer's riverboat casino clearly falls within the sales and use tax regulatory definition of "watercraft." 45 IAC 2.2-3-6(c)(2) specifically imposes use tax on Indiana watercraft purchased out of state. By these standards, the taxpayer's riverboat casino is tangible personal property and subject to the sales and use tax. Since there is a specific definition and imposition of sales and use tax on boats in the Sales and Use Tax Regulations, the Indiana Department of Revenue does not need to look to the property tax statute for assistance in classification of the gaming vessel as tangible personal property subject to the sales and use tax.

Alternatively, the taxpayer contends that if the Department finds that its gaming vessel is tangible personal property and qualifies for imposition of the sales and use taxes, then that gaming vessel qualifies for the public transportation exemption found at IC 6-2.5-5-27 as follows:

Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property.

To bolster its argument that the riverboat casino qualifies for the provision of public transportation exemption, the taxpayer offers evidence that the vessel's operation is regulated by the U.S. Department of Transportation and that those regulations are enforced by the U.S. Coast Guard.

The only purpose of the taxpayer's gaming vessel is the provision of an opportunity for people to gamble legally. Persons seeking transportation in the state of Indiana do not consider the taxpayer's services. The previously cited sales and use tax regulation specifically states that a ferry would not be subject to the imposition of tax. The taxpayer's boat can not be considered a ferry in that it doesn't transport anyone from one point to another point. At most the boat moves people in Indiana waters so that they can gamble legally. The taxpayer's riverboat casino does not qualify for the public transportation exemption from the sales and use tax.

FINDING

The taxpayer's first point of protest is denied.

2. Sales and Use Tax – Printing and Duplication

DISCUSSION

The audit assessed use tax on items purchased from a printing and duplication company. The taxpayer contends that it paid sales tax when it purchased the items. The taxpayer presented a letter from the printing and duplicating concern's accountant indicating that sales tax was paid at the time of purchase. The taxpayer also presented internally produced purchase orders indicating that sales tax was paid.

Sales tax is paid pursuant to the following provision 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 purchased printing and duplication supplies from a company that did not list the price separately on the invoice as required by the law. Further, the company was not registered as a retail merchant for collecting of sales tax with the Indiana Department of Revenue. Therefore, if the merchant collected sales tax, it did not do so as an agent for the state. The transaction did not comply with the requirements of the law.

FINDING

This point of the taxpayer's protest is denied.

3. Tax Administration – Negligence Penalty

DISCUSSION

Taxpayer's final point of protest concerns the imposition of the ten per cent negligence penalty pursuant to IC 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2(b) clarifies the standard for the imposition of the negligence penalty as follows:

> "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.

The audit assessed use tax on purchases in addition to those under protest. For example, the taxpayer failed to pay retail sales tax or remit use tax on many items clearly subject to the use tax such as dolls, sportswear, logos and bigheads costumes. The taxpayer's actions meet the requisite negligence standard.

FINDING

Taxpayer's final point of protest is denied.

DEPARTMENT OF STATE REVENUE

0320000239P.LOF

LETTER OF FINDINGS NUMBER: 00-0239
Withholding 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 specific issues.

ISSUE

Tax Administration – Penalty

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

Taxpayer protests the imposition of the penalty.

STATEMENT OF FACTS

The taxpayer is a riverboat casino. After a routine audit, the Indiana Department of Revenue assessed withholding tax, interest and penalty. The taxpayer protested the imposition of the penalty. Further facts will be provided as necessary.

Tax Administration – Penalty

DISCUSSION

The taxpayer protests the imposition of the ten per cent negligence penalty pursuant to IC 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2(b) clarifies the standard for the imposition of the negligence penalty as follows:

> 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 reach 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.

The taxpayer hired several out-of-state contractors. Even though the applicable law and regulations require withholding when hiring out-of-state contractors, the taxpayer failed to do so. The taxpayer's breach of its duty to follow clear instructions in the law and regulations constitutes negligence. The ten percent negligence penalty was properly imposed.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0320000421.LOF

LETTER OF FINDINGS NUMBER: 00-0421
Responsible Officer
Withholding Tax
For Tax Periods: 1988-1990

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 specific issues.

ISSUE

Withholding Tax – Responsible Officer Liability

Authority: IC 6-3-4-8(f), IC 6-8.1-5-1(b), Indiana Department of Revenue v. Safayan 654 N.E. 2nd 270 (Ind.1995)

The taxpayer protests the assessment of responsible officer liability for unpaid corporate withholding taxes.

STATEMENT OF FACTS

The taxpayer was vice-president and shareholder of a corporation that did not remit the proper amount of withholding taxes to Indiana. The taxpayer was personally assessed for the taxes and protested these assessments. More facts will be provided as necessary.

Withholding Tax – Responsible Officer Liability

DISCUSSION

The proposed withholding taxes were personally assessed against Taxpayer pursuant to IC 6-3-4-8(f), which provides that "In the case of a corporate or partnership employer, every officer, employee, or member of such employer, who, as such officer, employee, or member is under a duty to deduct and remit such taxes shall be personally liable for such taxes, penalties, and interest."

Indiana Department of Revenue assessments are prima facie evidence that the taxes are owed by the taxpayer who has the burden of proving that the assessment is incorrect. IC 6-8.1-5-1(b).

Pursuant to Indiana Department of Revenue v. Safayan 654 N.E. 2nd 270 (Ind.1995) at page 273: "The statutory duty to remit trust taxes falls on any officer or employee who has the authority to see that they are paid. The factors considered to determine whether a person has such authority are the following:

1. The person's position within the power structure of the Corporation;
2. The authority of the officer as established by the Articles of Incorporation, By-laws or employment contract; and
3. Whether the person actually exercised control over the finances of the business including control of the bank account, signing checks and tax returns or determining when and in what order to pay creditors.

Id. At 273.

The issue to be determined in this matter is whether or not the taxpayer was an officer or employee with the duty to remit the withholding taxes to the state of Indiana.

The taxpayer was a shareholder in the corporation and a vice-president. As a vice-president, the taxpayer could be found to be a person with the duty to remit withholding taxes to Indiana. The amount of power and authority a vice-president actually has varies from corporation to corporation. Therefore it will be necessary to consider the second and third indicia of authority as set out in the Safayan case.

The Articles of Incorporation do not give any indication of the actual authority of the taxpayer within the corporation structure. The corporate copy of the By-laws has been misplaced. Neither were the By-laws available from the Indiana Secretary of State. Testimony at the hearing indicated that there never was an employment contract between the corporation and the taxpayer.

The final indicia concerns the actual authority and control the taxpayer had over corporate activities, particularly financial activities. After the hearing, the taxpayer submitted several affidavits by former employees of the corporation. The affidavits all indicated that the taxpayer was merely peripherally involved in the operations of the corporation. He came to the office on an occasional and irregular basis. He had no authority to write checks or determine which creditors would be paid.

The taxpayer has satisfied his burden of proving that he was not a corporate officer with the duty to remit withholding taxes.

FINDING

The taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

1420000382.LOF

LETTER OF FINDINGS NUMBER: 00-0382
Special Fuel Tax
For Years 1995, 1996, and 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. Special Fuel Tax – Import of Fuel to Indiana

Authority: SF10-A; IC § 6-6-2.5-35

Taxpayer protests an assessment based on its out of state sale of fuel for import to Indiana.

II. Special Fuel Tax – Export Exemption

Authority: IC § 6-6-2.5-28; IC § 6-6-2.5-30; IC § 6-6-2.5-40; IC § 6-6-2.5-57; IC § 6-8.1-5-1; IC § 6-8.1-5-4; *Keller Oil Co. v. Indiana Dept of Revenue,* 512 N.E.2d 501 (Ind. Tax 1987)

Taxpayer protests an assessment of tax on fuel that may have been exported.

III. Special Fuel Tax – Dyed Fuel Deliveries

Taxpayer protests assessments of tax on certain dyed fuel deliveries.

IV. Special Fuel Tax – Transmix Fuel Transfer

Authority: IC § 6-6-2.5-30

Taxpayer protests denial of a deduction for fuel transferred to another company.

V. Special Fuel Tax – Exchange

Taxpayer protests disallowed exchange volume.

VI. Special Fuel Tax – Dyed Fuel

Taxpayer protests assessments of tax based on the Department's determination that tax on dyed fuel was not remitted to the state.

VII. Special Fuel Tax – Debit/Credit Entries

Taxpayer protests an adjustment based on erroneously generated invoices.

STATEMENT OF FACTS

Taxpayer, an international wholesale distributor of fuel with terminals in Indiana, sells fuel for use within and outside of the state.

I. Special Fuel Tax – Wholesale ID

DISCUSSION

Taxpayer protests an adjustment that included in the tax base special fuel that was withdrawn by taxpayer customers from terminals outside of Indiana and was then taken into Indiana by taxpayer's customers. Taxpayer argues that the audit report predicates taxpayer's duty to collect Indiana special fuel tax on an agreement by taxpayer to collect that tax. The SF10-A form signed and referenced by taxpayer states in relevant part that taxpayer:

Agree[s] to treat all out-of-state terminal removals of undyed special fuel, for export into Indiana, as if they were received in Indiana, and collect the Indiana special fuel tax from every purchaser.

And, as part of the explanation of this form that was cited by taxpayer as the basis for taxpayer's protest:

Option One: Elect the 'blanket' option. Under this option, the S/PS will continue to collect Indiana special fuel tax due on import sales into Indiana in the same manner which they have prior to July 1 [1994]. This alleviates administrative requirements, notice requirements, and reporting changes which are required under Option Two or Three.

This taxpayer signed this pursuant to IC § 6-6-2.5-35(j), which stated at the time of taxpayer's signing:

(j) The department, a licensed importer, the reseller to a licensed importer, and a licensed supplier or permissive supplier may jointly enter into an agreement for the licensed supplier or permissive supplier to precollect and remit the tax imposed by this chapter with respect to special fuel imported from a terminal outside of Indiana in the same manner and at the same time as the tax would arise and be paid under this chapter if the special fuel had been received by the licensed supplier or permissive supplier at a terminal in Indiana. If the supplier is also the importer, the agreement shall be entered into between the supplier and the department. However, any licensed supplier or permissive supplier may make an election with the department to treat all out-of-state terminal removals with an Indiana destination as shown on the terminal-issued shipping paper as if the removals were received by the supplier in Indiana pursuant to sections 28 and 35(a) of this chapter, for all purposes. In this case, the election and notice of the election to a supplier's customers shall operate instead of a three- (3) party precollection agreement. The department may impose requirements reasonably necessary for the enforcement of this subsection.

IC § 6-6-2.5-35(j) is explicit as it regards the effect of an election. It states in relevant part "any licensed supplier or permissive supplier may make an election with the department to treat all out-of-state terminal removals with an Indiana destination as shown on the terminal-issued shipping paper *as if the removals were received by the supplier in Indiana pursuant to sections 28 and 35(a) of this chapter, for all purposes."* Id *(emphasis added)* When a licensed or permissive supplier makes such an election, it also consents to the liability and duties that IC § 6-6-2.5-28 and 35(a) specify upon a receipt of special fuel. Thus, a licensed or permissive supplier that makes an election under IC § 6-6-2.5-35(j) thereby consents to the imposition of special fuel tax pursuant to IC § 6-6-2.5-28 upon the removal of special fuel from an out-of-state terminal shown as being destined for Indiana. It also makes itself liable for the tax on that fuel as the receiving supplier and assumes duties to invoice, precollect, and remit Indiana special fuel tax on the gallons it has so received- all of these taxpayer responsibilities paralleling taxpayer responsibilities at instate terminals.

Taxpayer does not provide an explanation or attempt to reconcile the cited language of SF10-A or IC § 6-6-2.5-35(j), merely noting that it interpreted the SF10-A as not requiring any reporting or collection on the taxpayer's part. Taxpayer is correct in stating that it is not *required* to collect the tax, however taxpayer's out-of-state terminal was never *required* to pay this tax. Taxpayer collected this tax on behalf of buyers intending to deliver the fuel to Indiana and not wishing to pay the resident state's fuel tax. If taxpayer did not permit the buyers this option, the buyer's, being under the resident state's jurisdiction, would have been required to pay the resident state's fuel tax; then Indiana's fuel tax, then seek a refund from the resident state. For either compassionate or commercially competitive reasons, the taxpayer has opted to collect and forward the Indiana tax from the resident state's refinery. Indeed, taxpayer's desire to continue this practice prompted taxpayer to not select option C on the SF10A form- the option not to collect Indiana fuel tax at this location.

Even the SF10-A explanation cited by the taxpayer in support of its argument states taxpayer, "… will *continue to collect* Indiana special fuel tax due… This alleviates administrative requirements, notice requirements, and *reporting changes* which are required under Option Two or Three" *(Emphasis added*) Taxpayer is an international wholesale distributor of fuel, for taxpayer to suggest it was lulled into complacency by the explanation of an option on a form, where said explanation clearly states an activity (the collection and reporting of Indiana fuel tax at the out-of-state terminal) already has and does exist and which is merely an explanation of an option that explicitly declares a resolve on taxpayers part to "collect the Indiana special fuel tax from every purchaser," is disingenuous at best. Taxpayer states no statutory basis for a reversal of this adjustment, nor does taxpayer explain its reluctance to select the "no tax" option on the form in question. Taxpayer protest is denied.

FINDINGS

Taxpayer protest denied.

II. Special Fuel Tax – Export Exemption

DISCUSSION

This concerns FOB Indiana sales. These sales were reported on taxpayer's returns as export sales. According to the auditor, all sales from a taxpayer's origin code to a customer with an Indiana Wholesale Identification Code (WIC number) were considered in-state sales and included as disallowed exports for this adjustment. In all cases, taxpayer maintains that these were export sales. Taxpayer argues that it has proof that falls into two general categories. The first is other information on the bill of lading, specifically, a stated destination, and a signed receipt at that location by the recipient. The second method was to get information from the customer and the customer's Indiana return showing that the shipment received from taxpayer was reported on taxpayer's customer's return as an export and was accepted as such on audit by the Indiana Department of Revenue. According to the taxpayer, some of its customer's out-of-state returns were also requested and the shipments reported by taxpayer as exports were purportedly traced to those returns.

The Special Fuel Tax in question is imposed by IC § 6-6-2.5-28, which instructs:

(a) A license tax of sixteen cents ($0.16) per gallon is imposed on all special fuel sold or used in producing or generating power for propelling motor vehicles except fuel used under section 30(a)(8) of this chapter. The tax shall be paid at those times in the manner, and by those persons specified in this section and section 35 of this chapter.

(b) The department shall consider it a rebuttable presumption that all undyed or unmarked special fuel, or both, received in Indiana is to be sold for use in propelling motor vehicles.

IC § 6-6-2.5-30 states:

(a) The following are exempt from the special fuel tax:

(1) Special fuel sold by a supplier to a licensed exporter for export from Indiana to another state or country to which the exporter is specifically licensed to export exports by a supplier, or exports for which the destination state special fuel tax has been paid to the supplier and proof of export is available in the form of a destination state bill of lading.

IC § 6-6-2.5-40(a) states in relevant part:

Each person operating a refinery, terminal, or bulk plant in Indiana shall prepare and provide to the driver of every vehicle receiving special fuel at the facility a shipping document setting out on its face the destination state as represented to the terminal operator by the shipper or the shipper's agent, except that an operator of a bulk plant in Indiana delivering special fuel into a vehicle with a capacity of not more than five thousand four hundred (5,400) gallons for subsequent delivery to an end consumer in Indiana is exempt from this requirement.

Additionally IC § 6-6-2.5-57 states:

(a) Each person operating a terminal in Indiana shall file monthly reports of operations within Indiana on forms prescribed by the department. The department may require the reporting of any information it considers reasonably necessary.

(b) For purposes of reporting and determining tax liability under this chapter, every licensee shall maintain inventory records as required by the department.

Additionally, the Indiana Tax court has held in its denial of a petition to enjoin collection of the Special Fuel Tax the following:

IND. CODE 6-8.1-5-4(a) requires persons such as the Petitioners to keep adequate records. Since it appears that Petitioner has not kept adequate records and since IC 6-8.1-5-1(a) permits the Respondent to use the best information available to calculate

the tax liability, it does not appear that Petitioner has a reasonable opportunity to prevail in the original tax appeal issue. *Keller Oil Co. v. Indiana Dept of Revenue*, 512 N.E.2d 501 (Ind. Tax 1987) at 504

Taxpayer alleges that it can demonstrate that sales were to eleven customers in the stated amounts below and accounted for as follows:

Customer 1

Customer's Illinois tax returns for 1995 and 1996 show the shipments reported by taxpayer as exports to have been delivered in, and reported to, Illinois. Taxpayer does not have access to customer's Illinois returns for 1997, but are pursuing alternative methods of verification.

Customer 2

Taxpayer acquired from the customer copies of the bills of lading, which indicate the destination and receipt at that destination of shipments of fuel.

Customer 3

Customer has furnished its tax returns for the period indicating that all purchases from Shell were exported. Additionally, the customer was audited for the period 1994-96 by the State of Indiana with no assessment resulting.

Customer 4

Customer reported that they were audited for the period by the State of Indiana. Exports were reported on the returns and were verified in the audit. Customer doesn't want to provide sales documentation or returns because they contain proprietary customer information. Customer provided an audit summary for the period.

Customer 5

Customer advised that the product was not exported and that Shell did not bill them for the tax.

Customer 6

Customer lost records.

Customer 7

Customer purchased by new entity -- No records available.

Customer 8

Customer exported the product. Copies of invoices provided.

Customer 9

Customer exported the product. Copies of the returns provided.

Customer 10

Customer exported the product. Copies of the returns provided.

Customer 11

Customer purchased by new entity– No records available.

The Department requested Bills of Lading on 5/21/98, 7/1/98, 11/17/98 (Information Document Requested forms for above dates in audit file) as well as an Auditor list requesting the documentation from April of 1999 and a 30 day notice from the Auditor in February of 2000 prior to this assessment being made. These forms have not been provided by taxpayer. Inasmuch as the transactions may-or may not- have been for export, the statutory language and its interpretation are unambiguous: Taxpayer "shall maintain inventory records as required by the department," (IC § 6-6-2.5-57). The Tax Court, in denying an order to enjoin collection of tax pending, states "…it appears that Petitioner has not kept adequate records and since IC 6-8.1-5-1(a) permits the Respondent to use the best information available to calculate the tax liability, it does not appear that Petitioner has a reasonable opportunity to prevail in the original tax appeal issue." *Keller Oil Co. v. Indiana Dept of Revenue,* 512 N.E.2d 501 (Ind. Tax 1987) at 504.

The statutory framework is crafted to provide a comprehensive accounting of fuel transactions across multiple taxpayers and innumerable transactions, thus minimizing the possibility of omissions such as occurred here. Taxpayer, in complete disregard of this framework, protests that the ad-hoc, self-selected documentation submitted should suffice to demonstrate that these transactions were not taxable. Taxpayer now invites the Department to disregard statutorily required documentation and procedures for claiming the export exemption. The Department respectfully declines.

FINDINGS

Taxpayer protest denied.

III. Special Fuel Tax – Dyed Fuel Deliveries

DISCUSSION

Taxpayer noted that some deliveries of dyed diesel fuel were not clearly reported as such and tax was assessed on them as subject to the special fuel tax. Taxpayer, however, has failed to submit documentation to support this contention. Absent such documentation, the protest cannot be sustained.

FINDINGS

Taxpayer protest denied.

IV. Special Fuel Tax – Transmix Fuel Transfer

DISCUSSION

Audit disallowed deductions of transmix fuel (fuel used as a buffer between grades of fuel in pipeline shipments) that was transferred by taxpayer to another company. Documentation was not provided at the time of audit. Taxpayer is offering to provide documentation, as required by IC § 6-6-2.5-30(a) (10). Absent the presentation of this documentation this protest cannot be sustained.

FINDINGS

Taxpayer protest denied.

V. Special Fuel Tax – Exchange

DISCUSSION

Taxpayer protests the disallowance of part of its exchange volume total. Taxpayer's customer reported fewer gallons received than Taxpayer reported delivered. This involves a dispute between the supplier (Taxpayer) and customer, inasmuch as both parties need to have their records in accord for Taxpayer to receive the credit. If taxpayer believes the customer has failed to correctly report the number of gallons, taxpayer's remedy lies with the customer, not the state. This (a tax appeal) forum exists to resolve a dispute between Taxpayer and the Department, and has no power over a third party's reporting in a transaction of this type.

FINDINGS

Taxpayer protest denied.

VI. Special Fuel Tax – Dyed Fuel

DISCUSSION

Special Fuel Tax was assessed on dyed fuel and not remitted to the State. Taxpayer concedes issue.

FINDINGS

Taxpayer protest withdrawn.

VII. Special Fuel Tax – Debit/Credit Entries

DISCUSSION

Taxpayer protests adjustments made by the auditor that are attributable to erroneously generated invoices. Taxpayer maintains that when an invoice was generated a document was produced, when the correction was made there was a correcting entry on the books, but no document was generated. The auditor picked up the invoices but did not pick up the correcting entries. Exclusion of adjusting entries would be inappropriate, therefore to the extent the adjustments were made, credit will be given.

FINDINGS

Taxpayer protest sustained.

DEPARTMENT OF STATE REVENUE

0420000437.LOF

LETTER OF FINDINGS NUMBER: 00-0437
Sales and Use Tax
Tax Administration – Penalty
For Years 1997 through 1999

NOTICE: Under Ind. Code 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 Tax – Imposition of Sales Tax on Exempt Items

Authority: IC 6-2.5-2-1;45 IAC 2.2-1-1; IC 6-2.5-5-2;45 IAC 2.2-2-1; IC 6-2.5-8-1; 45 IAC 2.2-2-2; IC 6-2.5-8-8;45 IAC 2.2-5-6; IC 6-2.5-9-8;45 IAC 2.2-8-12; IC 6-8.1-3-1;45 IAC 15-3-3; IC 6-8.1-3-4

The taxpayer protests the imposition of sales tax on tires sold to farmers.

II. Sales Tax – Imposition of Sales Tax on Sundries

Authority: IC 6-2.5-2-1; 45 IAC 2.2-2-1; IC 6-2.5-5-2; 45 IAC 2.2-2-1; IC 6-2.5-8-1; 45 IAC 2.2-2-2; IC 6-2.5-8-8; 45 IAC 2.2-5-6; IC 6-2.5-9-8; 45 IAC 2.2-8-12

The taxpayer protests the imposition of sales tax on various sundries sold to the public.

III. Use Tax – Imposition of Use Tax on Rental and Other Items

Authority: IC 6-2.5-3-1; 45 IAC 2.2-3-1; IC 6-2.5-3-2; 45 IAC 2.2-3-4; IC 6-2.5-3-4; 45 IAC 2.2-3-19; IC 6-2.5-3-5; 45 IAC 2.2-3-24; IC 6-2.5-4-10(a); 45 IAC 2.2-3-27

The taxpayer protests the imposition of use tax on uniforms and towels rented from a laundry service, and on various sundries used on site.

IV. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1; 45 IAC 15-11-2(b); IC 6-8.1-5-4

The taxpayer protests the imposition of the 10% negligence penalty.

STATEMENT OF FACTS

Taxpayer, an Indiana retail merchant, is the sole proprietor of a business specializing in selling and repairing tires. The majority of taxpayer's customer base consists of local farmers. Taxpayer also sells various sundries—soda, cigarettes, magazines and bagged snack items— to the public. Taxpayer purchases other items, such as coffee cups, filters, and various cleaning materials for use at his place of business. Taxpayer rents uniforms and towels from a laundry service for use on the premises. The Department audited taxpayer for tax years 1997 through 1999.

Because of taxpayer's inadequate recordkeeping practices, it was impossible for the Department to determine whether the tire sales and repairs qualified for the "exempt farm use" sales tax exemption provided by IC 6-2.5-5-2. Audit, therefore, proposed additional assessments of sales tax on taxpayer's tire sales and repairs. Taxpayer failed to collect and remit sales tax on the various sundries taxpayer offered for sale in addition to tires. Taxpayer failed to pay gross retail tax at the time of purchase of supplies for making coffee on the premises and for cleaning supplies and failed to self-assess remit use tax on these purchases. Taxpayer also failed to self-assess and remit use tax on the uniform and towel rental transactions. The Department imposed use tax on the coffee supplies and cleaning materials purchases and on the rental transactions. In addition, the Department imposed a 10% negligence penalty. Taxpayer timely protested the assessed taxes and penalty. Further information will be provided as necessary.

I. Sales Tax – Imposition of Sales Tax on Exempt Items

DISCUSSION

The taxpayer protests the imposition of sales tax on tires sold to farmers. Indiana Code section 6-2.5-2-1(a) establishes "[a]n excise tax, known as the state gross retail tax," to be "imposed on retail transactions made in Indiana." Moreover, IC 6-8.1-5-4 mandates that "[e]very person subject to a listed tax must keep books and records so that the department can determine the amount, if any, of the person's liability for that tax by reviewing those books and records." Records with the proper exemption information were not available for the tax years within the audit period.

Under IC 6-2.5-2-1(b), "[t]he 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.**" Pursuant to 45 IAC 2.2-2-2, "[t]he retail merchant, acting as an agent for the state of Indiana, must collect the tax. The tax is bourne [sic] by the customer. Consideration is a necessary element of the taxable transaction." Pursuant to these code sections and regulations, taxpayer should have collected and remitted gross retail tax on the sales of tires except for those exempt transactions allowed under IC 6-2.5-5-2.

Indiana Code section 6-2.5-8-8 provides in pertinent part:

(a) A person, authorized under subsection (b), who makes a purchase in a transaction which is exempt from the state gross retail and use taxes, may issue an exemption certificate to the seller instead of paying the tax. The person shall issue the certificate on forms and in the manner prescribed by the department. A seller accepting a proper exemption certificate under this section has no duty to collect or remit the state gross retail or use tax on that purchase.

During the audit, there was no way for the Department to distinguish between exempt and non-exempt cash sales. Therefore, sales tax was assessed on all cash tire sales during the audit period.

IC 6-8.1-3-1(a) states that the Department "has the primary responsibility for the administration, collection, and enforcement of the listed taxes." Under IC 6-8.1-1-1, the state gross retail and use taxes are "listed taxes." Taxpayer's duty to maintain proper records (IC 6-8.1-5-4) is two-fold: 1.) the collection and maintenance of exemption certificates enables taxpayer to prove that sales to certain customers are exempt from the imposition of sales and use taxes and 2.) the collection and maintenance of exemption certificates facilitates the Department's enforcement and collection of sales and use taxes which taxpayer, as a retail merchant, must collect and remit to the Department.

In this case, taxpayer's failure to collect and maintain exemption certificates has deprived taxpayer of the evidence needed to prove certain sales were exempt and deprived the Department of its ability to determine the correct amount of taxpayer's liability for the listed taxes, i.e., sales and use taxes. Therefore, the Department correctly assessed sales tax on all cash tire sales for the audit period.

FINDING

The taxpayer's protest is denied..

II. Sales Tax – Imposition of Sales Tax on Sundries

DISCUSSION

Taxpayer protests the imposition of sales tax on various sundries—soda, cigarettes, magazines, and bagged snack items--he sells to the public in addition to selling and repairing tires. Some of the items are sold at cost; some are sold at a 10% mark-up. Taxpayer did not collect and remit gross retail tax for these transactions.

Pursuant to IC 6-2.5-2-1(a), sales tax is "imposed on retail transactions made in Indiana." Taxable transactions occurred with each purchase of soda, cigarettes, magazines, and/or bagged snack item. Purchasers should have been charged the gross retail sales tax and taxpayer should have collected and remitted those amounts "as agent for the state" of Indiana.

FINDING

The taxpayer's protest is denied

III. Use Tax – Imposition of Use Tax on Coffee Supplies, Cleaning Materials, and Rental Items

Taxpayer protests the imposition of use tax on its purchases of coffee supplies, cleaning materials, and on the rental of uniforms and towels from a laundry service. No state gross retail tax was paid at the time of the purchases and rentals. Under IC 6-2.5-3-1 and 6-2.5-3-2, taxpayer must collect and remit use tax "on the storage, use, or consumption of tangible personal property." Section 6-2.5-3-2(a) provides in part:

> An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

Coffee filters, styrofoam cups, cleaning materials, uniforms, and towels are all tangible personal property. The coffee supplies are for consumption on the premises. The cleaning supplies are for use on the premises. No state gross retail tax was collected and remitted for these items at the time of purchase. Therefore, under IC 6-2.5-3-2(a), taxpayer should have self-assessed and remitted use tax on these items.

Taxpayer rents the uniforms and towels from a vendor for use in the tire sales part of the business. 45 IAC 2.2-4-27 provides that "the gross receipts from renting or leasing tangible personal property are taxable. This regulation only exempts from tax those transactions which would have been exempt in an equivalent sales transaction." And in this instance, selling uniforms and towels would not have been exempt from sales tax. Subsection (c) states that "[t]he rental or leasing of tangible personal property constitutes a retail transaction, and [t]he lessor must collect and remit the gross retail tax on the amount of actual receipts as agent for the state of Indiana." Therefore, under 45 IAC 2.2-3-19 and 45 IAC 2.2-4-27, taxpayer should have self-assessed and remitted use tax on the rental of uniforms and towels.

FINDING

The taxpayer's protest is denied.

IV. Tax Administration – Penalty

Taxpayer protests the Department's imposition of the 10% negligence penalty, arguing that he has followed the same system of recordkeeping for three generations, and such methodology does not rise to the level of negligence defined in 45 IAC 15-11-2(b).

Indiana Code 6-8.1-10-2.1(a)(3) authorizes the Department to impose a penalty on a taxpayer if he "incurs, upon examination by the department, a deficiency that is due to negligence." Indiana Administrative Code, Title 45, Article 15, Rule 11-2(b) provides in pertinent part:

> "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.

In determining whether or not to assess the 10% penalty, the Department looks for indicia of negligence as well as indicia of due diligence. Under IC 6-8.1-5-4, the taxpayer has an affirmative duty to maintain "books and records so that the department can determine the amount, if any, of the person's liability by reviewing those books and records." Since taxpayer did not use reasonable care or due diligence in maintaining the proper records for sales and use tax, negligence has occurred under 45 IAC 15-11-2(b).

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420000438.LOF

LETTER OF FINDINGS NUMBER: 00-0438
Sales and Use Tax
For Tax Years 1997-1999

NOTICE: Under Ind. Code § 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 Tax – Repair and Service Contracts

Authority: IC § 6-2.5-2-1; 45 IAC 2.2-4-2

Taxpayer protests the assessment of sales tax on sales of parts and materials used in service repair jobs.

II. Use Tax – Storage Tanks

Authority: IC § 6-2.5-3-2; 45 IAC 2.2-3-4

Taxpayer protests the assessment of use tax on petroleum storage tanks.

III. Tax Administration – Penalty

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2

Taxpayer protests the imposition of the 10% negligence penalty.

STATEMENT OF FACTS

The taxpayer is primarily engaged in three separate businesses. Division 1 is a licensed motor fuel dealer and bulk plant. This division sells gasoline, diesel fuel, heating oil and propane gas to customers in Indiana and Ohio. Division 2 is a full service electrical contractor and electrical repair service. This division performs lump sum contracts for improvements to realty and general electrical repairs to homes, farms, and businesses. Division 3 also performs both lump sum contracts for improvements to realty and general repair for all makes and types of heating and air conditioning systems for residential, agricultural, industrial and other business customers. The transactions at issue involve Division 3's lump sum contracts for general repair for heating and air conditioning systems. Taxpayer's business situs is located in Ohio; taxpayer conducts business in both Ohio and Indiana. An audit of taxpayer's business activities was conducted covering the tax years 1997 through 1999. The Department determined that taxpayer had neither billed nor collected sales tax from the sale of parts and materials used in its Indiana service repair jobs. The Department also determined that taxpayer had purchased exempt several petroleum storage tanks that were provided to several of their Indiana customers.

Taxpayer timely protested, and a hearing was scheduled for May 16, 2001. Taxpayer failed to appear. Therefore, this Letter of Findings is based on the information in the files, Indiana's tax code and administrative regulations, and relevant case law. Further information will be provided as necessary.

DISCUSSION

I. Sales and Use Tax – Repair and Service Contracts

Taxpayer protests the assessment of sales tax on the sale of parts and materials used in its Indiana repair jobs. Taxpayer contends "repair of furnaces, air conditioners, etc." constitutes "an improvement to real estate" such that taxpayer may bill customers for repairs on a lump sum basis. Denomination as a lump sum contract allows taxpayer to self-assess use tax on materials purchased instead of collecting sales tax on the materials transferred.

Contractors may bill customers on a "lump sum" basis. (45 IAC 2.2-4-23). A contractor is defined as "any person engaged in converting construction material into realty."" Furthermore, "the term 'contractor' refers to general or prime contractors, subcontractors, and specialty contractors, including...persons engaged in...plumbing, *heating,* electrical work..." (45 IAC 2.2-4-25, emphasis added). Taxpayer, therefore, is acting as a contractor—and may execute lump sum contracts—when installing heating and air conditioning units. However, taxpayer is not acting as a contractor when servicing and repairing such units. Rather, taxpayer is properly characterized as a service provider.

Generally, "persons engaging in repair services are servicemen with respect to the services which they render and retail merchants at retail with respect to repair or replacement parts." (45 IAC 2.2-4-2(c)). Taxpayer, therefore, should have collected sales tax on the repair parts transferred. (IC § 6-2.5-2-1). An exception to the collection requirement is outlined in 45 IAC 2.2-4-2(a). A service provider does not have to collect sales tax on the tangible personal property transferred if:

1. The serviceman is in an occupation which primarily furnishes and sells services, as distinguished from tangible personal property;
2. The tangible personal property purchased is used or consumed as a necessary incident to the service;
3. The price charged for tangible personal property is inconsequential (less than 10%) compared with the service charge; and
4. The serviceman pays gross retail tax or use tax upon the tangible personal property at the time of acquisition.

In taxpayer's case, there is no evidence to indicate that the price charged for the tangible personal property transferred was inconsequential (less than 10%) compared with the service charge. Absent compliance with the prescriptions of 45 IAC 2.2-4-2(a), taxpayer should have invoiced and collected the Indiana gross retail tax on all parts and materials used in providing repair services pursuant to IC § 6-2.5-2 and 45 IAC 2.2-4-2.

FINDING

Taxpayer's protest concerning the assessment of sales tax on parts and materials used in repair services contracts is denied.

II. Use Tax – Petroleum Storage Tanks

Taxpayer protests the assessment of use tax on petroleum storage tanks. Taxpayer does not charge customers who use the tanks. And if customers stop purchasing taxpayer's products, they cannot use the tanks. Indiana Code § 6-2.5-3-2 provides for the

imposition of a use tax on the "storage, use or consumption of tangible personal property in Indiana." The petroleum storage tanks fall squarely within the ambit of the statutory language. *See also* 45 IAC 2.2-3-4. Taxpayer should have assessed and remitted use tax on the petroleum storage tank transactions.

FINDING

Taxpayer's protest concerning the assessment of use tax is denied.

III. Tax Administration – Penalty

Taxpayer protests the Department's imposition of the 10% negligence penalty, arguing that prior audits have not found anything wrong with the way taxpayer fashions its service and repair contracts.

Indiana Code § 6-8.1-10-2.1(a)(3) authorizes the Department to impose a penalty on a taxpayer if he "incurs, upon examination by the department, a deficiency that is due to negligence." Indiana Administrative Code, Title 45, Article 15, Rule 11-2(b) defines negligence "as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." Indiana taxpayers have duties placed upon them by the Code and Administrative Regulations. If a taxpayer is careless or thoughtless, or disregards those duties, negligence results. Further, the Department is authorized to treat ignorance of the "listed tax laws, rules and/or regulations" as negligence.

In determining whether or not to assess the 10% negligence penalty, the Department looks for indicia of negligence as well as for indicia of due diligence. Taxpayer has been doing business within the state of Indiana for many years and is aware of its responsibilities under Indiana's tax code and administrative regulations. Taxpayer has not presented any evidence to support a finding of due diligence. Therefore, the penalty stands.

FINDING

The taxpayer's protest concerning the assessment of the 10% negligence penalty is denied.

DEPARTMENT OF STATE REVENUE

0320010035.LOF

LETTER OF FINDINGS NUMBER: 01-0035
Responsible Officer
Withholding Tax
For Tax Periods: 1988-1990

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 specific issues.

ISSUES

1. Withholding Tax – Responsible Officer Liability

Authority: IC 6-3-4-8(f), IC 6-8.1-5-1(b), Indiana Department of Revenue v. Safayan 654 N.E. 2nd 270 (Ind.1995)

The taxpayer protests the assessment of responsible officer liability for unpaid corporate withholding taxes.

STATEMENT OF FACTS

The taxpayer was vice-president and employee of a corporation that did not remit the proper amount of withholding taxes to Indiana. The taxpayer was personally assessed for the taxes and protested these assessments. More facts will be provided as necessary.

1. Withholding Tax – Responsible Officer Liability

Discussion

The proposed withholding taxes were personally assessed against Taxpayer pursuant to IC 6-3-4-8(f), which provides that "In the case of a corporate or partnership employer, every officer, employee, or member of such employer, who, as such officer, employee, or member is under a duty to deduct and remit such taxes shall be personally liable for such taxes, penalties, and interest."

Indiana Department of Revenue assessments are prima facie evidence that the taxes are owed by the taxpayer who has the burden of proving that the assessment is incorrect. IC 6-8.1-5-1(b).

Pursuant to Indiana Department of Revenue v. Safayan 654 N.E. 2nd 270 (Ind.1995) at page 273: "The statutory duty to remit trust taxes falls on any officer or employee who has the authority to see that they are paid. The factors considered to determine whether a person has such authority are the following:

1. The person's position within the power structure of the Corporation;
2. The authority of the officer as established by the Articles of Incorporation, By-laws or employment contract; and
3. Whether the person actually exercised control over the finances of the business including control of the bank account, signing checks and tax returns or determining when and in what order to pay creditors.

Id. At 273.

The issue to be determined in this matter is whether or not the taxpayer was an officer or employee with the duty to remit the

withholding taxes to the state of Indiana.

The taxpayer was a vice-president and employee of the corporation. As such, the taxpayer could be found to be a person with the duty to remit withholding taxes to Indiana. The amount of power and authority a vice-president or employee actually has varies from corporation to corporation. Therefore it will be necessary to consider the second and third indicia of authority as set out in the Safayan case.

The Articles of Incorporation do not give any indication of the actual authority of the taxpayer within the corporation structure. The corporate copy of the By-laws has been misplaced. Neither were the By-laws available from the Indiana Secretary of State's office. Testimony at the hearing indicated that there never was a formal, written employment contract between the corporation and the taxpayer.

The final indicia concerns the actual authority and control the taxpayer had over corporate activities, particularly financial activities. Affidavits presented after the hearing indicate that the taxpayer was a project manager, ran various jobs, and supervised the office. The taxpayer was a signatory on the corporate checking account and actually signed checks for the corporation. This indicates that the taxpayer did have adequate authority and control over corporate financial matters to have a duty to remit withholding taxes to the state.

The taxpayer contends that the president was actually the person responsible for remitting withholding taxes to Indiana. The president accepted that responsibility at the hearing. The law does not require, however, that only one person be considered the person with a duty to remit taxes to the state. In the Safayan case, the corporate president was held to be a responsible person even though the day to day operations were specifically delegated to a vice-president in his employment contract as manager. "A party may be liable for trust taxes without having exclusive control over the corporation's funds." Safayan at 274. The corporate president's acceptance of responsibility does not mean that the taxpayer did not also have a duty to remit the withholding taxes to Indiana.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0120010099.LOF

LETTER OF FINDINGS NUMBER: 01-0099
Individual Income Tax
For the Tax 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 the document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Imposition of the State's Individual Income Tax

Authority: U.S. Const. amend. XVI; Ind. Const. art X, § 8; IC 6-3-1-3.5 et seq.; IC 6-3-1-9; IC 6-3-1-12; IC 6-3-1-15; New York v. Graves, 300 U.S. 308 (1937); Merchants' Loan Trust Company v. Smietanka, 255 U.S. 509 (1921); Eisner v. Macomber, 252 U.S. 189 (1920); Doyle v. Mitchell, 247 U.S. 179 (1918); Stratton's Independence v. Hobert, 231 U.S. 399 (1913); United States v. Connor, 898 F2d 942 (3rd Cir. 1990); Wilcox v. Commissioner of Internal Revenue, 848 F2d 1007 (9th Cir. 1988); Coleman v. Commissioner of Internal Revenue, 791 F2d 68 (7th Cir. 1986); United States v. Koliboski, 732 F2d 1328 (7th Cir. 1984); United States v. Romero, 640 F2d 1014 (9th Cir. 1981); Snyder v. Indiana Dept. of State Revenue, 723 N.E.2d 487 (Ind. Tax Ct. 2000); Thomas v. Indiana Dept. of State Revenue, 675 N.E.2d 362 (Ind. Tax. Ct. 1997); Richey v. Indiana Dept. of State Revenue, 634 N.E.2d 1375 (Ind. Tax Ct. 1994)

Taxpayer is of the opinion that, because he is not a corporate entity, he is not subject to the Indiana individual adjusted gross income tax.

STATEMENT OF FACTS

Taxpayer filed Indiana individual income tax returns for 1998 and 1999. On both returns, taxpayer reported federal adjusted gross income of "0." Attached to taxpayer's 1999 return was an explanation in which taxpayer stated that, under the relevant Supreme Court decisions, taxpayer did not receive taxable income during 1999. Taxpayer requested and was erroneously granted a refund of taxes withheld for the tax years 1998 and 1999. Subsequently, the Department issued a "Notice for Payment" which is the subject of the taxpayer's protest.

DISCUSSION

I. Imposition of the State's Individual Income Tax

Taxpayer claims that the federal – and by implication, Indiana's – individual income tax is only applicable to corporate profits. Taxpayer argues that the Corporation Excise Tax Act of 1909, The U.S. Const. amend. XVI, and the Income Tax Act of 1913, 1916, and 1917 all impose a tax on the gain derived from capital or labor provided that the gain is realized from profits realized through the sale or conversion of capital assets.

Taxpayer has provided a number of Supreme Court cases which purportedly support taxpayer's basic contention. Taxpayer cites to Merchants' Loan Trust Company v. Smietanka, 255 U.S. 509 (1921) for the proposition that income tax can only be levied against corporate gains. In that case, the Court held that the when a provision in a will created a trust, the increase of the value of the trust resulted in taxable "income" under the provisions of the U.S. Const. amend. XVI. Id. In arriving at that decision, the Court stated that "the word [income] must be given the same meaning and content in the Income Tax Acts of Congress that was given to it in the Corporation Excise Tax Act and that what that meaning is has now become definitely settled by decisions of [the] court." Id. 519.

Taxpayer also cites to Eisner v. Macomber, 252 U.S. 189 (1920), in which the Court addressed the issue of whether the U.S. Const. amend. XVI permitted the government to tax a taxpayer's stock divided resulting from a corporation's accumulated profits. The Court held that the stock dividend did not involve the realization of a taxable gain but that the corporation's accumulated profits were simply capitalized or retained as surplus. Id. at 211. In effect, the taxpayer in Eisner did not realize a gain severed from and independent of the corporations' assets. Id. at 211-12. In reaching that decision, the Court stated that income is the "gain derived from capital, from labor, or from both combined." Id. at 201.

Taxpayer reads Merchant's Loan and Eisner together with certain other cases – Doyle v. Mitchell, 247 U.S. 179 (1918); Stratton's Independence v. Hobert, 231 U.S. 406 (1913) – as supporting his contention that the individual income can only be assessed against corporate gain. Taxpayer predicates this conclusion on selected case citations which, when taken together, purportedly limits the definition of "taxable income" to the definition originally established under the Civil War Income Tax Act of 1867. However, setting aside the question of the validity of taxpayer's legal analysis, taxpayer's conclusion concerning the definition of corporate income tax is ultimately irrelevant.

Taxpayer's legal analysis stands for nothing more than, when read in isolation and selectively divorced from the factual setting under which the decisions were reached, a legal argument can be proposed which will support any legal conclusion no matter how unjustified that conclusion is ultimately found. Taxpayer cites cases in which the Court was asked to determine what constituted *corporate income* under the corporate income and excise taxes in effect at the time the Court reached its conclusion. To apply Supreme Court decisions limited to determining the efficacy and application of corporate income taxes to issues related to individual income tax may yield a desired result but is not legally, logically, or intellectually sound.

As set out in the Indiana Constitution, "The general assembly may levy and collect a tax upon income, from whatever source derived, at such rates, in such manner, and with such exemptions as may be prescribed by law." Ind. Const. art X, § 8. The Indiana General Assembly exercised its constitutional prerogative by imposing an adjusted gross income tax on individuals and corporations. IC 6-3-1-3.5 et seq. In doing so, the General Assembly defined an individual subject to the adjusted gross income tax as a "natural born person, whether married or unmarried, adult or minor." IC 6-3-1-9.

Although not binding upon the state's practice of taxing the wages of its own citizens, the United States Supreme Court has definitively ruled on the question of whether a citizen's individual income may be subjected to an adjusted gross income tax. In New York v. Graves, 300 U.S. 308, 312-13 (1937), Justice Stone stated as follows:

> That the receipt of income by a resident of the territory of a taxing sovereignty is a taxable event is universally recognized. Domicile itself affords a basis for such taxation. Enjoyment of the privileges of residence in the state and the attendant right to invoke the protect of its laws are inseparable from the responsibility for sharing the costs of government.... A tax measured by the net income of residents is an equitable method of distributing the burdens of government among those who are privileged to enjoy its benefits. The tax, which is apportioned to the ability of the taxpayer to pay it, is founded upon the protection afforded by the state to the recipient of the income in his person, in his right to receive the income and in his enjoyment of it when received. These are rights and privileges which attach to domicile within the state. To them and to the equitable distribution of the tax burden, the economic advantage realized by the receipt of income and represented by the power to control it, bears a direct relationship. Neither the privilege nor the burden is affected by the character of the source from which the income is derived.

Since that 1937 decision, the federal courts have consistently, repeatedly, and without exception, determined that individual wages are income. United States v. Connor, 898 F2d 942. 943 (3rd Cir. 1990) ("Every court which has ever considered the issue has unequivocally rejected the argument that wages are not income"); Wilcox v. Commissioner of Internal Revenue, 848 F2d 1007, 1008 (9th Cir. 1988) ("First, wages are income."); Coleman v. Commissioner of Internal Revenue, 791 F2d 68, 70 (7th Cir. 1986) ("Wages are income, and the tax on wages is constitutional."); United States v. Koliboski, 732 F2d 1328, 1329 n. 1 (7th Cir. 1984) ("Let us now put [the question] to rest: WAGES ARE INCOME. Any reading of tax cases by would-be tax protesters now should preclude a claim of good-faith belief that wages – or salaries – are not taxable") (Emphasis in original); United States v. Romero, 640 F2d 1014, 1016 (9th Cir. 1981) ("Compensation for labor or services, paid in the form of wages or salary, has been universally held by

the courts of this republic to be income, subject to the income tax laws currently applicable.... [Taxpayer] seems to have been inspired by various tax protesting groups across the land who postulate weird and illogical theories of tax avoidance all to the detriment of the common weal [sic] and of themselves.").

In addressing the identical issue, the Indiana Tax Court has held that, "Common definition, an overwhelming body of case law by the United Sates Supreme Court and federal circuit courts, and this Court's opinion... all support the conclusion that wages are income for purposes of Indiana's adjusted gross income tax." Snyder v. Indiana Dept. of State Revenue, 723 N.E.2d 487, 491 (Ind. Tax Ct. 2000). *See also* Thomas v. Indiana Dept. of State Revenue, 675 N.E.2d 362 (Ind. Tax Ct. 1997); Richey v. Indiana Dept. of State Revenue, 634 N.E.2d 1375 (Ind. Tax Ct. 1994).

Taxpayer has set out a more generalized argument in which he questions the disparity between the income tax as applied to corporations and as applied to individuals. According to taxpayer, a corporation is entitled to reduce its corporate tax liability by the amount of wages it pays to its employees. In contrast, a corporate employee who receives a wage is not entitled to reduce his own tax liability upon receipt of those very same wages.

The taxpayer is certainly entitled to point out the numerous exceptions, deductions, and eccentricities contained within the federal and state tax codes. It is beyond question that corporate taxpayers are entitled to numerous exemptions which may strike the taxpayer – rightly or wrongly – as inequitable. However, it is perhaps appropriate to point out that individual taxpayers are also entitled to exemptions and exclusions to which corporate taxpayers are not entitled. Other than the observation that state and federal tax policies are subject to the shifting sands of corporate, individual, government, and societal needs and influences, it is beyond the scope of this Letter of Findings to justify or rationalize every provision of the federal and Indiana tax codes. Nonetheless, it is equally obvious that taxpayer cannot justify a conclusion – based upon the distinction between corporate and individual income tax treatment – that taxpayer is unilaterally entitled to remove himself from the tax liabilities imposed on each and every citizen of the republic.

Despite taxpayer's assertions that he somehow stands outside the taxing authority of the state, given the taxpayer had taxable income, is an "individual" as defined by IC 6-3-1-0, was a resident of Indiana for the years at issue (IC 6-3-1-12), and is a "taxpayer" as defined within IC 6-3-1-15, the statutes imposing the Individual's income tax apply with full force to taxpayer's wages.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0220010154P.LOF

LETTER OF FINDINGS NUMBER: 01-0154P
Gross Income Tax
Fiscal Years Ended 08/31/96, 08/31/97, 08/31/98

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 leases vehicles throughout the United States and had no business location in the State of Indiana. Taxpayer has leased vehicles in the state and was previously audited in 1994.

Taxpayer protests the penalty and states the assessments in the current audit do not result from any willful disregard for tax laws or regulations, but from personnel changes. Instead of accumulating and reporting all vehicle sales occurring within Indiana, only sales subject to sales tax were reported as Indiana gross income. Vehicle sales exempt from sales tax were erroneously omitted and this oversight was discovered during the auditor's examination. Procedures are now established to assure the timely payment of the gross income tax from all vehicles sold within Indiana.

I. Tax Administration – Penalty

DISCUSSION

Taxpayer was assessed a negligence penalty for failure to include all Indiana sales for gross income tax, the issue which was in the prior audit dated January 21, 1994.

Taxpayer, in a letter dated June 19, 2001 protested penalties assessed because there was no negligence or intentional disregard of Indiana tax regulations.

Taxpayer, however, failed to include all of its Indiana sales in gross income as required, which was the issue in a prior audit.

Taxpayer has not provided reasonable cause for its failure to report all Indiana income. The Department finds that a negligence penalty is proper.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420010155P.LOF

LETTER OF FINDINGS NUMBER: 01-0155P
Consumer Use Tax
Calendar Year Ended December 31, 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(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 an administrator of insurance products that was previously audited in 1995. The current audit assessed use tax for similar items and the taxpayer did not accrue use tax.

I. Tax Administration – Penalty

DISCUSSION

At issue is whether the taxpayer was negligent in reporting its consumer use tax. A prior audit containing identical issues was completed on July 31, 1995.

Taxpayer protests the penalty because it merged out of existence in 1998 and during the period under audit, was managed by employees who have been gone since 1998. Taxpayer further states that since it is no longer in business, the penalty is being enacted upon the survivors who had no input on how the predecessors ran their affairs.

A review of the current audit revealed the taxpayer made no attempt to self assess use tax on clearly taxable items and had no use tax accrual system in place. The penalty is appropriate as the taxpayer made no effort to self assess use tax and the issue was present in a prior audit.

Taxpayer has not provided reasonable cause to allow a waiver of the penalty assessed.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04980491.SLOF

SUPPLEMENTAL LETTER OF FINDINGS: 98-0491
State Gross Retail and Use Taxes
For the Years 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 the document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Sales/Use Tax Assessment on Manufacturer's Purchase of Labels: Applicability of the Gross Retail Tax to Purchases of UPC / Bar Code Labels Affixed to Taxpayer's Non-returnable Containers

Authority: IC 6-2.5-5-6; 45 IAC 2.2-5-14

Taxpayer protests the imposition of sales tax on the purchase of certain labels which are affixed to the taxpayer's non-returnable containers. The assessment was made when audit determined that, because the labels were not incorporated as a part of

the tangible personal property which taxpayer produces for resale, the initial purchase of the labels was subject to sales tax. Taxpayer argues that the purchase of the labels is exempt from sales tax because the labels are incorporated into the taxpayer's property made available for resale.

II. Sales and Use Tax Assessment on the Purchase of Printing Equipment

Authority: IC 6-2.5-5-3(b); Indiana Dept. of State Revenue v. Cave Stone, Inc., 457 N.E.2d 520 (Ind. 1983)

Taxpayer argues that the initial purchase of label printers was exempt from imposition of sales tax. Taxpayer maintains that the label printers are used in the direct production of the taxpayer's final product and, as such, the purchase of the label printers is exempt. The audit found to the contrary – determining that the printers did not qualify for the manufacturing exemption.

STATEMENT OF FACTS

Taxpayer manufacturers automobile safety parts such as lights, reflectors, and mirrors. These parts are manufactured in Indiana and then shipped to various distributors. Taxpayer requested a rehearing on certain of the issues addressed within the original Letter of Findings. The Department granted taxpayer's request and, although the taxpayer declined the opportunity to address the issues at an administrative hearing, this Supplemental Letter of Findings was based upon the taxpayer's written submission.

DISCUSSION

I. Sales/Use Tax Assessment on Manufacturer's Purchase of Labels

Taxpayer reasserts its original position that the purchase of certain labels is exempt from imposition of the state's gross retail (sales) tax. The labels at issue display UPC / Bar Code information and are fastened to the outside of the taxpayer's non-returnable containers. Inside these closed containers are multiple packages of either the taxpayer's finished goods or component parts destined for assembly elsewhere. The coded labels provide information which identifies the contents of the package and the quantity of items contained within the package. The labels serve to facilitate the movement and tracking of taxpayer's inventory within taxpayer's own warehouse facility and – according to taxpayer – serve the same purpose for the taxpayer's customers. Taxpayer asserts that the affixing of the labels is a mandatory pre-requisite to its distributor's acceptance of the packaged products. According to taxpayer, the distributors will not accept taxpayer's packaged goods if the package does not display one of the labels here at issue.

The audit determined that the labels were subject to sales tax because the labels were not "incorporated" into the taxpayer's manufactured products.

Taxpayer argues that IC 6-2.5-5-6 provides that statutory authority for its assertion that the labels are exempt from sales tax. The statute states in relevant part that, "Transactions 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 manufacturers, assembles, refines, or processes for sale in his business." In effect, taxpayer argues that the labels are "incorporat[ed] as a material part" of its automotive parts.

Departmental regulation 45 IAC 2.2-5-14 provides specific guidance in applying the general statutory rule. The regulation states that in order to find that material is incorporated into the property produced for resale, "[t]he material must be physically incorporated into and become a component of the finished product.... [t]he material must constitute a material or integral part of the finished product.... [t]he finished tangible personal property must be produced for sale by the purchaser." 45 IAC 2.2-5-14(d).

There can be little dispute that taxpayer's labels are an essential component within taxpayer's marketing and distribution process. Notwithstanding, the purchase of taxpayer's labels is not entitled to the manufacturing exemption afforded under IC 6-2.5-5-6 because the labels do not become a "material part" of the taxpayer's various automotive products. The labels do not "constitute a material or integral part of the finished product," (45 IAC 2.2-5-14(d)(2)) because the labels are not essential to the taxpayer's finished product and because the labels do not affect the performance or utility of that finished product. The labels are merely the ancillary means by which taxpayer's finished product finds its way to the ultimate consumer.

FINDING

Taxpayer's protest is respectfully denied.

II. Sales and Use Tax Assessment on the Purchase of Printing Equipment

Taxpayer argues that the initial purchase of label printers is exempt from imposition of the sales tax. Taxpayer predicates this argument upon the provisions of 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 of other tangible personal property." The court has determined that exempt equipment must constitute "an integral part of manufacturing and operate[] directly on the product during production." Indiana Dept. of State Revenue v. Cave Stone, Inc., 457 N.E.2d 520, 525 (Ind. 1983). In addition, the exempt equipment must have an "immediate link with the product being produced." Id.

Taxpayer's products consist of various automotive parts. Taxpayer's label printers act upon and produce UPC/ Bar Code labels. Accordingly, taxpayer's initial purchase of the label printers does not quality for a sales tax exemption under IC 6-2.5-5-3(b) because the label printers are not an integral part of the taxpayer's production process, and because the printers do not operate on the taxpayer's automotive products. Although the label printers may serve as indispensable part of taxpayer's overall manufacturing and distribution process, the printers stand outside of, and are removed from, taxpayer's actual production of automotive parts.

FINDING

Taxpayer's protest is respectfully denied.

DEPARTMENT OF STATE REVENUE
REVENUE RULING #2001-07 IT
August 21, 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.

STATEMENT OF FACTS

The Taxpayer is a foreign corporation that resells long distance telephone and Internet services to customers in Indiana and all other states. The Taxpayer also has broker relationships with third party vendors for the sale of products and services, including wireless communications, propane, and home heating oil. The Taxpayer does not resell these products and services but rather receives a commission for acquiring customers who deal directly with the third party vendors.

The Taxpayer conducts these business activities largely through its Internet website. Regarding its long distance telephone and Internet service resales, the Taxpayer solicits sales, facilitates billing, and provides customer support online. Customer invoices are posted on its website, and customer payments are remitted directly to the Taxpayer by credit card online. Paper billing through the mail is available by request. Regarding its brokering activities, the Taxpayer solicits customers for third party vendor products and services also through its website.

The Taxpayer relates that all of its sales and customer support functions are managed from its headquarters outside of Indiana. The Taxpayer further indicates that service offers customers make online are accepted or rejected by the Taxpayer outside of Indiana, and that the Taxpayer does not own or lease any property in any state other than the state of its headquarters.

The Taxpayer relates that it is registered in all states for required state transactional excise taxes (e.g., sales and use tax, telecommunications tax, and public utility fees) and that it has filed annual reports with all states in which it is registered to conduct business.

ISSUES, DISCUSSION, AND RULINGS

ISSUE I

Whether the Taxpayer's income from its Internet-based long distance telephone service resales, Internet service resales, and brokering activities is subject to Indiana adjusted gross income tax.

DISCUSSION I

IC 6-3-2-1 imposes adjusted gross income tax on adjusted gross income derived from sources within Indiana. IC 6-3-2-2(a) provides that adjusted gross income derived from Indiana sources includes income from "doing business" in Indiana. Rule 45 IAC 3.1-1-38, interpreting IC 6-3-2-2, provides that for apportionment purposes, a taxpayer is "doing business" in Indiana if it operates a business enterprise or activity in Indiana including, but not limited to, the following:

* * * *

(4) Rendering services to customers in Indiana;

* * * *

(7) Any other act in Indiana which exceeds the mere solicitation of orders so as to give the state nexus under P.L. 86-272 to tax its net income.

Long distance telephone and Internet service resales to customers in Indiana constitute "rendering services to customers in Indiana" under Rule 45 IAC 3.1-1-38(4). Moreover the provision of long distance telephone and Internet services to Indiana businesses and residences is business activity which exceeds the mere solicitation of orders in Indiana. Therefore, the Taxpayer's is "doing business" under IC 6-3-2-2 by rendering long distance telephone and Internet services in Indiana.

RULING I

The Taxpayer is required to file adjusted gross income tax and supplemental net income tax returns in Indiana. (Note that determinations applicable to adjusted gross income tax are also applicable to supplemental net income tax as provided by IC 6-3-8-2.)

ISSUE II

Whether the Taxpayer's income from its Internet-based long distance telephone service resales, Internet service resales, and brokering activities is subject to Indiana gross income tax.

DISCUSSION II

IC 6-2.1-2-2 imposes gross income tax on “taxable gross income derived from activities or businesses or any other sources within Indiana.” The Indiana Tax Court has outlined a three-part inquiry to determine whether non-resident income is subject to gross income tax:

(1) are the receipts “gross income,”

(2) is the gross income derived from “sources within Indiana,” and

(3) is the gross income that is derived from sources within Indiana “taxable gross income”?

First Nat’l Leasing and Fin. Corp. v. Ind. Dep’t of Revenue, 598 N.E.2d 640, 643 (Ind. Tax Ct. 1992).

(1) Gross Income

“Gross income” is defined by IC 6-2.1-1-2(a)(1) as “all the gross receipts a taxpayer receives... from trades, business, or commerce....” Gross receipts from long distance telephone resales, Internet service resales, and brokering activities all fall within the definition of gross income because they are received from commerce.

(2) Indiana Source

Income has an Indiana “source” when a taxpayer’s income-producing activities establish an Indiana “business situs.” *First Nat’l Leasing*, 598 N.E.2d at 643; *Indiana-Kentucky Elec. Corp. v. Indiana Dept. of State Revenue*, 598 N.E.2d 647 (Ind. Tax Ct. 1992). “Business situs” contributes to the establishment of gross income tax liability in Indiana, but is insufficient in and of itself to trigger the taxation of non-resident income. *First Nat’l Leasing*, 598 N.E.2d at 644.

Rule 45 IAC 1.1-1-3 explains:

(a) A “business situs” arises where possession and control of a property right have been localized in some business or investment activity away from the owner’s domicile.

(b) A taxpayer may establish a business situs in ways, including but not limited to, the following:

* * * *

(2) Performance of services.

* * * *

Consistent with Rule 45 IAC 1.1-1-3, Rule 45 IAC 1.1-2-5(a) states that gross income derived from “the provision of a service of any character within Indiana” is subject to gross income tax.

The sale of telecommunications, which includes long distance telephone and Internet services, to Indiana customers constitutes the performance of services in Indiana. 45 IAC 1.1-2-5(f)(2). As such, these sales establish an Indiana business situs under Rule 45 IAC 1.1-1-3.

The Taxpayer’s online acquisition of Indiana customers for third party vendors cannot be understood as the performance of services in Indiana because the activity takes place solely on the Internet. Therefore, commissions earned by the Taxpayer for its Internet-based gathering of Indiana customer information for third party vendor products and services does not establish an Indiana business situs under Rule 45 IAC 1.1-1-3.

(3) Taxable Gross Income

Taxation of nonresidents is basically limited to receipts from activities connected with a business situs. *First Nat’l Leasing*, 598 N.E.2d at 644. Specifically, taxpayer activities which establish business situs must be “more than minimal and not remote or incidental” to the income-producing transaction in order for the taxation of that income to be justified. *Indiana-Kentucky Elec. Corp.*, 598 N.E.2d at 663.

Rule 45 IAC 1.1-2-5(f)(2) deals specifically with the relationships and characteristics that must be present in order to tax telecommunication sales income in Indiana. The Rule states, “if the telecommunications originate or terminate in Indiana and are charged to an Indiana address, and the charges are not taxable under the laws of another state,” then Indiana gross income tax applies.

The Taxpayer’s long distance telephone and Internet service resales to Indiana customers clearly terminate in Indiana. Moreover the sales may be charged to Indiana addresses. Absent evidence presented by the Taxpayer of tax liability elsewhere, these sales are presumed to be taxable only in Indiana. Thus, Taxpayer’s long distance telephone and Internet service resales fall within the ambit of 45 IAC 1.1-2-5(f)(2).

RULING II

The Taxpayer’s income from long distance telephone service resales and Internet service resales is subject to Indiana gross income tax. The Taxpayer’s income from brokering activities is not subject to Indiana gross income tax.

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. Other taxpayers with substantially identical factual situations, however, 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, a 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 #2001-08 IT
August 1, 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.

ISSUES

Treatment of single member LLC electing under federal check-the-box regulations to be treated as a disregarded entity
Authority: Tax Policy Directive # 2
Qualification of company a taxpayer under Indiana Financial Institutions Tax ("FIT")
Authority: IC 6-5.5 et seq.
Treatment of income earned by a Factoring company under Indiana FIT
Authority: IC 6-5.5 et seq.
Attribution of interest income under Indiana FIT
Authority: IC 6-5.5-4-5
Elimination from Indiana gross income tax ("GIT") of income and deductions by member of a unitary group subject to GIT and another member of the unitary group subject to FIT
Authority: IC 6-2.1-2-11
Elimination of sales between members of unitary group, in computation of apportionment factor
Authority: 45 IAC 3.1-1.51 and 45 IAC 3.1-1-52
Classification and attribution of interest income derived from inter-company loans under FIT
Authority: IC 6-5.5-4-6

STATEMENT OF FACTS

Co. A is a publicly-traded Delaware corporation commercially domiciled in Indiana and taxed under subchapter C of the Internal Revenue Code of 1986 (IRC). Co. A is primarily a holding company with a number of operating subsidiaries. The largest operating subsidiaries are Co. B and Co. C.

Co. B is a Delaware limited partnership that has elected to be taxed as a corporation for federal and state income tax purposes. Co. B is commercially domiciled in Indiana and manufactures its products at facilities in Iowa, Tennessee, and Indiana. Co B sells its products to Co. C and to unrelated third parties throughout the United States. The partners of Co. B are Co. A, which is a 99% limited partner, and Co. C, which is a 1% general partner.

Co. C is a wholly owned subsidiary of Co. A, incorporated in Delaware and headquartered in Missouri. Co. C operates retail locations throughout the United States. These retail locations sell new and used products and parts for products. These locations also perform repair and maintenance services.

Co. A and its subsidiaries file a consolidated return for federal income tax purposes, and Co. A files an Indiana consolidated adjusted gross income tax return that includes those subsidiaries that have income from Indiana sources, including Co. B and Co. C. On a consolidated basis, the affiliated group generates in excess of $1 billion of revenue.

Co. B and Co. C make credit sales to customers and, therefore, generate accounts receivable in the normal course of their business operations. Some of these credit sales are made to Indiana customers. Co. B and Co. C offer a variety of payment terms to their customers. Some customers pay by check sent to lockbox locations and others pay by electronic funds transfer.

In order to achieve the most favorable borrowing rates against which the accounts receivable could be used as collateral, Co. B and Co. C plan to participate in an asset-backed securitization program with a national banking corporation and its conduit.

Co. A is considering creating a new corporation, Co. D, as a wholly owned subsidiary of Co. A. Co. D will be a corporation taxed under subchapter C of the IRC and commercially domiciled in Indiana. [Note: Co. D may be formed as a single member LLC electing to be taxed as a corporation] Co. D will have employees who will perform credit and collection services, cash applications, and oversight of the factoring and securitization program. Co. D cannot participate in asset-backed securitization programs because its operations do not enable it to qualify as a "bankruptcy remote" entity. Therefore, Co. D will create a single member limited liability company (Co. E). Co. E will qualify as a special purpose "bankruptcy remote" entity, as its activities will be limited to acquiring, owning, and financing accounts receivable. Co. E is prohibited from having other types of operations in order to qualify as a "bankruptcy remote" entity. Co. E will be a disregarded entity for federal income tax purposes and treated as a division of Co. D.

Co. D will purchase accounts receivable for cash without recourse, at an arm's length discount, from Co. B and Co. C. Co. D will sell to Co. E all or a portion of the accounts receivable purchased from Co. B and Co. C for cash, without recourse, at a discount. This transaction will be characterized as a sale for commercial law purposes. For federal income tax purposes, this transaction and all other transactions between Co. D and Co. E will be treated as intracompany transactions because Co. E is treated as a division of Co. D.

Co. E will sell the accounts receivable purchased from Co. D to a national banking corporation and its conduit. For federal income tax purposes, Co. E will be treated as having borrowed funds from the national banking corporation and its conduit. Since

Co. E will be treated as a division of Co. D for federal income tax purposes, all transactions entered into by Co. E will be treated as entered into by Co. D.

In addition to the income that it will earn as a result of the recovery of portions of the discount on the accounts receivable that it will purchase from Co. B and Co. C, Co. D will also earn interest on short-term investments of cash collections pending purchase of new accounts receivable and interest on intercompany loans that it makes to its affiliates, including Co. B and Co. C for general working capital.

RULING

Based solely and strictly on the information submitted in the request for ruling dated July 11, 2001, a copy of which is incorporated herein by reference, the Department hereby rules as follows:

1. Co. E will be classified as a disregarded entity under the federal "check-the-box" regulations and will be treated as a division of Co. D. (Note: Co. D may be formed as a single member LLC electing to be treated as a corporation for federal tax purposes.) For tax purposes Indiana will also treat Co. E as a division of Co. D in accordance with the provisions of Tax Policy Directive #2.
2. Under the analysis of its proposed business activity, Co. D will qualify as a taxpayer under the Indiana Financial Institutions Tax ("FIT") and shall report and pay any tax, which may be due, under the provisions of IC 6-5.5 et seq.
3. Co. D's income from the collection of accounts receivable will be the difference between the amount paid by customers in satisfaction of their accounts receivable and the amount paid by Co. D to purchase the accounts receivable from Co. B and Co. C. Since this discount will be derived from the prevailing market rates of interest and the creditworthiness of Co. B's and Co. C's customers, the recovery of this discount by Co. D will be classified as interest income under IC 6-5.5.
4. Co. B and Co. C sell products to their customers on credit. Under the proposed transactions, it would appear this extension of credit by Co. B and Co. C to their customers would constitute a consumer loan. Co. D will purchase these customer accounts receivable from Co. B and Co. C without recourse. The customers of Co. B and Co. C as obligors on the accounts receivable, will become customers of Co. D at the time the accounts receivable are sold. Co. D's interest income will be attributable to Indiana under IC 6-5.5-4-5 if such loans are made to an Indiana resident. Indiana will deem any customer to be an Indiana resident if such customer is commercially domiciled within Indiana or if such customer maintains a business situs within Indiana and such business situs is directly engaged in the sales transaction with Co. B or Co. C regardless of the company location from which the payment on the account receivable may be remitted.
5. Co. D will be included in the federal consolidated income tax return currently filed by the parent and its subsidiaries. For Indiana gross income tax ("GIT"), if an entity is subject to GIT and is a member of a unitary group of which a taxpayer subject to FIT is also a member, all income and deductions attributable to transactions between the entity and the unitary taxpayer which is subject to the FIT shall be eliminated in determining the amount of GIT imposed under IC 6-2.1-2-11. Thus Co. B and Co. C's receipts from the sale of accounts receivable to Co. D will not be subject to GIT. Additionally, any dividends that Co. A may receive from Co. D will not be subject to GIT.
6. Under the proposed transactions, Co. B and Co. C will have receipts from the sale of accounts receivable to Co. D, despite the fact that the accounts receivable will be sold at a discount, and Co. B and Co. C will have no net gain on these transactions. 45 IAC 3.1-1-51 provides that the denominator of the sales factor shall not include sales made between members of an affiliated group filing consolidated returns. 45 IAC 3.1-1-52 provides that the numerator of the sales factor shall not include sales made between members of an affiliated group filing consolidated returns. It is not the Department's position to penalize members of an affiliated group who would otherwise qualify to file a consolidated Indiana income tax return simply due to the requirement that a member would be required to file under IC 6-5.5. The Department therefore rules that Co. B and Co. C's receipts from the sale of accounts receivable to Co. D will be eliminated for purposes of the computation of Co. B and Co. C's apportionment factors for Indiana adjusted gross income tax and Indiana supplemental net income tax calculations.
7. For purposes of the Indiana FIT, Co. D's interest income from intercompany loans that it may make to affiliates for general working capital purposes shall be treated as interest income from unsecured commercial loans and attributed in accordance with IC 6-5.5-4-6. IC 6-5.5-4-6 provides that interest income from unsecured commercial loans must be attributed to Indiana if the proceeds of the loan are to be applied in Indiana. If it cannot be determined where the funds are to be applied, the income and receipts are attributed to the state in which the business applied for the loan. "Applied for" shall mean the initial inquiry or submission of a completed loan application, whichever occurs first.

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, changes in statute, a 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 #2001-08 ST
August 24, 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

Sales/Use Tax – Prepaid Telephone Services

Authority: IC 6-2.5-4-6, IC 6-2.5-4-13, IC 6-2.5-2-1

The taxpayer requests the Department to rule whether or not the taxpayer is required to collect sales tax on prepaid telephone services.

STATEMENT OF FACTS

The taxpayer sells prepaid telephone services. The taxpayer sells both prepaid local telephone service and prepaid long-distance service. The taxpayer purchases these services from another telecommunication provider.

The taxpayer bills its customers for local service on a flat rate, prepaid basis and does not collect sales tax on the billing. The taxpayer, however, when invoiced by the telecommunication provider, pays sales tax to the telecommunication provider.

The taxpayer sells long-distance service via prepaid telephone calling cards. The taxpayer does not collect sales tax on the sale of the calling cards, however, does pay the applicable sales tax to the telecommunication provider.

DISCUSSION

IC 6-2.5-4-6 provides that intrastate telecommunication services, including local and intrastate long-distance telephone services, are subject to sales tax. The statute states that a person is a retail merchant making a retail transaction when the person provides intrastate telecommunication service. Included in this definition of a retail merchant is a telecommunication provider that purchases telecommunication services from another telecommunication provider for the purpose of "reselling" the services to their customers.

Further, IC 6-2.5-4-13 states:

A person is a retail merchant making a retail transaction when a person sells:

1. a prepaid telephone calling card at retail;
2. a prepaid telephone authorization number at retail;
3. the reauthorization of a prepaid telephone calling card; or
4. the reauthorization of a prepaid telephone authorization number.

Pursuant to IC 6-2.5-2-1, retail transactions made in Indiana are subject to sales tax with the retail merchant required to collect sales tax on same.

It is clear then, the taxpayer is required to collect sales tax from its customers for prepaid local telephone service and prepaid long-distance telephone service, but, is not required to pay sales tax to its telecommunication providers.

RULING

The Department rules that the taxpayer is required to collect sales tax from its customers when it sells prepaid local telephone service and prepaid long-distance telephone service via a prepaid telephone calling card, but, is not required to pay sales tax to its telecommunication providers.

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.

STATE BOARD OF TAX COMMISSIONERS
RE: COUNTY COMPUTER SYSTEM CERTIFICATION

This policy statement is issued because the State Board of Tax Commissioners recognizes that the current rule governing computer standards for county assessment systems, 50 IAC 12, cannot be readily applied to the 2002 real property general reassessment. The existing provisions of 50 IAC 12 were promulgated in 1998, and were formulated based on the requirements of the 1995 reassessment manual (effective until March 1, 2002.) A new assessment manual was recently promulgated in response to the Indiana Supreme Court decision in Town of St. John v. State Board of Tax Commissioners. The 2002 Real Property Assessment Manual, incorporated by reference in 50 IAC 2.3, reflects an assessment process that is in some ways significantly different than that required under the 1995 Manual. Consequently, the existing computer standards contain requirements that are not entirely

consistent with the new assessment rules. To address this circumstance the State Board of Tax Commissioners (SBTC) intends, through the implementation of the policy and procedures outlined below, to honor the objectives of 50 IAC 12, and its specific provisions to the extent practical, and to certify assessment software and county assessment systems for the 2002 general reassessment. Formal amendments to 50 IAC 12 will be initiated at a later date.

Vendor Program Identification

7 All vendors of assessment software must submit each program that they offer in Indiana to the SBTC for review, and identify the counties where they either: (1) currently provide with the program; or (2) anticipate providing the program.
7 Vendors must identify all existing computer standards requirements (50 IAC 12) that their program does not comply with.

Program Requirements

7 All programs submitted for review must be capable of generating values consistent with the requirements of 50 IAC 2.3 (the 2002 real property assessment manual). This capability will be verified by demonstration of the functions identified on the 'Valuation Process Checklist' established by the SBTC and available upon request.
7 All programs must be capable of generating a ratio study. This capability will be verified using property data supplied by the SBTC.
7 All programs must meet the requirements specified by the Legislative Services Agency under the provisions of HEA 1499-2001 [P.L.198-2001]. These will be set out on a 'LSA Data Transfer Requirements' established by LSA, and available upon request (from LSA or the SBTC.) This capability will not be tested, but must be attested to by the vendor.
7 All programs must be able to export data organized according to the layout specifications in, and populate all fields specified in, the 'Critical Fields List for 2002' (established by the SBTC and available upon request), in flat ASCII files, using the codes specified in 50 IAC 12-17. This capability will be verified by demonstration.
7 All programs must have the ability to import data from the 'Critical Fields List for 2002' and incorporate it into its system for use in generating values under the requirements of 50 IAC 2.3. This requirement will not be tested, but must be attested to by the vendor.

Preliminary Certification

7 The vendor will be required to demonstrate to the SBTC that it meets the Program Requirements listed above and attest to the Program Requirements not tested.

Final Certification

7 The county assessor and the vendor will be required to identify the software and hardware that comprises the county assessment system that is to be certified.
7 The county assessor and the vendor will be required to attest that after sufficient study, demonstration, testing, and independent evaluation, they have concluded that the county system can smoothly and efficiently operate the vendor's program on the county's system in a manner that will conform to the requirements of the 2002 real property assessment manual, and the Program Requirements stated above.

Contract Provisions

7 As a condition of certification, the vendor's contract or contract amendment with the county will be required to include provisions and representations that are substantially similar to the requirements set out in 50 IAC 12, 50 IAC 13, and 50 IAC 14.
7 Vendors must include representations in their contracts that: (1) they are knowledgeable of the requirements of 50 IAC 2.3 (the 2002 real property assessment manual); (2) their programs meet the requirements of the existing computer standards (50 IAC 12) in all respects except those the vendors specifically identified in to the certification process; (3) their program, will operate on the county system in a manner that will conform to the requirements of the 2002 real property assessment manual, and the existing computer standards (50 IAC 12) in all respects except those they have specifically identified in the certification process.
7 The contract or contract amendment must provide for the vendor to reimburse the county for costs incurred as a result of the vendor's breach of the representations.
7 The certification will be automatically revoked, and contracts will become voidable by the county, as a result of the vendor's breach of the representations.

Counties (and Townships in Marion County) that use assessment system software that was developed in-house, and do not contract with a vendor, need only comply with the Final Certification requirements.

Questions regarding this policy statement may be directed to our Executive Secretary, Bill Waltz, by e-mail at bwaltz@tcb.state.in.us.

STATE BOARD OF TAX COMMISSIONERS
JON LARAMORE
CHAIRMAN