INDIANA BOARD OF TAX REVIEW
NONRULE POLICY STATEMENT 2004-01
Re: Lake County Assessors Participation in IBTR Hearings
Governing Statute: IC 6-1.1-4-34(j)
July 6, 2004

The Indiana Board of Tax Review (IBTR) will apply the following policies and practices in regard to a Lake County township assessor or county assessor attending and participating in Lake County assessment appeal hearings, as they are authorized under IC 6-1.1-4-34(j):

1. The IBTR Special Master will ask if the county assessor or township assessor (including a deputy or other authorized employee) is in attendance.
2. The IBTR Special Master will recognize any assessors in attendance, and state on the record that IC 6-1.1-4-34(j) allows the assessors to "attend and participate." Under the general authority of the IBTR, as the entity charged with conducting the adjudication, the IBTR Special Master may apply reasonable limits on exactly how the assessors will be allowed to participate. Such limits will be exercised as necessary to fulfill the primary function of the IBTR, to hear the taxpayer's appeal.
3. The IBTR Special Master will ask the assessor to identify, and state for the record, their intended role as one of the following:
   a. an observer;
   b. a participant, independent of the taxpayer;
   c. a supporter of the taxpayer;
   d. a supporter of the assessment;
   e. a witness to facts;
   f. an expert witness presenting an opinion; or
   g. a representative of the taxpayer.
4. The taxpayer must be present. Assessors cannot serve as a tax representative unless they are certified as a tax representative, have a Power-of-Attorney, and present evidence of their Disclosure to taxpayer client, all as is required by the IBTR tax representative rules. 52 IAC 1, *et seq*.
5. If the taxpayer is not present because the assessor was planning to represent the taxpayer at the hearing, but the assessor is not properly authorized under 52 IAC 1, the Special Master will reschedule the hearing.
6. If the assessor indicates they wish only to be an observer, and confidential information is brought out during the hearing, the assessor will remain liable as an assessing official for any improper disclosure of that information.
7. The assessor will be asked to confine their comments to matters directly relevant to the taxpayer's assessment – particularly if they are participating independent of the taxpayer.
8. The assessor may consult with the taxpayer rather than commenting on the record, if that is what the taxpayer desires.
9. If the assessor is speaking on behalf of the taxpayer, as a witness or otherwise at the taxpayer's request, the time used will be taken from taxpayer's allotted time; this point will be made at the outset of the hearing.
10. Assessors may testify to facts, but they will be asked, for the record, if they have firsthand knowledge.
11. Assessors may testify as assessing experts and give an opinion for the record.
12. An assessor acting independently must keep his comments to less than 5 minutes, to allow the hearing to stay on schedule.
13. A township assessor must be from the township in which the subject property is located if they want to do anything more than observe.
14. The taxpayer must express their approval on the record before an assessor may speak on their behalf.
15. The IBTR Special Master may guide the proceeding as necessary to keep matters focused on the issues relevant to the particular appeal being heard.

DEPARTMENT OF STATE REVENUE
INFORMATION BULLETIN #15
SALES TAX
AUGUST, 2004
(Replaces Bulletin #15 dated December 2002)

DISCLAIMER: Information bulletins are intended to provide non-technical 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 serve only as a foundation for further investigation and study of the current law and procedures related to its

subject matter.
SUBJECT: Application of Indiana Sales Tax to Sales of Gasoline and Special Fuels Sold Through Stationary Metered Pumps
REFERENCES: IC 6-2.5-7, 45 IAC 2.2-7

I. Gasoline: Calculating the Tax

A. The State Gross Retail (Sales) Tax applies to the total sales price of gasoline sold except for the part which constitutes Indiana Gasoline or Special Fuel Tax or Federal Excise Tax. The oil inspection fee cannot be backed out of the price to determine the net price of the fuel. (See Departmental Notice #12 for further information.)

With respect to the sale of gasoline or special fuel from a metered pump, the retail merchant shall collect for each unit sold an amount equal to:

1. The price per unit before the addition of state and federal taxes;
2. Multiplied by the current sales tax rate.

B. Aviation Fuel: The federal tax on aviation fuel is also subtracted from the total sales price before computing Indiana Sales or Use Tax.

C. Each seller is responsible for deducting the correct amount of state and federal excise tax in order to determine the base for computing sales or use tax. (See Departmental Notice #12 for the applicable state and federal excise tax rates.)

D. Price discounts and coupons offered by gasoline retailers will be treated the same as other coupons and discounts offered by other retailers. (See Information Bulletin #58)

EXAMPLE 1: A retailer offers a $.03 per gallon discount if the purchaser has a coupon card issued by the retailer. The gasoline will be sold for $.03 less than the pump price, and the retailer is required to remit the sales tax on the discounted price.

EXAMPLE 2: A manufacturer of a product offers a $1.00 discount for the purchase of gasoline. The manufacturer reimburses the retailer for the $1.00 discount. The retailer is required to remit the tax on the full price of the gasoline.

II. Prepayment of Sales Tax on Gasoline

At the time of purchase or shipment of gasoline from a qualified distributor, a retail merchant shall prepay to the qualified distributor the state gross retail tax. The amount of tax that must be prepaid under this section equals:

1. The prepayment rate per gallon of gasoline;
2.Multiplied by the number of invoiced gallons purchased or shipped.

The prepayment rate is the statewide average price per gallon, multiplied by the sales tax rate, multiplied by ninety percent (90%). The prepayment rate shall be determined semiannually, in June and December. The retail merchant must file monthly and remit sales tax which has been collected on the gasoline, less the amount of prepaid tax.

III. Exempt Sales of Gasoline Through a Stationary Metered Pump

A. All persons must pay the full pump price of gasoline sold through a stationary metered pump, whether or not an exemption certificate has been received from the purchaser.

B. If the gasoline is purchased for exempt use, the purchaser may recover sales tax paid by either of the following methods:

1. The purchaser must purchase the official form, STR-100 for gasoline. These receipts can be purchased at the Indiana Department of Revenue at cost. The signed receipts must be attached and filed on a Claim for Refund Form, (GA-110LMP). The request may be on a monthly, quarterly, semiannual, or annual status; or
2. If the purchase of gasoline is made through use of a credit card of a participating credit card company, and a proper exemption certificate has been filed by the cardholder, the company will credit the purchaser's account for the sales tax paid.

IV. Special Fuel: Calculating the Tax

A. Special fuels include those fuels commonly known as diesel fuel, LPG, propane, compressed natural gas, and compressed methane. Fuels which are not gasoline by statute will be considered a special fuel.

B. The Sales Tax is applied to the total sales price of the special fuel sold (except for the part which constitutes Indiana Special Fuel Tax or Federal Excise Tax) unless the retail merchant designates the metered pumps by a sign that reads "TRUCKS ONLY". To do this, a retail merchant must place at the pump a sign that states that fuel dispensed from the metered pump may only be placed in the fuel supply tanks of a truck. A sign that reads "TRUCKS ONLY" is sufficient to meet the requirements. If the purchaser does not issue an exemption certificate indicating that the vehicle is engaged in public transportation, and uses a "truck only" pump, the sales tax is required to be charged to the purchaser. The sales tax will be the sales tax rate times the raw price of the fuel which excludes state and federal excise taxes.

A retail merchant may not dispense special fuel from a metered pump that is designated for "TRUCKS ONLY" into the supply tank of a vehicle that is not a truck.

A retail merchant is not required to display the total price per unit of the special fuel on a metered pump, if that particular metered pump is designated for "TRUCKS ONLY".

C. Each seller is responsible for deducting the correct amount of state and federal excise tax in order to determine the base for computing sales or use tax.

V. Exempt Sales of Special Fuel Sold Through a Stationary Metered Pump Designated "TRUCKS ONLY"

A. The retail merchant may accept a properly completed exemption certificate from the purchaser of diesel or other special fuel where the sales tax is not required to be included in the pump price. The purchaser must be registered as a retail merchant.

B. Exemption certificate Form ST-105 is normally used to certify exempt use. Exemption certificate Form ST-135 may be used only if the purchaser is engaged in public transportation but is operating under another person's motor carrier permit. Farmers or others hauling their own products are not eligible for the exemption for persons engaged in public transportation. The purchaser must be predominately engaged in providing public transportation of persons or property.

VI. Exempt Sales of Special Fuel Through a Stationary Metered Pump with the Sales Tax Included in the Pump Price

A. All persons must pay the full pump price of special fuel sold through a stationary metered pump which is not designated for "TRUCKS ONLY", unless an exemption certificate has been received from the purchaser.

B. If the special fuel is purchased for exempt use and tax is paid, the purchaser may recover sales tax paid by either of the following methods:

1. The purchaser must purchase the official Form STR-100. These receipts can be purchased at the Indiana Department of Revenue at cost. The signed receipts must be attached and filed on a Claim for Refund Form, (GA-110LMP). The request may be on a monthly, quarterly, semiannual or annual basis; or
2. If the purchase of special fuel is made through use of a credit card of a participating credit card company, the company may credit the purchaser's account for the sales tax paid, if a proper exemption certificate has been filed by the cardholder.

VII. Display of Price on Pump

A. Gasoline. The pump price of all gasoline sold through a stationary metered pump must include the total price per unit, including state sales tax.

B. Special Fuel. Sales tax on the sale of special fuel sold through a stationary metered pump designated for "TRUCKS ONLY" may not be included in the pump price.

Sales tax on the sale of special fuel sold through a stationary metered pump which is not designated for "TRUCKS ONLY" must include the sales tax.

VIII. Advertised or Curb Price of Gasoline and Special Fuel

The retail merchant may not advertise a price which is different than the pump price required to be displayed on the metered pump.

If a retail merchant advertises special fuel at a price that does not include any gross retail taxes that may be due on the sale of the special fuel, the retail merchant must display in easily read lettering, above or below the advertised price, the words "EXEMPT TRUCKS ONLY".

IX. Service Station Nontaxable Transactions

A. Labor charges separately stated on repair orders are not subject to sales tax. (Sales tax must be collected on any parts used unless the purchaser issues an exemption certificate certifying exempt use.)

B. Charges for washes, lubrications, polishing, and waxing are not subject to sales tax. (The service station must pay sales or use tax on the purchase of any supplies consumed.)

X. Purchases by Service Stations

A. Sales or use tax is due on the purchase or use of all supplies, equipment, parts, building repairs, etc., which are not to be resold. Examples of such purchases are:

1. Grease and greasing equipment;
2. Car washing and waxing supplies, materials, and equipment;
3. Soap, towels, brooms, paint, and all other cleaning and maintenance items;
4. All tools, equipment, and utilities used in operating the station;
5. All products taken from stock for personal use by owners or given to employees as part of their compensation; or
6. Those items purchased to be given away as part of a sales promotion such as soft drinks, glassware, candles, etc.

Kenneth L. Miller
Commissioner

DEPARTMENT OF STATE REVENUE
INFORMATION BULLETIN #93
INCOME TAX
AUGUST 2004

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, the 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: Ethanol Production Tax Credit

REFERENCES: IC 6-3.1-28

INTRODUCTION

P.L.224-2003, SECTION 200, effective January 1, 2004 provides a new tax credit for ethanol production. The credits can be applied against the sales tax, the adjusted gross income tax, the financial institutions tax, and the insurance premiums tax.

I. ETHANOL PRODUCTION TAX CREDIT

Ethanol is defined as agriculturally derived ethyl alcohol. A taxpayer that produces ethanol at a facility located in Indiana that has the capacity to produce at least forty million (40,000,000) gallons of ethanol a year or which after December 31, 2003 increased its ethanol production capacity by at least forty million (40,000,000) gallons per year may qualify for the credit.

A taxpayer that produces ethanol is entitled to a credit against the taxpayer's state tax liability equal to the product of twelve and one-half cents ($.125) multiplied by the number of gallons of ethanol produced at the Indiana facility.

The total amount of credits allowed a taxpayer may not exceed a total of five million dollars ($5,000,000) for all taxable years. The total amount of credits for all taxpayers may not exceed ten million dollars ($10,000,000) in all taxable years.

II. APPLICATION FORM AND APPROVAL OF THE TAX CREDIT

Taxpayers desiring to claim the ethanol production tax credit must file a claim for credit on Form EP-100 Ethanol Production Credit Application, which is available at the Department's web site (www.in.gov/dor/taxforms/f&eforms).

The claim for credit must be completed by the taxpayer and filed with the Department for approval. The "approved" claim will be returned to the applicant to be attached to all returns for which the credit is taken. The credit can be filed on a monthly, quarterly, semi-annual or annual basis depending on which tax type the taxpayer is claiming the credit against. Failure to submit the approved EP-100 with the tax return will result in the credit being denied by the Department.

III. ADMINISTRATION OF THE TAX CREDIT

Qualifying taxpayers include pass through entities such as S Corporations, partnerships, limited liability companies, and limited liability partnerships. If the pass through entity is entitled to a credit, but does not have state tax liability to which the credit can be applied, a shareholder, partner, or member of the pass through entity is entitled to the credit in the same percentage as the person's distributive income to which the person is entitled.

If the credit is applied against the taxpayer's adjusted gross income tax, financial institutions tax, or insurance premiums tax, the credit shall be taken on the annual return filed by the taxpayer. If the credit is applied against a taxpayer's sales tax liability, the taxpayer is required to obtain a direct pay permit in accordance with IC 6-2.5-8-9. A taxpayer may not take a credit against sales tax collected as a retail merchant, but may take a credit against use tax due on its taxable purchases.

If the credit claimed exceeds the taxpayer's state tax liability for the taxable year, the taxpayer may carry over the excess to the following taxable years. The taxpayer is not entitled to a refund or carryback of any unused credits.

Kenneth L. Miller
Commissioner

DEPARTMENT OF STATE REVENUE

<u>IN REGARDS TO THE MATTER OF:</u>
HAMMOND LODGE 570
LOYAL ORDER OF MOOSE, INC.
DOCKET NO. 29-2004-0036

AMENDED DEPARTMENTAL ORDER

An administrative hearing was held on Tuesday, March 16, 2004 in the office of the Indiana Department of State Revenue, 100 N. Senate Avenue, Room N248, Indianapolis, Indiana 46204 before Bruce R. Kolb, Administrative Law Judge acting on behalf of and under the authority of the Commissioner of the Indiana Department of State Revenue.

Petitioner, Hammond Lodge #570, was represented by Gregory Francis, David Coppage, and Norman Chumley. Steve Carpenter appeared on behalf of the Indiana Department of State Revenue.

On January 5, 2004, the Department suspended the Petitioner from obtaining a "Festival" license for a period of two (2) years, and Petitioner was assessed civil penalties in the amount of seven thousand dollars ($7,000). The Petitioner protested in a timely manner. A decision was rendered April 28, 2004.

Following due consideration of the entire record, the Administrative Law Judge's Proposed Departmental Order is hereby amended and should read as follows:

The Petitioner's appeal is denied in whole. Petitioner is suspended from obtaining a "Festival" license for a period of two (2) years, and Petitioner is liable for penalties in the amount of seven thousand dollars ($7,000).

1) Administrative review of this proposed decision may be obtained by filing, with the Commissioner of the Indiana Department of State Revenue, a written document identifying the basis for each objection within fifteen (15) days after service of this proposed decision. IC 4-21.5-3-29(d).

2) Judicial review of a final order may be sought under IC 4-21.5-5.

THIS AMENDED DEPARTMENTAL ORDER SHALL BECOME THE FINAL ORDER OF THE INDIANA DEPARTMENT OF STATE REVENUE UNLESS OBJECTIONS ARE FILED WITHIN FIFTEEN (15) DAYS FROM THE DATE THE ORDER IS SERVED ON THE PETITIONER.

Dated: ____________________ ______________________________

Bruce R. Kolb / Administrative Law Judge

DEPARTMENT OF STATE REVENUE

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LETTER OF FINDINGS NUMBERS 96-0477, 96-0478 & 96-0413
SALES TAX and WITHHOLDING TAX
For Tax Periods: 1992-1995

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 specific issues.

ISSUES

I. Sales and Withholding Tax –Best Information Available Assessment

Authority: IC § 6-8.1-5-4; *Howland v. Indiana Department of Revenue,* Indiana Tax Court, 49T10-9611-TA-168, June 19, 2003

The taxpayer protests the Department's computation of tax due based on available records.

II. Sales and Withholding Tax – Validity of Extension Agreement

Authority: *Indiana Supreme Court D&M Healthcare, Inc. et al., v. Joseph E. Kernan, in his official capacity as Governor of the State of Indiana, et al.*; Indiana Supreme Court, 49S05-0310-CV-437, December 17, 2003

The taxpayer protests that an agreement to extend time for the audit was invalid.

STATEMENT OF FACTS

The taxpayers (hereinafter taxpayer) are 3 separate business entities operated by the same individual and selling and installing satellite dish systems throughout the audit period. Audits of each of these entities resulted in assessments for under payment of sales and use tax. One of the issues raised in the taxpayer's protest was the assessment of sales tax on labor charges for the satellite dish system installation. By mutual agreement, taxpayer and Department deferred the hearing on this assessment until the *Howland* case (*Howland v. Indiana Department of Revenue,* Indiana Tax Court, 49T10-9611-TA-168, June 19, 2003) was resolved by the tax court, agreeing at the time that the resolution of the *Howland* case would be dispositive of this issue. The *Howland* case was decided by the Indiana Tax Court in June of 2003 and taxpayers and Department held a hearing on the remaining issues, related to the assessment based on best information available and a question as to the validity of an extension of time for the 1992 audit. The hearing was held and final documents for Departmental review were submitted on February 16th, 2004. This letter of findings results.

I. Sales and Withholding Tax- Best Information Available Assessment

DISCUSSION

The overlying issue for the taxpayer's protest is the audit's assessment of tax based on inferences drawn from taxpayer federal returns and stated gross receipts of taxpayer. Taxpayer argued during the audit that insufficient time was provided for the preparation and presentation of records. Taxpayer now asserts that the passage of time has rendered the task of preparing and presenting the records overwhelming and onerous. The consistent theme throughout has been the request by the Department for source documentation and taxpayer's inability to provide the documentation.

As part of the protest taxpayer did submit additional documentation purporting to demonstrate the over reporting of income for the periods in question. A review of this documentation finds that the summary records provided cannot be reconciled to income as reported on the taxpayer's Federal 1120 returns for the period in question. Additionally, taxpayer documents again break out the service charge from the product cost, contrary to the holding in *Howland v Indiana Department of Revenue,* Indiana Tax Court, 49T10-9611-TA-168, arguing that the court ruled incorrectly on this matter and requesting the department overturn the court's ruling, a procedural impossibility (and absurdity) that the department respectfully declines.

Despite the absence of source documents, 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 department is required to accept assertions as to the nature of the transactions based solely on taxpayer's assertions. Taxpayer's argument, that the department is required to ignore available source documentation –including federal returns prepared and filed by taxpayer- and give credit for documentation not provided in light of the available source documentation demonstrating taxpayer's intentional misreporting and subsequent underpayment of tax, is not sustainable.

FINDING

The taxpayer's protest is denied.

II. Sales and Withholding Tax- Validity of Extension Agreement

Taxpayer argues that an extension of time that was executed by the auditor and taxpayer's representative was invalid due to a clerical error in its preparation. Taxpayer makes much of the fact that the year extended was written as "199" rather than "1992" As stated in the *Indiana Supreme Court D&M Healthcare, Inc. et al., v. Joseph E. Kernan, in his official capacity as Governor of the State of Indiana, et al.*; Indiana Supreme Court, 49S05-0310-CV-437, December 17, 2003, the applicable legal doctrine of "de minimis non curat lex" (the law does not redress trifles) requires a denial of this argument. Inasmuch as the only year at issue for the extension of time was 1992, and that subsequent to the error and after the execution of the extension of time no request was made by the taxpayer for clarification of the issue and the audit for the period at issue was allowed to continue without protest from taxpayer until taxpayer raised the issue during the protest period- well after the time for a new extension to be executed- indicate that the extension, as prepared and executed, was intended and understood and acted upon by both parties as applying to the 1992 period. Taxpayer, having affirmed through his representative a willingness to extend the time for assessment, cannot now assert that a clerical oversight, unobserved, unnoted, and unchallenged by either party at the time, can retroactively reverse this agreement.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20000017.LOF

LETTER OF FINDINGS NUMBER: 00-0017
USE TAX
For Years 1996, 1997, AND 1998

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. Use Tax—Activities exempted from use tax as "manufacturing"

Authority: IC 6-2.5-2-1; IC 6-2.5-4-1; IC 6-2.5-3-2; IC 6-2.5-5-3(b); 45 IAC 2.2-5-8(c); 45 IAC 2.2-5-26(d); 45 IAC 2.2-4-27; *Rotation Products Corp. v. Department of State Revenue*, 690 N.E.2d 795 (Ind. Tax Ct. 1998); *Ind. Dep't of State Revenue v. Interstate Warehousing, Inc.*, 783 N.E.2d 248 (Ind. 2003); 45 IAC 2.2-5-10(k); *Mid-America Energy Resources v. Indiana Dep't of State Revenue*, 681 N.E.2d 259 (Ind. Tax Ct. 1997); *Mechanics Laundry & Supply v. Indiana Dep't of State Revenue,* 650 N.E.2d 1223 (Ind. Tax Ct. 1995); *Schulte Oil Co. v. State Tax Comm'n*, 882 P.2d 65 (Okla. 1994)

Taxpayer protests the classification of certain production activities as not entitled to exemption from Indiana use tax by way of the manufacturing exemption.

II. Penalty—Ten percent negligence penalty imposed

Authority: IC 6-8.1-10-2.1(d)

Taxpayer requests waiver of the 10% negligence penalty imposed for failure to use ordinary business care.

STATEMENT OF FACTS

Taxpayer is a Delaware corporation that is commercially domiciled in Indiana. The company is in the business of processing, assembling, packaging, distributing, refurbishing, and repairing wireless communication products, primarily cellular telephones and related accessories. The audit determined that several items purchased for use in the business were not purchased for purposes of manufacturing, but rather were purchased for non-exempt uses such as for "kitting" and repair services and office use. A timely protest was filed, with this Letter of Findings resulting.

I. Use Tax—Manufacturing exemption

DISCUSSION

Pursuant to IC 6-2.5-2-1, a sales tax, knows as state gross retail tax, is imposed on retail transactions made in Indiana. Retail transactions involve the transfer of tangible personal property. IC 6-2.5-4-1. A complementary excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible property in Indiana if the property was acquired in a retail transaction. IC 6-2.5-3-2.

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 … processing … or finishing of other tangible personal property. IC 6-2.5-5-3(b). Equipment purchased for direct use in direct production must have an immediate effect on the article being produced. 45 IAC 2.2-5-8(c). Property has an immediate effect on the article being produced if it is an essential part of an integrated process that produced tangible personal property. *Id*.

Office supplies, magazines, pager rental, etc.

Taxpayer contends that it is in the business of processing, assembling, packaging, and distributing wireless communication products and that these activities allow it to make use of an exemption from the sales/use tax for items purchased in furtherance of its business. IC 6-2.5-5-3. The audit revealed several items of which no manufacturing purpose could be demonstrated. These items included office supplies and other items that are not directly incorporated into the finished product. IC 6-2.5-3-2 covers such items as office supplies and equipment, software, printed material, etc. Taxpayer failed to remit use tax on several of these items. Also, 45 IAC 2.2-5-26(d) specifically requires payment of use tax for magazines and periodicals that are not newspapers. Finally, 45 IAC 2.2-4-27 requires the payment of use tax for the rental of tangible personal property. The renting of pagers for office personnel is covered under this provision.

For all of these items, the taxpayer is respectfully denied.

"Kitting"

The taxpayer engages in an activity referred to as "kitting," whereby an unusable product with the potential to become a cell phone is transformed into a workable phone by such things as the installation of SIMM (single inline memory module) chips and batteries. The phones are eventually sold to consumers, albeit not by the taxpayer.

Under the analysis in *Mid-America Energy Resources v. Indiana Dep't of State Revenue*, 681 N.E.2d 259 (Ind. Tax Ct. 1997), the type of production subject to the manufacturing exemption is any activity that creates a marketable good from an unmarketable good. This classification was upheld in *Rotation Products Corp. v. Department of State Revenue,* 690 N.E.2d 795 (Ind. Tax Ct. 1998). The case of *Ind. Dep't of State Revenue v. Interstate Warehousing, Inc.*, 783 N.E.2d 248 (Ind. 2003) takes the analysis a step further in requiring that these marketable goods actually be sold to consumers at some point down the stream of commerce. This sale distinguishes the taxpayer's activities from the activities of the taxpayer in *Interstate Warehousing*, where the taxpayer lost because the liquid ammonia it produced was merely a byproduct of the chilling process that it sold to customers. The liquid ammonia itself was never sold to an ultimate customer. The taxpayer's "kitting" process produces a marketable good that is sold by its customers.

However, the regulations don't let taxpayer off the hook so easily. In order to be covered by the exemption, a processed or refined end product, however, must be substantially different from the component materials used. 45 IAC 2.2-5-10(k).

Here, taxpayer has merely taken the components of a cell phone and put them together. A functioning cell phone is substantially different from a non-functioning cell phone only in the metaphysical sense. Just as when a functioning cell phone breaks and does not cease to be a cell phone, a nonfunctioning cell phone does not become a cell phone merely because it has the capability of placing and receiving calls. One may have a different value in the hands of the end-user, but the test is not one of valuation. The test is of substantial change, and taxpayer has failed to prove to the Department that the change in this instance is substantial.

Therefore, with regard to its "kitting" activities, taxpayer is respectfully denied.

Refurbishing and repair work

In its written brief to the department, the taxpayer admits that a "substantial (but not complete) portion of the proposed assessment" is eligible for exemption pursuant to IC 6-2.5-5-3. (parentheses added). In recognition of this substantial portion, the auditor in her summary performed on October 18, 1999, allowed taxpayer to claim that 70% of its refurbishing activities fell under the exemption. The taxpayer claimed, and the auditor agreed, that the remaining 30% of the taxpayer's activities fell under the guise of "repair" work that is not exempt from tax. Repairs are not afforded the exemption status conferred by 45 IAC 2.2-5-8, and *Rotation Products*, cited by the taxpayer in its protest, affirms that notion when a general repair activity creates no new products. See also *Mid-America Energy Resources*, 681 N.E.2d at 263 and *Mechanics Laundry & Supply v. Indiana Dep't of State Revenue*, 650 N.E.2d 1223, 1229-30 (Ind. Tax Ct. 1995).

The court determined that, in its remanufacture process, the taxpayer in *Rotation Products* created a new product when it took an unusable roller bearing and created a new product, i.e., a remanufactured roller bearing. Similar to that, taxpayer creates a new product when it transforms unusable and inactive cell phones into usable and active cell phones that are ultimately sold at retail. An estimated 70% of taxpayer's business is in the manufacture of refurbished phones.

The remaining 30% of taxpayer activities are repairs, by which the activity undertaken restores usability to a once usable phone. The Indiana Tax Court, in *Rotation Products*, cites to an Oklahoma case in distinguishing between a repairer and a manufacturer. "Ordinarily a repairer furnishes labor and material to the owner of an article for the purpose of restoring its normal condition. In this situation, the article remains the property of those for whom the service is performed. A manufacturer, on the other hand, purchases the article it ultimately transforms into a usable product and then puts it on the market." 690 N.E.2d at 801 footnote 12, citing *Schulte Oil Co. v. State Tax Comm'n*, 882 P.2d 65 (Okla. 1994). It is through this distinction that exemptions for repair work can be denied, as it becomes clear that a repair does not result in the creation of a new product. Rather, repair results in the restoration of an existing product.

The Indiana case of *Mechanics Laundry* also lends itself to the finding that repair work is not to be considered the production of tangible personal property for which the exemption applies. In that case, the taxpayer's services of laundering and repairing soiled and damaged textiles were held to be non-exempt activities. 650 N.E. 2d at 1229-30. "Mechanics Laundry does not produce goods or items of tangible personal property. … Its washing machines, driers, and other equipment are not used in an overall process directed to the production of textiles. They are used to perpetuate textiles that were produced by others." *Id*.

Therefore, with regard to the 30% of the taxpayer's process that falls into the category of repair, the taxpayer is respectfully denied.

FINDINGS

The taxpayer is respectfully denied.

II. Penalty—Negligence penalty

IC 6-8.1-10-2.1(d) provides:

> If a person subject to penalty imposed under this section can show that the failure to file a return, pay the full amount of tax shown on the person's return, timely remit the 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.

With respect to the failure to remit use tax on office supplies, magazines, pager rental, etc., no reasonable cause is shown. With respect to the 30% of the taxpayer's refurbishing business that has been established to be repair work not subject to exemption from use tax, no reasonable cause is shown for the failure to remit use tax on items purchased in furtherance of these activities.

FINDINGS

The taxpayer is respectfully denied with regard to the 10% negligence penalty.

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 02-0348
Sales/Use Tax
For the Years 1998, 1999, 2000

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

ISSUES

I. Sales/Use Tax-Exemption for rental property

Authority: IC 6-2.5-5-8; 45 IAC 2.2-4-27.

Taxpayer protests the assessment of sales/use tax with respect to several additional assets, car mats, oil, oil filters, brake pads and parts, windshield washer fluid and blades, tire repairs and wheel nuts used in its rental automobiles

II. Tax Administration-Penalty

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

Taxpayer protests the imposition of penalty for negligence.

STATEMENT OF FACTS

Taxpayer is a business engaged in renting cars, primarily for insurance replacement for stolen and damaged vehicles. As part of its business, taxpayer purchased various supplies and equipment, including car mats, oil, oil filters, brake pads and parts, windshield washer fluid and blades, tire repairs and wheel nuts. As a result of audit, taxpayer was assessed use tax with respect to the property. In addition, various other purchases of the taxpayer were assessed use tax upon review of invoices showing that no sales tax had been paid at the time of purchase. Taxpayer protests the assessment of sales/use tax and penalty.

I. Sales Tax-Exemption for rental property

DISCUSSION

Taxpayer protests the imposition of sales/use tax with respect to its purchases of car mats, oil, oil filters, brake pads and parts, windshield washer fluid and blades, tire repairs and wheel nuts. While the rental of personal property is exempt from taxation under Ind. Code § 6-2.5-5-8, taxpayer claims that the exemption should extend to its purchases of various tangible personal property items based on the theory that the items are not "consumed" within the meaning of 45 IAC 2.2-4-27.

With respect to all of these items other than the car mats and windshield washer fluid, the items are not fuels or other items which are consumed within the meaning of the regulation; rather, the items are essentially part of the car, whose rental is exempt. However, with respect to the car mats and windshield washer fluid, taxpayer has not presented an argument that would permit the Department to recognize the exemption claimed by taxpayer for these items based on the items being part of the automobile or otherwise not consumable.

Taxpayer also protests the imposition of sales tax with respect to several assets, which taxpayer claims include labor charges or for which sales tax had been paid. The auditor removed certain items from the amount subject to tax after taxpayer provided additional evidence.

FINDING

Taxpayer's protest is sustained with respect to the tax imposed oil, oil filters, brake pads and parts, and windshield washer blades, tire repairs and wheel nuts. Taxpayer's protest is sustained to the extent taxpayer provided additional information to the auditor. Taxpayer's protest with respect to the tax due on car mats and windshield washer fluid is denied.

II. Tax Administration-Penalty

DISCUSSION

Taxpayer also protests the imposition of a 10% penalty for negligence. Penalty waiver is permitted if the taxpayer shows that the failure to pay the full amount of the tax was due to reasonable cause and not due to willful neglect. Ind. Code § 6-8.1-10-2.1. The Indiana Administrative Code further provides:

> (b) "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.
>
> (c) The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section. Factors which may be considered in determining reasonable cause include, but are not limited to:
>
> (1) the nature of the tax involved;
> (2) judicial precedents set by Indiana courts;
> (3) judicial precedents established in jurisdictions outside Indiana;
> (4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc.;
> (5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.
>
> Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

45 IAC 15-11-2.

Taxpayer has claimed that it was not willfully negligent, and therefore should not be subject to penalty. However, the test is not one of willful neglect, a standard tantamount to fraud. The standard is one of meeting the standard of care expected of a normal taxpayer, either in terms of filing or recordkeeping. Taxpayer has not presented any evidence that it met this standard.

FINDING

Taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420020478.LOF

LETTER OF FINDINGS NUMBER: 02-0478
Indiana Gross Retail and Use Tax
For 1999 and 2000

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

ISSUE

I. Propane Tanks – Use Tax.

Authority: IC 6-2.5-5-8; Tri-States Double Cola Bottling Co. v Department of State Revenue, 706 N.E.2d 282 (Ind. Tax Ct. 1999); Department of State Revenue v. Indianapolis Transit System, 356 N.E.2d 1204 (Ind. Ct. App 1976); 45 IAC 2.2-5-15(b); Black's Law Dictionary (7th ed. 1999).

Taxpayer protests the proposed assessment of Indiana use tax on the purchase price of propane storage tanks which taxpayer later furnished its customers. Taxpayer maintains that the tanks are "leased" to its customers and that, as a result, the tanks are not subject to the use tax assessment.

STATEMENT OF FACTS

Taxpayer is an Indiana corporation in the business of supplying customers with propane (L.P.) gas. Taxpayer has a business location out of which a limited number of retail sales take place. However, the bulk of taxpayer's business consists of delivering gas to its customers.

During 2001 and 2002, the Department of Revenue (Department) conducted an audit review of taxpayer's business records and tax returns. As a result of that review, the Department concluded that taxpayer owed additional amounts of use tax. Taxpayer disagreed with a portion of the assessment and submitted a protest to that effect. An administrative hearing was conducted during which taxpayer explained the basis for its protest. This Letter of Findings results.

DISCUSSION

Taxpayer purchased propane tanks which it then provided to its customers. In purchasing the tanks, taxpayer did not pay sales tax. The audit determined that the tanks were not purchased for an exempt purpose and assessed use tax accordingly. The audit did so because it concluded that, although the customers paid to use the tanks, the tanks were not "leased" to taxpayer's customers. The audit listed the following reasons justifying the conclusion that the tanks were not leased.

1. The tanks were placed on the customers' property for the convenience of the taxpayer in order to make it possible for taxpayer to sell propane to those customers.
2. Taxpayer retained complete control over the tanks, and the customers could not – under the contract agreement or state law – purchase propane from another dealer.
3. Taxpayer retained the right to enter and leave that portion of the customers' property on which the tanks were located.
4. The parties' lease agreement stipulated that the tanks would remain taxpayer's personal property.

Taxpayer maintains that its initial purchase of the propane tanks was not subject to imposition of the Indiana gross retail (sales) tax. Although taxpayer does not specifically say as much, presumably taxpayer is claiming an exemption pursuant to IC 6-2.5-5-8 which states in part that, "Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for resale, rental, or leasing in the ordinary course of his business without changing the form of the property." The exemption provided for under IC 6-2.5-5-8 is amplified at 45 IAC 2.2-5-15(b) which provides, as a general rule, that "[s]ales of tangible personal property for resale, rental or leasing are exempt from tax if all of the following conditions are satisfied: (1) The tangible personal property is sold to a purchaser who purchases this property to resell, rent or lease it; (2) The purchaser is occupationally engaged in reselling, renting or leasing such property in the regular course of his business; and (3) The property is resold, rented or leased in the same form in which it was purchased."

The Indiana courts have provided guidance in determining whether a transaction between parties constitutes a lease agreement. In Department of State Revenue v. Indianapolis Transit System, 356 N.E.2d 1204 (Ind. Ct. App 1976), the court of appeals stated that "[w]hether certain circumstances created a lessor – lessee... relationship between the parties is a matter of fact dependent on possession of and control over the property involved." Id. at 1209. While finding that the Department's regulation did not contain a definition of "lease," the Tax Court in Tri-States Double Cola Bottling Co. v Department of State Revenue, 706 N.E.2d 282 (Ind. Tax Ct. 1999), concluded that a "lease" constituted the "transfer of a right to possession and use of goods for a term in return for consideration." Id. at 285.

Taxpayer enters into agreements with its customers to provide the customers with propane tanks. The agreements fall into essentially two categories; small tank agreements and large tank agreements. In implementing the small tank agreements, taxpayer purchased 120 gallons tanks which cost approximately $200 each. Taxpayer then furnished those tanks to its customers charging each customer $40 per year. Despite the terms of the parties' agreement, taxpayer apparently did not require that each small tank customer purchase a minimum amount of gas each year. Rather, the records demonstrate that a number of the small tank customers purchased a negligible amount of propane each year. Nonetheless, each small tank customer was charged $40 annually regardless of the amount of propane which the customer purchased that year.

Taxpayer also bought larger tanks which were furnished to certain of its customers. The large tank customers were charged a flat fee of $1 per year. However – unlike the small tank customers – the large tank customers paid a premium on the gas which was supplied to the customer. For example, during one pricing period, taxpayer charged its large tank customers $.66 for each gallon of propane delivered to those customers. In contrast, during the same pricing period, taxpayer charged $.55 for each gallon of propane that was delivered to a customer which did not use one of the taxpayer's large tanks. In those instances in which the lesser price was charged, the customer owned his own tank, did not need one of taxpayer's large tanks, and avoided the $.11 "premium" which the large tank customers paid. The $.11 price differential represented the amount that the large tank customer paid taxpayer for the privilege of using one of taxpayer's large tanks. In effect, each large tank customer paid $1.00 per year plus an additional premium based upon that customer's gas usage. Under the terms of the parties' agreement, each large tank customer was required to make a minimum yearly propane purchase "equal to two times the stated capacity of said tank as a minimum purchase requirement." Therefore, if a large tank customer obtained a 500 gallon tank, that large tank customer was required to purchase a minimum of 1,000 gallons of propane each year. If the customer failed to do so, taxpayer had the option of replacing the 500 gallon tank with smaller capacity tank.

Taxpayer's small and large tank customers signed the same "lease agreement" when the customers acquired one of taxpayer's propane tanks. That agreement requires that the customer purchase "his entire requirements of Propane gas form [taxpayer] and permit[] no other person, firm or corporation to store or fill said tank with propane or to service said equipment without [taxpayer's] prior written consent."

The customer is required to "permit [taxpayer] or its Authorized representative free and unlimited ingress, egress and access to and from [customer's] premises to deliver propane gas, service, inspect, or maintain said tank and equipment."

Under the terms of the agreement, the customer is not permitted to "remove said tank or equipment from [the customer's] premises." In addition, the tank "remain[s] the personal property of [taxpayer]."

Taxpayer's agreements with both the small and large tank customers do not constitute lease agreements because the customers do not come into "possession" of the tanks. "Possession" means the right to "exercise control over something to the exclusion of all others." Black's Law Dictionary 1183 (7th ed. 1999). By the terms of the agreement, the customer is not entitled to move the tanks or to allow another supplier to fill the tanks with the competitor's propane supply. Of course, the tanks are located on the customers' property, but that does not mean that the customers have "possession." Although the tank is located on the customer's property, taxpayer retains most of the rights to control the tank. Unlike an actual lease agreement, the customer does not acquire the usual rights to control the object of the lease. Instead the tanks are merely an extension of the agreement by which taxpayer provides propane to its customers with the customer assessed an additional cost for the use of the storage container which – by nature of the transaction – is necessarily located on the customer's property. The fact that the parties' agreement is called a "lease" does not change the fact that taxpayer is not in the business of leasing propane tanks nor the fact that the customers are not interested in leasing propane tanks. Taxpayer's interest lies in selling its product to its customers and receiving compensation for the cost of doing so. The customers' interest is in obtaining that fuel. Given the fact that the tanks have a limited decorative or utilitarian value outside of their capability of storing taxpayer's propane, it is apparent that the object of the parties' agreement is the delivery, storage, and consumption of propane.

Neither the law nor the dictates of simple common sense allow a conclusion that taxpayer purchased the tanks in order to lease the tanks to its customers. Under IC 6-2.5-5-8, taxpayer is not "occupationally engaged" in the business of leasing storage tanks in the ordinary course of its business. Under 45 IAC 2.2-5-8(b), taxpayer is not "occupationally engaged" in renting propane tanks in the regular course of its business. Common sense dictates a finding that taxpayer is in the business of selling propane to customers who are interested in obtaining that fuel. The fact that the sale of propane necessarily involves the use of a storage container located on the customers' property does not alter the nature of the underlying transaction. Taxpayer is, of course, entitled to be fully compensated for the fact that it necessarily incurs expenses in delivering the propane to its customers. However, that compensation does not consist of lease payments.

FINDING

Taxpayer's protest is respectfully denied.

DEPARTMENT OF STATE REVENUE

0420020542.LOF

LETTER OF FINDINGS NUMBER: 02-0542
Sales and Use Tax
For the Years 1999, 2000, 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.

ISSUES

I. Sales and Use Tax-Supplies

Authority: IC 6-2.5-3-2 (a), IC 6-2.5-5-25 (a), IC 6-8.1-5-1, Sales Tax Division Information Bulletin #10 Revised February 10, 1986.

The taxpayer protests the assessment of use tax on certain supplies.

II. Tax Administration-Penalty

Authority: IC 6-8.1-10-2.1, 45 IAC 15-11-2.

The taxpayer protests the assessment of the negligence penalty.

STATEMENT OF FACTS

The taxpayer is a not-for-profit corporation created to receive, hold, administer and disburse funds to be used in promoting and advancing the general contracting industry in a certain geographic area of the state. The taxpayer provides assistance in construction employee apprenticeship programs, encouragement of programs to employ members of minority groups, advance skill training, supervisory training, construction technical education, safety education, accident prevention, and approved Red Cross certification program. After an investigation, the Indiana Department of Revenue, hereinafter referred to as the "department," assessed additional use tax, interest, and penalty. The taxpayer protested the assessment and a hearing was scheduled for April 27, 2004. No one appeared for the hearing. Therefore, this decision is based upon the information contained in the file.

I. Sales and Use Tax- Supplies

DISCUSSION

All tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC 6-8.1-5-1 (b). Indiana imposes an excise tax on tangible personal property stored, used, or consumed in Indiana unless the sales tax is paid on the transaction. IC 6-2.5-3-2 (a). Exemption from the use tax is granted to property used by qualified not-for-profit organizations under certain conditions at IC 6-2.5-5-25 (a) as follows:

> Transactions involving tangible personal property or service are exempt from the state gross retail tax, if the person acquiring the property or service:
>
> (a) is an organization which is granted a gross income tax exemption under IC 6-2.1-3-20, IC 6-2.1-3-21, or IC 6-2.1-3-22;
>
> (2) primarily used the property or service to carry on or to raise money to carry on the not-for-profit purpose for which it receives the gross income tax exemption; and
>
> (3) is not an organization operated predominantly for social purposes.

Sales Tax Division Information Bulletin #10 Revised February 10, 1986 further clarifies the exemption of not-for-profit corporation purchases for its own use from the use tax as follows:

> 1. In order to qualify for sales tax exemption on purchases as a not-for-profit organization the following conditions must prevail:
>
> (a) The organization must be named or described in IC 6-2.1-3-19, 6-2.1-3-20, 6-2.1-3-21 or 6-2.1-3-22. This includes not-for-profit organizations organized and operated exclusively for one or more of the following purposes... Educational....
>
> (c) The organization is not operated predominantly for social purposes.
>
> (d) In order for a purchase by a not-for-profit organization to qualify for exemption, the article purchased must be used for the same purpose as that for which the organization is being exempted. Purchases for the private benefit of any member of the organization or for any other individual, such as meals or lodgings, are not eligible for exemption. Purchases used for social purposes are never exempt.

The taxpayer provides a plan room where members from the construction industry can come to review building plans and blue prints for construction projects that are up for bids. In this room, drafting supplies, paper, and printing equipment are available for the contractors' use. The taxpayer did not pay sales tax when it purchased these supplies. Therefore, the department imposed use tax on the use of these items. The taxpayer argued that the use tax was improperly imposed because the items were used for an exempt purpose. The department disagrees with this conclusion. Rather the supplies are used for the private benefit of the individual members of the association. They are not used for the exempt activities of the organization.

FINDING

The taxpayer's protest is denied.

II. Tax Administration-Penalty

DISCUSSION

The taxpayer's final protest concerns the imposition of the ten percent (10%) negligence penalty pursuant to IC 6-8.1-10-2.1. Negligence is defined at 45 IAC 15-11-2(b) as "the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." Negligence is to "be determined on a case-by-case basis according to the facts and circumstances of each taxpayer." Id.

IC 6-8.1-10-2.1(d) allows the department to waive the penalty upon a showing that the failure to pay the deficiency was based on “reasonable cause and not due to willful neglect.” Departmental regulation 45 IAC 15-11-2 (c) requires that in order to establish “reasonable cause,” the taxpayer must demonstrate that it “exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed...” The taxpayer presented substantial evidence showing that it met this burden. The negligence penalty does not apply in this situation.

FINDING

The taxpayer’s protest is sustained.

DEPARTMENT OF STATE REVENUE

0420020569.LOF

LETTER OF FINDINGS NUMBER: 02–0569
Gross Retail and Use Tax—Adequate Documentation
Tax Administration—Penalty
For Tax Years 1999, 2000, 2001

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. Gross Retail and Use Tax—Adequate Documentation

Authority: IC § 6-8.1-5-1(b); IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-3-4; IC § 6-2.5-3-7; IC § 6-8.1-5-4(a); 45 IAC 15-3-8; 45 IAC 2.2-2-1; 45 IAC 2.2-3-4

Taxpayer protests the proposed assessments of Indiana’s use tax.

II. Tax Administration—Penalty

Authority: IC § 6-8.1-10-2.1; IC § 6-8.5-5-4(a); 45 IAC 15-11-2

Taxpayer protests the proposed assessment of the negligence penalty.

STATEMENT OF FACTS

Taxpayer is a heating and air conditioning contractor, selling and installing new heating and cooling systems pursuant to lump sum contracts. Because taxpayer failed to provide purchase invoices during the audit, the auditor could not verify that gross retail tax had been paid at the point of purchase; therefore, the auditor assessed use tax based on the best information available. Taxpayer then filed a protest, claiming documents were then available; the auditor was able to examine those documents and made some adjustments. However, taxpayer went forward with his protest. The remaining items at issue concern certain cash purchases for which taxpayer has no evidence he paid gross retail tax at the point of purchase. Additional facts will be added as necessary.

I. Gross Retail and Use Tax—Adequate Documentation

DISCUSSION

Taxpayer continues to protest the proposed assessment of Indiana use tax based on the best information available to the auditor at the time of the audit, and the 10% negligence penalty.

Taxpayer argued at the protest hearing that despite not having the evidence to show he paid gross retail tax, he did pay the tax on the cash purchases. Taxpayer claimed he did not mark up items after purchasing them, and that he did not keep his receipts, thinking that his cancelled checks would adequately fulfill his record-keeping responsibilities. Taxpayer during the tax years at issue was working full-time at another job, and starting up his own business with no accountant to help keep his books and records. Taxpayer admitted he thought his cancelled checks would be sufficient proof that he paid the state’s gross retail tax at the point of purchase.

Pursuant to IC § 6-8.1-5-1(b) and 45 IAC 15-5-3(8), a “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 assessment is made.” Pursuant to IC § 6-2.5-2-1, a “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.” *See also*, 45 IAC 2.2-2-1. Pursuant to IC § 6-2.5-3-2, an “excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana is the property was acquired in a retail transaction.” An exemption is provide in IC § 6-2.5-3-4 if “the property was acquired in a retail transaction and the state gross retail tax” was paid at the time of purchase. IC § 6-2.5-3-7 provides that a “person who acquires tangible personal property from a retail merchant for delivery in Indiana is presumed to have acquired the property for storage, use, or consumption in Indiana;” therefore, the presumption of taxability exists until rebutted. *See* *also*, 45 IAC 2.2-3-4.

Indiana taxpayers have the duty and responsibility under IC § 6-8.1-5-4(a) to "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." Taxpayer admitted he did not keep receipts from cash purchases. He is currently keeping the proper records and has an accountant now to keep him compliant and current with the Department's rules and regulations.

FINDING

Taxpayer's protest concerning the proposed assessments of Indiana's use tax is denied.

II. Tax Administration—Penalty

DISCUSSION

Taxpayer protests the imposition of the 10% negligence penalty. Indiana Code Section 6-8.1-10-2.1(d) states that if a taxpayer subject to the negligence penalty imposed under this section can show that the failure to file a return, pay the full amount of tax shown on the person's return, timely remit taxes 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. Indiana Administrative Code, Title 45, Rule 15, section 11-2 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 Indiana's tax statutes and administrative regulations.

In order for the Department to waive the negligence penalty, taxpayer must prove that its failure to pay the full amount of tax due was due to reasonable cause. Taxpayer may establish reasonable cause by "demonstrat[ing] that it exercised ordinary business care and prudence in carrying or failing to carry out a duty giving rise to the penalty imposed...." In determining whether reasonable cause existed, the Department may consider the nature of the tax involved, previous judicial precedents, previous department instructions, and previous audits.

Taxpayer made certain efforts to keep records. He attempted to comply with IC § 6-8.5-5-4(a) by keeping track of cancelled checks. The audit showed him he was in error. This was taxpayer's first audit and he has taken steps to rectify his error. In the Department's view, taxpayer has set forth a basis whereby the Department could conclude taxpayer exercised the degree of care statutorily imposed upon an ordinarily reasonable taxpayer. Given the totality of the circumstances, waiver of the penalty is appropriate in this instance because taxpayer was not willfully negligent; he merely made a mistake.

FINDING

Taxpayer's protest concerning the proposed assessment of the 10% negligence penalty is granted.

DEPARTMENT OF STATE REVENUE

01-20030012.LOF

LETTER OF FINDINGS NUMBER: 03-0012
Income Tax
For the Years 1999-2001

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

I. Income Tax-Cost of Goods Sold

Authority: IC 6-8.1-5-1(b).

The taxpayer protests the disallowance of certain expenses deducted as cost of goods sold on the federal Schedule C.

STATEMENT OF FACTS

The taxpayer operates a used car lot as a sole proprietor. He reports his income from the used car lot on a cash basis with Schedule C of the federal 1040 form. The Indiana Department of Revenue, hereinafter referred to as the "department," performed both a sales and use tax audit on the business and a personal income tax audit of the taxpayer. The sales tax audit and assessment was based on information provided by the Indiana Bureau of Motor Vehicles. The adjustment significantly increased the taxpayer's gross sales. Therefore, the taxpayer's Indiana adjusted gross income also increased. After receipt of the audit assessments, the taxpayer determined that he had not declared all expenses on his federal Schedule C. The taxpayer made changes to his Cost of Goods Sold and filed Amended Individual Income Tax Returns for the tax period 1999-2001. Upon review, the department accepted all but two of the additions to the Cost of Goods Sold. The first disallowed car was a new 1999 GMC 1500 purchased on February 18, 1999 from an area GMC dealer. It was sold at a local auto auction on September 14, 1999. The car's odometer reading was four (4) miles at the time of purchase and 6,420 miles at the time of sale. The other disallowed automobile was a new 2000 GMC 1500

4x4 purchased from the same dealer on September 15, 1999. At the time of purchase, the car's odometer registered 25 miles. At the time of audit, this car had not been sold and had an odometer reading of 30,200 miles. The taxpayer protested the department's disallowance of the deduction of the purchase prices of these two vehicles from the taxpayer's income. A telephone hearing was held and this Letter of Findings results.

I. Income Tax-Cost of Goods Sold

DISCUSSION

The taxpayer deducted the purchase prices of the two automobiles from its gross income as the cost of goods sold. The taxpayer supports this position by indicating that it actually sold one of the cars and advertised the other car for sale. The taxpayer argues that the miles were put on the cars by demonstrating them, using them to pick up parts, running necessary business errands, and driving to auto auctions. The department disallowed the deduction contending that the automobiles were purchased for personal use rather than resale. The department supports this contention by indicating that most cars purchased for resale by the used car business were used and these cars were new when purchased. The first car was sold at auction they day before the second car was purchased. Although the taxpayer placed ads to sell the second car, it was not sold during the audit period. Finally the taxpayer put a significant number of miles on each car – 6,216 on the first car and 30,175 on the second.

As a cash basis taxpayer, the purchase price of the second car cannot be deducted from the taxpayer's receipts on Schedule C as a cost of goods sold until the taxpayer actually sells it. Since the car was not sold during the audit period, it is not necessary to make the determination of whether the car was purchased for resale or for personal use.

It is a question of fact to determine if the first car was purchased for resale or personal use. Pursuant to IC 6-8.1-5-1 (b) all tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. The taxpayer argues that it actually sold the car and that proves that the car was purchased for resale. Considering all the facts, however, this argument is not persuasive. This car was purchased as a new car when most of the used car lot's cars were purchased as used cars. The taxpayer put close to 1,000 miles per month on the car. This is significantly more than normal use as a demonstrator and even a few trips to pick up a spare part for the dealership and attend auctions. Finally, it was sold the day before another new car was purchased. That new car was also driven in a manner indicating that it was for personal use rather than sitting on the lot as a car for resale. The taxpayer did not sustain his burden of proving that the first car was purchased for resale and its purchase price could be deducted from the taxpayer's income as a cost of goods sold.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

0420030022.LOF

LETTER OF FINDINGS NUMBER: 03-0022
Sales & Use Tax
For the Calendar Years 1999, 2000, & 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

I. Tax Administration – Penalty

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

The taxpayer protests the negligence penalty.

II. Tax Administration - Interest

Authority: IC 6-8.1-10-1

The taxpayer protests the interest assessment.

STATEMENT OF FACTS

The negligence penalty and interest were assessed on a Department audit conducted for the calendar years 1999, 2000, and 2001. The taxpayer is a bank located in Indiana.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty be waived as the taxpayer's employees were unaware of the requirement to pay use tax on the items listed in the audit report.

The Department points out the items were taxed in a previous audit.

The regulation which provides the guideline for penalty is as follows:

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

The Department finds the taxpayer was ignorant of tax duties. Ignorance is negligence and negligence is subject to penalty. As such, the Department finds the penalty proper and denies the penalty protest.

FINDING

The taxpayer's penalty protest is denied.

II. Tax Administration – Interest

DISCUSSION

The taxpayer argues the interest assessment should be adjusted to accrue through the period ending June 2002 instead of the period ending December 2002. The reason for this is because the audit was completed in March 2002 and the taxpayer did not get the assessment until November 2002. This prevented the taxpayer from paying the assessed tax until November 2002 which caused the taxpayer to be assessed additional interest.

The Department points out the audit was completed June 11, 2002 and the assessment was mailed October 29, 2002. The Department considers the assessment mailing timely. Furthermore, interest can not be waived according to statute. IC 6-8.1-10-1.

FINDING

The taxpayer's interest protest is denied.

DEPARTMENT OF STATE REVENUE

02-20030073.LOF

LETTER OF FINDINGS NUMBER: 03-0073
Corporate Income Tax
For the Years 1997-1999

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

ISSUES

I. Gross Income Tax-Imposition of Tax

Authority: IC 6-8.1-5-1 (b), IC 6-2.1-2-2(a)(2), 45 IAC 1.1-2-5(f)(2).

The taxpayer protests the imposition of tax on certain income.

II. Adjusted Gross Income Tax- Sales Factor for Apportionment

Authority: IC 6-3-2-1(a), IC 6-3-2-2(a), 20 NYCRR 4-4.3[d][2], 45 IAC 3.1-1-38.

The taxpayer protests the inclusion of certain revenue in the numerator of the sales factor for apportionment for the adjusted gross income tax.

STATEMENT OF FACTS

The taxpayer, commercially domiciled in New York, provides information and programming via satellite to customers throughout the United States. The taxpayer provides each customer the use of a fixed KU-band satellite dish, two video cassette recorders, 19-inch color television monitors and internal wiring. The taxpayer owns this equipment which is provided for the customer's use at no cost. The taxpayer also regularly services the equipment free of charge. If the customer were to stop using the taxpayer's services, the taxpayer would retrieve the equipment from the customer. All of the taxpayer's income is generated through national advertising sales that take place solely in the state of New York. The taxpayer's broadcasts originate from its studio in California. It has no employees in Indiana. Its only physical presence in Indiana is the television and satellite equipment it owns in the state. The taxpayer receives no payments in any form from those Indiana users.

After an audit, the Indiana Department of Revenue, hereinafter referred to as the "department," determined that there was no additional gross income tax liability for 1997 or 1998 and assessed additional gross income tax, interest, and penalty for 1999. In the audit, the department also included the taxpayer's revenue in the numerator of the sales factor for apportionment for the adjusted gross income tax. This change did not, however, result in an additional assessment of adjusted gross income tax. The taxpayer protested the assessment of gross income tax, redetermination of the numerator of the sales factor, and penalty. A hearing was held and this Letter of Findings results.

I. Gross Income Tax-Imposition of Tax

All tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC 6-8.1-5-1 (b).

The taxpayer's first protest concerns the department's imposition of gross income tax on its Indiana income. Indiana imposes a gross income tax on the "taxable gross income derived from activities or businesses or any other sources within Indiana by a taxpayer who is not a resident or a domiciliary of Indiana." IC 6-2.1-2-2(a)(2).

On January 1, 1999, a duly promulgated regulation became effective. That regulation defines "services performed within Indiana," for the telecommunications industry at 45 IAC 1.1-2-5(f)(2) as follows:

> ...sale of telecommunications, including telephone, telegraph, and non-cable television, 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.

To be considered income from an Indiana source and subject to the Indiana gross income tax, telecommunications must meet three tests. First, they must originate or terminate in Indiana. The taxpayer's signals sent to its Indiana customers clearly meet the first test of terminating in Indiana. Second, the fees for the services must be charged to an Indiana address. The taxpayer receives its income from advertisers located outside the state. No billings are sent to or fees received from the Indiana addresses of the taxpayer's Indiana customers. Since the subject services do not meet the second test, it is unnecessary to consider the third test. The subject telecommunication transmissions do not meet the standard to subject the taxpayer's income to Indiana gross income tax.

FINDING

The taxpayer's protest is sustained.

II. Adjusted Gross Income Tax-Sales Factor for Apportionment

DISCUSSION

The department recalculated the taxpayer's sales apportionment factor to include the taxpayer's Indiana advertising revenue in the numerator. Although this change has no effect on the taxpayer's proposed tax assessment, the taxpayer protested the change of the sales numerator. The taxpayer contends that since it had no employees in the state of Indiana and its sole source of income is advertising income sold outside of Indiana there is no basis for imposition of the Indiana adjusted gross income tax.

IC 6-3-2-1(a) imposes an adjusted gross income tax on "that part of the adjusted gross income derived from sources within Indiana of every nonresident person." IC 6-3-3-2(a) provides that adjusted gross income derived from sources within Indiana includes "income from doing business in this state."

The standard of "doing business in this state" is clarified at 45 IAC 3.1-1-38 as follows:

> For apportionment purposes, a taxpayer is "doing business" in a state if it operates a business enterprise or activity in such state including, but not limited to:
> (1) Maintenance of an office or other place of business in the state
> (2) Maintenance of an inventory of merchandise or material for sale distribution, or manufacture, or consigned goods
> (3) Sale or distribution of merchandise to customers in the state directly from company-owned or operated vehicles where title to the goods passes at the time of sale or distribution
> (4) Rendering services to customers in the state
> (5) Ownership, rental or operation of a business or of property (real or personal) in the state
> (6) Acceptance of orders in the state
> (7) Any other act in such state which exceeds the mere solicitation of orders so as to give the state nexus under P.L. 86-272 to tax its net income.

The taxpayer owns business personal property, fixed KU-band satellite dishes, video cassette recorders, 19-inch color television monitors, that is located in Indiana. The taxpayer also regularly services this personal property in Indiana. This servicing exceeds the mere solicitation of orders. Either of these conditions establishes sufficient nexus for Indiana to tax the proportion of adjusted gross income that comes from Indiana.

All of the taxpayer's income is derived from sales of advertising in the state of New York. In 1978, New York enacted a law considering the apportionment of advertising at 20 NYCRR 4-4.3[d][2] which provided, in pertinent part that:

> The broadcasting of... commercial messages by way of radio and television... is deemed to be a service. When a lump sum is received for such service, that lump sum shall be allocated to New York State and another state or states according to the number of listeners or viewers in each state.

This New York law indicates that New York does not tax the portion of the income from commercials on television that is derived from television viewers in other states. The department properly took the figure in the numerator of the Indiana sales factor from the taxpayer's books and records concerning the apportionment of the taxpayer's advertising income among the various states.

FINDING

The taxpayer's protest is denied.

DEPARTMENT OF STATE REVENUE

04-20030252.LOF

LETTER OF FINDINGS NUMBER: 03-0252
Gross Retail & Use Taxes
Penalty
For Years 1998, 1999, 2000, 2001

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. Gross Retail and Use Taxes—Agricultural exemption

Authority: IC § 6-8.1-5-1(b); IC § 6-2.5-2-1; IC § 6-2.5-3-1; IC § 6-2.5-3-4; IC § 6-2.5-3-6; IC § 6-2.5-3-7; IC § 6-2.5-5-1; IC § 6-2.5-5-2; 45 IAC 15-5-3(8); 45 IAC 2.2-2-1; 45 IAC 2.2-3-4; 45 IAC 2.2-5-1 through 45 IAC 2.2-5-7

Taxpayer protests the assessment of gross retail and use taxes on items obtained in retail transactions that taxpayer claims are entitled to the agricultural exemption.

II. Penalty—Request for Waiver

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

Taxpayer protests the imposition of the 10% negligence penalty on that portion of the assessment where the audit denied the agricultural exemption, and requests a waiver.

STATEMENT OF FACTS

Taxpayer operates a warehousing business as well as a number of different entrepreneurial endeavors. Taxpayer stores and repackages bulk liquid farm chemicals for several large companies. One of taxpayer's other business ventures included operating a farm on approximately two hundred (200) acres of the family land. The audit found that taxpayer was not in compliance with a number of Indiana's tax statutes and regulations, and made the requisite adjustments, including one denying taxpayer the agricultural exemption from the state's gross retail and use taxes. It is this denial that taxpayer is protesting. Additional facts will be added as necessary.

I. Gross Retail and Use Taxes—Agricultural exemption

DISCUSSION

Taxpayer protests the denial of its claim for application of the agricultural exemption to purchases connected to the farming operations. The auditor's rationale for denying the exemption focused on part of the two hundred (200) acres taxpayer uses to "showcase," for marketing and research purposes, different combinations of fertilizers and soils and their effect on crop productivity. During the audit years at issue, taxpayer participated in something called "Fields of Vision OnFarm," a yearly show and tell opportunity for taxpayer to exhibit results. The audit characterized taxpayer's agricultural activity as pure marketing and research and therefore denied the agricultural exemption. In reality, the farmed acreage was devoted to the growing and selling of corn and soybeans for profit, as evidenced by documents taxpayer produced at the hearing. It should be noted that, at the hearing officer's request, taxpayer searched for records to substantiate the agricultural exemption for the 2001 tax year. As there were none, taxpayer sent a letter to the Department admitting its tax liability for 2001. Therefore, that part of taxpayer's protest has, in effect, been withdrawn.

Pursuant to IC § 6-8.1-5-1(b) and 45 IAC 15-5-3(8), a "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 assessment is made." Pursuant to IC § 6-2.5-2-1, a "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." *See also*, 45 IAC 2.2-2-1. Pursuant to IC §§ 6-2.5-3-1 through 6-2.5-3-7, an "excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana is the property was acquired in a retail transaction." An exemption is provided in IC § 6-2.5-3-4 if "the property was acquired in a retail transaction and the state gross retail tax" was paid at the time of purchase. Taxpayers are personally liable for the tax. (IC § 6-2.5-3-6). IC § 6-2.5-3-7 provides that a "person who acquires tangible personal property from a retail merchant for delivery in Indiana is presumed to have acquired the property for storage, use, or consumption in Indiana;" therefore, the presumption of taxability exists until rebutted. *See also*, 45 IAC 2.2-3-4.

The standards for sustaining a claim for the agricultural exemption can be found at IC § 6-2.5-5-1, IC § 6-2.5-5-2, and 45 IAC 2.2-5-1 through 45 IAC 2.2-5-7. Both IC § 6-2.5-5-1 and IC § 6-2.5-5-2 exempt certain transactions involving particular items from the state's gross retail and use taxes if the following requirements are met: taxpayer must acquire the property for "direct use in the direct production of food or commodities for sale" and be 'occupationally engaged in the production of food or commodities" to be sold "for human or animal consumption." IC § 6-2.5-5-1. Secondly, "transactions involving agricultural machinery or equipment are exempt... if" taxpayer "acquires it for use in conjunction with the production of food or commodities for sale" and is "occupationally engaged in the production of food or commodities which he sells for human or animal consumption." IC § 6-2.5-5-2. Taxpayer's agricultural activities meet these statutory requirements. *See*, e.g., the lease executed between taxpayer and the landowner, Section Four, "Permissible Use." Taxpayer leased the property "for the purpose of producing crops." *See also*, invoices showing amounts taxpayer received as income from sales of soybeans and corn.

45 IAC 2.2-5-1 through 45 IAC 2.2-5-7 provide definitions for the important terms in the statutes. A farmer is someone "occupationally engaged in producing food or agricultural commodities for sale.... Only those persons, partnerships, or corporations whose intention it is to produce such food or commodities at a profit and not those persons who intend to engage in such production for pleasure or as a hobby qualify within this definition." 45 IAC 2.2-5-1(a). Taxpayer sold the crops produced through a somewhat complicated process involving selling to local elevators for "cash today" because farmers typically do not have easy access to transportation. Taxpayer chose someone to consolidate his crop with others at the point of distribution where it was stored and then delivered to the train for transport to a processing center.

A predominant use requirement appears nowhere in either the statutes or the regulations. *See*, 45 IAC 2.2-5-3(c)(1) and 45 IAC 2.2-5-4(b). That is, to receive the exemption, taxpayers can do what taxpayer in the instant case does: operate several different businesses for profit, simultaneously, including growing crops for profit, the only requirement for the exemption.

Taxpayer has provided sufficient evidence to show that it is entitled to the agricultural exemption for the transactions at issue.

FINDING

Taxpayer's protest concerning the audit's denial of the agricultural exemption on items purchased in connection with its business of growing crops, to the extent those items were actually used to produce crops for sale in 1998, 1999, and 2000, is granted.

II. Penalty—Request for waiver

DISCUSSION

Taxpayer protests the imposition of the 10% negligence penalty. Taxpayer argues that it had reasonable cause for failing to pay the appropriate amount of tax due because it reasonably believed it was entitled to the agricultural exemption for the retail transactions at issue.

Indiana Code Section 6-8.1-10-2.1(d) states that if a taxpayer subject to the negligence penalty imposed under this section can show that the failure to file a return, pay the full amount of tax shown on the person's return, timely remit taxes 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. Indiana Administrative Code, Title 45, Rule 15, section 11-2 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 Indiana's tax statutes and administrative regulations.

In order for the Department to waive the negligence penalty, taxpayer must prove that its failure to pay the full amount of tax due was due to reasonable cause. Taxpayer may establish reasonable cause by "demonstrat[ing] that it exercised ordinary business care and prudence in carrying or failing to carry out a duty giving rise to the penalty imposed...." In determining whether reasonable cause existed, the Department may consider the nature of the tax involved, previous judicial precedents, previous department instructions, and previous audits.

Taxpayer has set forth a basis whereby the Department could conclude taxpayer exercised the degree of care statutorily imposed upon an ordinarily reasonable taxpayer. Therefore, given the totality of all the circumstances, waiver of the penalty on that portion of the assessment due to denial of the agricultural exemption is appropriate in this particular instance.

FINDING

Taxpayer's protest concerning the proposed imposition of the 10% negligence penalty on the audit's denial of the agricultural exemption is granted.

DEPARTMENT OF STATE REVENUE

0220030406.LOF

LETTER OF FINDINGS: 03-0406
Indiana Corporate Income Tax
For the Years 1997, 1998, and 1999

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

ISSUES

I. Royalty Payments as Business Expenses.

Authority: IC 6-3-2-2(l); IC 6-3-2-2(m); Gregory v. Helvering 293 U.S. 465 (1935); Lee v. Commissioner of Internal Revenue, 155 F.2d 584 (2d Cir. 1998); Horn v. Commissioner of Internal Revenue, 968 F.2d 1229 (D.C. Cir. 1992); Commissioner v. Transp. Trading and Terminal Corp., 176 F.2d 570 (2nd Cir. 1949); Bethlehem Steel Corp. v. Ind. Dept. of State Revenue, 597 N.E.2d 1327 (Ind. Tax Ct. 1992).

Taxpayer argues that the Department of Revenue (Department) erred when it disallowed business expenses consisting of royalty payments paid to a related Delaware holding company.

II. Royalty Payment Amounts for 1999.

Authority: IC 6-8.1-5-1; IC 6-8.1-5-1(a); IC 6-8.1-5-1(b).

Taxpayer maintains that the Department's factual conclusion as to the amount of its 1999 royalty payments was erroneous.

STATEMENT OF FACTS

Taxpayer is an out-of-state company which manufacturers and sells electronic parts. As part of its business operation, taxpayer owned patents and trademarks. The patents and trademarks were attributable to inventions originated and produced by taxpayer and its various foreign and domestic affiliates.

Starting in 1991, taxpayer restructured ownership of its intellectual property including the patents and trademarks.

Prior to 1992, the ownership of the patents was held by taxpayer's "Patent Department." The "Patent Department" was one of taxpayer's wholly-owned subsidiaries. Effective September 1, 1992, taxpayer decided to reorganize its business operations and transformed its "Patent Department" into a separate corporation. Hereinafter, this newly formed "separate corporation" is referred to as the "Delaware holding company."

On September 2, 1992, taxpayer signed an agreement with Delaware holding company conveying and assigning to Delaware holding company all patent ownership rights to "inventions made from time to time by employees of [taxpayer] and... in the inventions described in such applications."

The September 2 assignment agreement was preceded by a "License Agreement" signed between taxpayer and Delaware holding company on September 1, 1992. The "License Agreement" granted taxpayer the exclusive right to use Delaware holding company's patents in its business operations. In addition, the Delaware holding company agreed to provide certain services related to the ownership of the patents. Delaware holding company agreed to maintain the patent registrations; investigate and prosecute patent infringements; investigate the "scope of the patents" and applicability of the relevant government property laws; and periodically conduct a "review of all [licensed] patent agreements and patent applications."

In consideration for the right to make use of the patents in its electronics part business, taxpayer agreed to pay Delaware holding company five percent of its sales revenue in the form of royalty fees.

On September 1, 1992, taxpayer and Delaware holding company entered into a second agreement indicating the taxpayer had assigned Delaware holding company rights to particular intellectual property previously licensed to taxpayer's international subsidiaries. Delaware holding company agreed to continue allowing the international subsidiaries the right to make use of this intellectual property. In return, Delaware holding company promised to pay taxpayer a portion of the license fees received from the international subsidiaries.

On January 1, 1993, taxpayer and Delaware holding company entered a third series of agreements in which taxpayer assigned Delaware holding company all of its "foreign trademark and service applications" along with its "common law marks... together with the goodwill of the business as symbolized by the marks." In an ancillary agreement, Delaware holding company agreed to license taxpayer the right to use the intellectual property in return for which taxpayer promised to pay Delaware holding company a royalty fee of one percent of its sales revenue.

During 2003, the Department conducted an audit review of taxpayer's business records and tax returns. The review resulted in an assessment of additional corporate income tax. Taxpayer disagreed with the results of the audit and submitted a protest to that effect. An administrative hearing was conducted during which taxpayer explained the basis for its protest. Subsequently, taxpayer determined that it would be appropriate to withdraw its challenge of two of the protested issues. However, taxpayer continues to challenge issues related to the payment of royalties to Delaware holding company. This Letter of Findings results.

DISCUSSION

I. Royalty Payments as Business Expenses.

During 1992 through 1994, taxpayer entered into a series of agreements by which it ostensibly transferred ownership of patents and trademarks to a wholly-owned Delaware holding company. The Delaware holding company agreed to perform certain particularized services in regard to maintaining that intellectual property. In return, taxpayer promised to pay Delaware holding company a royalty fee based upon taxpayer's sales. Taxpayer did so; it paid Delaware holding company approximately $159,000,000 in royalties during 1997, and it paid approximately $164,000,000 in royalties during 1998. Because – at the time of the audit review – exact business expense records were unavailable, the audit review estimated the amount of 1999 royalty payments based upon "the best information available." The audit estimated that taxpayer had paid approximately $121,000,000 in royalties during 1999. On its income tax returns, taxpayer deducted these royalty payments as business expenses.

During the audit review, the Department concluded that the royalty payments were not legitimate business expenses and disallowed the deductions. The audit did so because it found that the deduction "substantially diluted the federal taxable income that would be subject to Indiana adjusted gross and supplemental net income taxes and help[] to create net operating losses." The audit concluded that the royalty payments – and the underlying transfer of the intellectual property to Delaware holding company – were "transaction[s] with no true economic substance."

Taxpayer disagrees maintaining that the royalty payments were arm's-length payments to Delaware holding company for permission to use the patents and intellectual property. According to taxpayer, Delaware holding company is a "viable, substantive corporate entity with its own employees, office space, management, and on going operations." Taxpayer points out that Delaware holding company performs a number of legitimate functions by managing and maintaining the patents and intellectual property. Taxpayer indicates that Delaware holding company performs the following functions:

1. Delaware holding company conducts "clearance investigations" at the time taxpayer produces a potentially patentable new invention.
2. Delaware holding company "prosecutes" all domestic and foreign patent applications; i.e., it takes all the steps necessary to have patents actually issued in response to proposed applications.
3. Delaware holding company initiates legal proceedings related to potential patent infringements.

In addition to the above-listed description of Delaware holding company's responsibilities, taxpayer has provided information purporting to document the fact that Delaware holding company is an actual, honest-to-goodness corporate entity having its own employees, office space, management, and organizational structure all of which are directed toward maintaining and protecting Delaware holding company/taxpayer's patents and intellectual property.

The issue is whether the audit was justified in disregarding the royalty payments for purposes of calculating taxpayer's Indiana adjusted gross income.

IC 6-3-2-2(m) provides as follows:

> In the case of two (2) or more organizations, trades, or businesses owned or controlled directly or indirectly by the same interests, the department shall distribute, apportion, or allocate the income derived from sources within the state of Indiana between and among those organizations, trades, or businesses in order to fairly reflect and report the income derived from sources within the state of Indiana by various taxpayers.

In addition, IC 6-3-2-2(l) vests both taxpayers and the Department with authority to allocate and apportion a taxpayer's income within and among the members of a unitary group of related entities.

> 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 of any part of the taxpayer's business activity, if reasonable;
>
> (1) separate accounting;
> (2) the exclusion of any one (1) or more of the factors;
> (3) the inclusion of one (1) or more additional factors which will fairly represent the taxpayer's income derived from sources within the state of Indiana; or
> (4) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

Under IC 6-3-2-2(l), the audit was correct in disallowing the claimed business expenses in the form of royalty payments in order to "fairly represent the taxpayer's income derived from sources within the state of Indiana...." Id. Although the information provided by taxpayer does give evidence of the fact that Delaware holding performed a legitimate function by protecting the integrity of the patents and intellectual property, both the transfer of those properties to Delaware holding company and the resulting payment of substantial royalties are devoid of economic substance.

Prior to transferring ownership of the patents and intellectual property to Delaware holding company, there is no indication that any determination was made concerning the value of these properties. There is no indication that Delaware holding company gave any consideration in return for receiving ownership of the patents and intellectual property, which – by agreement of both taxpayer and the Department – consisted of property having both present and potential significant value. Instead, taxpayer apparently simply "assigned" these valuable properties to Delaware holding company without receiving any consideration in return. This seemingly arbitrary and one-sided transfer does not indicate that the transfer of the properties was a truly "arms-length" transaction.

In addition, the Delaware holding company was never a disinterested third-party at the onset of the initial property transfer or at the time it agreed to allow taxpayer continued use of the property. Although reconfigured in outward form, the Delaware holding company was at all times simply a wholly-owned division of the taxpayer's business operations. It would appear to be an inescapable conclusion that the patents and intellectual property were simply moved from one corporate pocket into another.

It is also noteworthy that after taxpayer assigned Delaware holding company ownership of the patents and trademarks, taxpayer then began to pay substantial sums of money for permission to use the very property which it once owned. During 1997, taxpayer paid Delaware holding company 159 million dollars; in 1998, taxpayer paid 164 million dollars; in 1999 taxpayer paid an estimated 121 million dollars. During these three years, taxpayer paid approximately $444,000,000 to Delaware holding company. Although it would appear that Delaware holding company is a viable business entity that performs certain legitimate services in connection with the patents and trademarks, the amount paid Delaware holding company seems wildly disproportionate to the services expected of Delaware holding company during this period.

The anomalous royalty payments are better understood in light of the fact that taxpayer and Delaware holding company have entered into a "revolving credit agreement." The agreement between the parties – as of 1999 – allows taxpayer to borrow up to $500,000,000 from Delaware holding company. As the Department understands this credit agreement, taxpayer is entitled to borrow from Delaware holding company the same money it paid in royalties. This conclusion is reinforced by the audit's finding that Delaware holding company paid taxpayer $180,000,000 in dividends to taxpayer during 1997 and paid $215,000,000 in dividends to taxpayer during 1998.

In sum, taxpayer transferred to wholly-owned Delaware holding company ownership of valuable intellectual property without receiving consideration in return. Delaware holding company performed certain services related to protecting the intellectual property. Taxpayer paid millions of dollars in the form of royalties for the right to use intellectual property which it transferred to Delaware holding company. Taxpayer received proportional sums from Delaware holding company in the form of dividends and loans. This arrangement enabled taxpayer to claim business expense deductions for the royalty payments and – presumably – the "interest" paid to Delaware holding company and attributable to the revolving credit agreement.

The Department is led to the conclusion that the audit was correct in disallowing the royalty payments as business expenses. The transfer of the patents and trademarks does not make any business sense. Instead, the transfer of the intellectual property to wholly-owned Delaware holding company, the payment of millions of dollars in the form of royalty payments for the right to use property which it gave away, and the "revolving credit agreement" by which taxpayer retrieved the royalty payments appear to be nothing more than a form of highly-stylized corporate theater.

In addition, the audit would have been justified in disallowing the royalty and interest deductions on the ground that the expenses were incurred as a result of a "sham transaction."

The "sham transaction" doctrine is well established both in state and federal tax jurisprudence dating back to Gregory v. Helvering 293 U.S. 465 (1935). In that case, the Court held that in order to qualify for a favorable tax treatment, a corporate reorganization must be motivated by the furtherance of a legitimate corporate business purpose. Id at 469. A corporate business activity undertaken merely for the purpose of avoiding taxes was without substance and "[t]o hold otherwise would be to exalt artifice above reality and to deprive the statutory provision in question of all serious purpose." Id at 470. The courts have subsequently held that "in construing words of a tax statute which describe [any] commercial transactions [the court is] to understand them to refer to transactions entered upon for commercial or industrial purposes and not to include transactions entered upon for no other motive but to escape taxation." Commissioner v. Transp. Trading and Terminal Corp., 176 F.2d 570, 572 (2nd Cir. 1949), *cert denied,* 338 U.S. 955 (1950). "[t]ransactions that are invalidated by the [sham transaction] doctrine are those motivated by nothing other than the taxpayer's desire to secure the attached tax benefit" but are devoid of any economic substance. Horn v. Commissioner of Internal Revenue, 968 F.2d 1229, 1236-37 (D.C. Cir. 1992). In determining whether a business transaction was an economic sham, two factors can be considered; "(1) did the transaction have a reasonable prospect, ex ante, for economic gain (profit), and (2) was the transaction undertaken for a business purpose other than the tax benefits?" Id. at 1337.

Taxpayer maintains that the transfer of its intellectual property to the Delaware holding company was made for a legitimate business purpose. Specifically, taxpayer points to the services Delaware holding company performed in protecting and maintaining the value of the intellectual property. However, the legitimate services Delaware holding company performed or in the manner in which Delaware holding company was compensated are not at issue. What is at issue is the validity of the initial transfer of the intellectual property and the consequent royalty payments. In this instance, there is nothing to indicate that the parties ever determined the value of the intellectual property before it was transferred. There is nothing to indicate that taxpayer ever received any consideration for the intellectual property at the time ownership of the property was transferred. There is no indication that the royalty payments were anything more than an arbitrary transfer of sums to a related entity.

The question of whether or not a transaction is a sham, for purposes of the doctrine, is primarily a factual one. Lee v. Commissioner of Internal Revenue, 155 F.2d 584, 586 (2d Cir. 1998). The taxpayer has the burden of demonstrating that the subject transaction was entered into for a legitimate business purpose. IC 6-8.1-5-1(b).

The taxpayer has failed to meet its burden of demonstrating that the transfer of the intellectual property to the Delaware holding company or that the royalty payments subsequently made were supported by any business purpose other than tax avoidance.

Taxpayer is, of course, entitled to structure its business affairs in any manner its sees fit and to vigorously pursue any tax advantage attendant upon the management of those affairs. However, in determining the nature of a business transaction and the resultant tax consequences, the Department is required to look at "the substance rather than the form of the transaction." Bethlehem Steel Corp. v. Ind. Dept. of State Revenue, 597 N.E.2d 1327, 1331 (Ind. Tax Ct. 1992). The transfer of the intellectual property and the royalty payments were purely matters of "form" and lack any business "substance."

FINDING

Taxpayer's protest is respectfully denied.

II. Royalty Payment Amounts for 1999.

At the time the original audit was conducted, it was not possible to determine the exact amount of royalty payments taxpayer paid Delaware holding company during 1999 because the payments were "included in broad categories and not broken down to individual expenses and amounts." Instead, the audit computed 1999 royalty payments based upon "the best information available." Based upon that available information, the audit found that taxpayer had paid 121 million dollars to Delaware holding company in the form of royalties during 1999.

Taxpayer now argues that the 121 million estimate was an overstatement of actual 1999 royalty payments. Taxpayer explains that it was not initially possible to provide the audit with more detailed information because it as "insufficiently staffed" and had recently "underwent significant management and staff level changes." Taxpayer maintains that it has subsequently reviewed its 1999 expenses and now finds that it paid approximately $99,000,000 in royalties during 1999.

The audit calculated the 1999 royalties under authority of IC 6-8.1-5-1 which states that, "If the department reasonably believes that a person has not reported the proper amount of tax due, the department shall make a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the department." IC 6-8.1-5-1(a).

The audit report's conclusion as to the amount of taxpayer's foreign source income expenses is presumed correct. "The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is correct." IC 6-8.1-5-1(b). The Department is not inclined to overturn the audit's finding as to the 1999 royalty payments based upon taxpayer's say-so because taxpayer has not met its burden of proving that the original assessment is *incorrect*; what taxpayer has done is advance an argument that is not entirely frivolous. The audit division is requested to review taxpayer's documentation and – to the extent taxpayer can substantiate its argument as the amount of 1999 royalties – make whatever adjustment it deems appropriate.

FINDING

To the extent taxpayer can substantiate its argument concerning the amount of royalties paid during 1999, taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

0320040073P.LOF

LETTER OF FINDINGS NUMBER: 04-0073P
Withholding Tax
For the month of April 2003

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

ISSUE

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2; 45 IAC 1-1-54

The taxpayer protests the late penalty.

STATEMENT OF FACTS

The late penalty was assessed on the late payment of a monthly withholding tax return for the month of April 2003.

The taxpayer is a company residing in Indiana.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty be waived as the tax return was missent to the taxpayer's residence instead of the taxpayer's business by the taxpayer's accountant. The taxpayer did not realize the tax form had been sent to his residence as his wife was hospitalized and the taxpayer did not open his mail until June 2003, whereupon the taxpayer realized the April return was overdue. Furthermore, the taxpayer argues he has a good compliance history.

With regard to the missent mail, the taxpayer is liable for the actions of an agent. In this case, the accountant. As such, the taxpayer is liable for the missent mail and fails to establish reasonable cause on this point. 45 IAC 1-1-54

With regard to the illness, the Department will waive penalty in the event of an incapacitating illness. However, the incapacitating illness must afflict the said taxpayer and prevent the taxpayer from performing tax duties. The Department does not feel the incapacitating illness on the part of the taxpayer's wife prevents the taxpayer from opening his mail and filing monthly tax returns on time. As such, the taxpayer fails to establish reasonable cause on this point.

With regard to the good compliance history that the taxpayer claims, the Department records show the Department has waived penalty on a previous liability. Due to the existence of a previous error, the Department does not feel the taxpayer has established a good compliance history. As such, the taxpayer fails to establish reasonable cause on this point.

45 IAC 15-11-2(b) states, "Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution,

or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer."

The Department finds the taxpayer inattentive to tax duties. Inattention is negligence and negligence is subject to penalty. As such, the Department finds the penalty proper and denies the penalty protest.

FINDING

The taxpayer's penalty protest is denied.

DEPARTMENT OF STATE REVENUE

0420040074P.LOF

LETTER OF FINDINGS NUMBER: 04-0074P
Sales Tax
For the month of April 2003

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

ISSUE

I. Tax Administration – Penalty

Authority: IC 6-8.1-10-2.1(d); 45 IAC 15-11-2; 45 IAC 1-1-54

The taxpayer protests the late penalty.

STATEMENT OF FACTS

The late penalty was assessed on the late payment of a monthly sales tax return for the month of April 2003.
The taxpayer is a company residing in Indiana.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty be waived as the tax return was missent to the taxpayer's residence instead of the taxpayer's business by the taxpayer's accountant. The taxpayer did not realize the tax form had been sent to his residence as his wife was hospitalized and the taxpayer did not open his mail until June 2003, whereupon the taxpayer realized the April returns were overdue. Furthermore, the taxpayer argues he has a good compliance history.

With regard to the missent mail, the taxpayer is liable for the actions of an agent. In this case, the accountant. As such, the taxpayer is liable for the missent mail and fails to establish reasonable cause on this point. 45 IAC 1-1-54

With regard to the illness, the Department will waive penalty in the event of an incapacitating illness. However, the incapacitating illness must afflict the said taxpayer and prevent the taxpayer from performing tax duties. The Department does not feel the incapacitating illness on the part of the taxpayer's wife prevents the taxpayer from opening his mail and filing monthly tax returns on time. As such, the taxpayer fails to establish reasonable cause on this point.

With regard to the good compliance history that the taxpayer claims, the Department records show the Department has waived penalty on a previous liability. Due to the existence of a previous error, the Department does not feel the taxpayer has established a good compliance history. As such, the taxpayer fails to establish reasonable cause on this point.

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

The Department finds the taxpayer inattentive to tax duties. Inattention is negligence and negligence is subject to penalty. As such, the Department finds the penalty proper and denies the penalty protest.

FINDING

The taxpayer's penalty protest is denied.

DEPARTMENT OF STATE REVENUE

0320040112.LOF

LETTER OF FINDINGS NUMBER: 04-0112
Sales and Withholding Tax
Responsible Officer
For the Tax Period April, 1999 – November, 1999

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

ISSUE

1. Sales Tax and Withholding Taxes -Responsible Officer Liability

Authority: IC 6-2.5-9-3, IC 6-3-4-8(f), IC 6-8.1-5-1(b).

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

STATEMENT OF FACTS

The Indiana Department of Revenue, hereinafter referred to as the "department," assessed sales taxes, withholding taxes, interest and penalty against the taxpayer as a responsible officer of a corporation that did not properly remit said trust taxes during the tax period April, 1999 through November, 1999. The taxpayer protested the assessment and a hearing was held.

1. Sales and Withholding Taxes-Responsible Officer Liability

DISCUSSION

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).

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 the 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."

The taxpayer provided significant documentation evidencing that he left his position with the corporation in November, 1998. Since the taxpayer was not an employee, officer, or member of the corporation from April, 1999 through November, 1999, the taxpayer cannot be held personally responsible for trust taxes that the corporation did not remit to the state.

FINDING

The taxpayer's protest is sustained.

DEPARTMENT OF STATE REVENUE

0420040143P.LOF

LETTER OF FINDINGS NUMBER: 04-0143P
Sales & Use Tax
For the Month of January 2003

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 superceded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration – Penalty

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

The taxpayer protests the late penalty.

II. Tax Administration – Interest

Authority: IC 6-8.1-10-1

The taxpayer protests the interest assessment.

STATEMENT OF FACTS

The late penalty and interest were assessed on the late filing of a monthly sales tax return for the month of January 2003.

The taxpayer is located in Indiana.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty be waived as the error was the result of an inadvertent miscalculation. Furthermore, the taxpayer cites a good payment history as a factor in waiving the penalty.

The Department points out the taxpayer has had a previous error with regard to the filing of monthly trust taxes. Because of the previous error, the Department does not feel the taxpayer has established a good payment history that would be a factor in waiving a penalty.

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

The Department finds the taxpayer was inattentive of tax duties as a result of the miscalculation. As inattention is negligence and subject to penalty, the Department finds the penalty proper and denies the penalty protest.

FINDING

The taxpayer's penalty protest is denied.

II. Tax Administration – Interest

Interest may not be waived according to statute. IC 6-8.1-10-1.

DEPARTMENT OF STATE REVENUE

0320040160P.LOF

LETTER OF FINDINGS NUMBER: 04-0160P
Withholding Tax
For the periods March 31,2002, June 30, 2002, September 30, 2002,
December 31, 2002, March 31, 2003 and June 30, 2003

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

ISSUE

I. Tax Administration – Penalty

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

The taxpayer protests the late penalty.

II. Tax Administration - Interest

Authority: IC 6-8.1-10-1

The taxpayer protests the interest assessment.

STATEMENT OF FACTS

The late penalty and interest were assessed on the late filing of a monthly withholding tax returns for the months of March 31, 2002, June 30, 2002, September 31, 2002, December 31, 2002, March 31, 2003, and June 30, 2003.

The taxpayer is a sole proprietorship located in Indiana.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty be waived as the errors were the result of the in-charge bookkeeper (the wife of the taxpayer) having an incapacitating illness. The incapacitating illness prevented the bookkeeper from properly filing the quarterly withholding tax returns for the aforementioned periods. The taxpayer did not become aware of the degree of the bookkeeper's illness until October 2003 upon counsel from the doctor.

The taxpayer also cites a good payment history as a factor in waiving the penalty.

With regard to the incapacitating illness, the Department waives penalty in the event of an incapacitating illness. In the instant case, the doctor's letter states the bookkeeper was incapacitated through the year 2003. Nothing was said about 2002.

With regard to the payment history, the Department notes the taxpayer has had several errors in previous periods. The Department does not feel the taxpayer has established a good payment history that would be a factor in waiving penalty.

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

The Department finds incapacitating illness to be cause in not filing the tax returns on time. The doctor's letter covers the periods of December 31, 2002, March 31, 2003, and June 30, 2003. Thus, the penalty protest is sustained for these three periods. The penalty protest is denied for the periods March 31, 2002, June 30, 2002, and September 30, 2002 as the doctor's letter did not cover these periods.

FINDING

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

II. Tax Administration – Interest

Interest may not be waived according to statute. IC 6-8.1-10-1.

DEPARTMENT OF STATE REVENUE

0420040161P.LOF

LETTER OF FINDINGS NUMBER: 04-0161P
Sales & Use Tax
For the periods August 31, 2002, October 31, 2002, November 30, 2002, April 30, 2003, May 31, 2003, June 30, 2003, July 31, 2003, and August 31, 2003

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

ISSUE

I. Tax Administration – Penalty

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

The taxpayer protests the late penalty.

II. Tax Administration – Interest

Authority: IC 6-8.1-10-1

The taxpayer protests the interest assessment.

STATEMENT OF FACTS

The late penalty and interest were assessed on the late filing of monthly sales tax returns for the months of August 31, 2002, October 31, 2002, November 30, 2002, April 30, 2003, May 31, 2003, June 30, 2003, July 31, 2003, and August 31, 2003.

The taxpayer is a sole proprietorship located in Indiana.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty be waived as the errors were the result of the in-charge bookkeeper (the wife of the taxpayer) having an incapacitating illness. The incapacitating illness prevented the bookkeeper from properly filing the monthly sales tax returns for the aforementioned periods. The taxpayer did not become aware of the degree of the bookkeeper's illness until October 2003 upon counsel from the doctor.

The taxpayer also cites a good payment history as a factor in waiving the penalty.

With regard to the incapacitating illness, the Department waives penalty in the event of an incapacitating illness. In the instant case, the doctor's letter states the bookkeeper was incapacitated through the year 2003. Nothing was said about 2002.

With regard to the payment history, the Department notes the taxpayer has had several errors in previous periods. The Department does not feel the taxpayer has established a good payment history that would be a factor in waiving penalty.

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

the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer."

The Department finds incapacitating illness to be cause in not filing the tax returns on time. The doctor's letter covers the periods of the calendar year 2003. Thus, the penalty protest is sustained for the periods April 30, 2003, May 31, 2003, June 30, 2003, July 31, 2003, and August 31, 2003. The penalty protest for the periods in the calendar year 2002 are denied. These periods are August 31, 2002, October 31, 2002, and November 30, 2002.

FINDING

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

II. Tax Administration – Interest

Interest may not be waived according to statute. IC 6-8.1-10-1.

DEPARTMENT OF STATE REVENUE

0320040162P.LOF

LETTER OF FINDINGS NUMBER: 04-0162P
Withholding Tax
For the Month of December 2003

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 superceded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Tax Administration – Penalty

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

The taxpayer protests the late penalty.

II. Tax Administration - Interest

Authority: IC 6-8.1-10-1

The taxpayer protests the interest assessment.

STATEMENT OF FACTS

The late penalty and interest were assessed on the late filing of a monthly withholding tax return for the month of December 2003.

The taxpayer is a local government organization located in Indiana.

I. Tax Administration – Penalty

DISCUSSION

The taxpayer requests the penalty be waived as the error was the result of the new Clerk-Treasurer being unaware of the early filing status.

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

The Department finds the taxpayer was ignorant of tax duties. As ignorance is negligence and subject to penalty, the Department finds the penalty proper and denies the penalty protest.

FINDING

The taxpayer's penalty protest is denied.

II. Tax Administration – Interest

Interest may not be waived according to statute. IC 6-8.1-10-1.
